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The President of the Legislative Council,
Legislative Council Complex,
Hong Kong.

Sir,

In accordance with the paper tabled in the Provisional Legislative Council on 11 February 1998 on the Scope of Government Audit in the Hong Kong Special Administrative Region — ‘Value for Money Audits’, I have the honour to submit my Report No. 69 on the results of value for money audits completed in accordance with the value for money audit guidelines laid down in the paper. These guidelines are also attached.

Yours faithfully,

David Sun

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The Director of Audit's Report No. 69 contains the following chapters:

Chapter	Subject
1	Administration of lump sum grants by the Social Welfare Department
2	Procurement and maintenance of government vessels
3	Hospital Authority's management of public hospital projects
4	Regulation of non-franchised bus and school private light bus services
5	Operation of the Land Registry
6	Regulation of hotels and guesthouses
7	Hong Kong Design Institute
8	Provision of government office accommodation and utilisation of government sites
9	Occupational safety and health

VALUE FOR MONEY AUDIT GUIDELINES

Value for money audit

Value for money audit is an examination into the economy, efficiency and effectiveness with which any bureau of the Government Secretariat, department, agency, other public body, public office, or audited organisation has discharged its functions. Value for money audit is carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and have been accepted by the Administration.

2. The guidelines are:

- firstly, the Director of Audit should have great freedom in presenting his reports to the Legislative Council. He may draw attention to any circumstance which comes to his knowledge in the course of audit, and point out its financial implications. Subject to the guidelines, he will not comment on policy decisions of the Executive and Legislative Councils, save from the point of view of their effect on the public purse;
- secondly, in the event that the Director of Audit, during the course of carrying out an examination into the implementation of policy objectives, reasonably believes that at the time policy objectives were set and decisions made there may have been a lack of sufficient, relevant and reliable financial and other data available upon which to set such policy objectives or to make such decisions, and that critical underlying assumptions may not have been made explicit, he may carry out an investigation as to whether that belief is well founded. If it appears to be so, he should bring the matter to the attention of the Legislative Council with a view to further inquiry by the Public Accounts Committee. As such an investigation may involve consideration of the methods by which policy objectives have been sought, the Director should, in his report to the Legislative Council on the matter in question, not make any judgement on the issue, but rather present facts upon which the Public Accounts Committee may make inquiry;
- thirdly, the Director of Audit may also consider as to whether policy objectives have been determined, and policy decisions taken, with appropriate authority;

- fourthly, he may also consider whether there are satisfactory arrangements for considering alternative options in the implementation of policy, including the identification, selection and evaluation of such options;
- fifthly, he may also consider as to whether established policy aims and objectives have been clearly set out; whether subsequent decisions on the implementation of policy are consistent with the approved aims and objectives, and have been taken with proper authority at the appropriate level; and whether the resultant instructions to staff accord with the approved policy aims and decisions and are clearly understood by those concerned;
- sixthly, he may also consider as to whether there is conflict or potential conflict between different policy aims or objectives, or between the means chosen to implement them;
- seventhly, he may also consider how far, and how effectively, policy aims and objectives have been translated into operational targets and measures of performance and whether the costs of alternative levels of service and other relevant factors have been considered, and are reviewed as costs change; and
- finally, he may also be entitled to exercise the powers given to him under section 9 of the Audit Ordinance (Cap. 122).

3. The Director of Audit is not entitled to question the merits of the policy objectives of any bureau of the Government Secretariat, department, agency, other public body, public office, or audited organisation in respect of which an examination is being carried out or, subject to the guidelines, the methods by which such policy objectives have been sought, but he may question the economy, efficiency and effectiveness of the means used to achieve them.

4. Value for money audit is conducted in accordance with a programme of work which is determined annually by the Director of Audit. The procedure of the Public Accounts Committee provides that the Committee shall hold informal consultations with the Director of Audit from time to time, so that the Committee can suggest fruitful areas for value for money audit by the Director of Audit.

CHAPTER 1

**Labour and Welfare Bureau
Social Welfare Department**

**Administration of lump sum grants by the
Social Welfare Department**

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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ADMINISTRATION OF LUMP SUM GRANTS BY THE SOCIAL WELFARE DEPARTMENT

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ADMINISTRATION OF LUMP SUM GRANTS BY THE SOCIAL WELFARE DEPARTMENT

Executive Summary

1. The Social Welfare Department (SWD) is responsible for developing and co-ordinating welfare services in Hong Kong. It provides subventions to non-governmental organisations (NGOs) for the provision of welfare services to the public. Welfare services provided by NGOs comprise elderly services, family and child welfare services, rehabilitation services, and youth and corrections services. Under these four areas of welfare services, there are some 140 types of services (e.g. elderly services include day care centres for the elderly and integrated home care services).

2. Before January 2001, subventions were provided to NGOs through the conventional subvention system, under which the SWD paid NGOs for the actual costs incurred in the delivery of recognised welfare services. In January 2001, a lump sum grant (LSG) subvention system was rolled out as a major revamp of the provision of funding to NGOs. NGOs receiving subventions under the conventional subvention system are not obliged to but may voluntarily opt for the LSG subvention system. In 2016-17, of the 170 NGOs receiving subventions from the SWD, 165 (97%) were under LSG subvention system, while the other five (3%) NGOs remained in the conventional subvention system. In 2016-17, the total amount of LSG subventions paid to the NGOs was \$12.5 billion.

3. LSG subvention is provided on an NGO basis. The annual amount of LSG subvention to an NGO is the sum of staff salaries, provision for provident funds and other charges (e.g. administrative expenses, utilities and overtime allowance for drivers), minus the NGO's fee income recognised by the SWD (e.g. monthly residential fee of \$1,994 for elderly nursing homes as at 1 April 2016). Under the LSG subvention system, NGO management has the autonomy and flexibility in the deployment of subvention resources to meet the service needs. Within the context of the Funding and Service Agreements (FSAs), which include the carrying out of FSA

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related activities and other support services, NGOs have flexibility in deploying the LSG subventions to pay their expenses (staff expenses and other operating expenses).

4. An NGO can retain unspent LSG subvention in a reserve (i.e. known as the LSG Reserve) to meet future spending. The cumulative reserve (separate from Provident Funds (PF) Reserve and Holding Account balances — see para. 8) is capped at 25% of the annual operating expenditure (excluding expenditure for provident funds) of the subvented services of the NGO. Any amount above the 25% cap is subject to claw-back and should be returned to the Government. The reserve can be used at the discretion of the NGO on FSA activities and FSA related activities.

5. The SWD draws up an FSA for each service (see para. 1) that a service unit of an NGO provides. For example, if a unit provides two services, two FSAs are drawn up and the SWD regards the unit as two “agreement service units” (ASUs). The FSA defines the welfare service to be provided by an ASU. It also stipulates the Output Standards (e.g. enrolment rates) and Outcome Standards (e.g. percentage of service users with improved capability in managing family problems) to be achieved by the ASU, Essential Service Requirements (ESRs — e.g. staff qualifications and opening hours of institutions) to be met by the ASUs, the need to observe the 16 Service Quality Standards (SQSs), and the need to follow the requirements laid down in the LSG Manual and LSG Circulars. The NGOs are also required to adopt the best practices laid down in the Best Practice Manual (BPM — see para. 22) developed under the auspices of the LSG Steering Committee (see para. 6). As at 31 March 2017, the SWD drew up FSAs for 2,691 ASUs of the 165 NGOs.

6. An LSG Steering Committee has been appointed by the Labour and Welfare Bureau (LWB) to monitor the implementation of the LSG subvention system and identify areas for improvement. An LSG Independent Complaints Handling Committee has also been set up to handle LSG-related complaints that cannot be satisfactorily addressed at the NGO level.

7. The Audit Commission (Audit) has recently conducted a review of the administration of LSGs by the SWD. In addition to data analyses and examination of the SWD records (covering NGOs and ASUs), Audit paid visits to: (a) five NGOs and five of their ASUs to examine specifically certain welfare services with underperformance in the period 2014-15 to 2016-17; and (b) six NGOs and 18 of their ASUs to examine their use of LSG subventions in general.

Financial monitoring

8. *Need to implement good practices on the use of reserves.* As at 31 March 2016, a total of \$4.7 billion of reserves was retained by NGOs. Of these reserves: (a) \$1.7 billion was LSG Reserve (see para. 4) held by 150 NGOs; (b) \$1.8 billion was balances in Holding Accounts held by 122 NGOs (the Holding Accounts arose because the SWD withheld the claw-back of LSG Reserves above the 25% cap (see para. 4) for three years from 2004-05 to 2006-07); and (c) \$1.2 billion was PF Reserve held by 159 NGOs. NGOs may use the LSG Reserves and Holding Account balances for FSA activities and FSA related activities, while PF Reserve can only be used for provident fund contributions. NGOs are expected to follow the guidelines of the BPM (see para. 5) relating to the use of the reserves. The aggregate amount of these reserves had risen by 38% from \$3.4 billion in 2011-12 to \$4.7 billion in 2015-16. In six of the NGOs visited by Audit (see para. 7(b)), Audit noted that some NGOs had planned their use of reserves. The SWD needs to: (a) take further measures to facilitate NGOs to share, adopt and implement the good practices relating to the use of reserves and disclose the use of reserves according to the BPM guidelines; (b) in circumstances where NGOs are unable to comply with the BPM guidelines, ensure that NGOs provide strong justifications and give consent for exemption where appropriate; and (c) keep in view the balances of reserves and where necessary, remind NGOs to take further measures to maximise the use of the reserves for enhancing FSA activities and FSA related activities (paras. 1.9, 2.3 to 2.5, 2.8, 2.10 and 2.11).

9. *NGOs with persistent LSG operating deficits.* Audit found that in 2015-16, 31 NGOs had incurred LSG operating deficits. Of these 31 NGOs, 14 had incurred deficits for three consecutive years from 2013-14 to 2015-16. Of these 14 NGOs, 8 had depleted their LSG reserves (i.e. LSG Reserves and Holding Account balances) and financed their operations from non-FSA sources (e.g. income from self-financing activities). The remaining 6 NGOs still had LSG reserves after offsetting their LSG deficits against their reserves. The SWD needs to: (a) ascertain the reasons for NGOs having persistent LSG operating deficits, and offer advice where warranted; and (b) keep under review the operation of those NGOs in deficits for possible financial viability issues and to ensure smooth provision of FSA activities to the public (paras. 2.13 and 2.15).

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10. ***Disclosure of NGOs' senior staff emoluments.*** In March 2003, the Director of Administration issued a Circular Memorandum (the Memorandum) requiring a subvented body to review and disclose annually the remunerations of its top three-tier staff unless it meets one or more of the exemption criteria (e.g. the average government subvention received in past four years constituted a proportion of 50% or less of the subvented body's average operating income in the same period). In 2015-16, of the 165 NGOs receiving LSG subventions, 66 (40%) were not exempted from the disclosure requirement. Audit found that: (a) ***Deferring the implementation of disclosure requirement.*** The effective date for implementation of the disclosure requirement was 1 April 2003. However, the SWD implemented the disclosure requirement with effect from a later date in 2009-10. There was no documentary evidence indicating that the Labour and Welfare Bureau (LWB) had approved deferring the implementation of the disclosure requirement; and (b) ***More NGOs may be required to disclose senior staff emoluments.*** In July 2017, the Director of Administration informed the SWD that the SWD's prevailing practice of reviewing and disclosing the remunerations of NGOs' top three-tier staff had been at variance with the intents of the Memorandum. The SWD had applied the 50% income threshold based on the consolidated operating income of the NGO instead of the operating income of the NGO under the purview of the LWB and the SWD. If the intents of the Director of Administration's Memorandum had been applied, more NGOs would have been required to disclose their senior staff emoluments. The SWD should discuss with the LWB on its planned actions in the coming annual review (paras. 2.18 to 2.20, 2.22 and 2.24).

11. ***Scope for improvement in accounting inspections.*** The SWD's Finance Branch conducts accounting inspections at NGO premises which include reviewing compliance with accounting and financial reporting requirements as laid down in the LSG Manual, and reviewing/advising on internal control procedures. Audit reviewed the accounting inspections conducted by the SWD's Finance Branch and found that: (a) in 2016-17, of the 53 NGOs involving a total of 120 ASUs planned to be inspected, inspections at 6 NGOs (11% of 53) involving a total of 21 ASUs (18% of 120) had not been conducted as planned; (b) some irregularities (e.g. inclusion of non-FSA expenses in LSG) and internal control weaknesses (e.g. in revenue collection and receipt) were commonly found in inspections of ASUs of NGOs; (c) internal control weaknesses of ASUs of some NGOs had existed for a long period of time; and (d) there are other risk factors that the Finance Branch had not been considered in formulating its risk-based inspections (e.g. NGOs with operating deficits) (paras. 2.30 and 2.33).

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12. ***Cross-subsidisation between LSG subventions and self-financing activities.*** It is common that NGOs providing FSA activities (including FSA related activities) also provide non-FSA activities. NGOs are not allowed to use LSG subventions to cross-subsidise non-FSA activities. Audit found that: (a) ***Need to apportion head office overheads.*** Each of the six NGOs visited by Audit had established a head office, which carried out central administrative and support functions for the respective NGO. In 2015-16, the six NGOs incurred overheads totalling some \$71.9 million for their head offices. For three NGOs, the head office overheads (ranging from \$10.5 million to \$22.2 million in 2015-16) had been allocated entirely to FSA activities; and (b) ***Need to adopt appropriate bases for apportioning overheads.*** The bases used by the two NGOs for apportioning the overheads between FSA activities and non-FSA activities were not always consistent and proportionate. For example, the emolument of \$1.57 million of an NGO's Chief Executive Officer for 2015-16 had been solely charged to FSA activities (paras. 2.36 to 2.40).

Self-assessment of service quality by non-governmental organisations

13. ***Inadequacies in conduct and reporting of self-assessment.*** NGOs are required to conduct and submit to the SWD self-assessment of attainment of Output Standards, Outcome Standards, ESRs and SQSs on a regular basis. Audit's examination of the Output/Outcome Standards reported by NGOs to the SWD in the period 2014-15 to 2016-17 revealed that: (a) there were cases where these Standards had not been accurately reported by NGOs, resulting in overstatement or understatement of performance reported; and (b) there was room for improvement in measuring service effectiveness. For example, in measuring the service effectiveness upon completion of training of service users, of the 30 cases of service users examined by Audit, an NGO conducted clinical assessments of 14 cases via telephone only, instead of on site. Furthermore, the NGO regarded training as having completed when service users had completed 10% or more of the planned training sessions (paras. 3.2, 3.6 and 3.7).

14. ***Inadequacies in implementation of SQSs.*** According to the SWD, as SQSs provide a broad overview of what the ASUs should do in order to deliver quality services, NGOs are expected to tailor-make their own SQS manuals to facilitate the attainment of SQSs. Audit visited 18 ASUs of 6 NGOs and found that: (a) there were cases of non-compliance with the NGOs' SQS manuals (e.g. two service users took

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temporary leave from an ASU for more than 7 days (ranging from 9 to 30 days) without the approval of the Superintendent); (b) 11 ASUs had not used the SWD's self-assessment checklist to assist their conduct of self-assessment on SQSs; and (c) an ASU's checklist indicated that the ASU had made available its annual reports and service pamphlets at its office in audio and Braille formats to service users. Audit, however, could not locate such documents in the ASU's office (paras. 3.10 to 3.12).

Monitoring of service delivery by Social Welfare Department

15. *Underperformance of NGOs.* If an ASU of an NGO is found to be non-conforming with the required performance standards, the NGO is required to submit to the SWD an action plan detailing how the service is to be improved. If an NGO fails to improve after repeated efforts, the ultimate sanction will be for the SWD to withdraw its LSG for the ASU in question. In the period January 2001 to September 2017, the SWD had exercised its power to terminate the LSG subvention of one NGO. Audit examined 20 ASUs that had underperformance in Output/Outcome Standards in three or more consecutive years in the five-year period 2012-13 to 2016-17. Audit found that although the NGOs concerned had submitted action plans to improve their services in each of the consecutive years, the underperformance persisted. In the five-year period, excluding the 6 ASUs whose subventions were based on caseloads attained (see para. 16 below), all the other 14 ASUs had received full LSG subventions (paras. 4.2 and 4.3).

16. *Subventions to NGOs based on caseloads attained.* In view of the unexpected low utilisation rates of the home care service for persons with severe disabilities (HCS) and the integrated support service for persons with severe physical disabilities (ISS), and in order to optimise the use of public money, subventions to the NGOs providing the HCS and the ISS have been pegged to the number of users served (i.e. caseloads) since April 2015 and August 2015 respectively. Of the six ASUs providing the HCS and the two ASUs providing the ISS, Audit visited two HCS ASUs and one ISS ASU. For each of the three ASUs visited, Audit examined 50 cases of users, covering the period from April 2015 to December 2016, to ascertain the adequacy of provision of subventions to NGOs based on caseloads attained by the ASUs (paras. 4.7 and 4.12). Audit found that:

- (a) *Need to review underperformance in provision of HCS and ISS.* While the eight ASUs (six ASUs providing the HCS and two ASUs providing the

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ISS) had attained the required caseloads and received full subventions from the SWD in 2015-16 and 2016-17, the ASUs had significant underperformance in the provision of the HCS and the ISS (e.g. for an ASU providing the HCS, while the agreed number of service hours to meet the care needs of service users in 2016-17 was 158,400, the actual number achieved was only 34,201);

- (b) ***Different determining factors used in computing caseloads.*** Different determining factors were used in computing caseloads by the three ASUs visited. While one ASU would include a case in the caseload when a person was admitted as a service user after assessing his/her eligibility for the service, the other two ASUs would include a case when a care plan had been formulated for the service user after admission;
- (c) ***Cases with no support services provided.*** There were cases where no support service (e.g. nursing care service) had been provided to the service users (e.g. of the 50 cases examined by Audit, for one ASU visited, 13 (26%) service users had no support services provided);
- (d) ***Delay in discharging service users.*** There was delay in discharging service users by two ASUs visited. Of the 28 cases where there was delay, in 22 cases, the service users could have been discharged in the last financial year but were instead discharged in the new financial year. As the SWD only takes into account the number of users discharged as at 31 March of the last financial year in calculating subventions to the ASUs in the new financial year, discharging users in the new financial year means that subventions would continue to be paid to the ASUs for the discharged service users;
- (e) ***Service users receiving both HCS and ISS.*** To avoid duplication of resources, a service user can be admitted into either the HCS or the ISS, but not both. Audit, however, found that in the three ASUs visited, four service users received both the support services under the HCS and the ISS; and
- (f) ***Need to review arrangement for calculating subventions to ASUs.*** In view of the three ASUs' higher-than-expected discharge rates (ranging from 27% to 38%), Audit recalculated the subventions provided to these ASUs in years 2015-16 and 2016-17 based on the number of daily active users

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instead of the number of active users as at 31 March of the last financial year (the SWD's methodology of calculating subventions to the ASUs providing the HCS and the ISS). Audit's recalculation, using the number of daily active users as the basis, indicated that potential savings in subventions of \$12.9 million in 2015-16 and \$4.1 million in 2016-17 to the three ASUs could be achieved. Savings in subventions realised could be used for the provision of other welfare services (paras. 4.10, 4.13, 4.14, and 4.19 to 4.22).

17. ***Inadequacy in setting of NGOs' performance standards.*** Output Standards and Outcome Standards, which are service-specific and are stipulated in FSAs drawn up with ASUs, spell out concretely the service performance standards expected of NGOs. However, Audit noted that of the 2,691 FSAs drawn up with ASUs as at 31 March 2017, 2,209 (82%) did not contain Outcome Standards. For example, of five ASUs providing the same welfare service, three ASUs were required to attain Outcome Standards while the other two were not so required (paras. 4.26 and 4.27).

18. ***Need to ensure service resources are properly used by NGOs.*** NGOs are allowed to use LSG subventions for carrying out FSA activities and FSA related activities. NGOs should consult the SWD in a timely manner as to what constitutes "FSA related" activities before conducting such activities. During Audit's visits to the 11 NGOs (see para. 7), Audit found that an ASU of one NGO had organised activities for children below the age of 6 and retired men who were not target service users under the FSA. The ASU had not sought clarification from the SWD on whether the activities were "FSA related" activities and could be carried out. Audit also found that, for another NGO's ASU, there is room for improvement in the management of emergency places to cater for children whose families have crisis and cannot provide proper care to the children. The residential period for these emergency places was 6 weeks. However, on the date of Audit's visit, of the 20 emergency places, 6 places had been occupied by children for more than 22 months to 31 months, and 13 unused places were reserved by social workers over the phone (one of the 13 places had been reserved for 72 days). Furthermore, in the period April 2016 to June 2017, of the 39 cases of reservations that had subsequently been cancelled by social workers, 9 had been reserved but unused for 5 to 7 months and 15 for 3 to 4 months (paras. 4.30 and 4.31).

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19. *Need to conduct comprehensive reviews of performance of ASUs with non-time-defined FSAs.* As at 31 March 2017, of the 2,691 FSAs, 985 (37%) were time-defined (i.e. they normally had an agreement period of three or five years) and 1,706 (63%) were non-time-defined (i.e. without a specified agreement period). Audit noted that while ASUs with time-defined FSAs are subjected to comprehensive reviews (i.e. taking into account the ASU's attainment on Output Standards, Outcome Standards, ESRs and SQSs, results of the SWD's performance visits (see para. 20) and complaints against the ASU), there are no such reviews for ASUs with non-time-defined FSAs (paras. 4.34 to 4.36).

20. *Inadequacies in conducting performance visits.* The SWD carries out performance visits to ASUs of NGOs to assess the performance of ASUs. Audit examined the SWD's records of the performance visits conducted in the period 2012-13 to 2016-17 and accompanied the SWD's staff in carrying out eight performance visits during May to July 2017. Audit found that: (a) as at 31 March 2017, of the 2,691 ASUs, 542 (20%) had never been visited by the SWD; and (b) in accompanying the SWD's staff in the conduct of performance visits, all the 25 service users interviewed by the SWD staff were pre-selected by the ASUs and some of the service users who were requested to complete questionnaires were selected by the ASUs. Furthermore, the samples for examination of ASUs' records pertinent to service operation were not always selected by the SWD's staff themselves (paras. 4.39, 4.41, 4.42 and 4.45).

21. *Need to improve the conduct of annual performance review.* Audit reviewed the annual performance review of the ASUs conducted by the SWD and found that: (a) the annual performance review covered only the attainment of Output Standards and Outcome Standards. There was no information, for example, on the attainment of other performance standards (i.e. the ESRs and the SQSs) and the results of performance visits conducted by the SWD; and (b) there was no evidence indicating that the results of annual performance review had been submitted to the SWD's directorate staff for their reference and deliberations (para. 4.47).

Governance and management matters

22. *Need to improve the implementation of BPM guidelines.* The BPM (see para. 5), which came into effect in July 2014, encourages NGOs to enhance their governance in financial management, human resource management as well as

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corporate governance and accountability. The BPM provides guidelines for 14 strategic items (e.g. “use of reserve” and “NGOs’ policies and procedures on complaints handling”). Seven of the 14 items are “Level One guidelines” which NGOs are expected to follow unless they have strong justifications not to do so, while the other 7 items are “Level Two guidelines” which NGOs are encouraged to adopt. NGOs have been given a transition period of three years (i.e. by 30 June 2017) to implement the guidelines. NGOs are required to submit self-assessment reports to the SWD to report the progress of implementing Level One guidelines, while the submission of such reports for Level Two guidelines is on a voluntary basis. Audit found that: (a) there were incidents where NGOs did not accurately report their implementation of the BPM guidelines in their self-assessment reports; (b) of the 165 NGOs which submitted 2015-16 self-assessment reports for Level One guidelines, 58 (35%) were late in submitting their reports; (c) of the 154 NGOs which submitted 2015-16 self-assessment reports for Level Two guidelines on a voluntary basis, only 38 had fully implemented the 7 items of the Level Two guidelines; and (d) during the development of the BPM, best practices were to be formulated for 18 items. In April 2014, subsequent to consultations with the welfare sector, best practices for 14 of the 18 items were formulated and incorporated as guidelines into the BPM. During 2014 to 2017, the SWD had made attempts to forge an agreement on the best practices to be formulated for the four outstanding items relating to human resource management (e.g. staff remuneration policy and pay policy with a clear salary structure and/or starting points), but to no avail (paras. 5.2 to 5.6, 5.8 and 5.9).

23. ***Need to adopt other good governance practices.*** The Efficiency Unit’s “Guide to Corporate Governance for Subvented Organisations” (the Guide) has been included as one of the references in the annex of the LSG Manual. Audit’s visits to the six NGOs revealed that there is room for these NGOs to adopt the good governance practices set out in the Guide. Audit found that: (a) only 2 of the 6 NGOs had compiled attendance rates of board/committee members; (b) in the period 2013-14 to 2015-16, in the six NGOs, the proportion of board/committee members who did not attend any board/committee meetings was as high as 21.2%. There were also cases where board/committee members with low attendance rates had been re-appointed to the board/committees; (c) only 2 NGOs had adopted a two-tier reporting system for declaration of interests; (d) for 4 NGOs, registration forms were not used to record members’ declaration of interests. For one NGO, not all members’ declaration forms were available for Audit’s inspection. Furthermore, for another NGO, only the directorships of board members were required to be declared. Other interests (e.g. pecuniary interest) were not required to be declared; and (e) as at 31 August 2017, 2 NGOs had not prepared strategic plans. One of the 2 NGOs had also not prepared action plans (paras. 5.13, 5.14, 5.16, 5.18 and 5.20).

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24. *Need to address the problem of high staff turnovers of NGOs.* During 2013-14 to 2015-16, staff turnovers of the six NGOs visited by Audit were on the high side, ranging from some 14% to 35%. One of the six NGOs did not have the practice of conducting exit interviews with staff leaving the organisation. Exit interviews conducted by the other 5 NGOs in 2015-16 indicated that, of the 274 staff leaving the NGOs, many (133 or 48.6%) left for job-related reasons. Audit further noted that pay-related issues had affected staff morale and stability at the six NGOs. While the LSG subvention to the NGO was based on staff being funded at mid-point salaries of the Government's pay scales, the determination of actual pay could be based on a number of factors including skillsets, grades, seniority, and experience of individual staff. Inevitably, some NGO staff were paid above the mid-point salaries or even above the maximum-point salaries, others were paid below the mid-point salaries. Salary setting for some ranks had not been transparent (paras. 5.27, 5.28 and 5.30).

Review of lump sum grant subvention system

25. *2008 review of the LSG subvention system.* In 2008, the LSG Independent Review Committee conducted a review of the LSG subvention system. Its review report contained 36 recommendations on ways to improve the system. In February 2009, the LWB and the SWD accepted in principle all the recommendations. Audit noted that there is room for improvement in the implementation of the recommendations: (a) *Need to obtain feedback from NGOs on actuarial or related studies conducted.* In one recommendation, the LSG Independent Review Committee recommended that the Government should make available an actuarial service for NGOs to apply for on a voluntary basis. The service aimed to enable NGOs to assess, through conducting actuarial studies, their ability to meet staff commitments and projected payroll cost. Since November 2014, NGOs have also been allowed to commission actuarial studies or related studies (e.g. a finance and human resource system review). At 31 July 2017, 11 NGOs had applied for funding (ranging from \$25,500 to \$841,500) from the Social Welfare Development Fund for conducting studies by external consultants. To ensure the proper use of the Fund and the usefulness of the studies, the SWD needs to obtain feedback from all NGOs that have conducted the studies and promulgate the feedback to NGOs; and (b) *Need to better manage potential conflicts of interest.* In another recommendation, the LSG Independent Review Committee recommended that a complaints handling committee should be set up to determine on LSG-related complaints. In April 2009, the LSG Independent Complaints Handling Committee (the Committee) was therefore established (see para. 6). Audit examined the minutes of the 31 Committee meetings

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held in the period April 2009 to March 2017 and found that: (a) a member of the Committee was the head of a school run by an NGO being complained. During July 2011 to November 2012, 7 complaints relating to the NGO were deliberated at four Committee meetings. Although the member was connected to the NGO, the member declared no potential conflicts of interest in declaration forms. In two of the four Committee meetings, the member had participated in discussions. In one of the meetings, the member had endorsed the results that the complaint was not substantiated; and (b) in 21 of the 31 Committee meetings, Committee members had declared potential conflicts of interest. However, none of the minutes of the meetings indicated that the Chairman had made decisions on the declarations in accordance with the guidelines adopted by the Committee (paras. 6.2 to 6.4, 6.6, 6.7, 6.9, 6.10 and 6.12).

26. *Need to conduct a review to optimise the LSG subvention arrangements.* This Audit Review has identified room for improvement in the administration of LSG subventions by the SWD and in the use of LSG subventions by NGOs (see paras. 8 to 24). More than eight years have lapsed since the LSG subvention system was last reviewed in 2008 (see para. 25). Meanwhile, Audit noted that individual members of the LSG Steering Committee, Members of the Legislative Council and the welfare sector had from time to time called for another review of the LSG subvention system. It is now an opportune time to conduct a further review to optimise the LSG subvention arrangements (paras. 6.17 and 6.18).

Audit recommendations

27. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Director of Social Welfare should:**

Financial monitoring

- (a) **take further measures to facilitate NGOs to share, adopt and implement the good practices relating to the use of reserves and disclose the use of reserves according to the BPM (para. 2.16(a));**
- (b) **in circumstances where NGOs are unable to comply with the BPM guidelines, ensure that the NGOs provide strong justifications and the SWD gives consent for exemption where appropriate (para. 2.16(b));**

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- (c) **keep in view NGOs' balances of reserves and where necessary, remind NGOs to take further measures to maximise the use of the reserves, as required by the BPM guidelines, for enhancing FSA activities and FSA related activities to better the provision of welfare services to the public (para. 2.16(c));**
- (d) **ascertain the reasons for some NGOs having incurred large or persistent LSG operating deficits and offer advice where warranted (para. 2.16(d));**
- (e) **keep under review the operation of NGOs in deficits for possible financial viability issues and offer advice where warranted (para. 2.16(e));**
- (f) **take immediate action to obtain covering approval, from the Secretary for Labour and Welfare, for deferring the implementation of the requirement for the review and disclosure of emoluments of NGOs' staff in top three tiers (para. 2.27(a));**
- (g) **take necessary follow-up action on the advice of the Director of Administration on the implementation of the requirement for the review and disclosure of emoluments of NGOs' staff in top three tiers (para. 2.27(b));**
- (h) **take measures to ensure that the accounting inspections are conducted as planned in the future and to assist NGOs to improve their internal controls and minimise occurrence of irregularities, and consider taking into account other risk factors in formulating plans for accounting inspections (para. 2.34(a), (b) and (d));**
- (i) **request the three NGOs (see para. 12) which have not apportioned the head office overheads between FSA activities and non-FSA activities to apportion such overheads (para. 2.41(a));**
- (j) **request the two NGOs that have anomalies in apportioning the overheads between FSA activities and non-FSA activities (see para. 12) to review their bases of apportionment and properly apportion the costs (para. 2.41(c));**

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- (k) **take measures to help NGOs adopt an appropriate basis for apportioning overheads between FSA activities and non-FSA activities (para. 2.41(d));**

Self-assessment of service quality by NGOs

- (l) **remind NGOs of the importance of accurate reporting of their Output/Outcome Standards and of the need to exercise due care in computing the Standards, and provide more guidelines to NGOs to facilitate and enhance their conduct of measurement of Outcome Standards (para. 3.8(a) and (b));**
- (m) **urge NGOs to take measures to ensure that their ASUs observe the requirements laid down in their own SQS manuals in the implementation of SQSs and encourage NGOs to make use of the self-assessment checklist on SQSs as well as remind NGOs to exercise due care in completing the self-assessment checklist (para. 3.13);**

Monitoring of service delivery by SWD

- (n) **closely monitor those ASUs of NGOs which have had persistent underperformance in the provision of services and instigate timely action, where warranted, to tackle cases of persistent underperformance in accordance with provisions in the LSG Manual (para. 4.4(a) and (c));**
- (o) **ascertain the reasons for the significant underperformance in the provision of the HCS and the ISS and determine the way forward for the two services (para. 4.24(a));**
- (p) **follow up with the ASUs to align their understanding and practices regarding the counting of HCS and ISS cases into the caseloads reportable to the SWD (para. 4.24(b));**
- (q) **remind case managers of the HCS and the ISS to ensure that necessary support services are provided to service users as far as possible (para. 4.24(c));**

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- (r) **provide to the ASUs more guidelines on discharging service users (para. 4.24(d));**
- (s) **take measures to address the issue of service users receiving both the HCS and the ISS (para. 4.24(e));**
- (t) **with a view to optimising the use of public money, explore the feasibility of fine-tuning the existing arrangements for calculating subventions to the ASUs providing the HCS and the ISS (para. 4.24(f));**
- (u) **to properly monitor the effectiveness of services provided by ASUs, step up efforts to set Outcome Standards with ASUs and incorporate such standards into the pertinent FSAs (para. 4.28);**
- (v) **remind NGOs that the SWD should be consulted prior to the conduct of activities which they regard as FSA related activities but not stipulated in FSAs (para. 4.32(b));**
- (w) **communicate with the NGO on how best to handle the cases of children occupying the emergency places longer than the stipulated periods (see para. 18) and set a reasonable timeframe for social workers to complete the admission procedures (para. 4.32(c) and (e));**
- (x) **consider conducting, on a periodic basis, comprehensive reviews of the performance of ASUs with non-time-defined FSAs (para. 4.37);**
- (y) **closely monitor the progress of special visitation programme visits (which are being conducted by the SWD to cover those ASUs which have never been visited) to accomplish the visits within the stipulated timeframe (para. 4.48(a));**
- (z) **take enhanced measures to ensure that, as far as possible, service users to be requested to complete questionnaires or interviewed are not pre-selected by ASUs and that the staff of the SWD responsible for conducting performance visits select samples for examination at ASUs themselves (para. 4.48(d) and (e));**

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- (aa) **consider extending the coverage of annual performance review (e.g. to include the attainment of ESRs and SQSs) (para. 4.48(h));**
- (ab) **take measures to ensure that the results of NGOs' compliance with the ESRs, SQSs, Output Standards and Outcome Standards are brought to the attention of the SWD's directorate periodically (para. 4.48(i));**

Governance and management matters

- (ac) **remind NGOs to provide accurate information on the progress of implementation of BPM guidelines and submit self-assessment reports in a timely manner (para. 5.11(a));**
- (ad) **enhance the promotion of Level Two guidelines among NGOs (para. 5.11(c));**
- (ae) **step up efforts to forge agreement between the NGOs' management and the staff side on the four items of the BPM relating to human resource management (para. 5.11(d));**
- (af) **make greater efforts to encourage NGOs to adopt the good practices outlined in the Efficiency Unit's Guide (para. 5.22);**
- (ag) **remind NGOs receiving LSG subventions to monitor their staff turnovers and take measures to address the problem of high staff turnovers (para. 5.31(a));**

Review of LSG subvention system

- (ah) **in order to help the conduct of actuarial studies or related studies in future, obtain feedback from all NGOs that have conducted the studies and promulgate the feedback to NGOs (para. 6.14(a));**
- (ai) **take measures to improve the management of potential conflicts of interest in the handling of complaints by the LSG Independent Complaints Handling Committee (para. 6.14(b)); and**

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- (aj) **in carrying out the review on the enhancement of the LSG subvention system, take into account the audit findings and recommendations in this Audit Report (para. 6.19).**

Response from the Government

28. The Director of Social Welfare agrees with the audit recommendations. The Secretary for Labour and Welfare has said that the LWB has tasked the SWD to set up a Task Force to work with stakeholders to conduct a review on the enhancement of the LSG subvention system. The review will take into account the audit findings and recommendations in this Audit Report.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 The Social Welfare Department (SWD) is responsible for developing and co-ordinating welfare services in Hong Kong. It provides subventions to non-governmental organisations (NGOs) for the provision of welfare services to the public.

1.3 Welfare services provided by NGOs comprise elderly services, family and child welfare services, rehabilitation services, and youth and corrections services (see Photographs 1 to 4). Under these four areas of welfare services, there are some 140 types of services. Examples are as follows:

- (a) ***Elderly services.*** The services include community care and support services for elderly persons (e.g. day care centres for the elderly, integrated home care services, and neighbourhood elderly centres) and residential care services for elderly persons (e.g. care and attention homes for the elderly and nursing homes);
- (b) ***Family and child welfare services.*** The services include a variety of family and child welfare services and programmes. Examples are family and child protective services for child abuse and spouse battering, day child care service, and adoption service;
- (c) ***Rehabilitation services.*** The services include rehabilitation services for persons with disabilities (e.g. pre-school service for children with disabilities, sheltered workshops, and care-and-attention homes for severely disabled persons) and preventive and rehabilitative services for drug abusers; and

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- (d) *Youth and corrections services.* The services include:
 - (i) outreaching social work service and school social work service, and provision of centre-based services for children and youth;
 - (ii) services for offenders, which include counselling, employment assistance and supportive services for offenders, discharged prisoners and ex-offenders; and
 - (iii) services for community development, which include community work and group services for the general public with particular focus on the needs of vulnerable groups, outreaching support, casework and group work services to assist street sleepers, ex-mentally ill persons, and ex-offenders to integrate into the community.

Photographs 1 to 4

Welfare services provided by NGOs

Photograph 1

Elderly services



Photograph 2

Family and child welfare services



Photograph 3

Rehabilitation services



Photograph 4

Youth and corrections services



Source: SWD records

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1.4 In 2016-17, the SWD paid subventions of \$12.5 billion in the form of lump sum grant (LSG — see paras. 1.8 to 1.19) to 165 NGOs for the provision of welfare services. Appendix A shows, for 2016-17, a breakdown of the welfare services provided by the 165 NGOs and the individual amounts of LSG subventions granted to them (Note 1).

Conventional subvention system

1.5 Prior to the establishment of the LSG subvention system in January 2001, subventions were provided to NGOs through the conventional subvention system. Today, the conventional subvention system is still in use alongside the LSG subvention system, albeit for a few NGOs only (see para. 1.20).

1.6 Under the conventional subvention system, the SWD pays NGOs for the actual costs incurred in the delivery of recognised welfare services. The system had been criticised in several areas including:

- (a) the system was rigid, inflexible, complex and bureaucratic with tight input control over NGOs by imposing standard staffing structures, levels of pay and staff qualifications. It involved elaborate rules and procedures in

Note 1: *In addition to the LSG subventions, the SWD also provides other subventions/subsidies to the NGOs:*

- (a) subventions to NGOs under the conventional subvention system (see para. 1.6);*
- (b) refund of rent and rates to NGOs and payments to NGOs for specific purposes (e.g. dementia supplement for the elderly with disabilities, anti-violence programme, and services for asylum seekers and torture claimants);*
- (c) other payments for welfare services (e.g. contracted residential care homes for the elderly and residential care places for the elderly purchased under the Nursing Home Place Purchase Scheme); and*
- (d) grants under the Lotteries Fund to finance the capital expenditure of welfare projects and the experimental projects with limited duration. The Lotteries Fund is mainly funded by the proceeds of the Mark Six Lottery.*

vetting of staff qualifications and reimbursement of expenses for procurement and recognised items. NGOs were not allowed to freely deploy resources (e.g. an NGO was not allowed to reallocate the resources among the services) or retain any surpluses. There was, therefore, no incentive for NGOs to encourage more effective use of resources to achieve lower costs, better value for money or improved services to users;

- (b) once subvention was provided to an NGO to run a particular service, it was seldom revised even when service needs had changed or the modes of operation required revamping. It did not encourage innovation and service re-engineering to meet changing community needs; and
- (c) there were inherent difficulties in defining and measuring results, particularly in terms of linking outcomes of service objectives with resource inputs.

1.7 In 1994, the Government commissioned a consultancy study to review the conventional subvention system. The study, completed in 1998, concluded that the system required a revamp including:

- (a) the conventional subvention system, which was an input-based funding system, should be changed so as to provide more flexibility to NGOs to manage their resources;
- (b) clearer sets of performance measures should be introduced to make subvented NGOs more accountable for their service quality; and
- (c) a cultural change should be initiated to arouse the sector's awareness of the need to deliver services in a responsive, cost-effective and competitive manner.

Lump sum grant subvention system

Key features of LSG subvention system

1.8 Subsequent to the consultancy study, the Government organised, from February to May 2000, a series of briefings for NGOs and attended meetings with

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various public organisations and advisory committees including the Panel on Welfare Services of the Legislative Council (LegCo), various advisory bodies (e.g. the Elderly Commission and the Social Welfare Advisory Committee), staff associations, individual LegCo Members, and numerous concern groups on details of the reform package. In January 2001, the LSG subvention system was rolled out as a major revamp of the provision of funding to NGOs. Under this system, annual funding is granted to individual NGOs on a lump sum basis. NGOs receiving subventions under the conventional subvention system (see para. 1.6) are not obliged to but may voluntarily opt for the LSG subvention system.

1.9 The aim of introducing the LSG subvention system was to enhance efficiency and effectiveness, improve quality, encourage innovation, strengthen accountability and provide flexibility, with a view to deploying resources in the most cost-effective manner to meet changing needs in the community. Under the LSG subvention system, NGO management has the autonomy and flexibility in the deployment of subvention resources to meet the service needs. Within the context of the Funding and Service Agreements (FSAs — see para. 1.18), which include the carrying out of FSA related activities and other support services (e.g. central administration and supervisory support), NGOs have flexibility in deploying their LSG subventions (except the provident funds — see para. 2.3(b)) to pay expenses including the following:

- (a) staff expenses: salary, allowances and personnel-related expenses (including fringe benefits) for their staff based on their own staffing structure and remuneration; and
- (b) other operating expenses.

LSG subvention is provided on an NGO basis. NGOs' management may redeploy LSG resources across service units as long as these are among the service units governed by FSAs after assessing needs. The operation of the LSG subvention system is described in more detail in paragraphs 1.12 to 1.19.

1.10 The Director of Social Welfare is responsible for ensuring that the social welfare services delivered by the SWD or NGOs are meeting the Government's policy objectives, and that they remain so in the light of changing circumstances. Thus, the SWD works closely with NGOs to review the effectiveness of the services rendered

and to obtain regular feedback from NGOs in the process of service planning and evaluation.

1.11 NGOs receiving Government subventions are responsible for effective planning and cost-effective administration of the services and activities governed by FSAs. In discharging this role under the LSG, NGOs are expected to build in an accountability mechanism and be flexible and proactive in responding to the changing needs of the community. NGOs receiving LSG and other social welfare subventions are directly accountable to the SWD and the public (e.g. through public disclosure of Annual Financial Reports (AFRs) — see para. 1.18(d)) for proper control and prudent use of public funds and for compliance with the conditions spelt out in the LSG Manual and other guidelines. It is the responsibility of NGOs' board and management to maintain proper control of the LSG and ensure that the use of LSG meets the requirements and objectives set out in FSAs. To avoid misunderstanding, NGOs should consult the SWD in a timely manner as to what constitutes FSA related activities before conducting such activities. NGOs must also take speedy actions to rectify any anomalies identified by the SWD.

Operation of LSG subvention system

1.12 ***Calculation of LSG subvention.*** The annual amount of LSG subvention to an NGO, which opted for the LSG subvention system in 2001, is the sum of items (a), (b) and (c) minus item (d) as described below:

- (a) ***Staff salaries.*** The salaries, known as “Benchmark” salaries and “Snapshot” salaries according to the SWD, were calculated based on the following principles:
 - (i) the “Benchmark” salaries for the LSG of each NGO were determined on the basis of the mid-point salaries of the Government's pay scales (Civil Servant Master Pay Scale and

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Model Scale 1) as at 31 March 2000 (Note 2) of the NGO's recognised staff establishments (Note 3) as at 1 April 2000;

- (ii) a "Snapshot" of staff strength of each NGO as at 1 April 2000 (i.e. "Snapshot Staff") was taken and its salary subvention for 2000-01 was projected. The "Snapshot" salaries were then compared with the "Benchmark" salaries;
- (iii) NGOs with "Snapshot" salaries above the "Benchmark" salaries received the "Snapshot" salaries. Their "Snapshot" salaries were reduced annually in steps of 2% per annum starting from 2008-09 (Note 4) to reach the "Benchmark" salaries so that NGOs delivering the same type and level of service would receive the same level of subvention; and
- (iv) for NGOs with "Snapshot" salaries below the "Benchmark" salaries, they received the "Benchmark" salaries in one step provided that their service had already been fully commissioned

Note 2: *After a review in the civil service, the salary levels of various civil service ranks were adjusted downward with effect from 1 April 2000. However, the higher pay scale as at 31 March 2000 was used as the initial level of funding to help NGOs adapt to the LSG funding mode.*

Note 3: *The SWD has set out recognised staff establishments for different types of services (see para. 1.3) provided by an NGO. These establishments are set for the purpose of calculating the subvention for the welfare services concerned and are not for benchmarking of manpower or staffing structure. Details of the establishments are available on the SWD website (http://www.swd.gov.hk/en/index/site_ngo/page_subventions/sub_modesofsub/id_2907/). As an example, according to the pertinent recognised staff establishment, for an NGO which runs a day care centre for the elderly with a capacity of 60 places, the centre would need 0.2 Social Work Officer, 1 Registered Nurse, 1.5 Enrolled Nurses, 1 Occupational Therapist II/ Physiotherapist II, 10 Personal Care Workers, 1 Clerical Assistant, 3 Workmen II, and 3 Motor Drivers.*

Note 4: *The reduction was planned to start from 2006-07. To facilitate NGOs to meet contractual commitments to "Snapshot Staff", the reduction was postponed to 2008-09. NGOs which had genuine financial difficulties were also allowed to further postpone to 2009-10. To meet such commitments, the SWD also provided special grants to NGOs (see para. 1.14).*

(otherwise in line with the agreed phased commissioning of the facility/service).

Thereafter, the NGO's staff salaries are adjusted annually according to the civil service pay adjustment;

- (b) ***Provision for provident funds.*** “Snapshot Staff” and “non-Snapshot Staff” are generally entitled to provident fund benefits. The NGO's provision for provident funds is calculated on an actual entitlement basis for “Snapshot Staff” (see para. 1.12(a)(ii)) and at 6.8% of the mid-point salaries of the Government's pay scales of the recognised staff establishments for “non-Snapshot Staff” recognised posts (i.e. in recognised staff establishments) (Note 5). When a member of the “Snapshot Staff” within the recognised staff establishment leaves the NGO, the provision of provident fund will be replaced by 6.8% of the mid-point salary of the recognised rank of that staff member in the “Snapshot” as at 1 April 2000 (the salary portion of the LSG remains unchanged, subject to the coming down to the “Benchmark” salaries (see para. 1.12(a)(iii));
- (c) ***Other charges.*** The provision of other charges refers to other miscellaneous operational expenses (e.g. administrative expenses, utilities, stores and equipment, programme expenses and food, etc.) and allowances (e.g. overtime allowance for drivers in day care centres for the elderly, incentive payments for sheltered workshop workers, etc.). Other charges are adjusted according to the Composite Consumer Price Index published regularly by the Census and Statistics Department; and
- (d) ***Recognised fee income.*** The SWD allows an NGO to make charges for its welfare services provided. Such charges are stipulated by the SWD (e.g. monthly residential fee of \$1,994 for elderly nursing homes and annual membership fee of \$21 for neighbourhood elderly centres as at 1 April 2016).

Note 5: *Provision of provident funds for “Snapshot Staff” is calculated as follows: 5% of the staff's monthly salaries for first 10 years of service; 10% for 11th to 15th years of service; and 15% for 16th or onward years of service. The number of “Snapshot Staff” had decreased from 21,638 as at 1 April 2000 to 6,395 as at 1 September 2016. The SWD does not maintain information on the number of “non-Snapshot Staff” employed by NGOs.*

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1.13 The above method of calculation of subvention also applies to an NGO that joined the LSG subvention system after 2001. However, the staff salaries are funded by the SWD according to the “Benchmark” salaries (see para. 1.12(a)(i)) prevailing at the time when the NGO joined the system (i.e. taking into account annual civil service pay adjustments). Furthermore, provision of provident funds is provided at 6.8% of the mid-point salaries of the Government’s pay scales of the recognised staff establishments (see para. 1.12(b)). In determining other charges, the SWD makes reference to the expenditure incurred for the provision of other similar services at that time.

1.14 *Special funding for NGOs.* In order to address NGOs’ concern over their financial viability, the SWD had provided additional special funding to NGOs subsequent to 1 April 2000, as follows:

- (a) an NGO might apply to the SWD for a Tide-Over Grant covering a five-year period from 2001-02 to 2005-06 for the NGO to honour their contractual commitments to “Snapshot Staff”. In the period, \$1,473 million had been paid to 125 NGOs;
- (b) after the termination of the Tide-Over Grant in 2005-06, an NGO might apply to the SWD for a Special One-off Grant to meet especially the NGO’s contractual commitments to “Snapshot Staff” as well as to meet the NGO’s financial commitments for service re-engineering and organisational restructuring as a result of transiting to the LSG subvention system. A Special One-off Grant of \$912.4 million had been approved for 124 NGOs (unspent balances were subject to clawback to the SWD);
- (c) in 2008-09, the Lotteries Fund Advisory Committee allocated a one-off grant of \$200 million for subvented NGOs to strengthen support and training for staff and enhance service quality;
- (d) in 2008-09, an additional \$200 million recurrent funding (about 3% of NGOs’ total recurrent subvention) was provided to help NGOs strengthen their administrative capacity; and
- (e) in 2014-15, another additional recurrent funding of \$470 million was allocated to NGOs to strengthen their central administrative and supervisory support, increase the provision for other charges (see para. 1.12(c)), and

recruit and retain paramedical staff more effectively or hire paramedical services to deliver their subvented services.

1.15 ***Retention of unspent funds.*** An NGO can retain unspent LSG subvention in a reserve to meet future spending. The cumulative reserve (separate from Provident Funds Reserve (PF Reserve) and Holding Account — see para. 2.3) is capped at 25% of the annual operating expenditure (excluding expenditure for provident funds) of the subvented services of the NGO. Any amount above the 25% cap is subject to claw-back and should be returned to the Government. The reserve can be used at the discretion of the NGO on FSA activities and FSA related activities.

1.16 ***Accountability of NGOs.*** Under the LSG subvention system, the SWD draws up an FSA for each service (see para. 1.3) that a service unit of an NGO provides. For example, if a unit provides two services, two FSAs are drawn up and the SWD regards the unit as two “agreement service units” (ASUs).

1.17 For services commencing after the establishment of the LSG subvention system, the duration of FSAs is three or five years depending on the types of services provided. For services commencing before the establishment, the FSAs are not subject to any time constraints.

1.18 An FSA defines the welfare service to be provided by an ASU. It also stipulates the following:

- (a) the Output Standards (e.g. enrolment rates, hours of training per service user, and number of street sleepers approached within one year) and Outcome Standards (e.g. percentage of service users with improved capability in managing family problems, and percentage of service users with improved self-esteem after receiving the service from the unit) to be achieved by the ASU;
- (b) Essential Service Requirements (ESRs) (e.g. staff qualifications, opening hours of institutions, and availability of appropriate equipment) to be met by the ASU;

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- (c) the need to observe the 16 Service Quality Standards (SQSs — see Appendix B). The SQSs apply unanimously to all ASUs of NGOs. The SQSs define the policies, procedures and practices that an ASU should have in place in order to deliver quality services to service users. For example, SQS14 states that an ASU should respect the service users' rights for privacy and confidentiality. An ASU is, therefore, required to have measures in place to ensure that personal care activities are conducted in a manner whereby the privacy and dignity of individual service users are respected; and
- (d) the need to follow the requirements laid down in the LSG Manual and LSG Circulars. The LSG Manual sets out, for example, the roles and responsibilities of the SWD and NGOs, the structure of the LSG (e.g. the 25% cap — see para. 1.15), and other operational guidelines (e.g. the need to submit to the SWD AFRs (Note 6) on the use of LSG subvention by NGOs). The LSG Circulars supplement the LSG Manual.

1.19 The NGOs are also required to adopt the best practices (which have been agreed by representatives of NGOs' management, staff side, service users and professional groups) laid down in the Best Practice Manual (BPM — see Appendix C) developed under the auspices of the LSG Steering Committee (see para. 1.24). The BPM aims to enhance NGOs' financial management, human resource management, as well as corporate governance and accountability. It comprises two levels of guidelines. Level One guidelines are those that NGOs are expected to follow unless they have strong justifications not to do so. Level Two guidelines are those that NGOs are encouraged to adopt. The BPM came into effect on 1 July 2014 and NGOs are given three years (i.e. by 30 June 2017) to review their existing policies and procedures with a view to meeting the best practice requirements of the BPM. More details on paragraphs 1.18 and 1.19 are provided in PARTs 2 to 5 of this Audit Report.

Note 6: *An NGO must prepare on cash accounting basis an AFR in respect of all its FSA activities (including support services to FSA activities) funded by the LSG as well as other social welfare subventions/subsidies (e.g. refund of rent and rates), and submit the AFR to the SWD together with the auditor's review report.*

NGOs joining LSG subvention system

1.20 In 2001, of the 182 NGOs under the conventional subvention system, 96 (53%) joined the LSG subvention system. In 2016-17, of the 170 NGOs receiving subventions from the SWD (Note 7), 165 (97%) were under the LSG subvention system, while the other five (3%) (Note 8) NGOs remained in the conventional subvention system.

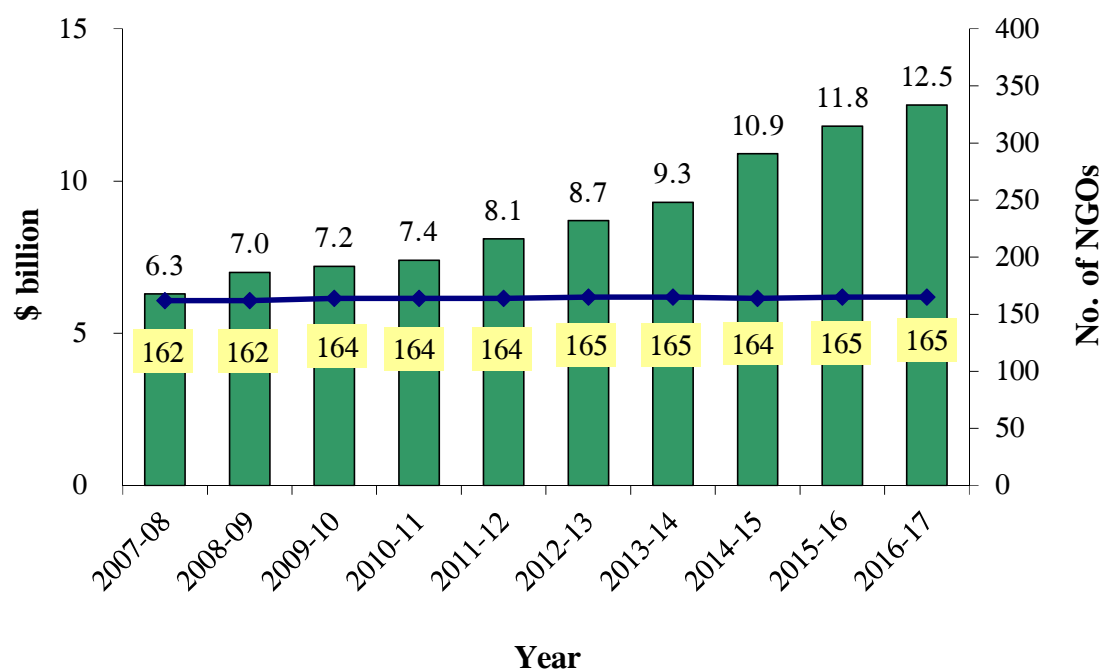
1.21 In the ten-year period 2007-08 to 2016-17, LSG subventions had doubled from \$6.3 billion in 2007-08 to \$12.5 billion in 2016-17 (see Figure 1). In 2016-17, LSG subventions granted to the 165 NGOs ranged from \$79,000 to \$1,121 million (see Table 1 and Appendix A). As at 31 March 2017, the SWD drew up FSAs for 2,691 ASUs of the 165 NGOs. Of the 2,691 ASUs, 717 (27%) ASUs were providing elderly services, 508 (19%) ASUs were providing family and child welfare services, 1,179 (44%) ASUs were providing rehabilitation services, and 286 (10%) ASUs were providing youth and corrections services.

Note 7: *The number of NGOs receiving SWD subventions decreased from 182 in 2000-01 to 170 in 2016-17.*

Note 8: *The five NGOs were Hong Kong Chiu Chow Po Hing Buddhism Association Limited, New Kowloon Women Association Limited, The Baptist Convention of Hong Kong, The Hong Kong Council of the Church of Christ in China, and The Society for the Aid and Rehabilitation of Drug Abusers. In 2016-17, these five NGOs received a total subvention of \$20.4 million from the SWD.*

Figure 1

LSG subventions (2007-08 to 2016-17)



Legend: ■ LSG subventions
◆ Number of NGOs

Source: SWD records

- Remarks:
1. The increase in subventions in the period 2007-08 to 2016-17 was due to reasons such as civil service pay and inflationary adjustments (see para. 1.12(a) and (c)), additional subventions for NGOs' new services or new ASUs and for enhancement of services and the LSG subvention system (see para. 1.14(c) to (e)).
 2. An NGO left the LSG subvention system in 2014-15 while another NGO joined the system in 2015-16.

Table 1

**LSG subventions granted to 165 NGOs
(2016-17)**

Subvention granted to each NGO (Note) (\$ million)	No. of NGOs	Total subventions granted (\$ million)
More than 200	22 (13%)	8,314 (66%)
More than 100 to 200	11 (7%)	1,779 (14%)
More than 50 to 100	12 (7%)	822 (7%)
50 or below	120 (73%)	1,615 (13%)
Total	165 (100%)	12,530 (100%)

Source: Audit analysis of SWD records

Note: The highest and lowest amounts of subvention granted were \$1,121 million and \$79,000 respectively.

Administration of LSG subventions by SWD

1.22 A number of branches of the SWD are responsible for the administration of the LSG subvention system:

- (a) ***Finance Branch.*** The Finance Branch carries out functions such as conducting income and expenditure analyses based on NGOs' AFRs and carrying out inspections of the accounting records of NGOs' ASUs. The inspections include reviewing compliance with accounting and financial reporting requirements as laid down in the LSG Manual, and reviewing/advising on internal control procedures. As at 30 June 2017, 14 staff of the Finance Branch were involved in the review of AFRs and accounting inspections;
- (b) ***Service Branches.*** There are a total of five Service Branches involved in LSG service matters, namely the Clinical Psychological Service Branch, the Elderly Branch, the Family and Child Welfare Branch, the

Rehabilitation and Medical Social Services Branch and the Youth and Corrections Branch. The Clinical Psychological Service Branch provides psychological assessment and psychotherapy to service users of the other four Service Branches. These other four branches are responsible for the planning, development and implementation of welfare services, which include services provided by NGOs receiving LSG subventions, to meet local community needs as well as for setting service specifications for NGOs' FSA activities (i.e. Output Standards, Outcome Standards and ESRs). As at 30 June 2017, the five Service Branches had 112 staff involved in LSG service matters; and

- (c) **Subventions Branch.** The Subventions Branch formulates, executes, reviews and interprets subvention rules and procedures. It also monitors and evaluates the quality of NGOs' welfare services. Monitoring and evaluation work includes:
- (i) examining the quarterly statistical information submitted by NGOs in respect of each ASU's performance on Output Standards and Outcome Standards (see para. 1.18(a));
 - (ii) examining the reports of annual self-assessment conducted by NGOs in respect of each ASU's compliance with ESRs and SQSs and achievement of planned targets of Output Standards and Outcome Standards (see para. 1.18);
 - (iii) conducting review visits/surprise visits in selected ASUs of NGOs to ascertain compliance with Output Standards, Outcome Standards, ESRs and SQSs; and
 - (iv) conducting on-site assessment of new ASUs and other ASUs with identified/suspected problem areas in service performance (Note 9).

Note 9: *The conduct of self-assessment by NGOs and the carrying out of other control functions by the SWD are the integral parts of the SWD's Service Performance Monitoring System. The System was established jointly by the SWD and NGOs receiving LSG subventions in 1999 to ensure that quality welfare services are provided to the public and to increase the accountability of both the SWD and the NGOs in service delivery.*

As at 30 June 2017, 36 staff in the Subventions Branch were involved in handling service performance monitoring, complaints handling, administrative support work and subvention matters (e.g. examining the report of annual self-assessment conducted by NGOs in respect of implementation of BPM — see para. 1.19).

1.23 An organisation chart covering the aforesaid branches of the SWD as at 30 June 2017 is shown at Appendix D.

LSG Steering Committee

1.24 In February 2001, an LSG Steering Committee (Note 10) was appointed by the Labour and Welfare Bureau (LWB) (i.e. the policy bureau of the SWD). The Committee is responsible for:

- (a) monitoring the implementation of the LSG subvention system and identifying areas for improvement;
- (b) discussing and suggesting solutions to problems arising from the implementation of the system;
- (c) facilitating communication and sharing of information and experience relating to the implementation of the system among the SWD, NGOs and their staff, and service users under the LSG subvention system;
- (d) monitoring the implementation of the recommendations of the review report on the LSG subvention system published by the LSG Independent Review Committee in December 2008 (see paras. 1.25 and 1.26); and
- (e) drawing up the BPM (see para. 1.19).

Note 10: *The LSG Steering Committee is chaired by the Director of Social Welfare and comprises two ex-officio members (i.e. Principal Assistant Secretary for Labour and Welfare (Welfare) and Assistant Director of Social Welfare (Subventions)) and 17 non-official members. Non-official members comprise representatives from NGOs' management, staff unions, service users and independent members of professional background.*

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LSG Independent Review Committee

1.25 In January 2008, an LSG Independent Review Committee (Note 11) was appointed by the LWB to review the LSG subvention system objectively, comprehensively and independently. The terms of reference of the Committee were:

- (a) to review the LSG subvention system with a view to assessing its overall effectiveness and identifying scope for improvement covering but not limited to:
 - (i) the overall implementation of the system;
 - (ii) the flexibility, efficiency and cost-effectiveness in the use of public funds and in service delivery by subvented NGOs;
 - (iii) the accountability and corporate governance of subvented NGOs;
 - (iv) the impact of the LSG on the quality of welfare service; and
 - (v) the handling of complaints related to the implementation of the system; and
- (b) to report findings and make recommendations to the Secretary for Labour and Welfare.

1.26 In December 2008, the LSG Independent Review Committee submitted to the Secretary for Labour and Welfare its review report, which concluded that the principles of the LSG subvention system were sound, the system was worth retaining, and every effort should be made to improve it. To this end, 36 recommendations on ways to improve the LSG subvention system (e.g. drawing up the BPM, reviewing the deadline for NGOs to submit AFRs and setting up an Independent Complaints Handling Committee) were made (see para. 6.2). The LWB accepted all the recommendations. The Committee was subsequently dissolved in December 2008.

Note 11: *The Committee comprised a non-official Chairman and four non-official members from different professional backgrounds (e.g. law and accounting).*

LSG Independent Complaints Handling Committee

1.27 In April 2009, an LSG Independent Complaints Handling Committee (Note 12) was set up in accordance with one of the 36 recommendations of the LSG Independent Review Committee. The Committee handles LSG-related complaints that cannot be satisfactorily addressed at the NGO level. The SWD provides secretariat support to the Committee. The secretariat screens complaints received, conducts direct investigation into complaints where necessary, and replies to complainants and NGOs concerned on outcomes of investigations on behalf of the Committee. The Committee relays decisions and recommendations to the SWD for following up with NGOs, and where appropriate, suggests improvements to the LSG subvention system.

1.28 In the period June 2009 to March 2017 (about eight years), the Committee received 1,241 complaints (see Table 2). The complaints were related to NGOs' compliance with service requirements, use of subventions and service performance.

Note 12: *The Committee comprises one Chairman, one Vice-chairman and six members. All of them are independent individuals from various backgrounds (e.g. law and medicine).*

Table 2
Complaints received by
LSG Independent Complaints Handling Committee
(2009-10 to 2016-17)

Year	No. of complaints
2009-10	106 (Note)
2010-11	153
2011-12	139
2012-13	141
2013-14	136
2014-15	155
2015-16	211
2016-17	200
Total	1,241

Source: SWD records

Note: The Committee started to receive complaints in June 2009.

1.29 Of the 1,241 complaints received, the LSG Independent Complaints Handling Committee investigated 127 complaints. These 127 complaints involved a total of 493 complaint issues. Of these 493 issues:

- (a) 423 (86%) issues were related to non-compliance with service requirements;
- (b) 56 (11%) issues were related to misuse of subventions; and
- (c) 14 (3%) issues were related to NGOs' management decisions on service provision.

Of the 493 complaint issues, 152 (31 %) complaint issues were either fully or partially substantiated.

Audit review

1.30 The Audit Commission (Audit) has recently conducted a review of the administration of LSGs by the SWD. The review has focused on the following areas:

- (a) financial monitoring (PART 2);
- (b) self-assessment of service quality by NGOs (PART 3);
- (c) monitoring of service delivery by the SWD (PART 4);
- (d) governance and management matters (PART 5); and
- (e) review of the LSG subvention system (PART 6).

Audit has found room for improvement in the above areas and has made recommendations to address the issues.

1.31 In conducting this review, Audit carried out data analyses and examination of records at the Finance Branch and the Subventions Branch and visited 11 NGOs (Note 13). Of the 11 NGOs, Audit paid visits to:

- (a) five NGOs and five of their ASUs to examine specifically certain welfare services with underperformance (e.g. home care service for persons with severe disabilities) in the period 2014-15 to 2016-17. These NGOs were identified from Audit's data analyses and examination of records conducted at the Subventions Branch, based on criteria such as persistent underperformance or sudden change of performance patterns (e.g. years of

Note 13: *According to the LSG Manual, the Director of Audit may carry out such examination as he thinks fit into the economy, efficiency and effectiveness with which the NGOs have used public resources in discharging their functions.*

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underperformance followed immediately by a year of good performance). These five NGOs were selected for case studies on areas examined in this audit review; and

- (b) six NGOs and 18 of their ASUs to examine their use of LSG subventions in general. Matters covered included governance, delivery of services and financial arrangements. The NGOs were selected from the 165 NGOs receiving LSG subventions in accordance with a number of factors including the amounts of 2016-17 LSG subventions, the types of welfare services provided, and other factors such as the results of NGOs' self-assessment of service performance (NGOs with relatively better performance were selected alongside those with not so good performance).

1.32 Of the 23 ASUs visited:

- (a) 3 ASUs were providing elderly services;
- (b) 4 ASUs were providing family and child welfare services;
- (c) 14 ASUs were providing rehabilitation services; and
- (d) 2 ASUs were providing youth and corrections services.

1.33 The 11 NGOs had the following salient features:

- (a) ***Welfare services.*** The 11 NGOs (7% of 165 NGOs in 2016-17) had in total 716 ASUs (27% of 2,691 ASUs in 2016-17) which were LSG-subvented. The services provided by the ASUs comprised all the four types of welfare services provided by NGOs (see para. 1.3), namely, elderly services (151 ASUs), family and child welfare services (152 ASUs), rehabilitation services (361 ASUs), and youth and corrections services (52 ASUs);
- (b) ***LSG subventions.*** In 2016-17, the LSG subventions granted to the 11 NGOs (see Table 3) totalled some \$3,546 million (28% of \$12.5 billion in 2016-17); and

Table 3

**LSG subventions granted to 11 NGOs visited by Audit
(2016-17)**

Subvention granted to each NGO (\$ million)	No. of NGOs visited by Audit
More than 200	7
More than 100 to 200	1
More than 50 to 100	1
50 or below	2
Total	11

Source: Audit analysis of SWD records

- (c) **Non-FSA activities.** Apart from providing FSA activities funded by LSG subventions, the 11 NGOs also conducted non-FSA activities to render other services for the public. The funding for non-FSA activities include income from activities conducted by NGOs on a self-financing basis and from other subventions/grants/subsidies provided by government departments. In 2015-16, consolidated income (including income from all sources) of the 11 NGOs totalled \$9,052 million (Note 14). Of this amount, more than 50% of the income was generated from non-FSA activities.

1.34 In this Audit Report:

- (a) the 5 NGOs visited by Audit (see para. 1.31(a)) are denoted as NGOs A to E;

Note 14: *As at the time of completion of the fieldwork of this audit in September 2017, the 2016-17 audited financial statements of the 11 NGOs were not yet available.*

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- (b) another 6 NGOs visited by Audit (see para. 1.31(b)) are denoted as NGOs F to K;
- (c) the 23 ASUs of these 11 NGOs visited by Audit are denoted as ASU A to ASU W; and
- (d) the other NGOs and ASUs for which Audit carried out examination of the SWD records at the Finance Branch and the Subventions Branch (see para. 1.31) but did not pay visits are denoted by numerical numbers (e.g. NGO 1 and NGO 2, and ASU 1 and ASU 2).

General response from the Government

1.35 The Director of Social Welfare welcomes Audit's review on the "administration of lump sum grants by the SWD" and agrees with the audit recommendations with a view to enhancing the financial monitoring, performance of service delivery as well as the governance and management of NGOs.

1.36 The Secretary for Labour and Welfare has said that the LWB has tasked the SWD to set up a Task Force to work with stakeholders to conduct a review on the enhancement of the LSG subvention system. The Task Force, comprising members from LWB, SWD, NGO management, staff side, service users and independent persons, will oversee and chart the review, including discussion of specific areas in the LSG environment to be covered in the review, the audit findings and recommendations in this Audit Report, examination of specific areas where data collection from the sector is required, and consideration of the findings and recommendations of the review.

Acknowledgement

1.37 Audit would like to acknowledge with gratitude the full cooperation of the staff of the SWD and the NGOs visited by Audit during the course of the audit review.

PART 2: FINANCIAL MONITORING

2.1 This PART examines the SWD's financial monitoring of NGOs receiving LSG subventions, focusing on the following issues:

- (a) reserves retained by NGOs (paras. 2.2 to 2.17);
- (b) disclosure of NGOs' senior staff emoluments (paras. 2.18 to 2.29);
- (c) accounting inspections (paras. 2.30 to 2.35);
- (d) cross-subsidisation between LSG subventions and self-financing activities (paras. 2.36 to 2.42);
- (e) controls over fixed assets and petty cash (paras. 2.43 to 2.46); and
- (f) review of NGOs' fees and charges (paras. 2.47 to 2.53).

Reserves retained by non-governmental organisations

2.2 As mentioned in paragraph 1.15, an NGO receiving LSG subventions is allowed to retain unspent funds (excluding those mentioned in para. 2.3) in a reserve, up to a cap of 25% of the annual operating expenditure of the NGO, to meet future spending on FSA activities and FSA related activities. This reserve is known as the LSG Reserve.

2.3 In addition to the LSG Reserve, an NGO also retains two other types of reserves, namely, the Holding Account and the PF Reserve:

- (a) ***Holding Account.*** In order to facilitate NGOs to achieve their financial viability and to honour contractual commitments to "Snapshot Staff" after the cessation of the Tide-Over Grant (see para. 1.14(a)) in 2006-07, the SWD withheld the claw-back of LSG Reserves above the 25% cap for three years from 2004-05 to 2006-07. The cumulative LSG Reserves as at

31 March 2007 are kept in an account known as the Holding Account of individual NGOs. According to the SWD, NGOs may use such balances for FSA activities and FSA related activities; and

- (b) **PF Reserve.** Provision for provident funds can only be used for provident fund contributions (e.g. for contributions to the Mandatory Provident Fund Schemes). For “Snapshot Staff”, the provident fund surplus (Note 15) is subject to claw-back as the provision is calculated on an actual entitlement basis, whereas for “non-Snapshot Staff”, the subvention is paid at 6.8% (Note 16) of the mid-point salaries of the recognised staff establishments (see para. 1.12(b)). While PF Reserve for “non-Snapshot Staff” is not capped by the 25% rule as in the case of LSG Reserve, NGOs have been advised to fully deploy their provident fund provisions and reserves for “non-Snapshot Staff” on provident fund contributions, including possibly special contributions to award “non-Snapshot Staff” for their good performance. The cumulative PF Reserve arises due to the following reasons:

- (i) when an NGO does not fill up the vacant posts soon or employs fewer “non-Snapshot Staff” than the recognised staff establishments while the provision of provident fund contributions is based on the recognised staff establishments (see Note 3 to para. 1.12(a)); and
- (ii) according to the SWD, it is not uncommon that NGOs provide their “non-Snapshot Staff” with the minimum 5% contributions as required under the Mandatory Provident Fund Schemes Ordinance (Cap. 485) and the staff may be salaried lower than the mid-point. This gives rise to the surplus of 1.8% (6.8% – 5%) in provision and the surplus between the actual provident fund contributions on paid salaries and the 6.8% of mid-point provisions.

Note 15: *Surplus in provident fund arises from the time lag between the provision of provident funds to “Snapshot Staff” and the time that the staff left their NGOs.*

Note 16: *The 6.8% contribution rate was set by the SWD.*

2.4 Table 4 shows a breakdown of reserves retained by NGOs in the period 2011-12 to 2015-16 while Table 5 shows an analysis of the balances of reserves retained by NGOs as at 31 March 2016.

Table 4

**Reserves retained by NGOs
(2011-12 to 2015-16)**

Reserve	As at 31 March				
	2012	2013	2014	2015	2016
	(\$ billion)				
LSG Reserve	0.7	0.8	0.9	1.4	1.7
Holding Account	1.9	1.9	1.8	1.8	1.8
PF Reserve	0.8	0.9	1.1	1.2	1.2
Total	3.4	3.6	3.8	4.4	4.7

Source: SWD records

Table 5

**Balances of reserves retained by NGOs
(31 March 2016)**

Balance	LSG Reserve (Note 1)	Holding Account (Note 2)	PF Reserve (Note 3)
	(No. of NGOs)		
Nil	15	22	6
> \$0 to \$100,000	5	7	7
> \$100,000 to \$1,000,000	33	31	58
> \$1,000,000 to \$5,000,000	60	30	49
> \$5,000,000 to \$10,000,000	16	19	15
> \$10,000,000 to \$20,000,000	11	9	11
> \$20,000,000 to \$30,000,000	9	6	10
> \$30,000,000 to \$40,000,000	4	6	3
> \$40,000,000 to \$50,000,000	2	3	2
> \$50,000,000 to \$60,000,000	3	2	0
> \$60,000,000 to \$70,000,000	3	3	1
> \$70,000,000 to \$80,000,000	2	1	1
> \$80,000,000 to \$90,000,000	0	1	0
> \$90,000,000 to \$100,000,000	1	0	0
> \$100,000,000	1	4	2
Total	165	144	165

Source: Audit analysis of SWD records

Note 1: The largest balance of NGOs' LSG Reserves was \$180 million.

Note 2: The largest balance kept in NGOs' Holding Accounts was \$170 million.

Note 3: The largest balance of NGOs' PF Reserves was \$112 million.

Need to implement good practices on use of reserves

2.5 As shown in Table 4, total reserves had risen by 38% from \$3.4 billion in 2011-12 to \$4.7 billion in 2015-16. Furthermore, the total balances of:

- (a) LSG Reserve had risen by 143% from some \$0.7 billion in 2011-12 to \$1.7 billion in 2015-16;
- (b) Holding Account had slightly decreased from \$1.9 billion to \$1.8 billion (Note 17) in the period 2011-12 to 2015-16; and
- (c) PF Reserve had increased by 50% from some \$0.8 billion in 2011-12 to \$1.2 billion in 2015-16.

Furthermore, as shown in Table 5, while the majority of the NGOs, regardless of their sizes of services and hence the subvention levels, had accumulated a balance of below \$30 million in LSG Reserve, Holding Account and/or PF Reserve, some NGOs had accumulated reserves in excess of \$100 million.

2.6 According to the Level One guidelines relating to the use of reserves (LSG Reserve and balance in Holding Account) of the BPM (see para. 1.19 and Appendix C), an NGO:

- (a) should maximise the use of the reserves in order to maintain or strengthen service delivery and implement strategic development plans, including building up a staff team with high quality; and
- (b) is required to, through convenient, effective and timely channels, disseminate information about the reserves in a reader-friendly format to staff members and the public. Such information should include briefly a plan on how the reserves will be used in the future.

Note 17: *While the Holding Account could be used to honour the contractual commitments with “Snapshot Staff” (see para. 2.3(a)), Audit noted that the number of “Snapshot Staff” had decreased by 70% from 21,638 as at 1 April 2000 (see para. 1.12(a)(ii)) to 6,395 as at 1 September 2016.*

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2.7 According to the Level One guidelines relating to the use of PF Reserve of the BPM (see Appendix C), NGOs are required to:

- (a) maximise the use of PF Reserve for “non-Snapshot” staff for the designated purpose so as to enhance staff morale and their sense of belonging to the organisations; and
- (b) use convenient, effective and timely channels to disseminate information about the PF Reserve to staff members, including a brief plan on how the PF reserve will be used in the future.

2.8 NGOs are expected to follow the Level One guidelines, which include the practices relating to the use of reserves, unless they have strong justifications not to do so. They are given a transition period of three years (i.e. by 30 June 2017) to meeting the requirements of the BPM (see para. 1.19).

2.9 At the meeting of the LegCo Panel on Welfare Services held on 13 March 2017, the SWD reported the progress of the implementation of the BPM and shared the good practices of NGOs on the use of LSG Reserve. According to the SWD, it had also organised the Envisioning Programme on BPM, which consisted of seminars and workshops, from September 2015 to February 2016 for the senior management and boards of directors of NGOs to learn and share experiences and good practices on financial management, human resource management, corporate governance and public accountability.

2.10 In six of the NGOs visited by Audit (see para. 1.31(b)) during March to September 2017, Audit noted that some NGOs had planned their use of reserves. For example, one NGO, which had a total reserve of some \$35 million (being some \$11 million for LSG Reserve and some \$24 million for Holding Account balance), had planned to use \$20 million for service improvements and project enhancements, and upgrading the library system of its information accessibility centre. Another NGO was considering using LSG Reserve for incentive payments to staff. Some NGOs were also contemplating the use of PF Reserves.

2.11 Audit considers that the SWD needs to take further measures to facilitate NGOs to share, adopt and implement the good practices relating to the use of reserves and disclose the use of reserves according to the BPM guidelines. In circumstances where NGOs are unable to comply with the BPM guidelines, the SWD needs to ensure that NGOs provide strong justifications and give consent for exemption where appropriate. The SWD also needs to keep in view the balances of reserves and where necessary, reminds NGOs to take further measures to maximise the use of the reserves for enhancing FSA activities and FSA related activities.

Need to keep under review NGOs with persistent LSG operating deficits

2.12 In reviewing the reserves of the 165 NGOs receiving LSG subventions, Audit noted that while most of the NGOs had recorded LSG operating surpluses, some NGOs had incurred LSG operating deficits (see Table 6).

Table 6

**LSG deficits of NGOs
(2013-14 to 2015-16)**

	2013-14	2014-15	2015-16
No. of NGOs	83	31	31
Total amount of deficit	\$99,310,229	\$35,950,950	\$57,454,757
Lowest amount of deficit	\$863	\$2,714	\$2,042
Highest amount of deficit	\$12,902,923	\$6,395,623	\$10,615,385
Average amount of deficit	\$1,196,509	\$1,159,708	\$1,853,379

Source: Audit analysis of AFRs

2.13 Audit also noted that of the 31 NGOs that had incurred LSG deficits in 2015-16 (see Table 6), 14 had incurred deficits for three consecutive years from 2013-14 to 2015-16. Of these 14 NGOs, 8 had depleted their reserves (i.e. LSG Reserves and Holding Account balances) by the end of 2014-15. These 8 NGOs

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financed their operations from other non-FSA sources (e.g. income from self-financing activities and donations and using their own reserves). Table 7 shows the 8 NGOs' financial positions for the years 2014-15 and 2015-16. Of the remaining 6 NGOs, the NGOs still had LSG reserves (i.e. LSG Reserves and Holding Account balances) after offsetting their LSG deficits against their LSG reserves (see Table 8).

Table 7

**Financing positions of eight NGOs having depleted their
LSG Reserves and Holding Account balances
(2014-15 and 2015-16)**

NGO	NGO's LSG deficit		NGO's overall operating surplus/(deficit) (Note 1)		NGO's overall reserve (Note 2)	
	2014-15 (\$)	2015-16 (\$)	2014-15 (\$)	2015-16 (\$)	2014-15 (\$)	2015-16 (\$)
NGO 1	(3,331,184)	(2,422,690)	25,560,821	(22,274,955)	55,756,621	32,684,207
NGO 2	(2,540,524)	(2,370,015)	46,546,051	52,025,542	805,650,494	834,727,626
NGO 3	(1,134,511)	(1,293,353)	1,044,230	(410,359)	8,944,617	8,128,412
NGO 4	(1,630,890)	(1,260,864)	8,531,101	3,859,683	54,388,120	56,985,844
NGO 5	(1,072,173)	(1,073,028)	19,873,549	15,664,619	260,708,236	270,047,074
NGO 6	(19,656)	(58,833)	2,867,150	46,638	16,155,210	16,200,818
NGO 7	(105,503)	(30,120)	492,791	285,428	14,801,161	15,086,589
NGO 8	(64,062)	(2,042)	1,638,511	1,663,405	6,451,671	6,775,135

Source: Audit analysis of AFRs and NGOs' consolidated financial statements

Note 1: The NGO's overall operating surplus/deficit comprises the LSG deficit and the surplus/deficit generated from operation of non-FSA activities (e.g. self-financing activities).

Note 2: The NGO's overall reserve was the cumulative amount of reserve after taking into account the NGO's overall operating surplus/deficit.

Table 8

**LSG deficits and reserves of six NGOs still having
LSG Reserves and Holding Account balances
(2013-14 to 2015-16)**

NGO	LSG deficits			LSG reserves as at 31 March 2016 (Note) (\$)
	2013-14 (\$)	2014-15 (\$)	2015-16 (\$)	
NGO K	(12,902,923)	(6,395,623)	(10,615,385)	46,454,078
NGO 9	(1,946,500)	(4,146,171)	(7,247,622)	48,815,711
NGO 10	(151,528)	(219,521)	(5,364,169)	73,306,038
NGO 11	(3,810,358)	(3,860,382)	(2,584,607)	16,450,408
NGO 12	(338,558)	(157,241)	(309,755)	1,051,185
NGO 13	(187,371)	(309,929)	(219,032)	1,758,924

Source: Audit analysis of AFRs

Note: Reserves included LSG Reserves and Holding Account balances.

Remarks: Figures in brackets represent deficits.

2.14 Audit further analysed the AFRs of NGOs 9 and K, which had incurred largest amounts of LSG deficits in 2015-16. They were also the two NGOs whose deficits had significantly increased in the period 2014-15 and 2015-16. Audit found that staff emoluments (including salaries, provident funds and allowances) accounted for 80% and 81% of the total expenditure of NGO 9 in years 2014-15 and 2015-16 respectively, while staff emoluments accounted for 70% and 72% of the total expenditure of NGO K in years 2014-15 and 2015-16 respectively. Table 9 shows that increases in expenditure on emoluments could be a reason for the NGOs' LSG deficits.

Table 9

**Staff emoluments of two NGOs
(2014-15 and 2015-16)**

Staff with annual emolument over \$500,000 (Note 1)	Number of staff		Increase in number of staff	Emoluments		Increase in emolument (\$ million)
	2014-15	2015-16		2014-15 (\$ million)	2015-16 (\$ million)	
NGO 9						
Between \$500,001 and \$1 million	29	36	7	22.6	28.6	6.0 (27%)
Over \$1 million	1	3	2			
	30	39				
NGO K						
Between \$500,001 and \$1 million	76	133	57	76.2	111.4	35.2 (46%)
Over \$1 million	15	19	4			
	91 (Note 2)	152 (Note 2)				

Source: Audit analysis of AFRs

Note 1: According to the LSG Manual, an NGO is required to disclose in the AFR the number of posts with annual personal emoluments of over \$500,000 paid by the LSG. The threshold was revised to \$700,000 in 2016-17.

Note 2: NGO K had 90 existing staff and one new recruit in 2014-15 and 152 existing staff in 2015-16 each receiving an annual emolument between \$500,001 and \$1 million or over \$1 million.

2.15 Under the LSG subvention system, NGOs are allowed flexibility in deploying LSG subventions within the context of FSAs for purposes including (but not limited to) staff expenses and other operating expenses (see para. 1.9). At an LSG Steering Committee Meeting (see para. 1.24) held in October 2003, the Director of Social Welfare stated that NGOs should enjoy autonomy in using LSGs or LSG Reserves on the condition that the regulations in the LSG Manual were complied with and the expenditure spent would not cause any financial difficulties to the NGOs. She, however, reminded that NGOs' management should bear in mind the accountability issue, both to the public and their staff. She reiterated that it was the SWD's responsibility to monitor NGOs' proper use of public resources and the subvention inspections (see para. 2.30) should continue to examine cases of irregular spending and would be conducted in line with the spirit of the LSG (i.e. promoting accountability and corporate governance). Audit considers that the SWD needs to ascertain the reasons for NGOs having persistent LSG operating deficits, and offer advice where warranted. The SWD also needs to keep under review the operation of those NGOs in deficits for possible financial viability issues and to ensure smooth provision of FSA activities to the public.

Audit recommendations

2.16 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **take further measures to facilitate NGOs to share, adopt and implement the good practices relating to the use of reserves (i.e. LSG Reserves, Holding Account balances and PF Reserves) and disclose the use of reserves according to the BPM;**
- (b) **in circumstances where NGOs are unable to comply with the BPM guidelines, ensure that the NGOs provide strong justifications and the SWD gives consent for exemption where appropriate;**
- (c) **keep in view NGOs' balances of reserves and where necessary, remind NGOs to take further measures to maximise the use of the reserves, as required by the BPM guidelines, for enhancing FSA activities and FSA related activities to better the provision of welfare services to the public;**

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- (d) **ascertain the reasons for some NGOs having incurred large or persistent LSG operating deficits and offer advice where warranted; and**
- (e) **keep under review the operation of NGOs in deficits for possible financial viability issues and offer advice to NGOs where warranted.**

Response from the Government

2.17 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) the SWD will take follow up actions as recommended;
- (b) the welfare sector has agreed to allow NGOs time to review and set out their policies and guidelines on the implementation of the BPM during the three-year period from 1 July 2014 to 30 June 2017. The analyses on the 2016-17 cycle will be available in early 2018. The SWD will sustain measures to monitor NGOs' compliance with the BPM and facilitate NGOs to share, adopt and implement good practices on optimal use of reserves and disclosure of the use of such reserves; and
- (c) the SWD will examine NGOs' LSG Reserve and their financial position as shown in their audited financial statements to ascertain their ongoing financial viability.

Disclosure of non-governmental organisations' senior staff emoluments

2.18 In March 2003, in the light of public concern, the Director of Administration issued a Circular Memorandum (the Memorandum) promulgating a set of guidelines for the control and monitoring of remuneration practices in subvented bodies by Directors of government bureaux and Controlling Officers of government departments. The guidelines require a subvented body to review and disclose annually the remunerations of its top three-tier staff (hereinafter referred to as the disclosure

requirement) unless it meets one or more of the following exemption criteria (Note 18):

- (a) the subvented body receives government subvention of less than \$10 million a year; or
- (b) government subvention constitutes a proportion of 50% or less of the subvented body's operating income whereby the proportion is the average government subvention received in the past four years to the average operating income in the same period; or
- (c) the emoluments of top three-tier staff of the subvented body are funded entirely by income from sources other than the government.

According to the Memorandum, the subvented bodies should submit annual reports on the review of the number, rank and remunerations of their senior staff to their responsible Directors of Bureaux who may, with justifications, approve individual bodies to submit biennial or triennial review reports. To enhance transparency, Directors of Bureaux will work out with those subvented bodies under their purview suitable arrangements for public disclosure of their review reports. For a multi-disciplinary organisation providing services which fall under programme areas of different Directors of Bureaux, a Director of Bureau would be responsible for that part of the review report covering those senior staff who operate services under his/her policy purview. The Secretary for Financial Services and the Treasury subsequently promulgated in a separate circular the consequential amendments (e.g. "no double

Note 18: *There are other exemption criteria as follows:*

- (a) *government funds are provided as subscription/sponsorship fees;*
- (b) *government funds are provided as fees for the procurement of services;*
- (c) *organisations where their top three-tier positions are filled entirely by civil servants; and*
- (d) *organisations that are subject to statutory provisions or decisions approved by the Executive Council/the LegCo on staffing matters and where the provisions/decisions are in conflict with the new guidelines or have prescribed separate monitoring and control mechanisms (e.g. the Hospital Authority and the institutions funded by the University Grants Committee).*

housing benefits” rule in the subvented sector) to various financial circulars, memoranda and relevant guidelines in March 2003.

Deferring the implementation of disclosure requirement

2.19 The effective date for the implementation of the disclosure requirement was 1 April 2003. However, according to the Memorandum, the Directors of bureaux may, with justifications, approve implementation on a later date.

2.20 Instead of April 2003, the SWD implemented the disclosure requirement with effect from a later date in 2009-10 (Note 19). In January 2010, in a paper submitted in a meeting of the LSG Steering Committee to seek the members’ views on the implementation details of the Memorandum, the SWD stated that as the LSG subvention system had only been implemented for a short period of time by the time of 2003 and the LSG Manual had to be revised to include the disclosure requirement, the SWD only implemented the disclosure requirement in 2009-10. Audit, however, noted that although the membership of the LSG Steering Committee includes a representative of the LWB, there was no documentary evidence indicating that the LWB had, in accordance with the requirement of the Memorandum (see paras. 2.18 and 2.19), approved deferring the implementation of the disclosure requirement.

Note 19: *In September 2017, the SWD informed Audit that since the implementation of the LSG subvention system in 2001, NGOs have been required to disclose their personal emolument expenditures including the number of posts with personal emoluments in excess of \$500,000 in the AFRs submitted to the SWD. Furthermore, during 2001 to 2012, NGOs were required to provide information on personal emoluments of the top three highest paid staff members of the service unit or central administration office during the SWD’s accounting inspections (see para. 1.22(a)).*

More NGOs may be required to disclose senior staff emoluments

2.21 The SWD has implemented the disclosure requirement since 2009-10. In applying the exemption criteria, the SWD has used “the NGO’s operating income from the SWD” (Note 20) for meeting the criterion regarding “government subvention” (see para. 2.18). Regarding the 50% income threshold (see para. 2.18(b)), the SWD has used the NGO’s consolidated operating income as the basis for determining whether the threshold is met (see also Note 22(a) to para. 2.24(a)). On a financial year basis, NGOs not meeting the exemption criteria should submit a review report on remuneration packages for staff in the top three tiers (Note 21) to the SWD by 31 October. Information in the review report includes the number of staff, staff ranks, total staff cost, and a breakdown of staff salaries, provident funds, cash allowances and non-cash benefits (e.g. medical and dental insurance). NGOs are also required to make public disclosure of the review reports through prescribed means (e.g. uploading the information to the NGOs’ websites or reporting the information in their annual reports). Since June 2017, the SWD has made available all the NGOs’ 2015-16 review reports on the SWD’s website by uploading the reports or hyperlinking to the reports posted on the NGOs’ websites.

2.22 In 2015-16, of the 165 NGOs receiving LSG subventions, 66 (40%) were not exempted from submission of the review reports (these 66 NGOs are marked with an asterisk in Appendix A). These 66 NGOs employed a total of 870 staff in top three tiers. Table 10 shows the emoluments of these 870 staff while Table 11 provides information on the 10 NGOs with the highest emoluments for first-tier staff.

Note 20: *NGOs’ operating income from the SWD includes LSG subventions and other subsidies from the SWD (e.g. rent and rates subsidies) but excludes certain payments for welfare services (e.g. contracted residential care homes for the elderly).*

Note 21: *According to the SWD, the first-tier staff is the executive head of the NGO who is directly responsible to the NGO Board/Management Committee. The second-tier staff are responsible to the executive head of the NGO while the third-tier staff are responsible to the second-tier staff.*

Table 10

**Emoluments of NGO staff in top three tiers
(2015-16)**

Range of total annual remuneration paid by LSG subventions/other subsidies	No. of staff	No. of NGOs
<i>First tier</i>		
≤ \$500,000	4	4
> \$500,000 to \$1 million	25	15
> \$1 million to \$1.5 million	31	31
> \$1.5 million to \$2 million	14	13
> \$2 million	3	3
Subtotal	77	66
<i>Second tier</i>		
≤ \$500,000	34	10
> \$500,000 to \$1 million	146	36
> \$1 million to \$1.5 million	41	18
> \$1.5 million to \$2 million	4	2
> \$2 million	0	0
Subtotal	225	66
<i>Third tier</i>		
≤ \$400,000	159	14
> \$400,000 to \$600,000	131	12
> \$600,000 to \$800,000	130	21
> \$800,000 to \$1 million	138	16
> \$1 million to \$1.2 million	6	2
> \$1.2 million to \$1.4 million	4	1
Subtotal	568	66
Total	870	

Source: Audit analysis of SWD records

Table 11

**Ten NGOs with highest emoluments for first-tier staff
(2015-16)**

	Emolument (Note) (a) (\$ million)	NGO's operating income from the SWD (see para. 2.21) (b) (\$ million)	Percentage of emolument to NGO's operating income from the SWD (c) = (a) ÷ (b) × 100%	No. of ASUs of NGO
1	2.1	575	0.4%	28
2	2.0	627	0.3%	83
3	2.0	392	0.5%	79
4	2.0	300	0.7%	42
5	1.9	311	0.6%	75
6	1.8	38	4.7%	7
7	1.8	238	0.8%	58
8	1.8	278	0.6%	54
9	1.6	381	0.4%	62
10	1.6	255	0.6%	51

Source: SWD records

Note: All the 10 NGOs had only one staff in the first tier.

2.23 In June 2013, the SWD saw a need to seek confirmation from the Administration Wing of the Chief Secretary for Administration's Office (the Administration Wing) on whether the use of "NGO's operating income from the SWD" was in line with the criterion of "government subvention" (which includes subventions received by an NGO from various Government bureaux/departments) (see para. 2.18(b)) insofar as exemption criteria are concerned. The SWD, therefore, sought clarification and advice from the Administration Wing on whether the exemption criteria that the SWD had adopted, particularly in exempting an NGO receiving 50% or less of its operating income from the SWD from the reporting requirement, were in line with the guidelines promulgated by the Memorandum. In July 2013, the Administration Wing asked the SWD to seek advice from the Financial Services and the Treasury Bureau (FSTB). According to the SWD, in late July 2013, the SWD contacted the FSTB which advised that it would need more time to consider the matter. The SWD could not find any records on the FSTB's response to the SWD. In October 2017, the FSTB informed Audit that there was no written correspondence between the SWD and the FSTB.

2.24 In January 2017, the SWD further sought clarifications from the Administration Wing and the FSTB. There followed a series of deliberations via e-mail exchanges and meetings among the SWD, the Administration Wing and the FSTB from January to June 2017 to clarify the meaning of the exemption criteria as stated in the Memorandum in the light of relevant records of past discussions. In July 2017, noting the SWD's plan to send reminder of the disclosure requirement to subvented NGOs shortly and after consulting the FSTB, the Administration Wing conveyed the following advice to the SWD:

- (a) in determining whether a subvented body should be subject to the review and reporting requirement, the relevant Director of Bureau/Controlling Officer should look at the part of the operating income relating to the subvented services under his/her purview, i.e. a bureau/department has to monitor only those subvented bodies that receive subventions from the bureau/department for its responsible service/policy area and when those subventions account for more than 50% of the operating income of the subvented bodies in that specific service/policy area. The SWD's prevailing practice has been at variance with the intents of the Memorandum (Note 22);
- (b) the responsibility for administering the 2003 Guidelines rests with the relevant Director of Bureau. Detailed arrangements for monitoring the remuneration practices should be left to the relevant Director of Bureau and any departure from the Memorandum should be justified. The SWD should discuss with the LWB on its planned actions in the coming annual review; and

Note 22: *The SWD's prevailing practice in calculating the 50% threshold and the calculation as intended by the Memorandum (see para. 2.18(b)) are compared below:*

- (a) *The SWD's existing calculation:*

$$\frac{\text{The NGO's operating income from the SWD}}{\text{Operating income of the NGO as a whole (in accordance with the NGO's audited consolidated financial statements)}} \times 100\%$$

- (b) *Calculation according to the intents of the Memorandum:*

$$\frac{\text{The NGO's operating income from the SWD}}{\text{Operating income of the NGO under the purview of the Secretary for Labour and Welfare/ the Director of Social Welfare}} \times 100\%$$

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- (c) the Administration Wing would, together with the FSTB, carry out a survey for the purpose of finding out from all relevant bureaux/departments how they have been implementing the Memorandum and whether they have encountered problems. It would analyse the findings and consider whether the Memorandum needs to be updated or revised (Note 23).

2.25 In August 2017, the SWD informed the Administration Wing (with a copy of the e-mail sent to the LWB) that the SWD would continue to adopt its existing way of disclosing the remunerations of NGOs' senior staff until the Administration Wing had completed its survey on how the bureaux/departments implement the Memorandum and confirmed whether the Memorandum was required to be updated or revised (see para. 2.24(c)).

2.26 In October 2017, the Administration Wing informed Audit that:

- (a) the advice given by the FSTB and the Administration Wing to the SWD in July 2017 (in para. 2.24) has clearly explained the intents of the Memorandum and pointed out that the SWD should discuss with the LWB on how to take forward this year's annual review. In other words, there is no need for the SWD and the LWB to wait until the completion of the survey in order to decide how they should implement the guidelines. While the survey serves the purpose of finding out how bureaux/departments have been implementing the guidelines, it is not intended as a means to ascertain the intents of the Memorandum, which have already been clearly explained to the SWD in July 2017;
- (b) as the Secretary for Labour and Welfare is responsible for administering the 2003 guidelines, whether the SWD should continue with its prevailing practice should be subject to the views of the Secretary for Labour and Welfare who should be satisfied that there is proper justification for the departure from the intents of the Memorandum or otherwise; and
- (c) the Administration Wing has finalised the design of the survey and issued the questionnaire concerned to all relevant bureaux in early October 2017.

Note 23: *The Administration Wing had informed Members of the LegCo the intents of the Memorandum at a closed-door case conference held in June 2017.*

Audit recommendations

2.27 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **take immediate action to obtain covering approval, from the Secretary for Labour and Welfare, for deferring the implementation of the requirement for the review and disclosure of emoluments of NGOs' staff in top three tiers; and**
- (b) **take necessary follow-up action on the advice of the Director of Administration (see para. 2.24).**

Response from the Government

2.28 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) the SWD has recently obtained covering approval from the Secretary for Labour and Welfare for the SWD to defer the implementation of the guidelines in the Memorandum to 2009-10; and
- (b) the SWD will take necessary follow-up action on the advice of the Director of Administration.

2.29 The Secretary for Labour and Welfare has also said that upon receipt of the SWD's written request, the LWB has given covering approval for the deferment.

Accounting inspections

2.30 According to the LSG Manual, NGOs should always ensure that adequate internal controls are in place having regard to the nature and sizes of their organisations and the services provided. The SWD has provided advice on internal control procedures in respect of important financial activities as part of the SWD's subvention inspection process. As mentioned in paragraph 1.22(a), the SWD's Finance Branch conducts accounting inspections at NGO premises which include reviewing compliance with accounting and financial reporting requirements

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as laid down in the LSG Manual, and reviewing/advising on internal control procedures (e.g. ascertaining the adequacy of internal controls and checking whether LSG subventions are properly used).

2.31 Prior to 2016-17, accounting inspections of all the 165 NGOs receiving LSG subventions were conducted on a uniform cycle basis. On-site inspections of the accounting records of NGOs' ASUs were conducted. In determining the number of ASUs to be inspected, the SWD's Finance Branch considered the following factors:

- (a) whether the ASUs had previously been inspected;
- (b) whether significant irregularities were found in previous inspections of the ASUs; and
- (c) whether the ASUs had incurred significant amounts of staff emoluments or other charges.

2.32 From 2016-17 onwards, the frequency of accounting inspections of the 165 NGOs may vary having regard to a host of risk factors, such as the amount of LSG subvention to the NGO and the number of the ASUs operated by the NGO.

Scope for improvement in conducting accounting inspections

2.33 Audit reviewed the accounting inspections conducted by the SWD's Finance Branch and found that:

- (a) in 2016-17, of the 53 NGOs involving a total of 120 ASUs planned to be inspected, inspections at 6 NGOs (11% of 53) involving a total of 21 ASUs (18% of 120) had not been conducted within 2016-17 as planned;
- (b) some irregularities and internal control weaknesses were commonly found in inspections of ASUs of NGOs (see Table 12);

Table 12

**Common irregularities and internal control weaknesses
found in accounting inspections
(2014-15 to 2016-17)**

	2014-15	2015-16	2016-17
No. of NGOs inspected	50	67	47
No. of ASUs inspected	96	143	99
	2014-15	2015-16	2016-17
	No. of NGOs		
<i>Irregularity found</i>			
Cross-subsidisation between FSA and self-financing activities/inclusion of non-FSA items in AFR/unrecognised rent and rates expenditure charged to LSG	5	14	16
Incorrect charging/reporting of provident funds	9	15	17
Omission of FSA or FSA related items in AFR	5	8	5
Inclusion of non-cash items (e.g. depreciation) in/exclusion of cash items from AFR	19	15	15
Non-compliance with procurement procedures	10	19	18
<i>Area of internal control weakness found</i>			
Revenue collection and receipt (e.g. receipt registers not prepared)	16	11	22
Payment (e.g. invoices not stamped with a “PAID” chop upon settlement of expenses)	15	15	18
Bank account and cheque (e.g. late preparation of bank reconciliation statements and cheques remained unrepresented for more than six months)	17	16	27
Petty cash (e.g. no acknowledged receipts of petty cash reimbursements)	12	10	11
Programme income and expenses (e.g. financial reports not promptly reviewed after completion of programmes)	13	13	11
Fixed assets (e.g. incomplete/incorrect fixed asset registers)	15	18	25

Source: Audit analysis of SWD records

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- (c) internal control weaknesses of ASUs of some NGOs had existed for a long period of time (see Table 13 for an example of NGO D having 90 ASUs as at November 2015); and

Table 13

Internal control weaknesses of NGO D's ASUs

	ASU (Note 1)		
	2008-09	2010-11	2013-14
<i>ASU of the NGO inspected (Note 2)</i>	1,2,3,4	1,5,6,7	8,9,10,11
<i>ASU having the following area of internal control weakness</i>			
Revenue collection and receipt	1,3,4	1,5,7	
Payment	1,2,3,4	1,5,6,7	
Bank account and cheque		1	
Petty cash		1,5,7	8,9,10,11
Advance of programme expenses to staff		5,7	9,10
Programme income and expenses	2,4		9,10,11
Fixed assets	1,2		8,10,11

Source: Audit analysis of SWD records

Note 1: The NGO's ASUs had also been inspected in 2016-17 but the inspection results had not yet been summarised by the Finance Branch as at the end of September 2017.

Note 2: Each number represents an ASU of the NGO.

- (d) there are other risk factors that the Finance Branch should consider in formulating its risk-based inspections (see para. 2.32). Such factors may include, for example, NGOs with operating deficits (see para. 2.12) and NGOs that were given qualified opinions by external auditors on their accounts. Audit noted that in 2014-15 and 2015-16, of the 165 NGOs,

4 had been given qualified opinions (e.g. because the auditor was not provided full set of statutory records).

Audit recommendations

2.34 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **ascertain the reasons why the accounting inspections at some NGOs have not been conducted as scheduled and take measures to ensure that the inspections are conducted as planned in the future;**
- (b) **take measures (e.g. arranging training seminars and experience sharing sessions on good accounting practices of NGOs) to assist NGOs to improve their internal controls and minimise occurrence (especially repeated occurrence) of irregularities;**
- (c) **for those NGOs that made no improvement in their internal controls or minimising the occurrence of irregularities (as shown in Table 13), consider the need for issuing a warning letter informing them that in accordance with the LSG Manual, the SWD may withhold or terminate LSG subventions if an NGO fails to exercise reasonable and prudent financial management or comply with the LSG requirements as laid down in the LSG Manual; and**
- (d) **consider taking into account other risk factors (e.g. NGOs operated in deficits with possible ongoing financial viability issues and NGOs whose accounts have been given qualified opinions by external auditors) in formulating plans for accounting inspections.**

Response from the Government

2.35 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD:

- (a) has completed accounting inspections at the six NGOs (see para. 2.33(a)) in the first half of 2017-18 and will deploy sufficient resources to conduct accounting inspections as planned;

- (b) will issue reminders to NGOs annually to remind them of their responsibility to ensure that adequate internal controls are in place and will consider taking follow up actions where warranted; and
- (c) will take into account various risk factors in formulating plans for accounting inspections.

Cross-subsidisation between lump sum grant subventions and self-financing activities

2.36 It is common that NGOs providing FSA activities (including FSA related activities) also provide non-FSA activities (see para. 1.33(c)). NGOs are not allowed to use LSG subventions to cross-subsidise non-FSA activities. This requirement has been stated in the following key documents:

- (a) according to the LSG Manual, LSG subventions are intended for operating FSA activities or FSA related activities. NGOs should ensure that financial transactions are separately identified into FSA activities and non-FSA activities; and
- (b) according to Financial Circular No. 9/2004 “Guidelines on the Management and Control of Government Funding for Subvented Organisations”, subvented organisations (e.g. NGOs) should ensure that there is no cross-subsidisation of self-financing activities by subvented programmes in money or in kind.

According to the LSG Manual, to avoid misunderstanding, NGOs should consult the SWD in a timely manner as to what constitutes “FSA related” activities before conducting such activities.

2.37 For the six NGOs visited by Audit (see para. 1.31(b)), LSG subventions accounted for 25% to 62% of an NGO’s total income in 2015-16 (see Table 14).

Table 14

**Sources of incomes of six NGOs visited by Audit
(2015-16)**

NGO	Source of incomes			
	LSG subvention	Other sources		
		Other government subventions/grants/subsidies (Note) (a)	Self-financing activities (b)	Total (c) = (a) + (b)
F	34 %	36 %	30 %	66 %
G	53 %	8 %	39 %	47 %
H	40 %	4 %	56 %	60 %
I	25 %	32 %	43 %	75 %
J	62 %	23 %	15 %	38 %
K	39 %	5 %	56 %	61 %

Source: Audit analysis of NGO records

Note: Other government subventions/grants/subsidies include those provided by the SWD (other than LSG subventions — see Note 1 to para. 1.4) and those provided by other government departments/bureaux.

Need to apportion head office overheads

2.38 Each of the six NGOs visited by Audit (see para. 1.31(b)) had established a head office, which carried out central administrative and support functions for the respective NGO. In 2015-16, the six NGOs incurred overheads totalling some \$71.9 million for their head offices. For three NGOs (NGOs F, G and H which received LSG subventions totalling some \$205 million in 2015-16), the head office overheads (e.g. salaries, insurance, telephone charges) had been apportioned between FSA activities and non-FSA activities.

2.39 Audit, however, noted that for the remaining three NGOs (NGOs I, J and K which received LSG subventions totalling \$471 million in 2015-16), apportionment of head office overheads had not been made. Instead, the head office overheads had been allocated entirely to FSA activities. This was a cause for concern because:

- (a) ***Considerable non-FSA activities.*** NGO head offices provided central administrative support to both FSA activities and non-FSA activities. The non-FSA activities could be considerable (e.g. 75% of NGO I's income in 2015-16 was derived from sources other than LSG subventions — see Table 14 in para. 2.37) and would have taken up a significant portion of head office overheads. Despite this, the head office overheads had not been apportioned; and
- (b) ***Large amounts of head office overheads.*** The head office overheads in 2015-16 amounted to some \$10.5 million for NGO I, some \$16 million for NGO J and some \$22.2 million for NGO K. These large amounts of overheads, however, had not been properly accounted for.

The SWD needs to request the NGOs concerned to rectify the anomaly (i.e. overheads had not been apportioned by the NGOs between FSA activities and non-FSA activities).

Need to adopt appropriate bases for apportioning overheads

2.40 Audit also noted that the bases used by the NGOs for apportioning the overheads between FSA activities and non-FSA activities were not always consistent and proportionate. Examples are shown in Cases 1 and 2. The SWD needs to request the NGOs to address the anomalies in these two cases.

Case 1

**Apportionment of staff salaries of central kitchen
(2016-17)**

1. NGO H had 5 service units, comprising 3 service units for the conduct of FSA activities (FSA units) and 2 service units for non-FSA activities (non-FSA units). NGO H's central administrative branch provided kitchen services to the 5 service units. The central kitchen had 7 kitchen staff.

2. The 2016-17 salaries of the 7 kitchen staff totalled some \$1.3 million, of which some \$940,000 (72%) was apportioned to FSA activities on the following basis:

Rank of kitchen staff	No. of staff	Salaries allocated to	
		FSA activities (3 FSA Units)	Non-FSA activities (2 non-FSA units)
Chief	1	} 72%	
Cook	4		
Cook	1		} 28%
Assistant cook	1		
Total	7		

The rationale for using the above basis had not been documented.

3. According to the records of NGO H, the vast majority (98%) of the meals prepared by the central kitchen in 2016-17 were served to service users. As at 31 March 2017, there were 257 service users, comprising 119 (46%) at the non-FSA units and 138 (54%) at the FSA units. The apportionment of 72% of kitchen staff salaries to the FSA units (see para. 2 above) did not appear to be in line with the fact that only 54% of the kitchen services were provided to service users at the FSA units. Upon enquiry in June 2017, NGO H informed Audit that the basis for allocating kitchen staff salaries was set a long time ago. In the past, there were more service users at the FSA units.

Source: Audit analysis of NGO H records

Case 2

Apportionment of water charges, artisan salaries and emolument of Chief Executive Officer (2016-17)

1. NGO G rented part of a building for operating an FSA unit and a non-FSA unit, which occupied 95% and 5% of the rented areas respectively.
2. NGO G dealt with the key costs of accommodation for 2016-17 as follows:
 - (a) **Rent and rates** (Note). The total amount of \$677,600 was apportioned between the FSA unit and the non-FSA unit according to the proportion of rented areas occupied by them (see para. 1 above);
 - (b) **Electricity charges**. The FSA unit and the non-FSA unit maintained separate electricity meters. According to its meter, the non-FSA unit was charged an amount of \$7,190 for its use of electricity;
 - (c) **Water charges**. The FSA unit and the non-FSA unit did not have separate water meters. Charges of \$193,488 in total were levied on NGO G for the use of water at the FSA unit and the non-FSA unit. The NGO allocated the \$193,488 entirely to the FSA unit; and
 - (d) **Artisan salaries**. An artisan was responsible for conducting repair and maintenance works for the FSA unit and the non-FSA unit. The NGO allocated the artisan's annual salaries of some \$200,000 entirely to the FSA unit.

Allocating water charges and artisan salaries entirely to the FSA unit was at variance with the apportionment of other costs of accommodation (see (a) and (b) above). The water charges and artisan salaries had been over-apportioned to the FSA unit.

3. Furthermore, Audit noted that the emolument of the NGO's Chief Executive Officer (\$1.57 million for 2015-16 — based on the latest available AFR) had been solely charged to FSA activities.

Source: Audit analysis of NGO G records

Note: Apart from LSG subventions, the SWD separately subvented the NGO's rent and rates and paid them on an actual basis.

Audit recommendations

- 2.41 **Audit has *recommended* that the Director of Social Welfare should:**
- (a) **request the three NGOs (i.e. NGOs I, J and K — see para. 2.39), which have not apportioned the head office overheads between FSA activities and non-FSA activities, to apportion such overheads;**
 - (b) **remind NGOs of the need to apportion head office overheads between FSA activities and non-FSA activities;**
 - (c) **request the two NGOs that have anomalies in apportioning the overheads between FSA activities and non-FSA activities (i.e. NGOs H and G — see Cases 1 and 2 in para. 2.40) to review their bases of apportionment and properly apportion the costs; and**
 - (d) **take measures to help NGOs adopt an appropriate basis for apportioning overheads between FSA activities and non-FSA activities.**

Response from the Government

2.42 The Director of Social Welfare agrees with the audit recommendations. She has said that the LSG Manual provides that NGOs should consult the SWD in a timely manner as to what constitutes “FSA related” activities before conducting such activities (see para. 2.36). The SWD will:

- (a) request the NGOs concerned (see paras. 2.39 and 2.40) to rectify the anomaly; and
- (b) issue reminders to NGOs annually to remind them of the need to properly apportion costs between FSA activities and non-FSA activities, and to provide advice to NGOs where required.

Controls over fixed assets and petty cash

2.43 Internal controls are fundamental to sound and prudent financial management. The LSG Manual has set out internal controls governing the conduct of financial activities by NGOs. Control of fixed assets and petty cash are two of these internal controls. According to the LSG Manual:

- (a) the key internal control procedures relating to fixed assets include:
 - (i) **Identification number.** Each item of assets should be labelled/marked with an assigned serial number;
 - (ii) **Fixed asset register.** A fixed asset register should be kept, and should contain details such as identification numbers, physical locations of assets and authorisation for disposal of assets; and
 - (iii) **Physical checking.** Checking of assets should be conducted at least once a year. Results and records of checking should be retained; and
- (b) the key internal control procedures relating to petty cash include:
 - (i) **Surprise cash counts.** Supervisors of ASUs or independent officers from NGO headquarters should conduct surprise cash counts for petty cash; and
 - (ii) **Frequency of cash counts.** Surprise cash counts should be conducted at irregular intervals and at least, say, three times a year.

Need to properly follow internal control procedures

2.44 For the six NGOs visited (see para. 1.31(b)), Audit noted cases where the internal control procedures as set out in the LSG Manual had not been properly followed. Details are as follows:

- (a) ***Internal control procedures for fixed assets.*** Against the specified control procedures (see para. 2.43(a)), Audit examined 160 fixed asset items (Note 24). Audit found that of these 160 cases examined:
- (i) in 16 (10%) cases, the fixed asset items did not have any identification numbers;
 - (ii) in 22 (13.8%) cases, there was incorrect or missing information in the fixed asset registers, i.e. wrong asset locations, wrong/missing identification numbers, wrong descriptions of assets, no record of an item (a 16 port router) which had been physically located by Audit, and no record of authorisation for an item (a mobile phone) which had been written off; and
 - (iii) in 2 (1.3%) cases, the items recorded in the NGO's fixed asset register could not be physically located; and
- (b) ***Internal control procedures for petty cash.*** Against the specified control procedures (see para. 2.43(b)), Audit examined 19 petty cash accounts (Note 25). Audit found that of these 19 cases examined:
- (i) in 2 cases, at the time of Audit's visits, there were no records indicating that cash counts had been conducted in the past year; and
 - (ii) in 18 cases, less than three surprise cash counts were conducted annually, falling short of the suggested frequency of at least three times a year (see para. 2.43(b)(ii)).

Note 24: *At the six NGOs (see para. 1.31(b)), Audit visited a total of eight service units. For each service unit, Audit examined 20 fixed asset items.*

Note 25: *The six NGOs and eight service units visited by Audit maintained a total of 19 petty cash accounts (3 maintained by NGOs' head offices and 16 by NGOs' service units).*

Audit recommendations

- 2.45 **Audit has *recommended* that the Director of Social Welfare should:**
- (a) **take measures to assist NGOs to properly follow the internal control procedures set out in the LSG Manual; and**
 - (b) **require NGOs to step up their internal controls (e.g. conducting supervisory checks to ensure the accuracy of fixed asset registers).**

Response from the Government

2.46 The Director of Social Welfare agrees with the audit recommendations. She has said that NGOs should properly follow the advice on internal control procedures set out in the LSG Manual. The SWD will issue reminders to NGOs annually to remind them of their responsibility to ensure that adequate internal controls are in place and will provide advice to NGOs where required.

Review of non-governmental organisations' fees and charges

2.47 As mentioned in paragraph 1.12(d), NGOs make charges for their welfare services provided. Such charges are deducted from the LSG subventions payable to the NGOs.

2.48 According to a memo issued by the then Secretary for the Treasury to the then Secretary for Health and Welfare (Note 26) in July 1999, the general principles of fee-charging in subvented welfare services are:

- (a) to ensure more equitable use of public resources, subsidy levels as well as fee structure should be designed in such a manner that users who could afford should be made to take a fair share of the financially responsible and contribute to the cost of service;

Note 26: *The policy portfolio on welfare matters of the Health and Welfare Bureau was taken over by the LWB with effect from 1 July 2007.*

- (b) fees and charges could serve as a demand management tool to reduce unnecessary demand. In this regard, a totally free or heavily subsidised service would easily lead to misuse and reduces the overall efficiency and effectiveness of use of resources; and
- (c) fees and charges were sources of revenue which should not be ignored to enable government to free and redirect public resources to increase or improve services.

Fees and charges not adjusted for a long period of time

2.49 Audit, however, noted that the current fees and charges for subvented welfare services have been frozen at the existing level (Note 27) since 1997-98 (some 18 years), except the fees for residential care services for the elderly and persons with disabilities, which were revised in 2000-01.

2.50 In 2012, a working group (Note 28) was set up by the SWD to review the fee charging practices for subvented welfare services. The working group proposed that all fees and charges should remain unchanged until 2015. From October 2015 onwards, however, all fees and charges should be adjusted upwards by 10% every year until a cumulative adjustment of about 35% was achieved to compensate for adjustments not made in the past. The working group estimated that the cumulative savings in LSG subventions for five years would be some \$417 million. In September 2017, the SWD informed Audit that the working group subsequently proposed the option of adjusting all the fees and charges ranging from 7% to 10% from October 2015 for examination. The SWD considered that the impact on service users and the arrangements for resuming the adjustment of fees and charges needed to be further deliberated. In the interim, the existing level of fees and charges were maintained while the annual review continued to be conducted.

Note 27: *Fees and charges for subvented welfare services can be found on the SWD's website (www.swd.gov.hk).*

Note 28: *The working group comprised representatives from the Service Branches, Social Security Branch, Finance Branch and Subventions Branch of the SWD.*

2.51 In March 2017, the working group proposed to adopt a modest approach on the fees and charges by making reference to certain factors (e.g. the social security assistance price index compiled monthly by the Census and Statistics Department). The adjustment for the year 2017-18 would be in the region of 2.8%. The SWD also stated that the cumulative fees adjustment (see para. 2.50) would be deliberated after resuming the fees adjustment mechanism in 2018-19. In May 2017, the SWD submitted a proposal for fee adjustment in 2018-19 to the LWB and the FSTB for comments and advice. According to the FSTB, it had indicated to the LWB in June 2017 that it would offer comments as soon as practicable upon receipt of the LWB's policy support. In October 2017, the LWB informed Audit that during September to October 2017, the LWB had discussed with the SWD the proposed fees adjustment in 2018-19, and had advised the SWD on the way forward.

Audit recommendations

2.52 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **based on the response from the LWB and the FSTB on the proposed fees adjustment for subvented welfare services in 2018-19, take necessary action accordingly;**
- (b) **review regularly fees and charges for subvented welfare services; and**
- (c) **deliberate on the way forward of making cumulative fees adjustment for subvented welfare services.**

Response from the Government

2.53 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD will:

- (a) review regularly the fees and charges for subvented services; and
- (b) based on the advice from the LWB and the FSTB, follow up the proposed fee adjustment in 2018-19, and deliberate on the way forward.

PART 3: SELF-ASSESSMENT OF SERVICE QUALITY BY NON-GOVERNMENTAL ORGANISATIONS

3.1 This PART examines self-assessment of service quality by NGOs, focusing on the following issues:

- (a) conduct and reporting of self-assessment (paras. 3.6 to 3.9);
- (b) implementation of SQSs (paras. 3.10 to 3.14); and
- (c) conduct of internal service inspections (paras. 3.15 to 3.18).

Self-assessment mechanism

3.2 In accordance with FSAs, ASUs are required to conduct self-assessment of attainment of Output Standards, Outcome Standards, ESRs and SQSs. They need to submit to the SWD's Subventions Branch:

- (a) a quarterly statistical report on the actual performance on Output Standards and Outcome Standards;
- (b) a half-yearly report on variances against the agreed levels of Output Standards and Outcome Standards; and
- (c) an annual self-assessment report on attainment in Output Standards and Outcome Standards, ESRs and SQSs.

With the exception of the report mentioned in (a) above, all other reports are to be submitted on an NGO basis covering all the NGO's ASUs.

3.3 In submitting the annual self-assessment report (see para. 3.2(c)), an NGO is also required to submit an action plan for addressing areas with underperformance (e.g. an Output/Outcome Standard not met). The NGO needs to report to the SWD

Self-assessment of service quality by non-governmental organisations

on the action taken and results achieved within a timeframe agreed with the SWD. According to the LSG Manual, if an NGO fails to achieve a reasonable standard of performance, the SWD may withhold or terminate its LSG subvention (Note 29).

3.4 As stipulated in the manual of the SWD's Service Performance Monitoring System (see Note 9 to para. 1.22(c)(iv)), the self-assessment mechanism respects and honours the corporate governance of the NGOs. It is the responsibility of the NGOs to ensure their ASUs' compliance with the requirements (i.e. Output Standards, Outcome Standards, ESRs and SQSs). Being an internal management process, an NGO may choose to conduct self-assessment at any point of time to evaluate its ASUs' compliance with the requirements and may adopt different approaches to evaluate its ASUs' performance. The NGO may also determine the frequency of self-assessment with regard to its operational needs.

3.5 Table 15 shows the number of incidents of underperformance in Output/Outcome Standards, ESRs and SQSs reported by NGOs in self-assessments in the period 2012-13 to 2016-17. The majority of incidents of underperformance (over 97%) were related to Output/Outcome Standards.

Note 29: *In the period January 2001 to September 2017, the SWD had exercised its power to terminate the LSG subvention for one NGO in November 2007. The SWD found that the NGO had irregularities such as re-employment of the dismissed Director without a recruitment process, serious delay in the submission of financial reports and self-reporting on service performance, allowing the Director to use his personal credit card to make NGO payments by instalments while making full reimbursement to him and failing to elect members of the NGO's Executive Committee after the resignation of five members.*

Self-assessment of service quality by non-governmental organisations

Table 15

Underperformance in Output/Outcome Standards, ESRs and SQSs reported by NGOs in self-assessment (2012-13 to 2016-17)

Area of service	2012-13		2013-14		2014-15		2015-16		2016-17	
	No. of underperformance	No. of NGOs involved	No. of underperformance	No. of NGOs involved	No. of underperformance	No. of NGOs involved	No. of underperformance	No. of NGOs involved	No. of underperformance	No. of NGOs involved
Elderly services	55 (13 %)	22	49 (13 %)	23	182 (34 %)	37	133 (29 %)	49	57 (16 %)	29
Family and child welfare services	159 (39 %)	35	153 (40 %)	34	163 (30 %)	35	113 (24 %)	35	132 (37 %)	38
Rehabilitation services	149 (36 %)	32	140 (37 %)	31	159 (30 %)	32	180 (39 %)	28	127 (36 %)	28
Youth and corrections services	51 (12 %)	17	38 (10 %)	16	32 (6 %)	15	39 (8 %)	15	38 (11 %)	13
Overall (Note)	414 (100 %)	70	380 (100 %)	70	536 (100 %)	75	465 (100 %)	88	354 (100 %)	78

Source: Audit analysis of SWD records

Note: An NGO might have underperformance in more than one area of service.

Conduct and reporting of self-assessment

Need to enhance accuracy of performance reported

3.6 Audit examined the Output/Outcome Standards reported by NGOs to the SWD in the period 2014-15 to 2016-17. Audit found that in three NGOs (covering three ASUs) of the 11 NGOs (covering 23 ASUs) visited (see para. 1.31), there were cases where these Standards had not been accurately reported by NGOs, resulting in overstatement or understatement of performance reported (see Table 16). Case 3 shows an example of such cases.

Self-assessment of service quality by non-governmental organisations

Table 16

**Overstatement/understatement of
Output/Outcome Standards reported by NGOs
(2014-15 to 2016-17)**

NGO	Description of Standard	Standard agreed in FSA	Standard reported by NGO (a)	Audit recalculation of Standard (b)	Overstatement (in bold)/ (understatement) of Standard (Note 1) (c) = (a) – (b)
ASU B of NGO B	Total number of service sessions of rehabilitation training service to be provided by physiotherapists/ occupational therapists in a year	2015-16: 14,520 2016-17: 15,840	2015-16: 6,359 2016-17: 9,528	2015-16: 6,154 2016-17: 9,510	2015-16: 205 2016-17: 18
ASU C of NGO C	Rate of achieving individual training and support plan in second 6 months	2014-15: 95 %	2014-15: 90.3 %	2014-15: 90.7 %	2014-15: (0.4 %)
	Number of sessions providing staff training programmes/workshops/ seminars in a year	2014-15: 4 2015-16: 4	2014-15: 12 2015-16: 18	2014-15: 15 2015-16: 15	2014-15: (3) 2015-16: 3
	Number of sessions providing public education programmes on community rehabilitation in a year	2014-15: 7 2015-16: 7	2014-15: 8 2015-16: 7	2014-15: 12 2015-16: 8	2014-15: (4) 2015-16: (1)
	Number of sessions providing consultation services to support groups and rehabilitation units in the community in a year	2014-15: 55 2016-17: 55	2014-15: 64 2016-17: 80	2014-15: 61 2016-17: 81	2014-15: 3 2016-17: (1)
	Rate of service users being satisfied with the overall services/programmes delivered to them in a year	2014-15: 80 %	2014-15: 100 %	2014-15: 97.5 %	2014-15: 2.5%
	Rate of carers being satisfied with the overall services/programmes delivered to them in a year	2014-15: 80 %	2014-15: 97.5 %	2014-15: 100 %	2014-15: (2.5 %)
	Rate of service users having positive gain in the score of Barthel Index-100 (Note 2)	2016-17: 70 %	2016-17: 94.1 %	2016-17: 71.4 %	2016-17: 22.7%
	Rate of service users having positive gain in the score of Lawton (Note 2)	2016-17: 70 %	2016-17: 100 %	2016-17: 63.6 %	2016-17: 36.4%

Self-assessment of service quality by non-governmental organisations

Table 16 (Cont'd)

NGO	Description of Standard	Standard agreed in FSA	Standard reported by NGO (a)	Audit recalculation of Standard (b)	Overstatement (in bold)/ (understatement) of Standard (Note 1) (c) = (a) – (b)
ASU J of NGO F	Total number of core programme sessions	2014-15: 700 2015-16: 700 2016-17: 700	2014-15: 1,815.5 2015-16: 1,685.0 2016-17: 1,532.5	2014-15: 1,755 2015-16: 1,400 2016-17: 1,397	2014-15: 60.5 2015-16: 285 2016-17: 135.5
	Total attendance at the core programme sessions	2014-15: 9,660 2015-16: 9,660	2014-15: 26,304 2015-16: 15,809	2014-15: 20,761 2015-16: 15,079	2014-15: 5,543 2015-16: 730

Source: Audit analysis of NGO records

Note 1: The reasons for overstatement/understatement of Output/Outcome Standards reported by NGOs included double counting of the number of programme sessions, and the use of incorrect measurement method by the NGO (see Case 3 in para. 3.6).

Note 2: Barthel Index-100 and Lawton are clinical assessment tools used to assess a person's performance in activities of daily living. The related Outcome Standards are proposed by the NGO concerned and not applicable to other NGOs.

Case 3

**Reporting of Output/Outcome Standards by an NGO
(2014-15 to 2016-17)**

1. In March 2017, the SWD made arrangement for Audit's visit to NGO C. In early May 2017, NGO C made revisions to its service statistics previously submitted for the period 2014-15 to 2016-17 after internal checking. Subsequently, when Audit went to visit the NGO in May 2017, the NGO had revised the reported Output/Outcome Standards for the period 2014-15 to 2016-17 as follows:

Year	Total number of reported Output Standards	Revised number of Output Standards	Total number of reported Outcome Standards	Revised number of Outcome Standards
2014-15	10	4	9	4
2015-16	10	4	9	4
2016-17	10	1	9	Nil

2. Audit noted that after the revision, the following Output/Outcome Standards, which were reported to have been met in the financial years 2014-15 and 2015-16, had become unmet:

Year	Description of Output/ Outcome Standard	Standard agreed in FSA	Reported by NGO	
			Before revision	After revision
2014-15	Rate of achieving individual training and support plan in second 6 months	95.0%	95.3%	90.3%
	Rate of service users having positive gain in the score of Lawton	70.0%	75.0%	60.0%
2015-16	Rate of achieving individual training and support plan in first 6 months	95.0%	95.6%	94.5%
	Rate of achieving individual training and support plan in second 6 months	95.0%	95.1%	93.7%

Case 3 (Cont'd)

3. Furthermore, for 2016-17, while the revised figures indicated that two of the Outcome Standards had been met, Audit's recalculation indicated that one of them had in fact not been met, as follows:

Description of Outcome Standard	Standard agreed in FSA	Standard reported by NGO after revision	Audit recalculation of Standard	Overstatement
Rate of service users having positive gain in the score of Barthel Index-100	70%	94.1%	71.4%	22.7%
Rate of service users having positive gain in the score of Lawton	70%	100%	63.6%	36.4%

4. In May 2017, the SWD explained to Audit that the mistake in calculating the rate of service users having positive gain in the scores of Barthel Index and Lawton might have been caused by a misunderstanding on the part of the NGO as the definition of the related Outcome Standards (see paras. 2 and 3) had been revised in the new FSA with the NGO in March 2017 for the period from 1 March 2017 to 29 February 2020. Given the increasing frailty level of the service users, achievement of the Outcome Standards have been revised to include not only service users having positive gain in physical abilities, but also service users who are only able to maintain such abilities. As the new FSA came into effect only from March 2017, the NGO was notified by the SWD in the same month that it should either adopt the old definition of Outcome Standards in preparing the full-year statistics of 2016-17 (i.e. from April 2016 to March 2017) or withhold the statistics of the last quarter of 2016-17 (i.e. from January to March 2017) in preparing the full-year statistics. The NGO reported a full-year statistics of 2016-17 but had mistakenly used the new definition of Outcome Standards in calculating the statistics, thereby leading to the error in reporting the Outcome Standards.

Case 3 (Cont'd)

Audit comments

5. According to the LSG Manual, it is the responsibility of NGOs' boards and management to maintain proper control of the LSG and ensure that the use of the LSG subvention meets the requirements and objectives set in the FSAs. According to the manual of the Service Performance Monitoring System (see Note 9 in para. 1.22(c)(iv)), NGOs are responsible for close monitoring of their Output/Outcome Standards so that they can make early detection and improvement in cases of unsatisfactory performance. The SWD needs to remind NGOs of the importance of accurate reporting of their Output/Outcome Standards. The SWD also needs to remind them of the need to exercise due care in computing the Standards.

Source: Audit analysis of NGO C records

Need to improve measurement of service effectiveness

3.7 According to the SWD, NGOs' assessments of the achievement of Outcome Standards are conducted through the use of methodologies such as user satisfaction surveys or evaluation between "pre-test" and "post-test" performance (e.g. the physical abilities of a service user before and after joining a service). It is important that NGOs properly conduct self-assessment to indicate the effectiveness of their services. Audit reviewed the self-assessment of service performance by two NGOs (Note 30) and found that there was room for improvement as shown in Case 4.

Note 30: Only 7 NGOs (covering 7 ASUs) of the 11 NGOs (covering 23 ASUs) visited by Audit had Outcome Standards (see separate audit findings in paras. 4.26 to 4.28). Audit examined the Outcome Standards of 2 of the 7 NGOs.

Case 4

**Measuring service effectiveness by two NGOs
(2014-15 to 2016-17)**

1. The two NGOs (NGOs C and D) evaluated the effectiveness of the rehabilitation training services provided by their day centres by measuring the rate of achieving the clinical outcomes defined in individual training plans of service users. Clinical outcomes included those measuring the service users' physical functioning, self-learnt skills and abilities in self-care activities and daily living. Clinical assessment of outcomes was conducted by physiotherapists or occupational therapists of the NGOs. According to the FSAs, the effectiveness of the services should be measured upon completion of training of service users.
2. For each of the two NGOs, Audit examined 30 cases of service users that had completed their rehabilitation training in the period 2014-15 to 2016-17 and found that:
 - (a) for NGO C, all clinical assessments were performed on site by physiotherapists or occupational therapists. On the other hand, for NGO D, of the 30 cases examined, the clinical assessments of 14 cases were conducted via telephone only; and
 - (b) for NGO C, service users that had attended all their planned training sessions were regarded as having training completed. NGO D, on the other hand, regarded training as having completed when service users had completed 10% or more of the planned training sessions.

Audit comments

3. Audit considers that the SWD needs to provide more guidelines to NGOs to facilitate and enhance their conduct of measurement of service effectiveness.

Source: Audit analysis of NGOs C and D records

Audit recommendations

- 3.8 **Audit has *recommended* that the Director of Social Welfare should:**
- (a) **remind NGOs of the importance of accurate reporting of their Output/Outcome Standards and of the need to exercise due care in computing the Standards;**
 - (b) **provide more guidelines to NGOs to facilitate and enhance their conduct of measurement of Outcome Standards; and**
 - (c) **in conducting review visits to NGOs (see para. 4.40(a)), identify and disseminate NGOs' good practices in the conduct of their self-assessment of the achievement of Outcome Standards.**

Response from the Government

3.9 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) it is the SWD's existing practice to advise NGO heads by way of management letters to critically examine their self-reporting mechanisms and take appropriate actions to ensure that due and accurate reporting is made when inaccurate self-assessment on Output/Outcome Standards is detected by the SWD during a review of their annual self-assessment reports;
- (b) it is also the existing practice that the SWD will advise NGOs to review their quality checking mechanisms whenever there are wrong calculations spotted in the statistics returns on Output/Outcome Standards during service performance visits;
- (c) the SWD will draw up guidelines for NGOs to enhance their conduct of measurement of Outcome Standards where necessary; and

- (d) the SWD will disseminate through appropriate means (such as meetings with service operators and uploading information onto the SWD's website) the NGOs' good practices in the conduct of their self-assessment of the achievement of Outcome Standards.

Implementation of Service Quality Standards

3.10 SQSs (see para. 1.18(c) and Appendix B) inform service users what can be expected of the ASUs in providing welfare services. According to the SWD, as SQSs provide a broad overview of what the ASUs should do in order to deliver quality services, NGOs are expected to tailor-make their own SQS manuals to facilitate the attainment of SQSs.

Need to enhance NGOs' compliance with SQSs as promulgated in their own manuals

3.11 Audit visited 18 ASUs of the 149 ASUs in 6 NGOs (see para. 1.31(b)) and found that there were cases of NGOs not complying with the SQSs as promulgated in their manuals. Details of the non-compliance are shown in Table 17. Table 18 also shows examples of such non-compliance.

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Table 17

NGOs' non-compliance with SQSs promulgated in their manuals

SQS	NGO F			NGO G		NGO H	NGO I	NGO J	NGO K
	ASU F to I	ASU J (Note)	ASU K (Note)	ASU L to N	ASU O	ASU P to R	ASU S and T	ASU U and V	ASU W
SQS 1			×						×
SQS 2		×		×		×			
SQS 3		×	×		×		×		
SQS 4		×	×						
SQS 5	×	×	×						
SQS 7	×	×	×			×			×
SQS 9	×	×	×	×	×	×	×	×	×
SQS 10				×			×		×
SQS 11				×					
SQS 13	×	×	×	×		×			
SQS 14	×	×	×						
SQS 15								×	

Source: Audit visits to NGOs

Note: ASUs J and K are located in the same premises.

Remarks: Each “×” denotes one case of non-compliance.

Self-assessment of service quality by non-governmental organisations

Table 18

Examples of NGO's non-compliance with SQSs promulgated in their own manuals

SQS	Requirement laid down in NGO's SQS manual/non-compliance (in italic)
SQS 1: Service information The service unit ensures that a clear description of its purpose, objectives and mode of service delivery is publicly available.	The ASU should provide and distribute updated service information to the public. The information includes service objective, application requirements and entry and exit procedures for the services. <i>Information on service exit procedures was not available to the public.</i>
SQS 2 Review and update policies and procedures The service unit should review and update the documented policies and procedures, describing how it will approach key service delivery issues.	The ASU should review and update its policies and procedures on a regular basis, ranging from one to three years. <i>7 of 16 requirements contained in the SQS manual had not been reviewed in years 2007 to 2015 (i.e. 9 years).</i>
SQS 3 Records The service unit maintains accurate and current records of service operations and activities.	The ASU should keep accurate and updated record on service operation and activities. <i>There was overstatement of Output Standards by an ASU for years 2014-15 to 2016-17.</i>
SQS 4 Roles and responsibilities The roles and responsibilities of all staff, managers, the Management Committee and/or the Board or other decision-making bodies should be clearly defined.	The ASU should display the organisation chart and areas of responsibilities of each division in the ASU's office. <i>An organisation chart and areas of responsibilities of each division of an ASU were not displayed in the ASU's office as required.</i>
SQS 5 Human resources The agency/service unit implements effective staff recruitment, contracting, development, training, assessment, deployment and disciplinary practices.	If the staff's application for reimbursement of course fee is approved, the amount of reimbursement would be decided by the Service Manager and the maximum amount is two-thirds of the course fee. <i>Each staff was entitled to a maximum amount of reimbursement of \$500 a year. For a course fee not exceeding \$500, the staff could receive 100% reimbursement while the maximum amount of reimbursement allowed was two-thirds of the course fee.</i>
SQS 7 Financial management The service unit implements policies and procedures to ensure effective financial management.	Assets over \$1,000 and all computer or computer-related products should be registered in the fixed asset register. <i>Two fixed asset items, which cost less than \$1,000 (\$910 and \$998), were included in the fixed asset register. On the other hand, there were six computer/computer-related items not included in the fixed asset register.</i>

Self-assessment of service quality by non-governmental organisations

Table 18 (Cont'd)

SQS	Requirement laid down in NGO's SQS manual/non-compliance (in italic)
SQS 9 Safe physical environment The service unit takes all reasonable steps to ensure that it provides a safe physical environment for its staff and service users.	Fire drill should be conducted at least once a year. <i>No fire drill was conducted in 2016.</i>
SQS 10 Entry and exit The service unit ensures that service users have clear and accurate information about how to enter and leave the service.	Temporary leave of service users from a residential home for more than 7 days should be approved by the Superintendent. <i>In the period December 2016 to May 2017, two service users left the residential home for more than 7 days (ranging from 9 to 30 days). The Superintendent's approval had not been sought for any of these cases.</i>
SQS 11 Needs of service users The service unit has a planned approach to assessing and meeting service users' needs (whether the service user is an individual, family, group or community).	For admission of new entrants, the ASU is required to conduct home visits to assess service users' needs. <i>The ASU had not done so.</i>
SQS 13 Private property The service unit respects the service users' rights in relation to private property.	The ASU should inform the service users that any lost items found would be handled according to the procedure of found property. <i>The notice relating to procedures for claiming lost property was displayed in an ASU of the NGO but was not displayed in another two ASUs of the same NGO.</i>
SQS 14 Privacy and confidentiality The service unit respects the service users' rights for privacy and confidentiality.	The ASU should display a notice informing service users and visitors the arrangement of the CCTV surveillance, such as its purpose and the period of retaining the recorded CCTV video. <i>The ASU only displayed a notice indicating that the CCTV was in operation. The details of the arrangement of the CCTV surveillance were not displayed at public areas.</i>
SQS 15 Complaints Each service user/staff member is free to raise and have addressed, without fear of retribution, any complaints he or she may have regarding the agency or the service unit.	The ASU should respond to a complaint within 15 days from the date of receipt of a complaint. <i>The ASU failed to do so.</i>

Source: Audit visits to NGOs

Need to make use of self-assessment checklist

3.12 As mentioned in paragraph 3.11, Audit found that there were cases of non-compliance with the NGOs' SQS manuals. To facilitate NGOs to conduct self-assessment on SQSs, the SWD has developed a self-assessment checklist for use by NGOs. This checklist helps NGOs ensure that in carrying out self-assessments, all the 16 SQSs are covered and properly handled with remedial action taken if warranted. Audit examined the use of the checklist by the 18 ASUs (see para. 3.11) in 2016-17 and found that:

- (a) 11 ASUs had not used the checklist to assist their conduct of self-assessment on SQSs; and
- (b) 7 ASUs had used the checklist. In one case, however, the ASU's completed checklist indicated that the ASU made available its annual reports and service pamphlets at the ASU's office in audio and Braille formats to facilitate the provision of NGO information to the service users. During Audit's visit to the ASU, audio and Braille formats of the documents could not be located in the ASU's office.

Audit recommendations

3.13 **Audit has recommended that the Director of Social Welfare should:**

- (a) **urge NGOs to take measures to ensure that their ASUs observe the requirements laid down in their own SQS manuals in the implementation of SQSs;**
- (b) **encourage NGOs to make use of the self-assessment checklist, which is available on the SWD's website, in conducting self-assessment on SQSs; and**
- (c) **remind NGOs to exercise due care in completing the self-assessment checklist (see para. 3.12).**

Response from the Government

3.14 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) it has been stipulated in individual signed FSAs that they are obliged to meet the requirements of 16 SQSs;
- (b) it is the SWD's existing practice to issue management letters to all NGOs every year requiring them to submit self-assessment reports on their individual ASUs' compliance with ESRs, SQSs, Output/Outcome Standards; and
- (c) the SWD will remind NGOs to exercise due care in conducting annual self-assessment on compliance with SQSs and make use of the self-assessment checklist through the management letters annually.

Conduct of internal service inspections

3.15 Audit noted that of the 6 NGOs visited (see para. 1.31(b)), 4 had conducted internal service inspections on their own initiative to ensure the quality of services provided. The internal service inspections were carried out in the following manner:

- (a) the NGOs appointed designated staff or set up inspection teams to conduct the inspections; and
- (b) in conducting the inspections, the designated staff or inspection teams reviewed the NGOs' SQS manuals (see para. 3.10) and examined ASUs' compliance with the requirements of the SQSs as promulgated in their own manuals.

Room for improvement in internal service inspections

3.16 Audit appreciates the 4 NGOs' (i.e. NGOs F, G, J and K) initiative of conducting internal service inspections, but noted areas for further improvement in the conduct of such inspections, as follows:

- (a) ***Inspection programmes.*** Of the 4 NGOs, 2 had laid down programmes for inspections. For the other 2 NGOs, there were no programmes or timetables for inspecting the NGO's various ASUs. These other 2 NGO's inspection teams only conducted ad hoc inspections;
- (b) ***Surprise inspections.*** None of the 4 NGOs conducted inspections on a surprise basis. ASUs were informed of the inspections in advance; and
- (c) ***Following up non-compliance cases.*** None of the 4 NGOs had established procedures for following up cases of non-compliance identified during inspections. Furthermore, of the 4 NGOs, 2 had not taken any follow-up actions.

Audit recommendation

3.17 **Audit has *recommended* that the Director of Social Welfare should encourage NGOs to put in place an internal service inspection mechanism, having regard to the need for laying down inspection programmes, conducting surprise inspection, and following up non-compliance cases.**

Response from the Government

3.18 The Director of Social Welfare agrees with the audit recommendation. She has said that conduct of internal service inspections is not a requirement under the Service Performance Monitoring System. The SWD will, however, encourage NGOs, having regard to their own circumstances, to put in place an internal service inspection mechanism with a view to enhancing their internal controls and monitoring of service performance.

PART 4: MONITORING OF SERVICE DELIVERY BY SOCIAL WELFARE DEPARTMENT

4.1 This PART examines matters relating to the monitoring of service delivery by the SWD, focusing on the following issues:

- (a) underperformance of NGOs (paras. 4.2 to 4.5);
- (b) subventions to NGOs based on caseloads attained (paras. 4.6 to 4.25);
- (c) setting of NGOs' performance standards (paras. 4.26 to 4.29);
- (d) use of service resources by NGOs (paras. 4.30 to 4.33);
- (e) renewal of FSAs (paras. 4.34 to 4.38); and
- (f) performance visits and conduct of annual performance review (paras. 4.39 to 4.49).

Underperformance of non-governmental organisations

4.2 According to the LSG Manual, to continuously improve service quality, if an ASU of an NGO is found non-conforming with the required performance standards (e.g. Output/Outcome Standards), the NGO is required to submit to the SWD an action plan detailing how the service is to be improved. An action plan specifies:

- (a) the reasons for not achieving the performance standards;
- (b) the actions taken or to be taken to meet the agreed level of performance standards as stipulated in the FSA; and
- (c) the planned timeframe for completion of the actions proposed.

If the NGO fails to improve after repeated efforts, the ultimate sanction will be for the SWD to withdraw its LSG subvention for the ASU in question.

Persistent underperformance despite actions taken

4.3 Audit examined 20 ASUs that had underperformance in Output/Outcome Standards (Note 31) in three or more consecutive years in the five-year period 2012-13 to 2016-17. Audit found that although the NGOs concerned had submitted action plans to improve their services in each of the consecutive years, the underperformance persisted. Audit further noted that in the five-year period, excluding the 6 ASUs receiving subventions based on caseloads attained (see paras. 4.6 and 4.10), all the other 14 ASUs had received full LSG subventions. Case 5 shows an example of the persistent underperformance of an ASU which is not subject to caseloads attained or other specific conditions.

Note 31: *The 20 ASUs (of 14 NGOs) were selected from the self-assessment reports submitted by the 165 NGOs receiving LSG subventions in the period 2012-13 to 2016-17.*

Monitoring of service delivery by Social Welfare Department

Case 5

Persistent underperformance of an ASU (2012-13 to 2016-17)

1. Since 1986, ASU 12 of NGO 14 has provided inter-country adoption services to children who need adoption placement and a suitable local home cannot be found. These children are mostly wards of the Director of Social Welfare (Note 1) with special needs due to mental or physical disabilities, health problems, older age or complex family backgrounds.

2. In the five-year period 2012-13 to 2016-17, of the five Output Standards as stipulated in the FSA, underperformance was noted in four Output Standards in all the five years:

Output Standard	Agreed level of performance	Performance achieved				
		2012-13	2013-14	2014-15	2015-16	2016-17
Number of home studies completed in a year	20	12 -40%	10 -50%	5 -75%	3 -85%	3 -85%
Number of wards of the Director of Social Welfare (Note 1) placed overseas in a year	15	8 -47%	9 -40%	9 -40%	5 -67%	2 -87%
Number of children placed for overseas adoption by relatives in a year	2	0 -100%	0 -100%	0 -100%	0 -100%	0 -100%
Number of local adoption cases requiring assistance in seeking consent from parents staying outside Hong Kong or seeking overseas home approval completed in a year	18	15 -17%	14 -22%	12 -33%	13 -28%	14 -22%
Number of cases requiring assistance in tracing background information or re-establishing contacts completed in a year	10	22 220%	11 110%	21 210%	15 150%	22 220%

Case 5 (Cont'd)

3. Over the five-year period, the NGO had taken actions to improve the ASU's performance. These actions included, for example, advocating the adoption needs of children and soliciting overseas partner NGOs' help in seeking adoption by circulating updated lists of children on the adoption waiting list. Despite the actions taken, underperformance persisted.

4. Audit further noted that the ASU's persistent underperformance had in fact existed before 2012-13, and that the SWD had taken the following actions to address the underperformance in the years 2012 to 2017:

- (a) in mid-2012, the SWD considered deploying the existing subvention to the ASU for the NGO's other operating services, for example, the cross-boundary and inter-country casework service (Note 2). However, the idea was later dropped as the SWD had no further plans to expand such service in the near future;
- (b) in September 2012, the SWD discussed with the ASU the need to review the FSA and the possibility of reduction of the ASU's resources as an option. In response, the NGO counter-proposed to specialise the ASU's service in placing older and "hard to place" children. Since there was no new idea in the NGO's counter-proposal, it was not taken on board. Discussion on the matter was subsequently postponed;
- (c) in June 2014, the SWD resumed the review of the FSA with the ASU and proposed deletion of two Output Standards. In July 2014, the ASU counter-proposed to keep the two Output Standards with downward adjustment to their output levels (see the first two Output Standards in the Table above and para. (d) shown below). Revamping or adjusting the remaining Output Standards was also suggested. The SWD further reviewed the counter-proposal of the ASU. According to the SWD, having regard to the expressed interest of relevant bodies from overseas countries in the inter-country adoption programme in Hong Kong, the SWD saw the need to continue to use ASU 12 to establish overseas adoption partners to strengthen the inter-country adoption programme and enhance the adoption prospect of children in need of adoption placements. In the period 2012-13 to 2016-17, the following full LSG subventions had been provided to the ASU; and

Monitoring of service delivery by Social Welfare Department

Case 5 (Cont'd)

	2012-13	2013-14	2014-15	2015-16	2016-17
LSG subvention (\$ million)	1.98	2.10	2.16	2.26	2.39

(d) in April 2017, after further discussion between the SWD and the ASU, a revised FSA was drawn up and was implemented from 1 July 2017 onwards. Under the revised FSA, the level of achievement had been adjusted for some Output Standards. For example:

- (i) the “number of home studies completed in a year” has been adjusted from 20 to 10; and
- (ii) the “number of wards of the Director of Social Welfare placed overseas in a year” of 15 and the “number of children placed for overseas adoption by relatives in a year” of 2 have been combined and adjusted to 7.

Furthermore, four new Output Standards had been added to the revised FSA. For example:

- (i) the “number of overseas adoption agencies or central authorities with which direct partnership for inter-country adoption established in a year”; and
- (ii) the “number of visits/briefings arranged for overseas officials and non-officials to share the inter-country adoption programme of the Hong Kong Special Administrative Region in a year”.

According to the SWD, these new Output Standards are targeted to expand the network of the adoption partners overseas with a view to increasing the prospect of identifying more suitable adoptive homes overseas and hence the adoption chances of children in need. As the newly added outputs may compensate for the adjustments made to other Output Standards, the amount of subvention to the ASU had remained unchanged.

Case 5 (Cont'd)

5. In September 2017, the SWD also informed Audit that:
- (a) NGO 14 has been providing subvented inter-country adoption service in Hong Kong for a long time. According to the SWD, with the Adoption Ordinance (Cap. 290) as amended in 2004 having been implemented since 2006, an accreditation system has been put in place to allow NGOs duly accredited by the Director of Social Welfare to provide inter-country adoption service in Hong Kong. Under the accreditation system, NGO 14, together with two other NGOs (operated on a self-financing basis), have been accredited to make arrangements for the adoption of infants and proceed with their placement for inter-country adoption. In recent years, the total number of children available for adoption and the number of inter-country adoption applications involving relatives have been fluctuating. All these have contributed to the ASU not meeting some Output Standards of the FSA in the past years; and
 - (b) the revised FSA with new Output Standards and adjustments made to some existing Output Standards will better reflect the requirements expected of the ASU in inter-country adoption service taking into account the changing environment. It is necessary to maintain the subvented inter-country adoption programme to ensure stability and continuity of the service, with continuous review and close monitoring of the ASU's performance vis-à-vis the revised FSA.

Source: Audit analysis of SWD records

Note 1: Wards of the Director of Social Welfare are children/juveniles in respect of whom the Director of Social Welfare has been appointed as their legal guardian under section 34(1)(a) of the Protection of Children and Juveniles Ordinance (Cap. 213).

Note 2: The cross-boundary and inter-country casework service helped families handle and solve problems arising from geographical separations.

Audit recommendations

- 4.4 **Audit has *recommended* that the Director of Social Welfare should:**
- (a) **closely monitor those ASUs of NGOs which have had persistent underperformance (say, underperformance in a number of consecutive years) in the provision of services;**
 - (b) **in cases where full subventions are paid to the ASUs with persistent underperformance, critically review whether the payments are fully justified; and**
 - (c) **instigate timely action, where warranted, to tackle cases of persistent underperformance of ASUs in accordance with provisions in the LSG Manual.**

Response from the Government

4.5 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD has recently set up the Service Performance Monitoring Committee to monitor services with persistent underperformance and deliberate appropriate follow-up measures.

Subventions to non-governmental organisations based on caseloads attained

4.6 Under the four areas of welfare services, there are some 140 types of services (e.g. the elderly services consist of services such as day care centres for the elderly, integrated home care services, etc.) (see para. 1.3). Of these 140 types of services, for the following 2 services, LSG subventions are provided to NGOs based on caseloads attained (see para. 4.7) (Note 32):

Note 32: *For the other types of services, full year subventions (payable on a monthly basis) are provided to NGOs without subjecting to caseloads attained or other specific conditions.*

- (a) ***Home care service for persons with severe disabilities*** (hereinafter referred to as HCS). The HCS aims at strengthening support for persons with severe disabilities and relieving the stress of family members/carers through the provision of a package of home-based support services meeting the personal care, training and nursing care needs of persons with severe disabilities to facilitate their integration into the community. The target service users are persons with severe intellectual/physical disabilities who are on the waiting list for subvented residential care services (e.g. Hostel for Severely Physically Handicapped Persons, Hostel for Severely Mentally Handicapped Persons and Care and Attention Home for Severely Disabled Persons), persons with severe intellectual and/or physical disabilities assessed to be eligible for the HCS in accordance with the assessment tool of the SWD, students attending special schools for children with severe intellectual and/or physical disabilities and family members/carers of the service users; and

- (b) ***Integrated support service for persons with severe physical disabilities*** (hereinafter referred to as ISS). The ISS aims at strengthening support for persons with severe physical disabilities and relieving the stress of family members/carers through formulation of well-coordinated care plans at both stages of pre-discharge and post-discharge from hospitals and the provision of a package of home-based support services meeting their personal care, training and nursing care needs to facilitate their integration into the community. The target service users are persons with severe physical disabilities requiring respiratory support medical equipment and constant attendance, or persons with tetraplegia (paralysis of all four limbs).

4.7 Since the introduction of the HCS and the ISS, there have been six ASUs (of six NGOs) providing the HCS and two ASUs (of two NGOs that also provide the HCS) providing the ISS. The HCS and the ISS were introduced in March 2014 (Note 33) and November 2014 respectively. For the HCS, full year subventions (payable on a monthly basis) were provided to the NGOs at the start of the service in March 2014. For the ISS, having regard to the experience of the HCS which showed a gradual process of intake of service users upon service roll-out, only two-thirds of full year subventions (payable on a monthly basis) were provided to the NGOs during the first nine-month period from November 2014 to July 2015. In view of the

Note 33: *The HCS operated on a pilot scheme in the period March 2011 to February 2014.*

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unexpected low utilisation rates of the HCS and the ISS and in order to optimise the use of public money, the subvention arrangements for the HCS and the ISS have been reviewed and revised by the SWD since April 2015 and August 2015 respectively. Under the revised arrangements, annual subventions (payable on a monthly basis) to the NGOs are pegged to the number of users served, as follows:

- (a) for the HCS, an ASU is required to attain an agreed level of caseload which is defined as the “total number of cases provided with social work intervention including counselling and support service to the service users and their family members/carers”. The ASU will receive:
 - (i) 100% of the subvention when it attained 75% or above of the agreed number of cases;
 - (ii) 75% of the subvention when it attained 50% or above but less than 75% of the agreed number of cases; and
 - (iii) 50% of the subvention when it attained less than 50% of the agreed number of cases; and
- (b) for the ISS, an ASU is required to attain an agreed level of caseload which is defined as the “total number of cases provided with case management service including counselling and support service to the family members/carers”. The ASU will receive:
 - (i) 100% of the subvention when it attained two-thirds of the agreed number of cases; and
 - (ii) two-thirds of the subvention when it attained less than two-thirds of the agreed number of cases.

4.8 According to the SWD:

- (a) calculation of subvention for an ASU in a new financial year is based on the number of active users being handled by the ASU as at 31 March of the last financial year. The number of active users comprises existing and new users served minus the number of users discharged in the last financial year (Note 34). Furthermore, within the new financial year, when an ASU attains a higher number of users served (through admission of new users) and that number entitles the ASU to a higher amount of subvention (see para. 4.7(a) and (b)), the ASU needs to inform the SWD so that the latter will adjust upwards the amount of subvention with effect from the respective date that the ASU reaches the higher number of users served; and
- (b) within the new financial year, while the SWD will adjust upwards the amount the subvention when an ASU attains a higher number of users served, the SWD will not make downward adjustment of subvention by taking into account the number of users discharged by the ASU during the year. This is because:
 - (i) actual services have been delivered by the ASU within the year for users who were subsequently discharged and therefore the subvention provided should reflect the ASU's inputs for these discharged users; and
 - (ii) the subvention principle mentioned in (i) above is based on the assumption that as users of the HCS and the ISS normally have long-term care needs, the discharge rates of these two services would be relatively low.

In September 2017, the SWD further informed Audit that downward adjustment of subvention during the year may trigger staff cutting which may in turn affect the service provision of an ASU, and that adjusting subventions frequently may increase administrative burden. The SWD will

Note 34: *The ASUs providing the HCS or the ISS are required to report to the SWD on a quarterly basis (broken down into individual months), among other information, the number of users served and the number of users discharged in the quarterly statistical reports (see para. 3.2(a)).*

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therefore only take into account the number of users discharged when it calculates the subvention to the ASU in a new financial year based on the number of active users as at 31 March of the last financial year (see (a) above).

4.9 Tables 19 and 20 show the number of users (i.e. existing and new users) served as reported by the six HCS ASUs and the two ISS ASUs respectively to the SWD in the period 2015-16 to 2016-17. In this period, after the eight ASUs had served more than 75% or two-thirds of users, they all received 100% subventions (see para. 4.7(a) and (b)) from the SWD. In 2016-17, the total subventions received by them amounted to some \$275 million (ranging from each receiving some \$23 million to some \$44 million).

Table 19

**Number of users served by HCS ASUs
(2015-16 and 2016-17)**

	ASU	2015-16		2016-17	
		No. of users served		No. of users served	
		Agreed	Actual	Agreed	Actual
Total number of cases provided with social work intervention including counselling and support service to the service users and their family members/carers (see para. 4.7(a))	ASU A	499	571	630	742
	ASU B	458	504	500	668
	ASU 13	500	478	500	595
	ASU 14	406	415	500	549
	ASU 15	469	544	625	788
	ASU 16	406	430	500	587

Source: SWD records

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Table 20

**Number of users served by ISS ASUs
(2015-16 and 2016-17)**

	ASU	2015-16		2016-17	
		No. of users served		No. of users served	
		Agreed	Actual	Agreed	Actual
Total number of cases provided with case management service including counselling and support service to the family members/carers (see para. 4.7(b))	ASU E	422	376	449	482
	ASU 17	425	345	450	500

Source: SWD records

Need to review underperformance in provision of HCS and ISS

4.10 As mentioned in paragraph 4.9, all the eight ASUs providing the HCS or the ISS, after meeting the caseload requirements, received full subventions from the SWD in 2015-16 and 2016-17. Audit, however, noted that other than attaining the required caseloads, the ASUs had significant underperformance in the provision of the HCS and the ISS (see Tables 21 and 22).

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Table 21

**Performance in provision of HCS
(2015-16 and 2016-17)**

Output Standard	ASU	2015-16		2016-17	
		Agreed level of performance (No.)	Performance achieved (No.)	Agreed level of performance (No.)	Performance achieved (No.)
Total number of service hours to meet the care needs of service users in a year	ASU A	125,400	25,407	158,400	34,201
	ASU B	116,160	6,972	126,720	12,350
	ASU 13	126,720	43,358	126,720	51,265
	ASU 14	102,960	24,000	126,720	28,896
	ASU 15	118,800	34,336	158,400	49,937
	ASU 16	108,108	19,053	133,056	38,856
Total number of service sessions of rehabilitation training service provided by physiotherapists/occupational therapists in a year	ASU A	15,675	5,200	19,800	6,667
	ASU B	14,520	6,359	15,840	9,528
	ASU 13	15,840	2,543	15,840	6,615
	ASU 14	12,870	4,471	15,840	6,760
	ASU 15	14,850	8,040	19,800	12,586
	ASU 16	13,514	3,074	16,632	6,370
Total number of service sessions of nursing care service provided by nurse/health care staff in a year	ASU A	10,450	1,163	13,200	1,190
	ASU B	9,680	2,033	10,560	4,553
	ASU 13	10,560	4,158	10,560	4,016
	ASU 14	8,580	2,885	10,560	4,004
	ASU 15	9,900	3,124	13,200	3,781
	ASU 16	9,009	1,053	11,088	6,552

Source: SWD records

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Table 22

Performance in provision of ISS (2015-16 and 2016-17)

Output Standard	ASU	2015-16		2016-17	
		Agreed level of performance (No.)	Performance achieved (No.)	Agreed level of performance (No.)	Performance achieved (No.)
Total number of service hours of personal care and support, home making, home respite and escort service in a year	ASU E	38,173	4,379	40,559	15,668
	ASU 17	38,628	13,462	40,900	23,728
Total number of sessions of rehabilitation training service to be provided by physiotherapists/occupational therapists in a year	ASU E	11,760	2,768	12,495	6,088
	ASU 17	11,900	4,923	12,600	9,221
Total number of sessions for training therapy assistants/care workers to be provided by physiotherapists/occupational therapists in a year	ASU E	2,809	1,287	2,985	2,292
	ASU 17	2,985	860	3,160	1,856
Total number of service sessions to be provided by nurse/health care staff in a year	ASU E	9,240	1,410	9,818	8,969
	ASU 17	9,350	4,348	9,900	8,634

Source: SWD records

4.11 Audit considers that the SWD needs to ascertain the reasons for the significant underperformance in the provision of the HCS and the ISS and determine the way forward for the two services.

Other room for improvement in provision of subventions based on caseloads attained

4.12 Audit visited two HCS ASUs (ASU A and ASU B) and one ISS ASU (ASU E) during March to May 2017. For each of the ASUs visited, Audit examined 50 cases of users (150 in total), covering the period from April 2015 to December 2016 (Note 35), to ascertain the adequacy of using caseloads attained by the ASUs as the determinant in calculating the provision of subventions. Audit's examination revealed room for improvement as shown in paragraphs 4.13 to 4.24.

4.13 ***Different determining factors used in computing caseloads.*** As mentioned in paragraph 4.7, subventions to the NGOs are pegged to the number of users served (i.e. caseloads). In visiting the three ASUs (see para. 4.12), Audit noted that different factors were used in computing caseloads by the ASUs. ASU B would include a case in the caseload reportable to the SWD when a person was admitted as a service user after assessing his/her eligibility for the service. On the other hand, ASU A and ASU E would include a case when a care plan had been formulated for the service user after admission. Audit considers that the SWD needs to provide guidelines to the ASUs offering the HCS and the ISS to help them count cases into the caseloads so as to ensure that the caseloads reported to the SWD are proper. In September 2017, the SWD informed Audit that ASUs had different understanding on the points of time for counting the cases into their caseloads and that it would follow up with the ASUs to align their understanding and practices.

4.14 ***Cases with no support services provided.*** Audit's examination of the case files of service users of the three ASUs revealed that there were cases where no support services had been provided to the users. Support services refer to

Note 35: *The HCS and the ISS have been subjected to revised subvention arrangements since April 2015 and August 2015 respectively (see para. 4.7). Under the revised arrangements, in calculating the amounts of subventions for the ASUs providing the ISS, the SWD also took into account the number of users served for the period from April to July 2015 (instead of from August 2015). Accordingly, Audit's examination of cases of users started from April 2015.*

rehabilitation, nursing and/or personal care services. For example, it was stated in a service user's care plan that support services such as nursing care, personal care, rehabilitation training and home respite service would be provided to the user. There was, however, no indication in the service user's case file that such services had been provided. Audit examined 50 cases in each of three ASUs and found that of the 50 cases (see para. 4.12) of:

- (a) ASU A, 13 (26 %) had no support services provided; and
- (b) ASU B, 11 (22 %) had no support services provided.

4.15 Audit's further examination of the case files of service users of ASU A also revealed that in the period 2014-15 to 2016-17, the proportion of service users who had not been provided with support services had been on the increase (see Table 23).

Table 23

**Service users of ASU A not provided with support services
(2014-15 to 2016-17)**

Year	Caseload (Note 1)	No. of service users not provided with support services
2014-15 (Note 2)	190	11 (6%)
2015-16 (Note 2)	571	59 (10%)
2016-17 (up to December 2016)	660	91 (14%)

Source: Audit analysis of NGO A records

Note 1: The caseload is the cumulative caseload after excluding service users discharged on or before 31 March 2015 (i.e. before the introduction of the revised subvention arrangements — see para. 4.7).

Note 2: In 2014-15, ASU A received full year subvention. It has been subjected to the revised subvention arrangement since April 2015 (see para. 4.7).

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4.16 In September 2017, the SWD informed Audit that in addition to support services, case management and counselling are also key components of the HCS and the ISS. Case managers of the HCS and the ISS are responsible for conducting needs assessment and on-going case reviews, formulating individual care plans, collaborating with different stakeholders and rendering appropriate services to service users and their carers (e.g. family members). For the benefits of service users, Audit considers that the SWD needs to remind case managers to ensure that necessary support services are provided to service users as far as possible.

4.17 ***Delay in discharging service users.*** According to the SWD, service users of the HCS may be discharged if any one of the following conditions is met:

- (a) the service user has been admitted to long-term placement of subvented residential care service;
- (b) the service user has been hospitalised for a period of more than three months without a discharge plan;
- (c) the service user has decided to terminate the service;
- (d) the service user has died; or
- (e) the impairment level, health condition, supportive network and environmental conditions of the service user have improved or strengthened to a level that he/she is able to live independently or with little assistance.

4.18 Regarding the ISS, according to the SWD, service users may be discharged in the following general circumstances:

- (a) the service user has decided to terminate the service; or
- (b) the service user has died; or
- (c) the impairment level, health condition, supportive network and environmental conditions of the service user have improved or strengthened to a level such that the ISS is no longer required.

4.19 Audit's examination of the 150 cases indicated that there was delay in discharging service users. In some cases, service users could have been discharged in the last financial year but were instead discharged in the new financial year. As the SWD only takes into account the number of users discharged as at 31 March of the last financial year (see para. 4.8(a)), discharging users in the new financial year means that subventions would continue to be paid to the ASUs for the discharged users. Details are as follows:

- (a) of the 50 cases of ASU A examined by Audit, in 11 (22%) cases, there was delay in discharging the service users;
- (b) of the 50 cases of ASU B examined by Audit, in 17 (34%) cases, there was delay in discharging the service users. An example of delay is shown in Case 6; and
- (c) of the 28 (11 + 17, (see (a) and (b) above)) cases, in 22 cases, the users were discharged in the new financial year.

Case 6

Delay in discharging a service user by ASU B

- March 2015: A service user was admitted by ASU B for the provision of the HCS (see para. 4.6(a)).
- August 2015: The spouse of the service user informed ASU B that the service user wanted to terminate the HCS as the service user did not need the service anymore.
- September 2015 to March 2016: ASU B attempted to contact the service user and her spouse but in vain.
- April 2016: The service user was discharged from the HCS. She could, however, have been discharged in the period August 2015 to March 2016. In fact, in this period, no support service under the HCS had been provided to her.
- This case was included as a caseload reported to the SWD in 2016-17.

Source: NGO B records

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Audit considers that the SWD needs to provide to the ASUs more guidelines on discharging service users.

4.20 *Service users receiving both HCS and ISS.* According to the SWD, to avoid duplication of resources, a service user requiring integrated home-based support service can be admitted into either the HCS or the ISS, but not both. Audit, however, noted that in the period April 2015 to December 2016:

- (a) 12 service users of ASUs A, B and E had registered for both the HCS and the ISS; and
- (b) of these 12 service users, according to the case files of the service users, 4 users received both the support services under the ISS provided by ASU E of NGO E and the support services under the HCS provided by ASU A of NGO A.

Audit considers that the SWD needs to take measures to address the issue of service users receiving both the HCS and the ISS.

4.21 *Need to review existing arrangements for calculating subventions to ASUs.* As mentioned in paragraph 4.8(b), based on the assumption that users of the HCS and the ISS normally have long-term needs, and the discharge rates of these services would be relatively low, the SWD therefore will not make downward adjustment of subventions to the ASUs providing the HCS or the ISS during a financial year. However, Audit's examination of the 150 cases (i.e. 50 cases for each of the ASUs — see para. 4.12) revealed that in 19 cases (13%), i.e. 5 for ASU A, 7 for ASU B and 7 for ASU E, the users were discharged within 90 days after admission (Note 36). Audit further analysed the discharge rates of the three ASUs from April 2015 to December 2016 and found that the discharge rates in fact ranged from 27% to 38% (see Table 24). In September 2017, the SWD informed Audit that the higher-than-expected discharge rates might be attributed to the high level of frailty and unstable medical conditions of the target users who were all persons with severe disabilities.

Note 36: *The users had been discharged for reasons such as death or transferred to other rehabilitation services.*

Table 24

**Profile of users of ASUs
(1 April 2015 to 31 December 2016)**

ASU	No. of active users as at 31.3.2015 (Note) (a)	No. of users admitted between 1.4.2015 and 31.12.2016 (b)	Total no. of users (c) = (a) + (b)	No. of users discharged between 1.4.2015 and 31.12.2016 (d)	Discharge rate (e) = (d) ÷ (c) × 100%
ASU A	190	584	774	281	36%
ASU B	211	493	704	266	38%
ASU E	136	374	510	139	27%

Source: NGO A, B and E records

Note: The figures excluded users discharged on or before 31 March 2015 (i.e. before the introduction of the revised subvention arrangements — see para. 4.7).

4.22 In view of the higher-than-expected discharge rates, Audit recalculated the subventions provided to the three ASUs in years 2015-16 and 2016-17 (up to 31 December 2016) based on the number of daily active users (i.e. the number of existing and new users minus the number of users discharged on a daily basis — see para. 4.8(a)) instead of the number of active users as at 31 March of the last financial years (see para. 4.8(a) and (b)). Audit found that, based on Audit's recalculation, potential savings in subventions could be achieved (\$12.9 million in 2015-16 and \$4.1 million in 2016-17) as shown in Table 25.

Table 25

**Potential savings in subventions to ASUs
(2015-16 and 2016-17)**

ASU	2015-16 (Note 1)		2016-17 (up to December 2016)	
	Amount of potential savings (\$ million)	Percentage of annual subvention	Amount of potential savings (\$ million)	Percentage of annual subvention
ASU A	5.5	17%	1.7	5%
ASU B	4.6	15%	Nil (Note 2)	
ASU E	2.8	16%	2.4	14%
Total	12.9		4.1	

Source: Audit analysis of NGO A, B and E records

Note 1: For HCS (provided by ASU A and ASU B), Audit's recalculation began from April 2015 (see para. 4.7). For ISS (provided by ASU E), Audit's recalculation began from August 2015 (see para. 4.7).

Note 2: The ASU still met the "75%" caseload requirement (see para. 4.7(a)) after Audit's recalculation and therefore there was no potential saving in subvention.

4.23 In Audit's view, with a view to optimising the use of public money (see para. 4.7), the SWD needs to explore the feasibility of fine-tuning the existing arrangements for calculating subventions to the ASUs providing the HCS and the ISS (see para. 4.8(a) and (b)) so as to identify potential savings in subventions. For example, instead of calculating the subventions in a new financial year based on the number of active users as at 31 March of the last financial year, the SWD could consider calculating the subventions in a new financial year based on other ways of counting active users in the last financial year. Savings in subventions realised could be used for the provision of other welfare services.

Audit recommendations

4.24 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **ascertain the reasons for the significant underperformance in the provision of the HCS and the ISS and determine the way forward for the two services;**
- (b) **follow up with the ASUs to align their understanding and practices regarding the counting of HCS and ISS cases into the caseloads reportable to the SWD;**
- (c) **remind case managers of the HCS and the ISS to ensure that necessary support services are provided to service users as far as possible;**
- (d) **provide to the ASUs more guidelines on discharging service users;**
- (e) **take measures to address the issue of service users receiving both the HCS and the ISS; and**
- (f) **with a view to optimising the use of public money, explore the feasibility of fine-tuning the existing arrangements for calculating subventions to the ASUs providing the HCS and the ISS.**

Response from the Government

4.25 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD has kick-started a review of the HCS and the ISS since July 2016. Some supportive activities conducted by physiotherapists, occupational therapists, nurses and care staff, such as coaching/training sessions provided for carers, case consultations/assessments/reviews, design and monitoring of home modification works, etc., which were not recognised as service output in the past, have already been included as reportable output to truly reflect the performance of both services. As far as the HCS and the ISS are concerned, the SWD will:

- (a) **ascertain the reasons for underperformance;**

- (b) provide more guidelines on the counting of cases into the caseloads, provision of support services in accordance with the agreed care plans, and discharge of service users, etc.;
- (c) set up a case cross-checking mechanism among the service operators of the HCS and the ISS to avoid service users receiving support services from both the HCS and the ISS; and
- (d) explore the feasibility of fine-tuning the existing arrangements for calculating subventions for the ASUs providing the services.

Setting of non-governmental organisations' performance standards

4.26 According to the SWD, Output Standards and Outcome Standards, which are service-specific and are stipulated in FSAs drawn up with ASUs (see para. 1.18), spell out concretely the service performance standards expected of NGOs. Though not all ASUs have Outcome Standards, Output Standards have been agreed with and set for every ASU. Nevertheless, the SWD stated in the LSG Steering Committee meeting in 2009 that the SWD would advise NGOs to incorporate Outcome Standards relating to users' satisfaction in the FSAs of new ASUs and when reviewing the existing FSAs as far as possible.

Need to incorporate Outcome Standards into more FSAs

4.27 Audit noted that of the 2,691 FSAs drawn up with ASUs as at 31 March 2017 (see para. 1.21), 2,209 (82%) did not contain Outcome Standards. Case 7 shows an example where for the same service, some ASUs were required to attain Outcome Standards while some were not so required.

Case 7

**ASUs providing the same service had different requirements
for attaining Outcome Standards**

1. Five ASUs (of three NGOs) were providing refuge centre service for temporarily accommodating women who were victims of family violence or in immediate danger of family violence. Of the five ASUs, two ASUs (operated by two NGOs) joined the LSG subvention system in 2001, whereas the other three ASUs (operated by one NGO) joined the LSG subvention system after 2001 and were receiving LSG subventions.

2. Audit noted that of the five ASUs, the two ASUs that joined the LSG subvention system in 2001 were not required to attain Outcome Standards. The other three ASUs, however, were required to attain Outcome Standards (5 standards for each of the three ASUs), which were stipulated in their FSAs. These Outcome Standards included, for example, user satisfaction rate and percentage of clients who had acquired basic skills in protecting and planning for themselves and their children.

3. In December 2016, the SWD revised the FSAs of the ASUs as a result of the allocation of additional resources for the provision of child care service delivered by the ASUs. However, Outcome Standards were only included in the revised FSAs of the three ASUs that joined the LSG subvention system after 2001. Outcome Standards had still not been set and incorporated into the revised FSAs of the other two ASUs (Note).

4. In September 2017, the SWD informed Audit that with a view to putting in place the Outcome Standards, a review on the non-time-defined FSAs of the two ASUs had started in September 2017.

Source: SWD records

Note: In September 2017, the SWD informed Audit that it had included two Outcome Standards in each of the two ASUs' quarterly statistical reports (see para. 3.2(a)). The ASUs were therefore required to provide information for performance monitoring purpose.

Audit recommendation

4.28 Audit has *recommended* that the Director of Social Welfare should, to properly monitor the effectiveness of services provided by ASUs, step up efforts to set Outcome Standards with ASUs and incorporate such standards into the pertinent FSAs.

Response from the Government

4.29 The Director of Social Welfare agrees with the audit recommendation. She has said that:

- (a) performance standards are clearly set for every ASU for the monitoring of the effectiveness of its service delivery; and
- (b) the SWD has started and will set Outcome Standards, as appropriate, for new ASUs and for existing ASUs when their FSAs are reviewed.

Use of service resources by non-governmental organisations

4.30 As mentioned in paragraph 1.9, NGOs are allowed to use LSG subventions for carrying out FSA activities and FSA related activities. According to the LSG Manual, NGOs receiving LSG are accountable to the SWD and the public for the proper and prudent use of public funds. It is the responsibility of NGOs' boards and management to maintain proper control of LSG subventions and ensure that the use of LSG subventions meets the objectives and requirements set out in FSAs and complies with the conditions spelt out in the LSG Manual. To avoid misunderstanding, NGOs should consult the SWD in a timely manner as to what constitutes "FSA related" activities before conducting such activities (see para. 2.36). NGOs are expected to ensure that LSG subventions are spent in the most cost-effective manner and for the intended purposes.

Need to ensure service resources are properly used

4.31 During Audit's visits to the 11 NGOs (see para. 1.31), Audit found that there was room for improvement in the use of service resources by two ASUs (of two NGOs). Details are shown in Cases 8 and 9.

Case 8

Provision of activities by a children and youth centre

1. ASU J, which is a children and youth centre, provides service users with activities responding to their personal, social and developmental needs. According to the latest FSA, the target service users are children and young people between the ages of 6 and 24. The agreed level of Output Standards for the "total number of core programme sessions within one year" and the "total attendance at the core programme sessions in one year" are 700 and 9,660 respectively. While the emphasis of the centre must be on core-programmes (e.g. socialisation programmes to enhance interpersonal and family relationships), non-core programmes (i.e. those that enable children and young people to use their leisure time constructively) may also be run.
2. Audit found that in the period 2014-15 to 2016-17 (up to January 2017):
 - (a) the ASU organised activities for children below the age of 6 and retired men who were not target service users under the FSA;
 - (b) 316 core programme sessions (with 6,604 attendance) and 3,027 non-core programmes (with 14,081 attendance) were organised for them;
 - (c) the figures stated in 2(b) above were included in the reporting of the attainment of Output Standards (through self-assessment — see para. 3.2) to the SWD; and
 - (d) six staff (comprising two social workers, two welfare workers and two welfare assistants) of the ASU were responsible for organising activities for children under 6 and retired men. Their salaries were fully paid from the LSG.

Case 8 (Cont'd)

3. According to LSG Manual, NGOs are expected to ensure that the LSG is spent for the intended purposes, i.e. in this case, providing activities to children and young people between the ages of 6 and 24. Furthermore, NGOs should consult the SWD in a timely manner as to what constituted “FSA related” activities before conducting such activities (see para. 4.30). Audit, however, noted that the ASU had not sought clarification from the SWD on whether the provision of activities for children below 6 and retired men were “FSA related” activities and could be carried out. Up to the end of August 2017, there was no evidence indicating that the SWD had given its consent for the provision of such activities by the ASU.

4. In September and October 2017, the SWD informed Audit that a recent service review on Integrated Children and Youth Centres (ICYSCs) was underway. The review reaffirmed that the service provision of the ICYSCs was for children and youth between the ages of 6 and 24. Nevertheless, given that working with significant others (e.g. parents and siblings, etc.) was essential in social work intervention with the problems associated with the development of children and youth, the SWD had agreed with the NGOs operating ICYSCs that the immediate significant others of children and youth, even below age 6 and above age 24, could be regarded as affiliated members of the centres. Programmes and activities aiming at resolving the problems of the children and youth and building up family cohesion could be regarded as FSA related activities organised for the well-being of the children and youth. As the target service users of both ICYSCs and children and youth centres are the same, the agreement with the sector under the recent review will equally apply to the latter.

Audit comments

5. The SWD needs to determine whether the activities provided by ASU J to children under six and retired men (who may or may not be the significant others such as parents of the children/youth) are FSA related activities and instigate remedial action where necessary. The SWD also needs to remind NGOs that the SWD should be consulted prior to the conduct of activities which they regard as FSA related activities but not stipulated in FSAs.

Source: Audit analysis of NGO F records

Case 9

Provision of children residential home by an ASU

1. ASU S operates a residential home for children providing out-of-home care for children who cannot be adequately taken care of by their families due to family problems such as illness, death, desertion, imprisonment of the parents or carers. The service of residential home for children is a support service to the needy families for taking care of their children before the children can be restored home or a long-term welfare plan (e.g. adoption) is arranged. According to the FSA, the target children are those from birth to two years of age. The approved capacity of the residential home is 104 places.
2. Of the 104 places, the SWD required the ASU to provide 20 places as emergency placements to cater for children whose families have crisis and cannot provide proper care to the children. When the service was introduced in 2004, the duration of stay at the residential home was set at not more than 3 months. The residential period for emergency places was revised to 6 weeks in around 2011 but subject to an extension for another 3 weeks on a need basis. To cater for the service need of individual cases, extension of stay is allowed provided that there is a genuine need and the social worker concerned of the referring unit of an NGO has obtained parental consent and worked out a concrete long-term welfare plan for the child (e.g. the child has been waitlisted for long-term residential care services or there is concrete plan for home restoration). Furthermore, approval from the supervisor of the referring unit and the superintendent of ASU S are also required.
3. Applications for emergency places, which are offered on a first-come-first-served basis, must be made through referral of the SWD or NGOs' social workers. Social workers may contact the ASU for availability of emergency placement. Admission can be arranged subject to emergency placement being available and the necessary procedures (e.g. case intake, acquisition of parental consent and medical checkup for the child) being completed. According to the SWD, extension of stay at emergency places is allowed if there is a genuine need and the necessary procedures are completed. The ASU will conduct case reviews for cases involving stay of longer than 6 months to make alternative arrangements for the children as soon as practicable. The ASU will not put children on a waiting list once all the 20 places are reserved or occupied.

Case 9 (Cont'd)

4. Audit found that as at 20 June 2017 (date of audit visit), of the 20 emergency places:

- (a) 6 places had been occupied by children for more than 22 months to 31 months, as opposed to a residential period for emergency places of 6 weeks. These 6 places had been extended for 32 to 45 times (3 weeks each time). Of the 6 children, a child did not have any welfare plan at the time of approval for extension; and
- (b) 13 places were reserved by social workers over the phone. One of the 13 places had been reserved for 72 days. Audit further examined the reservation records for the period April 2016 to June 2017 and found that of the 39 cases of reservations that had subsequently been cancelled by the social workers, 9 had been reserved for 5 to 7 months and 15 for 3 to 4 months.

Audit comments

5. There is room for improvement in the management of emergency places (see para. 4.32(c) to (e)).

Source: Audit analysis of NGO I records

Audit recommendations

4.32 **Audit has recommended that the Director of Social Welfare should:**

- (a) **determine whether the activities provided by ASU J to children under six and retired men are FSA related activities and instigate remedial action where necessary;**
- (b) **remind NGOs that the SWD should be consulted prior to the conduct of activities which they regard as FSA related activities but not stipulated in FSAs;**

- (c) **communicate with the NGO of ASU S on how best to handle the cases of children occupying the emergency places longer than the stipulated periods, bearing in mind that there may be other children in need of the places;**
- (d) **remind the NGO of ASU S of the need to require social workers of referring units of NGOs to work out long-term welfare plans for all children occupying the emergency places in a timely manner; and**
- (e) **urge the NGO of ASU S to admit cases requiring urgent placement at the earliest possible time, and set a reasonable timeframe for social workers of referring units to complete the admission procedures.**

Response from the Government

4.33 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) for Case 8, the FSA states that the target group of children and youth centre refers to children and young persons aged between 6 and 24. Activities provided for participants beyond this age range are normally not regarded as FSA activities. The SWD will follow up on the case. In the event of any subvented resources being deployed for non-FSA related activities, the NGO would be requested to apportion the costs in respect of rent, rates, utility charges and personal emoluments funded by social welfare subventions, etc.;
- (b) it is stipulated in the LSG Manual that to avoid misunderstanding, NGOs should consult the SWD in a timely manner as to what constitutes “FSA related” activities before conducting such activities (see para.2.36). The SWD will issue reminders to NGOs annually reminding them to consult the SWD prior to the conduct of activities which they regard as FSA related activities but not stipulated in FSAs;
- (c) the purpose of emergency placement is to cater to the urgent residential care need of children due to family crisis. While emergency placement is on a first-come-first-served basis, referring workers in actual operation will need time to complete necessary procedures (e.g. obtaining parental

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consent and arranging medical check-up for children prior to their admission to emergency placement);

- (d) the SWD has required the ASU to admit children in need of urgent out-of-home care as soon as possible as long as the information required for admission has been furnished;
- (e) the SWD has required the ASU to set a reasonable timeframe for referring workers to complete the admission procedures and to review the utilisation rate of the service closely;
- (f) the SWD has requested the ASU to follow up closely with referring workers on cases requiring extension of stay and to ensure that necessary approval and long-term care plan are in place to justify the need for extension; and
- (g) the SWD will step up the review and monitoring of the utilisation of the service and duration of stay of the admitted cases with the ASU to ensure that the service is meeting the urgent residential care needs of needy children.

Renewal of Funding and Service Agreements

4.34 As at 31 March 2017, the SWD had drawn up FSAs with 2,691 ASUs of the 165 NGOs. Of the 2,691 FSAs, 985 (37%) were time-defined (i.e. they normally had an agreement period of three or five years) and 1,706 (63%) were non-time-defined (i.e. without a specified agreement period). According to the SWD's records, in the years before 2001, subventions for subvented services were allocated on a non-time-defined basis. Since 2001, subventions for new services have been allocated on a time-defined basis.

Need to conduct comprehensive reviews of performance of ASUs with non-time-defined FSAs

4.35 All ASUs, both under time-defined FSAs and non-time-defined FSAs, are subject to the same monitoring system, i.e. all of them are required to submit quarterly statistical reports on the actual performance on Output/Outcome Standards, half-yearly report on variance against the agreed levels of Output/Outcome Standards,

annual self-assessments on attainment in Output/Outcome Standards (see para. 3.2(a) to (c)) and are subjected to performance visits (see para. 4.39). Besides, their performance of Output/Outcome Standards is reviewed annually by the SWD (see para. 4.46). In addition, upon the end of agreement period of a time-defined FSA, the SWD's Subventions Branch will conduct a comprehensive review of the performance of the ASU concerned for the purpose of renewing the FSA. The review will take into account the ASU's attainment on Output Standards, Outcome Standards, ESRs and SQSs (reported through self-assessment — see para. 3.2), results of the Branch's performance visits (see para. 4.39) and complaints against the ASU. After the review, the Branch will provide a review report to the relevant Service Branch (see para. 1.22(b)) for information and consideration in respect of the ASU's service. Finally, approval will be sought from the Director of Social Welfare for the renewal of the FSA.

4.36 Comprehensive reviews provide a more complete picture of the performance of ASUs as they evaluate in one go the results of the ASUs' self-assessment, the outcomes of the Subventions Branch's performance visits and potential maladministration reported through public complaints. Audit, however, noted that while ASUs with time-defined FSAs are subjected to comprehensive reviews, there are no such reviews for ASUs with non-time-defined FSAs.

Audit recommendation

4.37 **Audit has *recommended* that the Director of Social Welfare should consider conducting, on a periodic basis, comprehensive reviews of the performance of ASUs with non-time-defined FSAs (particularly those ASUs with persistent underperformance).**

Response from the Government

4.38 The Director of Social Welfare agrees with the audit recommendation. She has said that:

- (a) the ASUs with non-time-defined FSAs are subject to the same level of monitoring as the ASUs with time-defined FSAs. In fact, all ASUs' performance of Output/Outcome Standards is reviewed by the SWD annually regardless of whether their FSAs are time-defined or not; and

- (b) the SWD will consider conducting comprehensive reviews of the ASUs with non-time-defined FSAs on a periodic basis.

Performance visits and conduct of annual performance review

Performance visits

4.39 As mentioned in paragraph 1.22(c)(iii), the SWD carries out visits to ASUs of NGOs to assess the performance of ASUs. The purpose of the visits is to ensure that NGOs comply with the terms and requirements stipulated in FSAs. These performance visits are conducted by a Service Performance Monitoring Team (the Team) of the SWD's Subventions Branch. The Team is headed by one Senior Social Work Officer and supported by five Social Work Officers and one Assistant Social Work Officer.

4.40 Performance visits comprise:

- (a) ***Review visits (i.e. pre-arranged visits) and surprise visits.*** The Team aims to conduct review visits or surprise visits to selected ASUs of each of the 165 NGOs at least once in a three-year cycle (the current cycle is 2015-16 to 2017-18) (Note 37). The ASUs are selected on the following basis:
 - (i) for an NGO with 10 ASUs or less, one ASU to be selected on a random basis; and
 - (ii) for an NGO with more than 10 ASUs, for each type of services shown in paragraph 1.3, one ASU to be selected from every 10 ASUs on a random basis.

In each review/surprise visit to an ASU, all ESRs and 4 of the 16 SQSs will be examined. The performance of ASUs in respect of Output/Outcome Standards will be examined when SQS 3 (i.e. the service unit maintains

Note 37: *According to the SWD's records, surprise visits accounted for about 20% of its review visits and surprise visits in a three-year visit cycle.*

accurate and current records of service operations and activities) is selected for examination (Note 38);

- (b) ***On-site assessments.*** On-site assessments are conducted at ASUs with new services launched, for services of which the operating NGOs have no previous experience in running, and at ASUs with suspected performance problems (e.g. ASUs with continuous non-compliance of performance standards and with problems in drawing up or implementing action plans for improving performance). The purpose of on-site assessments is to collect on-site information or evidence to facilitate assessment and monitoring of performance of ASUs as well as to initiate early intervention in problems identified and formulation of action plans as appropriate; and
- (c) ***Special visitation programme (SVP) visits.*** In December 2015, in order to meet the rising expectations on greater public accountability and service monitoring, the SWD initiated and the LSG Steering Committee approved an SVP for implementing over a five-year period from 2016-17 to 2020-21. The SVP aims to conduct review visits at ASUs which have never been visited before. Under the SVP, with the exception that 2 instead of 4 SQSs are examined, review visits are to be conducted in the same way as described above (see para. 4.40(a)).

In carrying out the above four types of performance visits (i.e. review visits, surprise visits, on-site assessments and SVP visits), the staff of the Team solicit feedback from service users on ASUs' services through questionnaires and face-to-face interviews.

4.41 Audit examined the Team's records of the performance visits conducted in the period 2012-13 to 2016-17 and accompanied the Team's staff in carrying out eight performance visits (comprising the four types of performance visits) during May to July 2017. Audit found room for improvement in areas shown in paragraphs 4.42 to 4.45.

Note 38: *According to the SWD, in the current monitoring cycle of 2015-16 to 2017-18, SQS 3 is a mandatory SQS selected for assessment for all community services.*

Need to closely monitor conduct of performance visits at ASUs that have never been visited

4.42 As at 31 March 2017, of the 2,691 ASUs, 542 (20%) had never been visited by the Team. While the SVP aims to cover those ASUs which have never been visited, Audit noted that there is a risk that the SVP could not be accomplished within the timeframe due to the following reasons:

- (a) according to the SWD's SVP plan, the Team would visit 556 ASUs in the period 2016-17 to 2020-21. Given that the Team only visited 55 ASUs (10%) in 2016-17 and planned to visit another 53 ASUs (10%) in 2017-18, the progress so far appeared to be on the slow side; and
- (b) in addition to the SVP visits, the Team would still need to conduct review/surprise visits as well as on-site assessments (see para. 4.40(a) and (b)). In the previous three-year visit cycle from 2012-13 to 2014-15, the Team conducted review/surprise visits to 315 ASUs, while in the period from 1 April 2012 to 31 March 2017, the Team conducted 104 on-site assessments.

4.43 In September 2017, the SWD informed Audit that it was in accordance with the implementation plan that fewer visits would be conducted in 2016-17 and 2017-18 while more visits would be conducted between 2018-19 and 2020-21. This was because the Team needed to accord priority to complete those selected review/surprise visits under the current monitoring cycle from 2015-16 to 2017-18. As measures had been put in place (including streamlining the arrangement for visits under the SVP and applying a special one-off arrangement for fewer visits in the monitoring cycle from 2018-19 to 2020-21), the SWD considered that the existing manpower could cope with the visits under the SVP. While the number of on-site assessments needed to be conducted every year was dependent on the number of new ASUs falling into the requirement under on-site assessments, the head of the Team had closely monitored the implementation of all types of visits by requesting Team members to report progress quarterly so as to ensure all visits were on schedule.

4.44 Audit considers that the SWD needs to closely monitor the progress of SVP visits in order to accomplish the SVP within the timeframe as appropriate. The SWD also needs to review its approach in conducting SVP visits and the normal review/surprise visits (e.g. reviewing the need to change from the random-based

(see para. 4.40(a)) to a risk-based visit approach by focusing on ASUs with a larger number of non-compliance with SQSs) to ensure that they are conducted efficiently and effectively. Moreover, given that the Team only has six staff (excluding the head of the Team) responsible for the performance visits of about 2,700 ASUs, the SWD needs to assess the Team's manpower need.

Need to improve conduct of performance visits

4.45 Audit noted that there were inadequacies in the conduct of performance visits as follows:

- (a) ***Service users pre-selected by ASUs.*** During performance visits (i.e. review visits, surprise visits, on-site assessments and SVP visits), the Team will solicit feedback from service users on ASUs' services by requesting them to complete questionnaires or carrying out interviews with them. In accompanying the Team's staff in the conduct of 8 performance visits (see para. 4.41), Audit found that:
 - (i) in 8 visits, the 25 service users interviewed by the Team were pre-selected by the ASUs; and
 - (ii) in 4 visits, of the 9 service users requested to complete questionnaires, 5 were selected by the ASUs.

In September 2017, the SWD informed Audit it was the usual practice for the Team to interview service users pre-arranged by ASUs for collecting their views and comments on the SQSs under examination and on the service delivery of the ASUs. On top of the pre-arranged service users, there were some other service users randomly selected by the Team for completing the questionnaires. Sometimes, no suitable service users were available on site for random selection (e.g. in ASUs providing non-centre-based service without walk-in service for service users). To maintain impartiality in obtaining feedback from service users, Audit considers that the SWD needs to take enhanced measures to ensure that, as far as possible, service users to be requested to complete questionnaires or interviewed are not pre-selected by ASUs (e.g. for ASUs having walk-in service users, such users are always selected by the Team's staff);

- (b) *Samples for examination selected by ASUs.* During performance visits, the Team's staff will examine ASUs' records pertinent to service operation on a sample basis. Audit, however, noted that the samples for examination were not always selected by the Team's staff themselves. For example, in an accompanied visit in late May 2017, when examining the procurement procedures under SQS 7 (i.e. the service unit implements policies and procedures to ensure effective financial management) at an ASU, the Team's staff did not select the samples for examination by themselves. They requested the staff of the ASU to provide them with two quotations obtained from suppliers for review. In September 2017, the SWD informed Audit that requesting the two samples of quotations from the ASU was to ascertain whether there were records to support that the ASU had considered opportunities for introducing efficiencies/containing costs in the supply of services or products. To maintain independence and objectivity of the examinations, Audit considers that the Team's staff should always select samples for examination at ASUs themselves; and
- (c) *Need to follow up inaccurate self-assessment reports.* In the performance visits conducted by the Team in the period 2012-13 to 2016-17, the Team identified 14 underperformance cases which had not been shown in the self-assessment reports of 13 NGOs. Of these 14 underperformance cases, 11 related to ESRs (e.g. on the opening hours of the institutions and employment of essential staff) and 3 related to SQSs (e.g. on safety matters). There were, however, no records indicating that the Team had taken any follow up actions relating to the inaccurate self-assessment reports. In September 2017, the SWD informed Audit that it would issue a "Record on Area for Improvement" on-site and request the NGO to submit an action plan within four weeks for rectification if non-compliance on ESRs or SQSs was identified during a performance visit. Regarding the inaccurate self-assessment on Output Standards and Outcome Standards, it was the SWD's practice to issue a management letter to advise the NGO's Head to critically examine the NGO's self-reporting mechanism and take appropriate actions to ensure that due and accurate reporting will be made in future. The SWD said that it might cover the inaccurate self-assessment on ESRs and SQSs in the management letter in future.

Conduct of annual performance review

4.46 The SWD's Subventions Branch conducts annually a performance review on the attainment of Output Standards and Outcome Standards by all ASUs. The following information is produced by the Branch in an annual performance review:

- (a) a list of ASUs with underperformance in Output Standards and Outcome Standards in the year;
- (b) a list of ASUs with complete attainment of Output Standards and Outcome Standards in the year; and
- (c) an analysis of the performance and action plans of ASUs with underperformance.

According to the SWD, the above results of annual performance review are provided to the Chief Social Work Officer of individual Service Branches for information and comments.

4.47 Audit found room for improvement in the conduct of annual performance review as follows:

- (a) the annual performance review covered only the attainment of Output Standards and Outcome Standards. There was no information, for example, on the attainment of other performance standards (i.e. the ESRs and the SQSs) and the results of performance visits conducted by the Subventions Branch; and
- (b) there was no evidence indicating that the results of annual performance review had been submitted to the SWD's directorate staff (including the Director of Social Welfare) for their reference and deliberations. It would be particularly desirable to submit review results relating to ASUs with non-time-defined FSAs, as these FSAs, though subject to annual performance review of Output/Outcome Standards, they are not subjected to comprehensive reviews as in the case of time-defined FSAs (see paras. 4.35 and 4.36).

Audit recommendations

4.48 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **closely monitor the progress of SVP visits in order to accomplish the SVP within the stipulated timeframe;**
- (b) **review the approach to conducting SVP visits and review/surprise visits (e.g. reviewing the need to change from the random-based to a risk-based visit approach) to ensure that they are conducted efficiently and effectively;**
- (c) **assess the manpower need of the Team of the SWD's Subventions Branch responsible for the conduct of performance visits;**
- (d) **take enhanced measures to ensure that, as far as possible, service users to be requested to complete questionnaires or interviewed are not pre-selected by ASUs;**
- (e) **take enhanced measures to ensure that the staff of the Subventions Branch responsible for conducting performance visits select samples for examination at ASUs themselves;**
- (f) **remind NGOs to rectify the irregularities noted during performance visits;**
- (g) **consider including inaccurate self-assessment on ESRs and SQSs in management letters issued to ASUs;**
- (h) **consider extending the coverage of annual performance review (e.g. to include attainment of ESRs and SQSs); and**
- (i) **take measures to ensure that the results of NGOs' compliance with the ESRs, SQSs, Output Standards and Outcome Standards are brought to the attention of the SWD's directorate periodically.**

Response from the Government

4.49 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) all types of service performance visits are being monitored closely with the progress reported on a quarterly basis. The SWD will closely monitor the progress of the SVP implementation which is on schedule as planned;
- (b) the SWD will review regularly the approach to conducting review/surprise visits and to assess the manpower need with a view to ensuring efficient and effective conduct of performance visits;
- (c) the SWD will, as appropriate, ensure that service users involved in the assessment are not pre-selected by ASUs, and the staff conducting performance visits select samples for examination at ASUs;
- (d) it is the SWD's existing practice that if non-compliance on ESRs or SQSs is identified during a service performance visit, a "Record on Area for Improvement" will be issued on-site and the NGO be asked to submit within four weeks an action plan for rectification. The SWD will remind NGOs to rectify the irregularities;
- (e) the SWD will consider including inaccurate self-assessment on ESRs and SQSs in the management letters issued to ASUs;
- (f) the SWD will consider including ASUs' attainment of ESRs and SQSs in annual performance review; and
- (g) the assessment results for the monitoring cycle from 2012-13 to 2014-15 covering NGOs' compliance with ESRs, SQSs and Output/Outcome Standards had been brought to the attention of the SWD's directorate in January 2016. The SWD will keep the directorate posted of the service performance in every monitoring cycle.

PART 5: GOVERNANCE AND MANAGEMENT MATTERS

5.1 This PART examines matters relating to the governance and management of NGOs, focusing on the following issues:

- (a) implementation of BPM guidelines (paras. 5.2 to 5.12);
- (b) adoption of other good governance practices (paras. 5.13 to 5.23); and
- (c) addressing the problem of high staff turnovers of NGOs (paras. 5.24 to 5.32).

Implementation of Best Practice Manual guidelines

5.2 Under the auspices of the LSG Steering Committee (see para. 1.24), a BPM (see para. 1.19) for NGOs receiving LSG subventions has been developed with the welfare sector including NGOs' management, staff side, service users and professional bodies. The BPM, which came into effect in July 2014, encourages the NGOs to enhance their governance in financial management, human resource management as well as corporate governance and accountability.

5.3 The BPM provides guidelines for 14 strategic items (see Appendix C), such as “use of reserve” and “NGOs' policies and procedures on complaints handling”. For 7 of the 14 items, the guidelines are “Level One guidelines” i.e. those that NGOs are expected to follow unless they have strong justifications not to do so. For the other 7 items, the guidelines are “Level Two guidelines” i.e. those that NGOs are encouraged to adopt.

5.4 NGOs have been given a transition period of three years (i.e. by 30 June 2017) to review their existing policies and procedures, and make necessary amendments and proper arrangements for implementing the guidelines. For each financial year from 2014-15 to 2016-17, each NGO is required to report to the SWD its progress of implementing Level One guidelines by submitting a self-assessment

report, showing the position as at 31 March of the year, to the SWD by end of October of the year. For Level Two guidelines, submission of the self-assessment reports is on a voluntary basis (Note 39). According to the NGOs' latest self-assessment reports submitted to the SWD, as at 31 March 2016, of the 165 NGOs receiving LSG subventions:

- (a) 98 (59.4%) NGOs had fully implemented Level One guidelines for all the 7 items (see Table 26); and

Note 39: *The voluntary submission of self-assessment reports has been agreed by the LSG Steering Committee.*

Table 26

**Implementation of Level One guidelines by 165 NGOs
(31 March 2016)**

Individual items	No. of NGOs		
	Implemented	In progress	Not yet implemented
Financial management			
1. Maximised use of LSG reserve	124 (75.2%)	41 (24.8%)	0 (0%)
2. Status of LSG reserve	132 (80.0%)	33 (20.0%)	0 (0%)
3. Use of PF reserve	106 (64.2%)	58 (35.2%)	1 (0.6%)
4. Status of PF reserve	131 (79.4%)	33 (20.0%)	1 (0.6%)
Human resource management			
5. Salary adjustment	157 (95.2%)	8 (4.8%)	0 (0%)
Corporate governance and accountability			
6. Composition, duties and responsibilities on handling complaints at different levels	146 (88.5%)	19 (11.5%)	0 (0%)
7. NGOs' policies and procedures on complaints handling	148 (89.7%)	17 (10.3%)	0 (0%)
	No. of NGOs		
All items implemented	98 (59.4%)		
Some items implemented	67 (40.6%)		
Total	165 (100%)		

Source: SWD records

- (b) 154 (93%) NGOs voluntarily submitted self-assessment reports on the implementation of Level Two guidelines for 2015-16. Of these 154 NGOs, 38 (24.7%) had fully implemented Level Two guidelines for all the 7 items (see Table 27).

Table 27

**Implementation of Level Two guidelines by 154 NGOs
(31 March 2016)**

Individual items	No. of NGOs		
	Implemented	In progress	Not yet implemented
Financial management			
1. Optimal level of LSG reserve	62 (40.3%)	67 (43.5%)	25 (16.2%)
Corporate governance and accountability			
2. Communication	100 (65.0%)	41 (26.6%)	13 (8.4%)
3. Terms of office of the governing board	95 (61.7%)	35 (22.7%)	24 (15.6%)
4. Roles of governing board	99 (64.3%)	43 (27.9%)	12 (7.8%)
5. Delineation of roles and responsibilities of the governing board	108 (70.1%)	36 (23.4%)	10 (6.5%)
6. NGOs' decision making on important management issues of SWD-subvented services	70 (45.5%)	62 (40.2%)	22 (14.3%)
7. NGOs' decisions made on important management issues of SWD-subvented services	67 (43.5%)	67 (43.5%)	20 (13.0%)
	No. of NGOs		
All items implemented	38 (24.7%)		
Some items implemented	104 (67.5%)		
No items implemented	12 (7.8%)		
Total	154 (100%)		

Source: SWD records

Need to ensure accuracy of self-assessment reports

5.5 According to the SWD, it makes use of NGOs' self-assessment reports (see para. 5.4) to know about the progress of implementation of the BPM guidelines. In examining the self-assessment reports of the six NGOs visited (see para. 1.31(b)), Audit noted inadequacies relating to the reporting and implementation of the guidelines, as follows:

- (a) ***Self-assessment reports not entirely accurate.*** Audit found incidents where the NGOs did not accurately report their implementation of the BPM guidelines. For example, in their 2015-16 self-assessment reports, NGO I reported that it had fully implemented the Level One guidelines for "maximised use of LSG reserve" while NGO K reported that it had fully implemented the Level Two guidelines for "optimal level of LSG reserve". Audit noted that, to fulfil the requirement of the BPM, NGOs' governing boards/management committees are required to discuss the matters in their meeting(s) at least once a year, and the discussion has to be put on record. However, the relevant minutes of the NGOs for 2014-15 and 2015-16 did not show that the matters concerned had been discussed;
- (b) ***Declining to comply with Level One guidelines by an NGO.*** NGO 6 was one of the 67 NGOs (see Table 26 in para. 5.4(a)) which had not fully implemented Level One guidelines. NGO 6 informed the SWD that it would not implement the Level One guidelines for two items (i.e. "use of PF reserve" and "status of PF reserve"), as its LSG subvention represented only about 11% of its operating income and its staff emoluments were not entirely subvented by the SWD. Level One guidelines are those that NGOs are expected to follow unless they have strong justifications not to do so. Audit, however, noted that the SWD had not followed up with the NGO which declined to implement Level One guidelines for the two items. In September 2017, the SWD informed Audit that it had followed up with NGO 6 earlier in the month. NGO 6 had agreed to take action to comply with the requirement. The compliance would be reflected in the self-assessment report to be submitted by NGO 6 by 31 October 2017; and
- (c) ***Self-assessment reports not submitted in a timely manner.*** Of the 165 NGOs which submitted 2015-16 self-assessment reports for Level One guidelines (see para. 5.4(a)), 107 (65%) submitted their reports on time while 58 (35%) were late in submitting their reports. In one case, the delay was over 30 days (see Table 28).

The SWD needs to take measures to address the above inadequacies.

Table 28

**Submission of progress reports by NGOs
(2015-16)**

Delay (No. of days)	No. of NGOs	
Nil	107 (65%)	
1 to 10	38 (23%)	} 58 (35%)
11 to 20	14 (8%)	
21 to 30	5 (3%)	
31 to 40	1 (1%)	
Total	165 (100%)	

Source: Audit analysis of SWD records

Need to better promote Level Two guidelines

5.6 As pointed out in paragraph 5.4, for Level Two guidelines, self-assessment reports are submitted on a voluntary basis. Nevertheless, it is encouraging to see that of the 165 NGOs receiving LSG subventions as at 31 March 2016, 154 (93%) had reported the progress of implementing the Level Two guidelines. However, as shown in Table 27, there were only 38 NGOs that had fully implemented the 7 items of the Level Two guidelines. For items such as “optimal level of LSG Reserve” and “NGOs’ decisions made on important management issues of SWD-subsented services”, the progress of implementation was relatively on the slow side. Furthermore, Audit noted that of the 154 NGOs that had reported progress of implementing Level Two guidelines, 12 had indicated in their self-assessment reports that they had not implemented any of such guidelines (see Table 27 in para. 5.4).

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5.7 Audit considers that the SWD needs to enhance the promotion of Level Two guidelines among NGOs, so as to solicit their greater support for implementing Level Two guidelines.

Need to expedite formulation of best practices for human resource management

5.8 During the development of the BPM, it was proposed that best practices were to be formulated for 18 items. In April 2014, subsequent to consultations with the welfare sector, best practices for 14 of the 18 items were formulated and incorporated as guidelines into the BPM. The four items for which best practices had not been formulated and incorporated into the BPM were related to human resource management, covering the following matters:

- (a) staff remuneration policy with due recognition of work experience and good performance, including a policy that allows staff salaries to go beyond the equivalent ranks' mid-points of the Government's pay scales if applicable;
- (b) pay policy with a clear salary structure and/or starting points, with communication channels for collecting views from staff;
- (c) policy on the transfer of posts, renewal and termination of employment contracts and recognition of work experience when drawing up employment contracts; and
- (d) transparent and accountable decision making with regard to staff contracts (i.e. the rules and procedures to be made known to existing and prospective staff of the NGO concerned).

5.9 During April 2014 to March 2017, the SWD had made attempts to forge an agreement on the best practices to be formulated for the four outstanding items and to incorporate them into the BPM, but to no avail. Key developments were as follows:

- (a) **December 2015.** At a meeting of the LSG Steering Committee, it was noted that the SWD planned to complete the discussion with the welfare sector about the incorporation of the four items into the BPM in 2016;

- (b) **November 2016.** At a meeting of the Working Group on the Implementation Details of BPM (BPM Working Group — Note 40), it was noted that more time was needed for both NGOs' management and the staff side to consider and agree on the matter; and
- (c) **March 2017.** The SWD reported to the LegCo Panel on Welfare Services that the BPM Working Group would continue to discuss the four outstanding items with the welfare sector, and that members of the Working Group considered that more time would be needed for NGOs' management and the staff side to consider possible options of the criteria and procedures for agreement and implementation by the welfare sector.

5.10 To enhance the governance on human resource management, Audit considers that the SWD needs to step up efforts to forge agreement between the NGOs' management and the staff side on the best practices for the four items relating to human resource management, and to incorporate them into the BPM.

Audit recommendations

5.11 **Audit has recommended that the Director of Social Welfare should:**

- (a) **remind NGOs to provide accurate information on the progress of implementation of BPM guidelines and submit self-assessment reports in a timely manner;**
- (b) **consider conducting checking of the implementation of Level One guidelines by NGOs;**
- (c) **enhance the promotion of Level Two guidelines among NGOs, so as to solicit their greater support for implementing Level Two guidelines; and**

Note 40: *In November 2013, the LSG Steering Committee endorsed the formation of a BPM Working Group. The Working Group is chaired by an Assistant Director of the SWD with representatives from the LSG Steering Committee and the welfare sector.*

- (d) **step up efforts to forge agreement between the NGOs' management and the staff side on the four items of the BPM relating to human resource management.**

Response from the Government

5.12 The Director of Social Welfare agrees with the audit recommendations. She has said that:

- (a) the SWD will remind NGOs to provide accurate information when they submit the self-assessment reports on the progress of implementation of the BPM;
- (b) the SWD has taken various measures to facilitate NGOs' implementation of the BPM in order to provide opportunities for NGOs to share experiences and good practices identified in the implementation of the BPM;
- (c) the SWD will launch a pilot exercise for on-site checking of NGOs' implementation of Level One items of the BPM;
- (d) the SWD will enhance the promotion of Level Two guidelines among NGOs; and
- (e) the SWD has prepared a preliminary draft of the contents of the four outstanding items of the BPM for deliberation by the BPM Working Group in their previous meetings. The SWD will forge agreement among the NGO management, the staff side and service users on the outstanding items.

Adoption of other good governance practices

5.13 The Efficiency Unit has published a corporate governance guide entitled "Guide to Corporate Governance for Subvented Organisations" (the Guide) issued in 2015. The aim of the Guide is to provide advice on good practices in corporate governance for all those responsible for management and oversight of subvented agencies. To help NGOs develop and maintain good practices in corporate governance, the Guide has been included as one of the references in the annex of the LSG Manual.

5.14 Audit's visits to the six NGOs (see para. 1.31(b)) revealed that there is room for these NGOs to adopt the good governance practices set out in the Guide, for example, the practices for engaging members' participation, managing conflicts of interest and strategic planning (see paras. 5.15 to 5.22).

Need to better engage members' participation

5.15 The Guide sets out that NGOs need to:

- (a) record and monitor the attendance of board members and take action to improve the attendance of those with low attendance; and
- (b) pay particular attention to attendance records of board members being considered for re-appointment.

5.16 Audit's visits to the six NGOs revealed that:

- (a) only 2 NGOs (NGOs H and K) had compiled attendance rates of board/committee members;
- (b) in the period 2013-14 to 2015-16, according to the minutes of the six NGOs' board and committee meetings, the proportion of board/committee members who did not attend any board/committee meetings was as high as 21.2% (see Table 29); and

Table 29

**Board/committee members of six NGOs with no attendance
(2013-14 to 2015-16)**

NGO	No. of members who did not attend any board/committee meetings		
	2013-14	2014-15	2015-16
F	1 (2.9%)	2 (5.9%)	3 (9.7%)
G	11 (17.5%)	10 (14.7%)	10 (14.7%)
H (Note)	0 (0%)	0 (0%)	2 (8.0%)
I	7 (21.2%)	5 (14.7%)	6 (19.4%)
J	3 (10.7%)	3 (4.0%)	6 (8.0%)
K	0 (0%)	2 (4.4%)	2 (5.1%)

Source: Audit analysis of NGO records

Note: Some minutes of meetings could not be located by the NGO for audit examination. The Table was compiled based on the available minutes.

Remarks: Figures in brackets are the percentages of members with no attendance in the year.

- (c) in the period 2013-14 to 2015-16, there were cases where board/committee members with low attendance rates had been re-appointed to the board/committees. For example, NGO I had re-appointed a board member and a committee member, despite the fact that they did not attend any meetings in three years prior to the appointment.

Need to improve management of conflicts of interest

5.17 According to the Guide, conflicts of interest may arise when a board member or an employee has the opportunity to influence the organisation's business

or other decisions in ways that could lead to personal gain or advantage of any kind. As such:

- (a) organisations should set out requirements to avoid conflicts of interest, and the course of action to be taken when a member faces a real or apparent conflict of interest situation;
- (b) organisations should consider adopting a “two-tier reporting system”, whereby in addition to reporting conflicts of interest at board meetings as and when they arise, board members should disclose their general interest on appointment to the board and annually thereafter; and
- (c) the declaration shall be made on a registration form, which should be made available for public inspection.

5.18 Audit examination of the declaration of conflicts of interest by board members of the six NGOs revealed that:

- (a) only 3 NGOs (NGOs F, J and K) had documented their procedures on requiring board members to declare interests;
- (b) only 2 NGOs (NGOs F and K) had adopted a two-tier reporting system;
- (c) for 4 NGOs (NGOs G, H, I and J), registration forms were not used to record members’ declaration of interests; and
- (d) for NGO F, not all members’ declaration forms were available for Audit inspection. For NGO K, only the directorships of board members were required to be declared. Other interests (e.g. pecuniary interest) were not required to be declared.

Room for improvement in strategic planning

5.19 According to the Guide, without established plans to guide an organisation’s actions, staff’s efforts would be unfocused and resources could be misused. The Guide sets out that:

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- (a) strategic planning determines where an organisation is going over the next year or more;
- (b) strategic planning broadly covers the formulation of action/strategic plans to achieve the organisation's goals and objectives; and
- (c) the focus of a strategic plan is usually on the entire organisation, while the focus of a business plan is usually on a particular service or programme.

5.20 Audit's visits to the six NGOs revealed that as at 31 August 2017:

- (a) for 4 NGOs (NGOs F, G, J and K), strategic plans had been prepared for the entire organisation. For the other 2 NGOs (NGOs H and I), no such strategic plans had been prepared; and
- (b) for 5 NGOs (NGOs F, G, I, J and K), action plans had been prepared for individual ASUs. For the remaining NGO (NGO H), no such action plans had been prepared.

For one NGO (NGO H), both the strategic plan and action plan had not been prepared.

5.21 A summary of audit findings on governance practices for the six NGOs visited are given in Table 30.

Table 30

Summary of audit findings on governance practices of six NGOs

Audit finding	NGO F	NGO G	NGO H	NGO I	NGO J	NGO K
<i>Members' attendance</i>						
Attendance rates of board/committee members compiled (see para. 5.16(a))	No	No	Yes	No	No	Yes
Board/committee members with no attendance at meetings (see para. 5.16(b))	Yes	Yes	Yes	Yes	Yes	Yes
Members re-elected despite low attendance (see para. 5.16(c))	Yes	Yes	No	Yes	Yes	No
<i>Conflicts of interest</i>						
Procedures on requiring board members to declare interests documented (see para. 5.18(a))	Yes	No	No	No	Yes	Yes
Two-tier reporting system for declaring interests adopted (see para. 5.18(b))	Yes	No	No	No	No	Yes
Declaration forms used for declaring interests (see para. 5.18(c))	Yes	No	No	No	No	Yes
Where declaration forms were adopted, the forms were available for inspection and properly used (see para. 5.18(d))	No	N.A.	N.A.	N.A.	N.A.	No
<i>Strategic planning</i>						
Strategic plans for the entire organisation prepared (see para. 5.20(a))	Yes	Yes	No	No	Yes	Yes
Action plans for individual ASUs prepared (see para. 5.20(b))	Yes	Yes	No	Yes	Yes	Yes

Source: NGO records

Audit recommendation

5.22 Audit has *recommended* that the Director of Social Welfare should make greater efforts to encourage NGOs to adopt the good practices outlined in the Efficiency Unit’s “Guide to Corporate Governance for Subvented Organisations”.

Response from the Government

5.23 The Director of Social Welfare agrees with the audit recommendation. She has said that the “Guide to Corporate Governance for Subvented Organisations” of the Efficiency Unit is already one of the references included in Annex 12 of the LSG Manual for NGOs to develop and maintain good practices in corporate governance. The SWD will make further efforts to promote it.

Addressing the problem of high staff turnovers of non-governmental organisations

5.24 Manpower is an important concern in the development of social welfare services in Hong Kong. In July 1987, the SWD and the Hong Kong Council of Social Service (see Note 1 to Appendix A) jointly set up the Joint Committee on Social Work Manpower Requirements (formerly known as the Joint Committee on Social Welfare Manpower Planning System). The Joint Committee undertakes the collection and analysis of information on the demand and supply of social work personnel in Hong Kong with a view to keeping track of the manpower situation and facilitating manpower planning in the social work field.

5.25 In the Joint Committee’s annual reports of 2014 to 2016, increasing turnover of social work posts in Hong Kong was noted (see Table 31).

Table 31

**Turnover of social work posts in Hong Kong
(2013-14 to 2015-16)**

Year	No. of social work posts	Turnover
2013-14	13,269	12.20 %
2014-15	13,907	13.40 %
2015-16	14,453	15.20 %

Source: Annual reports published by the Joint Committee on Social Work Manpower Requirements

- Remarks:*
1. According to the 2016 report of the Joint Committee, turnover refers to the number of occurrences of social work personnel (including but not limiting to Registered Social Workers) leaving any organisations for whatever reasons in a specified period, regardless of whether they have joined or would join the field again. If a social work person has resigned from more than one job or more than one organisation during the period, he/she would be counted more than once depending on the total number of jobs that he/she has left.
 2. According to the Social Workers Registration Board, as at 9 October 2017, there were 22,146 Registered Social Workers.

5.26 The Joint Committee's statistics on turnover (see Table 31 above) covered social work personnel working for LSG-subvented NGOs (in respect of both FSA activities and non-FSA activities) and those working for other organisations (Note 41). The SWD did not separately compile turnover statistics for LSG-subvented NGOs.

Note 41: Other organisations included government departments (e.g. the SWD), government-subvented special schools, local training institutions offering social work training programmes (e.g. universities), and NGOs which were self-financing or receiving government funding other than the LSG.

High staff turnovers at NGOs visited by Audit

5.27 Audit collected information on staff turnovers from the six NGOs visited (see para. 1.31(b)). Table 32 shows that, during 2013-14 to 2015-16, staff turnovers of the six NGOs were on the high side, ranging from some 14% to 35% (Note 42). Furthermore, for some NGOs, staff turnovers had increased over the period.

Table 32

**Turnovers of staff at six NGOs visited by Audit
(2013-14 to 2015-16)**

NGO	No. of staff as at 31.3.2016	2013-14	2014-15	2015-16
F	222	18.44%	19.50%	20.93%
G	462	29.41%	28.92%	35.23%
H (Note)	143	31.25%	22.53%	15.22%
I	131	18.71%	28.57%	23.66%
J	896	13.73%	14.01%	16.57%
K	876	16.47%	15.52%	14.63%

Source: NGO records

Note: NGO H's figures covered the period from November of the year to October of the ensuing year.

Causes of staff turnovers

5.28 Of the six NGO visited, one NGO (NGO H) did not have the practice of conducting exit interviews with staff leaving the organisation. For the other 5 NGOs,

Note 42: According to the Manpower Statistics Survey conducted by the Hong Kong Institute of Human Resource Management in February 2017, the staff turnover rate in Hong Kong (based on information gathered from 76 companies representing a total of 102,425 employees) for the second half of 2016 was 10.5%.

Audit analysed the results of exit interviews (Note 43) conducted by the NGOs in 2015-16. Table 33 shows that, of the 274 staff leaving the NGOs, many (133 staff or 48.6%) left for job-related reasons.

Table 33

**Reasons for staff leaving NGOs visited by Audit
(2015-16)**

Reason	No. of staff	Percentage
Family reasons	46	16.8%
No specific reasons	22	8.0%
Personal reasons (e.g. taking working holidays)	25	9.1%
Contract expired/termination by NGOs	19	6.9%
Retirement	12	4.4%
Other reasons	16	5.8%
Work in other industries	1	0.4%
Job hunting	58	21.2%
Job conditions (e.g. salaries)	47	17.2%
Job nature	28	10.2%
Total	274	100%

Source: Audit analysis of NGO records

5.29 The NGOs' records further indicated that, for the 28 staff who left the NGOs due to "job nature" (see Table 33 above), their concerns included heavy workloads, long working hours, work pressure and the need for working shifts.

Note 43: *Exit interviews were conducted only for staff who were willing to participate in the interviews.*

Governance and management matters

5.30 Audit further noted that, at the six NGOs visited, there were pay-related issues which might have impacted staff morale and stability. These issues are as follows:

- (a) ***Salary setting not transparent.*** In 4 NGOs (NGOs F, G, J and K), pay scales had been established for each rank of staff. In the remaining 2 NGOs (NGOs H and I), pay scales had only been established for some ranks. For example, while NGO H had established pay scales for two ranks (i.e. Personal Care Worker and Workman), there were no pay scales for all other ranks (e.g. Health Worker and Social Worker). Salary setting for these other ranks had not been transparent (Note 44); and
- (b) ***NGO staff paid below mid-point salaries of government pay scales.*** As mentioned in paragraph 1.12(a)(i), in calculating the LSG subvention to an NGO for “non-Snapshot Staff”, mid-point salaries of the Government’s pay scales were used. In practice, the determination of actual pay could be based on a number of factors including different skillsets, grades, seniority, and experience of individual staff. Some NGO staff were paid above the mid-point salaries or even above the maximum-point salaries of the Government’s pay scales (see Table 34). In contrast, there were NGO staff who were paid below the mid-point salaries (see Table 35).

Note 44: *According to NGO H, the salaries of staff other than Personal Care Worker and Workman were discussed and reviewed at the NGO’s management committee meetings.*

Table 34

**Examples of NGO staff paid above
mid-point salaries of Government's pay scales
(2016-17)**

NGO	Rank	Maximum salary at NGO (\$)	Mid-point salary of Government's pay scale (\$)	Difference (\$)
F	Workshop Instructor II	37,570	34,085	3,485 (10.2%)
F	Social Work Assistant	32,470	29,455	3,015 (10.2%)
G	Artisan	20,050 (Note)	17,685	2,365 (13.4%)

Source: Audit analysis of NGO records

Note: The amount was higher than the Government's maximum-point salary by \$1,210 (6.4%).

Table 35

Examples of NGO staff paid below
mid-point salaries of Government's pay scales
(2016-17)

NGO	Rank	Maximum salary at NGO (\$)	Mid-point salary of Government's pay scale (\$)	Difference (\$)
G	Welfare Worker	22,565	23,970	1,405 (5.9%)
G	Health Worker	17,810	22,560	4,750 (21%)
G	Clerical Assistant	13,640	16,590	2,950 (17.8%)
H	Personal Care Worker	14,470	16,590	2,120 (12.8%)
H	Workman II	12,620	13,190	570 (4.3%)
I	Cook	15,805	17,685	1,880 (10.6%)
J	Child Care Worker	16,000	23,970	7,970 (33.3%)
J	Motor Driver	17,080	17,685	605 (3.4%)

Source: Audit analysis of NGO records

Audit recommendations

5.31 Audit has *recommended* that the Director of Social Welfare should:

- (a) remind NGOs receiving LSG subventions to monitor their staff turnovers and take measures to address the problem of high staff turnovers;
- (b) remind NGOs receiving LSG subventions to review their pay scales and structures as well as to enhance transparency and communication with staff on salary matters;

- (c) **promulgate among NGOs the good practice of conducting exit interviews with staff leaving their organisations so as to enable NGOs to gain better insight into staff's concerns; and**
- (d) **step up efforts to forge agreement between the NGOs' management and the staff side on the four items of the BPM relating to human resource management (see also para. 5.11(d)).**

Response from the Government

5.32 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD will:

- (a) remind NGOs to monitor and review their human resource management issues, including staff turnovers and proper remuneration of staff;
- (b) remind NGOs to review their pay scales and structures as well as to enhance transparency and communication with staff with a view to maintaining a stable and effective workforce for provision of quality subvented services;
- (c) promulgate among NGOs the good practice of conducting exit interviews with staff leaving their employment; and
- (d) forge agreement among the NGO management, the staff side and service users on the outstanding items of the BPM.

PART 6: REVIEW OF LUMP SUM GRANT SUBVENTION SYSTEM

6.1 This PART examines issues relating to the review of the LSG subvention system and explores the way forward.

2008 review of lump sum grant subvention system

6.2 In 2008, the LSG Independent Review Committee conducted a review of the LSG subvention system (see para. 1.25). The review report contained 36 recommendations (see Appendix E) on ways to improve the system, which covered areas such as staff arrangements and financial issues (Note 45).

6.3 In February 2009, the LWB and the SWD accepted in principle all the 36 recommendations and agreed that the LSG subvention system could be improved. The SWD subsequently implemented the 36 recommendations (including the compilation of a BPM — see para. 1.19). Audit noted that there is room for improvement in the implementation of the recommendations (see paras. 6.4 to 6.14).

Need to collect feedback on actuarial or related studies conducted

6.4 In the 2008 review, the LSG Independent Review Committee recommended that the Government should make available an actuarial service for NGOs to apply for on a voluntary basis (see para. 2 in Appendix E). The service aimed to enable NGOs to assess, through conducting actuarial studies, their ability to meet “Snapshot Staff” commitments and projected payroll costs.

Note 45: *Other areas covered were flexibility, efficiency and cost-effectiveness in the use of public funds and in service delivery by subvented NGOs; accountability and corporate governance of subvented NGOs; quality of welfare service; and handling of complaints related to implementation of the LSG.*

6.5 Prior to November 2014, the SWD used its departmental expenditure to conduct two pilot actuarial studies for two NGOs at a total cost of \$1.98 million (one at \$1.1 million and the other at \$880,000). The actuarial studies were carried out by an external consultant. According to the SWD, in the course of the studies, the two NGOs had meetings with the SWD to share views on the actuarial studies. An NGO also shared its feedback on the studies in a briefing session held for other NGOs. The NGO concluded that:

- (a) it was always good to have an additional service;
- (b) whether the consultant's recommendations would work depended on the management's mentality and how supportive the staff were; and
- (c) it would be a waste of resources and time if an NGO used the actuarial service involuntarily and provided insufficient or incomplete information to the consultant in a reserved manner.

6.6 In a November 2014 meeting of the LSG Steering Committee, it was stated that based on the experiences of the pilot actuarial studies that had shed light on the financial situation of NGOs and provided them with a clearer picture on how to fulfil their contractual commitments to staff, the SWD recommended and the Committee approved the making use of funding of the Social Welfare Development Fund (Note 46) to commission actuarial studies or related studies (e.g. a finance and human resource system review and actuarial study commissioned by one of the 11 NGOs — see para. 6.7). According to the SWD, such studies would facilitate NGOs to acquire objective analysis and projections on their LSG and PF Reserves, and dovetail with the implementation of BPM.

6.7 As at 31 July 2017, 11 NGOs (excluding the two NGOs that were covered in the pilot actuarial studies) had applied for funding from the Fund and their studies were being conducted by external consultants. The amount for the studies ranged

Note 46: *The Social Welfare Development Fund, set up with \$1 billion injection from the Lotteries Fund, provides funding for NGOs to conduct different welfare projects (e.g. training and professional development for their board members, management and other staff, as well as for upgrading their business systems and conducting studies to enhance their service delivery). The Fund is managed by the SWD.*

Review of lump sum grant subvention system

from \$25,500 to \$841,500. The 11 NGOs are required to submit annual reports on the progress (i.e. whether the project is on or behind schedule) and evaluation of the output/outcome (e.g. the NGO's financial viability to meet the contractual commitment to staff in respect of payroll requirement) of the studies.

6.8 In September 2017, the SWD informed Audit that it is not mandatory for NGOs to adopt the consultants' recommendations as the consultants only provide recommendations for the board of directors and NGO management to decide on the options to be adopted. Furthermore, NGOs are not required to inform the SWD of whether and what follow-up actions (e.g. implementation of recommendations) have been taken on the consultants' recommendations as conducting actuarial studies or related studies is a voluntary facilitating measure.

6.9 To ensure the proper use of the Social Welfare Development Fund and the usefulness of the actuarial studies or related studies, Audit considers that the SWD needs to obtain feedback from all NGOs that have conducted the studies (including the 11 NGOs after their studies have been completed) and promulgate the feedback to NGOs. This would help the conduct of studies in future.

Need to better manage potential conflicts of interest

6.10 Another recommendation of the LSG Independent Review Committee in the 2008 review was that a complaints handling committee should be set up to determine on LSG-related complaints (see para. 33 in Appendix E). In April 2009, the LSG Independent Complaints Handling Committee (see para. 1.27) was established to review complaints (see paras. 1.28 and 1.29 for complaints received).

6.11 The LSG Independent Complaints Handling Committee adopted the following guidelines in the management of conflicts of interest in the handling of LSG-related complaints:

- (a) a "one-tier reporting system" is to be used, whereby when a member (including the Chairman) of the Committee has a potential conflict of interest in a matter placed before the Committee, he/she should make full disclosure of his/her interest;

- (b) potential conflict of interest situations include employment with an organisation which is connected with a matter under consideration by the Committee (Note 47);
- (c) the Chairman shall decide whether the member disclosing an interest may speak or vote on the matter, may remain in the meeting as an observer, or should withdraw from the meeting; and
- (d) all cases of declaration of interests shall be recorded in the minutes of the meeting.

6.12 Having regard to the above guidelines, Audit examined the minutes of the 31 Committee meetings of the LSG Independent Complaints Handling Committee held in the period April 2009 to March 2017 and found that:

- (a) ***Potential conflicts of interest not declared.*** A member of the Committee was the head of a school run by the NGO being complained. During July 2011 to November 2012, 7 complaints relating to the NGO were deliberated at four Committee meetings. Prior to the holding of each of the four meetings, although the member was connected to the NGO, the member declared no potential conflicts of interest in declaration forms (contrary to the SWD's requirement — see para. 6.11(a)). In two of the four meetings, the member had participated in discussions. In one of the meetings, the member had endorsed the results that the complaint was not substantiated. In September 2017, the SWD informed Audit that the member might not have perceived that there was a potential conflict of interest, as education and welfare services under the same NGO were operating separately and independently. Audit considers that the Committee should regularly remind the members to observe the requirement of full disclosure of his/her interests; and

Note 47: *Potential conflict of interest situations include “a directorship, partnership, advisory or client relationship, employment or other significant connection with a company, firm, club, association, union or other organisation which is connected with, or the subject of, a matter under consideration by the committee”.*

Review of lump sum grant subvention system

- (b) ***Decisions not made.*** In 21 of the 31 meetings, Committee members had declared potential conflicts of interest. However, none of the minutes of meetings indicated that the Chairman had made decisions on the declarations as required (see para. 6.11(c)).

6.13 Audit considers that the SWD needs to take measures to improve the management of potential conflicts of interest in the handling of complaints by the LSG Independent Complaints Handling Committee. These measures may include reminding members to observe the Committee's guidelines and documentation of the Chairman's decisions on the declarations (see para. 6.11).

Audit recommendations

6.14 **Audit has *recommended* that the Director of Social Welfare should:**

- (a) **in order to help the conduct of actuarial studies or related studies in future, obtain feedback from all NGOs that have conducted the studies and promulgate the feedback to NGOs; and**
- (b) **take measures to improve the management of potential conflicts of interest in the handling of complaints by the LSG Independent Complaints Handling Committee.**

Response from the Government

6.15 The Director of Social Welfare agrees with the audit recommendations. She has said that the SWD will:

- (a) encourage NGOs to conduct actuarial or related studies and share good practices; and
- (b) facilitate the LSG Independent Complaints Handling Committee to strengthen the reporting of potential conflicts of interest and record the Chairman's decisions in the minutes.

Way forward

6.16 In January 2001, the LSG subvention system was introduced as a major revamp of the provision of funding for NGOs. In 2016-17, some 97% of NGOs had joined the system.

6.17 This Audit Review has identified room for improvement in the administration of LSG subventions by the SWD and in the use of LSG subventions by NGOs, which include:

- (a) ***Financial monitoring.*** While some NGOs had accumulated a large reserve balance, some had incurred LSG operating deficits in consecutive years and depleted their reserves. Individual NGOs are yet to maximise the use of reserves for enhancing the provision of welfare services to the public. NGOs need to properly apportion overheads between FSA activities and non-FSA activities and to improve their internal controls and minimise occurrences of irregularities (see PART 2 of this Audit Report);
- (b) ***Self-assessment of service quality by NGOs.*** There were cases where Output Standards had not been accurately reported by NGOs. There is a need for NGOs to enhance the conducting and reporting of self-assessment of service performance and to ensure compliance with SQSs (see PART 3 of this Audit Report);
- (c) ***Monitoring of service delivery by the SWD.*** There is scope for the SWD to improve the management of the provision of subventions to NGOs based on caseloads attained by them, to ensure that the provision of full subvention to NGOs with persistent underperformance is justified and that the resources of NGOs are properly used, and to enhance the conduct of performance visits and provision of management information to the SWD's directorate (see PART 4 of this Audit Report); and
- (d) ***Governance and management matters.*** NGOs could do better in implementing the BPM guidelines and adopt more good governance practices. Enhanced governance on human resource management would help address the high staff turnovers at individual NGOs (see PART 5 of this Audit Report).

Review of lump sum grant subvention system

6.18 More than eight years have elapsed since the LSG subvention system was last reviewed in 2008 (see para. 6.2). Meanwhile, Audit noted that individual members of the LSG Steering Committee, Members of the LegCo and the welfare sector had from time to time called for another review of the LSG subvention system. Audit considers that it is now an opportune time to conduct a further review to optimise the LSG subvention arrangements. In this regard, in October 2017, the Director of Social Welfare informed Audit that the Government has planned to set up a Task Force to work with stakeholders of the welfare sector to conduct a review on the enhancement of the LSG subvention system.

Audit recommendation

6.19 **Audit has *recommended* that the Director of Social Welfare should, in carrying out the review on the enhancement of the LSG subvention system, take into account the audit findings and recommendations in this Audit Report.**

Response from the Government

6.20 The Director of Social Welfare agrees with the audit recommendation. The Secretary for Labour and Welfare and the Director of Social Welfare have said that the Secretary has tasked the SWD to set up a Task Force to work with stakeholders to conduct a review on the enhancement of the LSG subvention system. The Task Force, comprising members from the LWB, the SWD, NGO management, staff side, service users and independent persons, will oversee and chart the review, including discussion of specific areas in the LSG environment to be covered in the review, the audit findings and recommendations in this Audit Report, examination of specific areas where data collection from the sector is required, and consideration of the findings and recommendations of the review.

Appendix A
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

**Subventions to 165 non-governmental organisations
under lump sum grant subvention system
(2016-17)**

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
1	Tung Wah Group of Hospitals	✓	✓	✓	✓	230	1,120,711,594
*2	Caritas - Hong Kong	✓	✓	✓	✓	157	907,676,811
*3	Po Leung Kuk	✓	✓	✓	✓	146	659,517,041
*4	Hong Kong Sheng Kung Hui Welfare Council Limited	✓	✓	✓	✓	83	621,351,550
*5	The Neighbourhood Advice- Action Council	✓	✓	✓	✓	79	406,986,291
*6	SAHK			✓		62	392,392,094
*7	The Salvation Army	✓	✓	✓	✓	105	370,409,967
*8	Yan Chai Hospital	✓	✓	✓	✓	80	353,289,516
*9	Fu Hong Society			✓		79	324,040,850
*10	Hong Kong Christian Service	✓	✓	✓	✓	75	286,489,446
*11	The Hong Kong Society for the Aged	✓				42	285,931,703
*12	New Life Psychiatric Rehabilitation Association			✓		54	284,526,204
*13	Hong Chi Association			✓		60	256,010,437
*14	Christian Family Service Centre	✓	✓	✓	✓	50	252,804,770
*15	The Boys' and Girls' Clubs Association of Hong Kong		✓	✓	✓	44	249,923,742
*16	Hong Kong Family Welfare Society	✓	✓		✓	27	234,149,032
*17	Hong Kong Lutheran Social Service, the Lutheran Church - Hong Kong Synod Limited	✓	✓	✓	✓	64	232,677,975
*18	Heep Hong Society		✓	✓		58	228,336,608
19	Hong Kong Young Women's Christian Association	✓	✓	✓	✓	49	223,202,091
20	The Hong Kong Federation of Youth Groups		✓	✓	✓	31	211,715,412
*21	The Mental Health Association of Hong Kong			✓		51	207,609,024
*22	Yang Memorial Methodist Social Service	✓	✓	✓	✓	30	204,318,501

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
*23	ELCHK, Social Service Head Office	✓	✓	✓	✓	38	195,129,558
24	Haven of Hope Christian Service	✓	✓	✓		32	192,427,248
25	St. James' Settlement	✓	✓	✓	✓	41	191,719,010
26	Pok Oi Hospital	✓	✓	✓	✓	32	173,554,036
27	Chinese Young Men's Christian Association of Hong Kong	✓		✓	✓	30	166,839,331
*28	Heung Hoi Ching Kok Lin Association	✓				14	165,572,774
*29	Wai Ji Christian Service			✓		39	158,497,507
*30	Hong Kong Children and Youth Services	✓	✓	✓	✓	28	157,753,218
31	Sik Sik Yuen	✓	✓	✓		33	140,100,563
*32	The Hong Kong Society for the Blind			✓		21	124,412,903
*33	The Society of Rehabilitation and Crime Prevention, Hong Kong			✓	✓	15	112,942,256
34	Yan Oi Tong	✓	✓	✓	✓	22	92,060,489
*35	Hong Kong Playground Association				✓	11	91,124,728
*36	Baptist Oi Kwan Social Service	✓	✓	✓	✓	23	80,878,962
*37	International Social Service Hong Kong Branch		✓	✓	✓	28	73,526,384
38	Stewards Limited			✓	✓	17	71,401,343
*39	Aberdeen Kai-fong Welfare Association Social Service Centre	✓			✓	8	66,771,996
*40	The Chinese Rhenish Church Hong Kong Synod	✓	✓	✓	✓	25	63,886,028
41	Alice Ho Miu Ling Nethersole Charity Foundation	✓				2	63,235,468
*42	Helping Hand	✓				10	60,175,488
*43	Richmond Fellowship of Hong Kong			✓		14	54,669,022
*44	Society of Boys' Centres		✓		✓	5	53,413,219
*45	Chi Lin Nunnery	✓				4	50,781,151
46	Hong Kong Society for the Protection of Children		✓	✓		48	49,741,467
47	The Lok Sin Tong Benevolent Society, Kowloon	✓				9	49,621,415

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
*48	Hong Kong Student Aid Society Limited		✓	✓	✓	19	48,302,653
*49	Asia Women's League Limited	✓				9	46,727,161
*50	The Hong Kong Buddhist Association	✓	✓	✓	✓	10	44,545,377
*51	Methodist Epworth Village Community Centre, Social Welfare	✓			✓	6	44,360,566
*52	Sheng Kung Hui St. Christopher's Home Limited		✓			30	42,747,192
*53	The Hong Kong Society for the Deaf			✓		13	38,639,075
*54	Hong Kong PHAB Association	✓		✓	✓	13	37,638,511
55	The Hong Kong Council of Social Service (Note 1)					1	37,406,038
*56	Hong Kong Chinese Women's Club	✓	✓	✓		7	36,243,632
57	The Hong Kong Society for Rehabilitation			✓		4	34,222,100
*58	Scout Association of Hong Kong				✓	3	33,991,730
59	The Yuen Yuen Institute	✓				8	33,971,614
60	The Tsung Tsin Mission of Hong Kong Social Service	✓	✓	✓	✓	18	33,729,557
*61	Chung Shak Hei (Cheung Chau) Home for the Aged Limited	✓				8	33,253,434
*62	The Mongkok Kai-Fong Association Limited	✓			✓	5	33,126,756
*63	Ching Chung Taoist Association of Hong Kong Limited	✓				8	31,884,014
*64	Chung Sing Benevolent Society	✓				8	31,652,142
*65	The Women's Welfare Club (Eastern District) Hong Kong	✓	✓	✓		9	30,824,986
*66	Pentecostal Church of Hong Kong	✓	✓	✓		15	28,667,991
*67	Kiangsu Chekiang and Shanghai Residents (Hong Kong) Association	✓				6	28,195,343
*68	Chuk Lam Ming Tong Limited	✓				4	28,168,116
69	Methodist Centre	✓	✓		✓	4	27,510,400
*70	The Hong Kong Tuberculosis, Chest and Heart Diseases Association	✓				3	27,088,996

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
*71	Yuen Long Town Hall Management Committee Limited	✓	✓		✓	5	26,624,943
72	Fung Kai Public School	✓				5	22,210,110
*73	The Mother Superior of the Congregation of Our Lady of Charity of the Good Shepherd of Angers at Hong Kong		✓		✓	4	20,959,442
74	Association of Baptists for World Evangelism (Hong Kong) Limited	✓	✓		✓	8	20,437,893
*75	The Hong Kong Bodhi Siksa Society Limited	✓				3	19,647,363
76	Christian and Missionary Alliance Church Union Hong Kong Limited	✓	✓	✓		17	17,937,121
*77	Hong Kong Juvenile Care Centre		✓		✓	2	17,854,395
*78	Asbury Methodist Social Service	✓			✓	3	16,154,275
79	The Church of United Brethren in Christ Hong Kong Limited				✓	2	15,735,261
80	Ebenezer School and Home for the Visually Impaired			✓		4	14,835,934
81	The Free Methodist Church of Hong Kong	✓		✓	✓	4	14,662,880
*82	The Hong Kong Catholic Marriage Advisory Council		✓			1	14,438,326
*83	The Kowloon Women's Welfare Club	✓	✓			3	14,155,739
*84	Kwun Tong Methodist Social Service	✓	✓		✓	3	14,135,213
85	Association for Engineering and Medical Volunteer Services	✓		✓		5	14,048,412
*86	Hong Kong and Macau Lutheran Church Social Service Limited	✓				4	14,023,085
*87	The Hong Kong Down Syndrome Association			✓		7	13,757,075
*88	The Superioress of the Sisters of the Precious Blood		✓			2	13,747,200
*89	Hong Kong-Macao Conference of Seventh - Day Adventists	✓			✓	3	13,128,526
90	The Association of Evangelical Free Churches of Hong Kong	✓	✓	✓		12	12,433,142
91	Youth Outreach		✓		✓	3	12,428,495

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
92	The Christian New Being Fellowship Limited				✓	1	11,546,836
93	Hong Kong Evangelical Church Social Service Limited	✓				2	11,452,609
94	Evangelical Free Church of China - Evangel Children's Home		✓			2	11,056,853
*95	The ABM Hong Kong Swatow Baptist Church Community Service Association				✓	2	10,699,900
*96	Tung Lum Nien Fah Tong Limited	✓				3	10,397,938
97	United Christian Nethersole Community Health Service	✓				2	9,366,230
98	The Samaritan Befrienders Hong Kong		✓			2	9,355,427
99	Project Care		✓			7	8,885,988
100	Women's Welfare Club Western District, Hong Kong	✓	✓	✓		9	8,515,009
101	Mother's Choice		✓	✓		3	8,340,997
102	The New Territories Women and Juveniles Welfare Association Limited	✓	✓	✓		11	8,088,120
103	Harmony House Limited		✓			1	7,966,150
104	Zion Social Service Limited				✓	1	7,886,424
105	The Operation Dawn Limited				✓	1	7,731,770
106	Tung Sin Tan Home for the Aged	✓				2	7,673,712
107	Chinese Evangelical Zion Church Limited				✓	1	7,547,322
108	Hong Kong and Kowloon Kaifong Women's Association	✓	✓	✓		12	7,510,160
109	Sai Kung District Community Centre Limited				✓	1	7,364,482
110	International Church of the Foursquare Gospel Hong Kong District Limited	✓				2	7,279,161
111	Hong Kong Christian Mutual Improvement Society	✓				2	6,974,405
112	Hong Kong Mutual Encouragement Association Limited	✓				2	6,933,359
113	The Child Development Centre			✓		1	6,784,281

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
114	New Life Church of Christ Hong Kong Limited	✓				2	6,705,802
115	Fung Ying Seen Koon	✓				2	6,655,423
116	The Barnabas Charitable Service Association Limited				✓	1	6,582,373
117	Hong Kong Red Cross			✓		3	5,653,319
118	Watchdog Limited			✓		1	5,283,459
119	Baptist Mid-Missions	✓	✓	✓		7	5,152,770
120	Lutheran Philip House Limited		✓	✓		9	4,922,216
121	Christian Concern for the Homeless Association		✓			1	4,483,872
122	The Mission Covenant Church Limited	✓		✓		2	4,370,403
123	Suen Mei Speech and Hearing Centre			✓		1	4,106,360
124	Hong Kong Federation of Handicapped Youth			✓		3	4,067,101
125	The Boys' Brigade, Hong Kong				✓	1	3,843,747
126	Hong Kong Blind Union			✓		3	3,749,850
127	Hong Kong Rehabilitation Power			✓		3	3,697,783
128	Kowloon City Baptist Church	✓				1	3,680,129
129	Yuk Chi Resource Centre Limited			✓		1	3,596,082
130	The Lam Tin Estate Kai Fong Welfare Association Limited	✓				1	3,577,278
131	Hong Kong West Point Baptist Church	✓				1	3,559,925
132	Jordan Valley Kaifong Welfare Association	✓				1	3,545,638
133	International Women's League Limited	✓				1	3,541,473
134	China Peniel Missionary Society Incorporation	✓				1	3,519,794
135	Christian Nationals' Evangelism Commission Grace Light Neighbourhood Elderly Centre	✓				1	3,514,777
136	Asian Outreach Hong Kong Limited	✓				1	3,513,391
137	The Endeavourers Hong Kong	✓				1	3,503,375
138	Hop Yat Church, the Church of Christ in China	✓				1	3,490,036

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
139	Hong Kong Women Foundation Limited	✓				1	3,488,140
140	International Buddhist Progress Society (Hong Kong) Limited	✓				1	3,487,649
141	Tsim Sha Tsui District Kaifong Welfare Association	✓				1	3,486,990
142	Light and Love Home Limited	✓				1	3,473,556
143	Agency for Volunteer Service	✓				1	3,452,397
144	Shamshuipo Kai Fong Welfare Advancement Association	✓				1	3,233,498
145	Cheung Chau Rural Committee Integrated Youth Centre				✓	1	3,064,260
146	Tai Hang Residents' Welfare Association				✓	1	2,978,488
147	Hans Andersen Club				✓	1	2,972,352
148	Hong Kong and Macau Regional Centre of the World Fellowship of Buddhists Limited		✓	✓		7	2,793,305
149	Hong Kong Paralympic Committee and Sports Association for the Physically Disabled			✓		1	2,430,092
150	Lok Chi Association Limited			✓		1	2,345,791
151	Hong Kong Federation of the Blind			✓		1	2,320,979
152	The Nesbitt Centre Limited			✓		1	2,298,865
153	Sisters of the Immaculate Heart of Mary		✓	✓		5	2,279,330
154	Sheng Kung Hui St. Simon's Social Services		✓	✓		6	2,256,528
155	Against Child Abuse Limited		✓			1	2,229,487
156	Society for Community Organization				✓	1	2,194,866
157	Hong Kong Sports Association for Persons with Intellectual Disability			✓		1	2,176,193
158	Alice Lan and Vera Shen Education Fund Limited		✓	✓		5	1,877,534
159	Association for the Rights of Industrial Accident Victims Limited			✓		1	1,400,548
160	Five Districts Business Welfare Association		✓	✓		4	1,221,591

Appendix A
(Cont'd)
(paras. 1.4, 1.21, 2.22
and 5.24 refer)

	NGO	Services provided				No. of ASU (see para. 1.21)	LSG subvention (2016-17) (\$)
		Elderly Services	Family and Child Welfare Services	Rehabilitation Services	Youth and Corrections Services		
161	Sheng Kung Hui St. Matthias' Church Nursery School Limited		✓	✓		3	1,213,510
162	Society of St. Vincent de Paul		✓	✓		3	1,021,675
163	Cheung Sha Wan Kai Fong Welfare Association Lam Tam Yin Wah Day Nursery		✓	✓		3	921,831
164	Emmanuel Church			✓		1	671,165
165	First Assembly of God Church		✓			1	79,476 (Note 2)
Total						2,691	12,529,602,042

Source: SWD records

Note 1: Instead of providing welfare services directly to the public, the Hong Kong Council of Social Service plays a coordinating role between the Government and NGOs. It is a representative of NGOs committed to sustaining and developing welfare services in Hong Kong. In July 2017, the Council has 461 NGO members. Of these 461 NGOs, 127 NGOs received LSG subvention in 2016-17.

Note 2: The subvention was granted to a nursery for providing extended hours of child care service.

*Remarks: * denotes the NGOs which were required to submit to the SWD the review reports on remuneration packages for staff in top three tiers in 2015-16 (see para. 2.21).*

Service Quality Standards (31 March 2017)

Principle 1: Provision of information

The purpose and objectives of the service should be clearly defined and its mode of operations transparent for the benefit of staff, existing and potential service users, and the general community.

SQS 1. ***Service information.*** The service unit ensures that a clear description of its purpose, objectives and mode of service delivery is publicly available.

SQS 2. ***Review and update policies and procedures.*** The service unit should review and update the documented policies and procedures, describing how it will approach key service delivery issues.

SQS 3. ***Records.*** The service unit maintains accurate and current records of service operations and activities.

Principle 2: Service management

The service unit should manage its resources effectively and in a manner consistent with flexibility, innovation and continuous improvement in the quality of service delivered to service users.

SQS 4. ***Roles and responsibilities.*** The roles and responsibilities of all staff, managers, the Management Committee and/or the Board or other decision-making bodies should be clearly defined.

SQS 5. ***Human resources.*** The agency/service unit implements effective staff recruitment, contracting, development, training, assessment, deployment and disciplinary practices.

SQS 6. ***Planning, evaluation and feedback.*** The service unit regularly plans, reviews and evaluates its own performance, and has an effective mechanism whereby service users, staff and other interested parties can provide feedback on its performance.

SQS 7. ***Financial management.*** The service unit implements policies and procedures to ensure effective financial management.

SQS 8. ***Legal obligations.*** The service unit complies with all relevant legal obligations.

SQS 9. ***Safe physical environment.*** The service unit takes all reasonable steps to ensure that it provides a safe physical environment for its staff and service users.

Principle 3: Service to users

The service unit should identify and respond to specific service users' needs.

SQS 10. ***Entry and exit.*** The service unit ensures that service users have clear and accurate information about how to enter and leave the service.

SQS 11. ***Needs of service users.*** The service unit has a planned approach to assessing and meeting service users' needs (whether the service user is an individual, family, group or community).

Principle 4: Respect for service users' right

The service unit should respect the rights of the service users in all aspects of service operations and delivery.

SQS 12. ***Informed choices.*** The service unit respects the service users' rights to make informed choices of the service they receive as far as practicable.

SQS 13. ***Private property.*** The service unit respects the service users' rights in relation to private property.

SQS 14. ***Privacy and confidentiality.*** The service unit respects the service users' rights for privacy and confidentiality.

SQS 15. ***Complaints.*** Each service user and staff member is free to raise and have addressed, without fear of retribution, any complaints he or she may have regarding the agency or the service unit.

SQS 16. ***Freedom from abuse.*** The service unit takes all reasonable steps to ensure that service users are free from abuse.

Source: SWD records

Remarks: For each of the 16 SQSs, there is elaboration on how the SQS should be implemented.

Best Practice Manual **(31 March 2017)**

Level One guidelines

Financial management

Management of LSG reserve

1. Maximised use of reserve
 - NGOs are required to ensure that the reserve is fairly, reasonably, properly and effectively used for the intended purposes as stipulated by the SWD.
 - NGOs should maximise the use of the reserve in order to maintain or strengthen service delivery and implement strategic development plans, including building up a staff team with high quality.
2. Status of reserve
 - NGOs are required to, through convenient, effective and timely channels, disseminate information about the LSG reserve in a reader-friendly format to staff members and the public. Such information should include briefly a plan on how the reserve will be used in the future.

Use of PF reserve for non-Snapshot staff

3. Use of reserve
 - NGOs are required to maximise the use of PF reserve for non-Snapshot staff for the designated purpose so as to enhance staff morale and their sense of belonging to the organisations.
4. Status of reserve
 - NGOs are required to use convenient, effective and timely channels to disseminate information about the PF reserve to staff members, including a brief plan on how the PF reserve will be used in the future.

Human resource management

Salary package policy and administration

5. Salary adjustment
 - NGOs are required to spend the subvention for salary adjustment for the designated purpose by making timely adjustment to the salary for all staff members subvented by the LSG.

Corporate governance and accountability

Roles and duties of NGOs in complaints handling

6. Composition, duties and responsibilities on handling complaints at different levels
 - For LSG-related complaints, NGOs are required to develop a sound mechanism and policy to clearly spell out the personnel in handling complaints at different levels and their respective responsibilities and duties at each level.
 - NGOs are required to ensure that all levels of staff involved in complaints handling are free from any conflict of interest.
 - NGOs are required to ensure that both the complainant and the parties being complained against are aware that the complaint concerned is being handled in accordance with the procedures set out by the NGOs/the LSG Independent Complaints Handling Committee.
7. NGOs' policies and procedures on complaints handling
 - For LSG-related complaints, NGOs are required to strictly follow established policies and procedures, as well as the personnel composition to handle the complaints in a fair manner, with appropriate monitoring and appeal/review mechanisms.
 - NGOs are required to comply with the LSG Independent Complaints Handling Committee's complaints handling procedures and requirements in handling the complaints concerned.

Level Two guidelines

Financial management

Management of LSG reserve

1. Optimal level of reserve
 - NGOs should, having regard to their sizes and actual needs, develop planning and evaluation mechanisms on their own to determine the appropriate level of reserve, and monitor it effectively through appropriate years of projection.
 - NGOs should be cautious but not be too conservative or aggressive when estimating the required amount of accumulated LSG reserve.

Corporate governance and accountability

Management Strategies

2. Communication
 - NGOs should establish effective channels of communication between the governing board, the management, staff and service users, to ensure that feedback from staff and service users on LSG-related matters can be received.
3. Term of office of the governing board
 - NGOs should establish a succession mechanism for their governing board members, where there are no such restrictions in relevant legislation or constitution, to ensure the sustainable development of the board.
4. Roles of governing board
 - Regarding LSG-related matters, NGOs should enhance the knowledge of their board members on the NGOs and their SWD-subvented services through various effective and appropriate arrangements so as to strengthen their leading roles.

Responsibilities of the governing board and NGOs' decision making on important management issues of SWD-subvented services under LSG subvention system

5. Delineation of roles and responsibilities of the governing board
 - The roles, responsibilities and membership of the governing board and the relevant committees should be clearly defined and put on record.
 - NGOs should properly delineate the terms of reference between governing board members and senior management.
6. NGOs' decision making on important management issues of SWD-subvented services
 - NGOs should consult their staff and service users on important issues that affect them.
 - According to paragraph 5.6 of the LSG Manual, generally speaking, the NGO's governing board should consult the staff first before there are any changes that may affect them, including:
 - (a) changing the existing establishment structure;
 - (b) changing the remuneration package or the working conditions; and
 - (c) re-engineering and rationalising the service delivery modes, and the corresponding manpower redeployment that may become necessary.
 - According to paragraph 5.8 of the LSG Manual, NGOs should consider involving service users as far as practicable in service re-engineering, changing the existing service delivery mode, and monitoring compliance with service performance standards. Service users' feedback may be obtained through a variety of means such as service user liaison groups, discussions or opinion surveys.

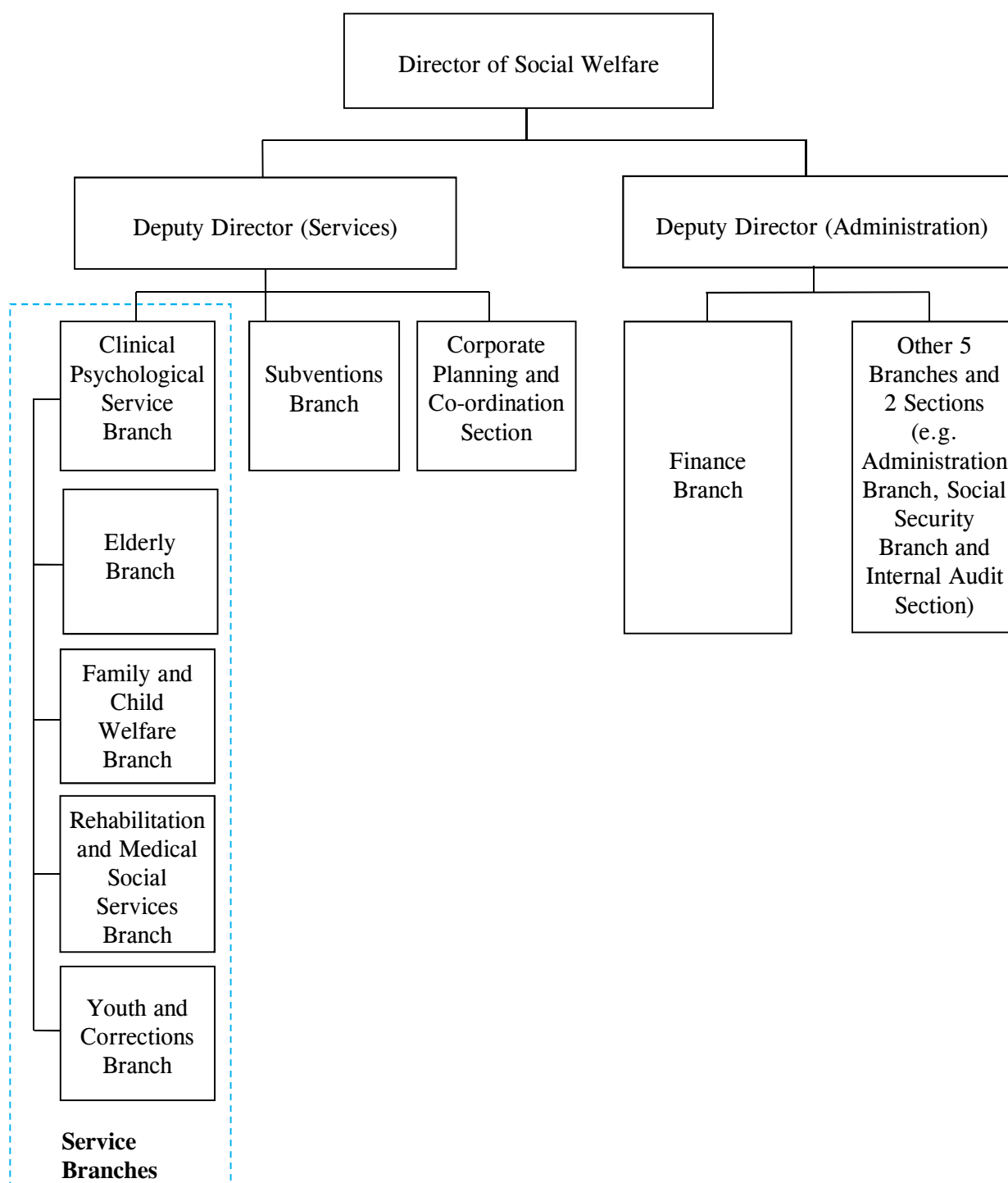
Appendix C
(Cont'd)
(paras. 1.19, 2.6, 2.7
and 5.3 refer)

7. NGO's decisions made on important management issues of SWD-subservated services
- NGOs should disseminate to their staff and services users in a timely manner the decisions made on important management issues related to the LSG subvention system.

Source: SWD records

Remarks: In the BPM, there is further elaboration on how each of the 14 guidelines should be implemented.

**Social Welfare Department
Organisation chart (extract)
(30 June 2017)**



Source: SWD records

**Recommendations of the
Lump Sum Grant Independent Review Committee
(2008)**

Recommendations relating to Staffing Arrangements

1. A Best Practice Manual for NGOs on various management issues such as human resource policies, the level of reserves and their gainful deployment, corporate governance and accountability, etc., should be developed by the welfare sector, with professional input from management experts if necessary. LSG Steering Committee should work with the sector in drawing up this Manual.
2. The Government should make available an actuarial service for NGOs to assess their ability to meet Snapshot Staff commitments. Application for this service should be on a voluntary basis.
3. As a good management practice for NGOs, the additional funding provided in line with civil service salary adjustments should be spent solely on staff in subvented services.
4. In budgeting for non-subvented services, NGOs need to factor in pay adjustments, so that they may be in a better position to meet staff expectations when subvented services receive additional funds for pay adjustments.
5. The SWD should collect data on staff turnover and wastage rates for the purpose of monitoring the sector's overall manpower position. The Government should invite the Advisory Committee on Social Work Training and Manpower Planning to monitor closely the manpower supply in the welfare sector, so as to ensure a stable supply of professional staff.
6. The Government should set up a \$1 billion Social Work Development Fund to support training, capacity enhancement initiatives and service delivery enhancement studies. Grants should be allocated to NGOs on LSG based on the merit of their applications.

**Recommendations relating to Financial Issues and
Interactions between the Government and NGOs**

7. In view of the changing service needs, the Government should institute a review mechanism whereby appropriate advisory bodies such as Social Work Advisory Committee, the Elderly Commission, the Rehabilitation Advisory Committee, etc. may oversee the systematic review of welfare services and ensure that stakeholders' views are taken into account in the review process.
8. In exceptional and justifiable cases, the SWD should allow NGOs to advance the subventions for other charges.
9. In managing their reserves, NGOs should take into account their Snapshot Staff commitments, as well as the need for service enhancement and staff development.
10. The SWD should establish a mechanism whereby NGOs which anticipate financial difficulties can alert SWD in advance, so that remedial measures can be taken as appropriate before the NGOs concerned exhaust their reserves.
11. NGOs should fully deploy the PF provisions and reserves for non-Snapshot Staff on PF contributions, including possibly special contributions to award non-Snapshot Staff for their good performance.
12. Recognising NGOs' achievements in enhancing efficiency and productivity under the Enhanced Productivity Programme / Efficiency Savings, it is recommended that the need for additional funding should only be justified by a systematic review of service needs.
13. The LSG Steering Committee should be reconstituted to strengthen its role and composition, so that it can lead the sector in the continuous development of LSG subvention system.
14. For the sake of transparency, the SWD should be prepared to explain, at the request of individual NGOs, the basis of their LSG calculations.

Appendix E
(Cont'd)
(paras. 6.2, 6.4
and 6.10 refer)

15. The SWD should revise the LSG Manual in consultation with stakeholders, update it regularly, and announce changes on SWD's website in the first instance. NGOs should also be notified instantaneously by email.
16. The SWD should rationalise the Agency Officer system (with an NGO recognised as one agency) with a team of officers who are familiar with the rules and operations of the Subventions, Finance and Service Branches and can provide prompt advice to NGOs on all LSG-related issues. The resources thus released may be redeployed to step up existing work such as quality inspections or implement new initiatives.

Recommendations relating to Flexibility, Efficiency and Cost-effectiveness

17. The SWD should conduct a thorough review of its audit procedures to ensure that they are effective in monitoring the use of public funds and do not compromise NGOs' flexibility under the LSG subvention system.
18. To avoid misunderstanding, NGOs should consult the SWD in a timely manner as to what constitute "Funding and Service Agreement (FSA)-related" activities before conducting such activities.
19. The SWD should streamline its financial reporting requirements, including dropping the requirement for NGOs to provide analyses of incomes and expenditures by programme area and by FSA.
20. The SWD should review the deadline for NGOs to submit their AFRs, taking into account the practicability of the requirement.
21. The SWD should set up a help desk to provide management advice to small NGOs and to facilitate their collaborative efforts. To help small NGOs develop, the SWD should also make available additional resources for them to strengthen their administrative and professional support. Small NGOs may apply for grants up to \$300,000 (or 10% of its LSG, whichever is lower) each year for a total of four years.

Appendix E
(Cont'd)
(paras. 6.2, 6.4
and 6.10 refer)

22. The definition of “small NGOs” should be standardised so that the assistance to them can be more targetted and effective. For this purpose, small NGOs should more appropriately be defined as NGOs with an annual LSG of less than \$5 million and an annual expenditure below \$10 million.
23. Small NGOs may consider submitting joint proposals to enhance their competitiveness in the bidding of new services. While NGOs participating in such joint ventures have to identify a representative to sign the FSA and liaise with SWD, the NGOs should also enter into an agreement among themselves to set out clearly their individual contributions and shared responsibilities.
24. In inviting bids for new services, the SWD should make known to prospective bidders the relative weighting of the various aspects of a proposal in the marking scheme.
25. NGOs should carefully consider their resource implications before preparing service proposals. NGOs should also take into account the views of their staff and share with them the considerations in submitting service proposals.
26. The SWD should look into the possibility of simplifying the process for the allocation of new services, such as introducing a two-stage tendering process, so that resources can be saved both in the preparation of service proposals and in the vetting of the proposals.
27. As per Recommendation 6, a new Social Work Development Fund should be established and should take over the function of the Business Improvement Project Scheme. It is for SWD to consider whether NGOs should still be required to contribute at the present or at a lower level to the projects supported by the new fund.

**Recommendations relating to Accountability and
Corporate Governance of Subvented NGOs**

28. A formal public accountability framework should be in place for NGOs to disclose their AFRs as submitted to the SWD, so that they will also be accountable to the public for the proper and prudent use of public funds.
29. The SWD should fully consult the NGOs with a view to implementing the Government guidelines on the monitoring of remunerations of senior executives in subvented bodies.

Recommendations relating to the Quality of Welfare Services

30. The SWD should conduct more frequent service performance inspections and surprise visits, and systematically collect service users' feedback.
31. The Government, having regard to Social Work Advisory Committee's recommendations, should work more closely in partnership with the sector to establish a practicable and sustainable mechanism for implementing a visionary welfare plan for Hong Kong.

Recommendations relating to the Handling of Complaints

32. Complaints made by service users and staff against subvented NGOs or their service units should be handled, in the first instance, by the NGOs concerned according to their established policy. How their management and governing boards should better perform their respective roles in this regard should be addressed in the sector's Best Practice Manual.
33. An Independent Complaints Handling Committee should be set up to determine on LSG-related complaints that cannot be satisfactorily addressed at the NGO level and recommend improvements to LSG subvention system. The Director of Social Welfare should be informed of Independent Complaints Handling Committee's decisions and recommendations, and should take follow-up actions as appropriate.

Recommendations on Other Related Issues

34. For anonymous complaints, where SWD does not require any feedback from, or investigation by, the NGO, it should make that clear to the NGO to avoid unnecessary work.
35. The SWD should review the Lotteries Fund vetting procedures and funding rules, and consider, inter alia, the following improvements, so as to make better use of Lotteries Fund:
 - (a) increase the agency cap of the Block Grant to 1.5%;
 - (b) for furniture and equipment items, lower the threshold for major grant applications to \$50,000;
 - (c) where a project is carried out under the supervision of Authorised Persons or consultants, the Government should consider placing more reliance on their professional certification to expedite the vetting process; and
 - (d) where a project is proposed to be named after a donor, the SWD may maintain the requirement that the donor makes a contribution of at least 20% of the project cost, but of which only an amount equal to 10% of the project cost will be used to offset the Lotteries Fund grant, while the NGO concerned may use the remainder to upgrade the project.
36. The SWD should, in response to the labour market situation, provide additional resources for three years to welfare NGOs which need to employ paramedical staff or hire their services, so that they may offer more competitive salaries to recruit and retain these staff.

Source: Review report on the LSG subvention system of the LSG Independent Review Committee

Acronyms and abbreviations

AFRs	Annual Financial Reports
ASUs	Agreement service units
Audit	Audit Commission
BPM	Best Practice Manual
ESRs	Essential Service Requirements
FSAs	Funding and Service Agreements
FSTB	Financial Services and the Treasury Bureau
HCS	Home care service for persons with severe disabilities
ICYSCs	Integrated Children and Youth Services Centres
ISS	Integrated support service for persons with severe physical disabilities
LegCo	Legislative Council
LSG	Lump sum grant
LWB	Labour and Welfare Bureau
NGOs	Non-governmental organisations
PF Reserve	Provident Funds Reserve
SQSs	Service Quality Standards
SVP	Special visitation programme
SWD	Social Welfare Department

CHAPTER 2

Marine Department

<p>Procurement and maintenance of government vessels</p>

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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PROCUREMENT AND MAINTENANCE OF GOVERNMENT VESSELS

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PROCUREMENT AND MAINTENANCE OF GOVERNMENT VESSELS

Executive Summary

1. According to the Stores and Procurement Regulations (SPRs), the Marine Department (MD) is the designated endorsement authority and agent for procurement of government vessels. It aims to provide cost-effective marine transport services to government departments. The Government Fleet Division (GFD) of the MD is responsible for the design, procurement and maintenance of government vessels, and managing the Government Dockyard which is the operational and maintenance base of government vessels. As at 31 March 2017, the government fleet comprised 848 vessels under the operational control of 14 government departments. Among the 848 vessels, 115 were mechanised vessels, 72 were high-speed craft and the remaining 661 were smaller size or non-mechanised vessels. New vessels are purchased to maintain or improve the safety and efficient operation of the departments. As at 31 August 2017, there were 28 ongoing projects with funding approval of \$2,653 million for the procurement of 94 new vessels for seven government departments. In 2016-17, the MD spent \$139.4 million on the procurement of maintenance services for the government fleet and \$141.9 million on the procurement of maintenance materials. The Audit Commission (Audit) has recently conducted a review to examine the MD's work on the procurement and maintenance of government vessels with a view to identifying areas for improvement.

Procurement of government vessels

2. The Government New Construction Section (GNCS) under the GFD is responsible for the procurement of government vessels, such as liaising with user departments on their requirements, designing, procuring and supervising the construction of new vessels. According to a GFD Circular of 2008, in planning for the replacement of aged vessels, the GFD would usually conduct condition assessments not more than three years before the expiry of their expected lifespans. Depending on the hull types, the expected lifespans of vessels ranged from 8 to 20 years. The duration for acquiring new vessels generally takes three to five years (paras. 1.6 and 2.2).

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3. ***Ageing of major government vessels.*** Audit analysis revealed that the average ages of the four major classes of government vessels had increased significantly in the past 10 years from 2007 to 2016, i.e. from 12.3 to 16.1 years for major mechanised vessels, from 7.8 to 13.2 years for minor mechanised vessels, from 5.4 to 14.2 years for high-speed craft (large type) and from 10.7 to 13 years for high-speed craft (medium type). As at 31 March 2017, 76 (41%) of 187 mechanised vessels and high-speed craft had served beyond their expected lifespans by 1 to 12 years, up from 33 (18%) of 183 such vessels in March 2012. Timely replacement of aged vessels is important for operational effectiveness and efficiency (paras. 2.3, 2.4 and 2.7).

4. ***Five-year rolling plan/10-year replacement plan not prepared until December 2016.*** According to the GFD Circular of 2008, the GFD would compile a five-year rolling plan on procuring new or replacement government vessels each year. However, the GFD had not done so until December 2016 when it started to work out with major user departments a tentative 10-year vessel replacement plan. According to the MD, the GFD Circular had been under review since its issue in 2008, and setting up a rigid mechanism for replacing government vessels simply according to their expected lifespans might not necessarily serve well the purpose of meeting the operational needs of the user departments. In examining the July 2017 vessel replacement plan provided by the MD, Audit found that only 54 (71%) of the 76 vessels (see para. 3 above) serving beyond their expected lifespans had been included in the replacement plan. For the remaining 22 (29%) vessels not included in the plan, the MD had not conducted condition assessments for 2 vessels (for one year and six years respectively after passing their expected lifespans) and there were inadequate follow-up actions on the condition assessment results for 18 of the other 20 vessels (paras. 2.2, 2.5 and 2.6).

5. ***Slow progress in implementing vessel procurement projects.*** As at 31 August 2017, the MD was managing 25 ongoing procurement projects for 90 vessels of the four major classes (see para. 3 above), eight of which were approved by the Finance Committee (FC) of the Legislative Council and the remaining 17 projects were approved by the Legislative Council in the context of the Appropriation Bill or by the Financial Secretary. Five of the eight FC approved projects could not meet their target dates of vessel delivery (from August 2013 to March 2017). The delays ranged from 5 months to 4 years up to August 2017, with three projects still in tender stage. As a result of the delays, additional commitments totalling \$33.2 million (14% in excess of the approved funding) were required to cater for the increase in construction costs of the 8 vessels involved in four of these

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five projects. For the other 17 projects, seven (involving 19 vessels) were approved before 2013-14. The progress of three projects was particularly slow, i.e. they were still in the tender stage some five years after funding approval. As a result of the delays, additional commitments totalling \$58.77 million (37% in excess of the approved funding) were required to cater for the increase in construction costs of the 19 vessels involved in the seven projects (paras. 2.9 and 2.10). Factors contributing to the delays in implementing vessel procurement projects are summarised in paragraphs 6 to 9 below.

6. *Long time taken to review the marking scheme for tender assessment.* It had been the practice of the MD to use a marking scheme for assessing tenders of a vessel procurement project with value exceeding \$1.43 million. Upon the request of the Central Tender Board (CTB) in December 2009, the MD tasked the GNCS to conduct a review of the tender marking scheme in consultation with relevant parties (e.g. the Department of Justice (DoJ)). In the event, the review was completed in October 2012 when the CTB approved the revised marking scheme. During the almost three-year period from December 2009 to October 2012, 9 projects for the procurement of 29 vessels with total approved funding of \$263.7 million were postponed for periods ranging from 4 months to 2.8 years pending the finalisation of the review. According to the SPRs, departments may consider the use of a marking scheme for tender evaluation where the quality of the service/product to be procured is of paramount importance. There was no record to show that the MD had responded to DoJ's suggestion of December 2010 to review the need for using a marking scheme. It turned out that the GNCS only used marking schemes for 3 projects after the CTB's approval in October 2012. There was also no record of the MD's senior management's monitoring of the GNCS's work on the marking scheme review from 2010 to 2012 (paras. 2.12 to 2.15).

7. *Shortage of Surveyors of Ships (SoSs).* The SoSs in the GNCS play the role of marine engineers and naval architects in the construction of new vessels. However, the MD has been experiencing difficulties in recruiting SoSs since 2007. While the MD had implemented some stop-gap measures in the recruitment exercises (such as relaxation of requirements on language proficiency and granting of incremental credit for working experience) since 2014, the average number of SoSs successfully recruited in each exercise was only 3.2 against the targets of 7 to 10 recruits. For the GNCS, the MD obtained approval to create time-limited SoS posts in 2013 and 2016 to speed up the clearance of vessel procurement project backlog. However, from March 2013 to March 2017, the GNCS continued to carry 1 to 3 SoS vacancies. As a result, the MD informed relevant user departments in

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2013 and 2015 that there would be delays in the vessel procurement projects due to the shortage of SoS grade staff. In 2016, the Steering Committee on Systemic Reform of the MD (Steering Committee) set up by the Transport and Housing Bureau (THB) recommended a grade structure review to address the critical manpower shortage and succession problems of the SoS and Marine Officer grades staff (paras. 1.13 and 2.17 to 2.21).

8. ***Slow progress in outsourcing project management work to clear backlog.*** With the addition of 4 new procurement projects after the approval of the revised marking scheme in October 2012 (see para. 6 above), there were a total of 13 outstanding projects (costing over \$1.43 million each) up to April 2013. As another measure to clear the backlog, the MD obtained funding of \$35.44 million from the THB in October 2013 to engage consultants from 2014-15 to 2016-17 to manage 10 projects for the procurement of 26 vessels. However, up to August 2017, the MD only engaged consultants to assist in the management of 6 procurement projects of 16 vessels. Of the backlog of 13 procurement projects, only 3 had been completed. Of the 10 outstanding projects, 5 were still in the tender stage. Audit considers that the MD needs to expedite action to clear the backlog, including speeding up the outsourcing of project management work to consultants (paras. 2.23, 2.24 and 2.27).

9. ***Discrepancies in tender documents.*** In examining a delayed procurement project for replacing an aged MD vessel, Audit noted that the delay was partly attributable to the discrepancies found between the tender notice and the tender document in relation to the overall length and breadth of the vessel during the tender evaluation process in August 2016. When granting approval to the MD for cancellation of the tender, the Government Logistics Department Tender Board commented that the cancellation could have been avoided had the MD exercised due diligence in the preparation of the tender notice and the tender document. In April 2017, the procurement contract was re-tendered. As a result, the project was delayed by one year when comparing the closing dates of the first tender and the re-tender. There is a need for the MD to step up the checking of the accuracy and consistency of tender documents (paras. 2.28 and 2.29).

10. ***Frequent machine failure of two new vessels.*** In February 2015, two new patrol launches were delivered and formally accepted by the MD after completion of the necessary acceptance tests. During the warranty period from February 2015 to February 2016, defects including abnormal shutdown of the generator set and frequent

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shutdowns of the outboard engines were found in one of the launches. As a result of repair works for the defects, the total downtime of the launch from February 2015 to March 2017 was 196 days (27% of a 2-year period). As for the second launch which also experienced problems with its generator set and one of its outboard engines mainly after the warranty period, its downtime was 22.5 days during the warranty period and 103 days in the year immediately after the warranty period. While the total downtime appeared excessive for new vessels, up to August 2017, the MD had not conducted a review in this regard (paras. 2.33 and 2.35).

Maintenance of government vessels

11. According to its Controlling Officer's Report (COR), the MD aims to provide cost-effective maintenance services to the user departments. Maintenance work includes preventive service and running repair (which is corrective in nature). The MD has outsourced most of the vessel maintenance work (over 90% in terms of contract value). The Maintenance Section of the GFD is responsible for administering the maintenance contracts and providing in-house maintenance service such as urgent minor repairs. An on-line computerised information system, known as the Government Fleet Information System (GFIS), is employed to coordinate the maintenance activities and support services (paras. 1.9 to 1.11 and 3.2).

12. *Vessel availability rate on a decreasing trend.* The MD's work on the maintenance of government vessels is important to support the work of various user departments, especially the disciplined services departments in carrying out law enforcement and emergency duties. The MD has set a performance target at 87% in its COR to monitor the availability of government vessels to all users. Audit's examination revealed that the vessel availability rates as reported by the MD decreased from 88.8% in 2007 to 86.1% in 2016. For three years in 2009, 2015 and 2016, the availability rates were below the target of 87%, ranging from 86.1% to 86.4% (para. 3.3).

13. *Inadequacies in reporting vessel availability rates.* While the MD stated in its COR that the target vessel availability rate was set for all users, Audit found that the reported availability rates in fact only covered two of four major classes of government vessels (i.e. major mechanised vessel and high-speed craft (large type)). Audit also found that the downtime for repair carried out outside the Government Dockyard was not taken into account in the calculation of the availability rates as the MD considered that the vessels in such cases were still under the control and operation

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of the user departments. The current practice of calculating and reporting the vessel availability rate without any explanatory note may cause misunderstanding to users of the COR. In Audit's view, the MD needs to consult relevant stakeholders (including user departments and the THB) in this regard (paras. 3.5 and 3.6).

14. ***Increase in downtime of major government vessels.*** From 2012 to 2016, the total downtime of four major classes of government vessels due to preventive service and running repair increased from 6,583 days by 24.6% to 8,201 days, while the total number of such vessels only increased from 183 by 2.2% to 187. The average downtime per vessel had increased from 36 days in 2012 by 22% to 44 days in 2016. While the main reason for the increase in downtime was the ageing problem of the government fleet, Audit has found room for improvement in managing the preventive service and running repair (paras. 3.7 to 3.9):

- (a) ***Preventive maintenance scheduling.*** At the beginning of each year, the MD provides a preventive maintenance schedule to each user department showing the budgeted downtime of each of the specified vessels in the schedule. The scope of maintenance work is drawn up based on the defect list provided by the user department and the MD's pre-docking inspections of the vessels concerned. Based on the MD's records, the total extra downtime (i.e. actual maintenance downtime exceeding budget) increased by sevenfold from 55 days in 2012 to 457 days in 2016. Extra downtime is disruptive to the normal operation of the user departments and should be minimised as far as possible. The MD needs to look into the contributing factors (such as extra work not covered in service contracts and waiting time for spare parts) to see whether there is room for improvement (paras. 3.10 to 3.12); and
- (b) ***Running repair.*** While the MD has put in place procedures for monitoring the downtime for running repair, there is also a need to review running repair cases occurring shortly after preventive service to see if there are lessons to be learnt. Based on the MD's records as at 25 July 2017, there were five such repair cases, including a case whereby a high-speed craft sustained serious flooding of the engine within two months after receiving preventive service (para. 3.13).

15. ***Need to enhance competition in the procurement of maintenance services.*** The MD lets out its maintenance contracts by either term contracts (for providing

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specific types of maintenance service such as engine maintenance) or one-off contracts (for providing preventive service of a particular vessel or small-scale urgent repair service). In 2016-17, the MD had 33 term contracts at a total estimated contract value of \$29.1 million all awarded by quotations. Among the 33 term contracts, Audit noted that 23 (70%) were each awarded to the only bidder, indicating that there had been limited competition in the procurement exercises. There is a need to explore measures to make the contracts more attractive to potential bidders (paras. 3.15 and 3.18):

- (a) ***Measures taken to lengthen the duration of one-year term contract.*** Of the 33 term contracts in 2016-17, 16 (48%) were one-year contracts (for 3 consecutive terms in 15 cases and for 2 consecutive terms in one case). Audit noted that the MD had commenced a review of the term contracts' duration since January 2017. Up to August 2017, 21 out of 25 term contracts had been awarded with a two-year term. Among these 21 two-year term contracts, 8 were one-year contracts, 5 were 1.5-year contracts and 8 were 2-year contracts in their respective preceding terms (para. 3.19); and
- (b) ***Need to consider bundling of similar services in a single contract.*** Audit examination of the 16 one-year term contracts in 2016-17 (see (a) above) revealed that 9 (56%) contracts were for providing related services, e.g. 6 contracts were for the repair and maintenance of engines of police vessels/speed craft. Audit noted that these 9 contracts were of small values, ranging from \$0.49 million to \$1.4 million. The MD needs to consider bundling related maintenance services into reasonably sizeable contracts to reduce the cost of contract administration and make them more attractive to potential bidders (para. 3.20).

Management of maintenance materials

16. ***Need to take timely follow-up action on obsolete/dormant stocks.*** The MD spent, on average, \$132.2 million a year on procuring maintenance materials. As at 31 March 2017, the value of some 17,000 stock items of maintenance materials was \$274 million. After a stock review in July 2013, the Supplies Services Unit (SSU) of the Finance Section identified 8,023 items of slow-moving stock (i.e. those without movement for over five years). In April 2015, the SSU indicated that it intended to review the 8,023 slow-moving items by phases. In July 2016, 68 of 547 items covered in the first phase review were disposed of. According to the MD, follow-up action

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on the remaining 7,476 (8,023 less 547) items could only be taken starting from January 2017 because there was a need to prioritise reform work of the GFD and the need to identify expertise to undertake the task. However, the delay of some 4 years before taking follow-up action on such items is unsatisfactory as any obsolete/dormant stock could not be disposed of in a timely manner to save storage space and realise any resalable value where commercial disposal is applicable. Moreover, with the lapse of time, the slow-moving stock had increased to 8,412 items (5% up from 8,023 in 2013) with a total value of \$73 million as of June 2017 (34% up from \$54.6 million in 2013) (paras. 4.2, 4.3 and 4.5 to 4.8).

17. ***Deficiencies of the GFIS for stock management purposes.*** Notwithstanding the system enhancements in 1999 and 2015, some intended benefits of the GFIS could not be realised. For example, the re-order levels generated by the GFIS could not fully reflect the current stock replenishment practice of the Government Dockyard. Moreover, while the GFIS could generate barcodes for inventory items in the Government Dockyard stores, Audit found that they could not be used to automate the stock management operations (para. 4.10).

18. ***Management of dangerous goods in the Government Dockyard.*** In the course of repairing or maintaining government vessels in the Government Dockyard, the MD's in-house staff and contractors are required to handle dangerous goods (such as diesel and petrol, oxygen and acetylene gas cylinders, and paints and thinner) controlled under the Dangerous Goods Ordinance (Cap. 295). While the provisions of the Ordinance do not apply to the Government, the MD is committed to minimising potential hazards and risks, and ensuring that all its staff and workers work in a safe and healthy environment (paras. 4.1 and 4.14). Audit examination revealed the following issues in the management of dangerous goods in the Government Dockyard:

- (a) ***Handling of diesel and petrol.*** According to the MD, while user departments had been advised to keep the quantity of fuel in a vessel to the minimum before it entered the Government Dockyard for service, there might be practical difficulties to do so for vessels returning for unscheduled running repairs or vessels of the law enforcement agencies which needed to carry certain quantities of fuels for operational reasons. In 2016, the fuel tanks of 39 petrol-fuelled vessels arriving at the Government Dockyard for maintenance/repair were 68% full on average. As a result, the Government Dockyard had to handle large quantity of petrol unloaded from these vessels. According to the MD's consultancy study of 2016-17, there

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was a long travelling distance for the transfer of fuels from the defueling area to the designated dangerous goods stores. Manual handling of fuels further increased the possibility of accidents (paras. 4.17(a) and 4.18(a));

- (b) ***Storage of oxygen and acetylene cylinders.*** According to GFD (Government Dockyard) Safety Management Manual, maintenance contractors (which bring along their own oxygen and acetylene cylinders to the Government Dockyard for welding and cutting of metal) should keep their number of gas cylinders at a minimum and keep excessive gas cylinders in the specified dangerous goods stores. However, Audit found that the MD had not tracked the quantities of oxygen and acetylene cylinders stored/used by the maintenance contractors in the Government Dockyard. According to the MD's 2016-17 consultancy study, gas cylinders were not returned to the designated stores after daily operation due to the long distance from the boat repair sheds. Audit inspections in August 2017 revealed that such practice had continued (paras. 4.14(b), 4.17(b) and 4.18(b)); and
- (c) ***Storage of paints and thinner.*** According to the MD's 2016-17 consultancy study, the long distance from the boat repair sheds also discouraged the return of unused paints and thinner to the designated dangerous goods stores after daily operation. Audit examination revealed that on 5 occasions in 2017, paints of 399 to 579 litres and thinner of 65 to 124 litres were issued to the maintenance contractors for painting work of 5 vessels. According to the MD, the entire painting operation might take about 10 days depending on various factors such as vessel size, weather and humidity. There was no record to show that the unused paints/thinner had been returned to the dangerous goods stores after daily operation (paras. 4.17(c) and 4.18(c)).

In March 2017 the MD engaged another consultant to provide advice on how the Government Dockyard could better manage the dangerous goods to meet both its operational needs and the requirements of the Dangerous Goods Ordinance. While waiting for the completion of the study in 2018, the MD needs to implement additional interim measures to minimise the safety hazards (paras. 4.19 and 4.20).

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Audit recommendations

19. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Director of Marine should:**

- (a) improve the overall planning for the procurement of new and replacement government vessels (para. 2.36(a));**
- (b) sustain the improvement measures taken in monitoring the GFD's work to ensure the timely delivery of vessel procurement projects (para. 2.36(b));**
- (c) expedite action to clear the backlog of vessel procurement projects, including implementing the Steering Committee's recommendations in addressing the manpower shortage and succession problems of SoS grade staff (para. 2.36(c));**
- (d) step up the checking of the accuracy and consistency of tender documents (para. 2.36(d));**
- (e) closely monitor the decreasing trend in vessel availability rates and take effective measures to achieve the target rate of 87% (para. 3.26(a));**
- (f) explore if there are better ways to report vessel availability rates in the COR (para. 3.26(b));**
- (g) closely monitor the increasing trend in downtime and take effective measures to minimise the extra downtime for preventive service (para. 3.26(c));**
- (h) continue to enhance competition in the procurement exercises of vessel maintenance services (para. 3.26(e));**
- (i) step up stock review to identify slow-moving stock items and take timely follow-up actions to dispose of any obsolete/dormant stock (para. 4.12(a)); and**

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- (j) **implement additional interim measures to minimise the safety hazards in the Government Dockyard (para. 4.21(b)).**

Response from the Government

- 20. The Government agrees with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 Hong Kong has a sheltered natural harbour which provides good access and a safe haven for vessels calling at the port. The Marine Department (MD), under the policy directives of the Transport and Housing Bureau (THB) and headed by the Director of Marine, is responsible for all navigational matters in Hong Kong and the safety standards of all classes and types of vessels.

1.3 According to the Stores and Procurement Regulations (SPRs), the MD is the designated endorsement authority and agent for procurement of government vessels. The MD aims to provide cost-effective marine transport services to government departments. In 2016-17, the MD incurred expenditure of \$562.3 million (Note 1) on the management of the government fleet which involved:

- (a) coordinating the procurement of new government vessels and monitoring their construction and commissioning;
- (b) performing planned and unplanned maintenance of government vessels; and
- (c) operating its crewed fleet and providing marine transport services to other government departments.

1.4 The MD is organised into five divisions and an Administration Branch with an establishment of 1,411 staff as at 31 March 2017 (see Appendix A for an extract of the MD's organisation chart). The Government Fleet Division (GFD) is responsible for the design, procurement and maintenance of government vessels. The GFD manages the Government Dockyard which occupies a site of 9.8 hectares on

Note 1: *This included, among other things, the capital costs of vessels acquired by the MD but not those acquired by other user departments at their own costs.*

Introduction

Stonecutters Island (including an 8.3-hectare protected water basin) and serves as the operational and maintenance base of government vessels (Note 2).

Government fleet

1.5 As at 31 March 2017, the government fleet comprised 848 vessels of different types, power ratings, speeds and sizes under the operational control of 14 government departments (see Appendix B), which were all maintained by the MD. Of these vessels, the MD managed 58 vessels for its port operations and for serving other government departments which did not have their own fleets (Note 3). The 848 government vessels comprised 94 major mechanised vessels, 21 minor mechanised vessels, 72 high-speed craft and 661 smaller size or non-mechanised vessels (e.g. lighters, beach craft/rafts, dinghies and inflatable boats). The 94 major mechanised vessels were operated in the following manner:

- (a) 25 vessels were manned and operated by MD crew staff. These vessels were used for supporting the MD's operations and meeting the marine transport needs of other departments which did not have their own fleets;
- (b) 16 vessels were under the operational control of 6 government departments (e.g. the Immigration Department (ImmD) and Department of Health) but their crews were provided and managed by the MD; and
- (c) 53 vessels were manned and operated by the staff of the departments concerned (e.g. the purpose-built vessels of the Hong Kong Police Force (HKPF) and Fire Services Department (FSD)).

The government vessels are essential for the safe and efficient operation of the 14 departments. Photographs 1(a) to (f) show some examples of the government vessels.

Note 2: *The dockyard has 10 docking covered sheds, four movable canopies and 30 open-yard docking spaces for repair and maintenance of vessels. The dockyard also has a ship-lift system and three ship travel hoists capable of dry-docking vessels of up to 750 tonnes.*

Note 3: *These vessels included patrol launches, purposely built conveyance launches, pontoons and some specialised vessels such as hydrographic survey launches and explosive carriers.*

Photographs 1(a) to (f)

Examples of government vessels

<p>(a) Major mechanised fireboat of the FSD</p> 	<p>(b) Minor mechanised vessel of the Agriculture, Fisheries and Conservation Department</p> 
<p>(c) High-speed craft (large type) of the HKPF</p> 	<p>(d) High-speed craft (medium type) of the HKPF</p> 
<p>(e) Lighter of the MD</p> 	<p>(f) Beach craft of the Leisure and Cultural Services Department</p> 

Source: MD records

Procurement of government vessels

1.6 The Government New Construction Section (GNCS) under the GFD (see Appendix A) is responsible for the procurement of vessels for government departments, such as liaising with user departments on their requirements on new vessels, designing, procuring, and supervising the construction of new vessels. As of March 2017, the Section had an establishment of 11 staff, mainly of the Surveyor of Ships (SoS) grade and the Ship Inspector grade (Note 4).

1.7 The procurement process of a government vessel mainly comprises three stages:

- (a) **Planning.** The GNCS discusses and finalises with a user department its proposed requirements, carries out a feasibility study, preliminary design and market research, and prepares a paper with budgetary estimates and recurrent cost consequences for consideration by the Standing Committee on Government Craft (SCOGC — Note 5). After endorsement by the SCOGC, the user department seeks approval of funds from the appropriate authority (e.g. the Finance Committee (FC) of the Legislative Council);
- (b) **Tendering and contract award.** After securing funding, the GNCS finalises the technical specifications, compiles tender documents and invites tenders (Note 6). A tender assessment panel will examine tender submissions and

Note 4: *There were 4 SoS grade staff (also see Table 5 of para. 2.20), 6 Ship Inspector grade staff and 1 Senior Clerical Officer.*

Note 5: *The SCOGC advises government departments on vessel procurement matters to ensure cost-effectiveness. Chaired by the Assistant Director of Marine (Government Fleet), its members include officers from different sections of the GFD.*

Note 6: *According to the SPRs, tender procedures shall be used for the procurement of stores and services exceeding the financial limit of \$1.43 million while quotation procedures may be used for procurement within \$1.43 million (with the exception of consultancy services and services for construction and engineering works which are subject to different financial limits), e.g. obtaining at least five written quotations for purchases with a value over \$50,000.*

make recommendations to the relevant authorities (Note 7) for the award of contracts; and

- (c) ***Delivery and deployment.*** Upon the award of a contract, the GNCS will monitor the shipbuilding contractor for the construction and delivery of the new vessel, arrange acceptance tests and sea trial, and distribute the vessel to the user department.

1.8 In 2013, the MD obtained funding of \$35.44 million from the THB to engage consultants to manage 10 new vessel procurement projects. The need for outsourcing some of the project management work arose from a major review of the tender marking scheme conducted from December 2009 to October 2012 during which time all vessel procurement projects by way of tender (i.e. those costing more than \$1.43 million — see Note 6 to para. 1.7(b)) and using marking scheme were held up (see paras. 2.12 and 2.13).

Maintenance of government vessels

1.9 The Maintenance Section (MS) of the GFD (see Appendix A) is responsible for maintaining the 848 government vessels (see para. 1.5). As of March 2017, the Section had an establishment of 106 staff (Note 8).

1.10 According to the MD, inspection and maintenance work required to be carried out on government vessels can be generally classified as follows:

Note 7: *According to the SPRs, the approving authorities of tenders are: (a) the Departmental Tender Committee for procurement (except works) not exceeding \$5 million; (b) the Government Logistics Department Tender Board for procurement of stores/services (non-works)/revenue contracts not exceeding \$30 million (\$15 million prior to July 2017); (c) Public Works Tender Board for procurement of works and related services not exceeding \$100 million; and (d) the Central Tender Board for procurement of all tenders exceeding the financial limits of the above tender committee/boards.*

Note 8: *There were 3 SoS grade staff, 14 Ship Inspector grade staff, 10 Mechanical Inspector grade staff, 6 Electrical Inspector grade staff, 14 Works Supervisors, 13 Senior Artisans, 43 Artisans, 1 Air-conditioning Inspector and 2 Clerical Assistants.*

Introduction

- (a) ***Pre-docking inspection.*** It is conducted on mechanised vessels and speed craft to identify whether there are major maintenance items that need to be followed up in the coming preventive service (see item (b) below);
- (b) ***Preventive service.*** It is a scheduled maintenance service for a government vessel conducted in suitable intervals in accordance with the operating mode and conditions of the vessel. For a more comprehensive maintenance/repair, a vessel is usually lifted on a dry-dock for an overall inspection, repair and other necessary maintenance services; and
- (c) ***Running repair.*** It is corrective in nature and is carried out for a vessel under emergency condition or after an accident to bring it back to a safe and operative condition for the user department.

1.11 The MD has outsourced most of the vessel maintenance work (over 90% in terms of contract value — Note 9). Staff of the MS administer the maintenance contracts, monitor the progress and standard of the contractors' work, and carry out necessary inspection and testing prior to the delivery of repaired vessels to relevant user departments. The MD stocks maintenance materials at the stores of the Government Dockyard and supplies such materials to its contractors and in-house staff for carrying out maintenance and repair work. To maximise maintenance efficiency and vessel availability, an on-line computerised information system, known as the Government Fleet Information System (GFIS), is employed to coordinate the maintenance activities and support services.

Expenditure on procurement and maintenance of government vessels

1.12 As at 31 August 2017, there were 28 ongoing projects with funding approval of \$2,653 million for the procurement of 94 new vessels (Note 10) for seven government departments. In 2016-17, the MD spent \$139.4 million on the

Note 9: *The remaining in-house vessel maintenance work is mainly related to workshop jobs and minor urgent repairs. The MD has estimated the notional contract value of the in-house maintenance work by reference to the costs of labour and materials involved.*

Note 10: *The 94 vessels comprised 49 mechanised vessels, 41 speed craft, 3 mechanised inflatable boats and 1 lighter.*

procurement of maintenance services for the government fleet and \$141.9 million on the procurement of maintenance materials.

Reform of the MD

1.13 In response to the call for a systemic change in the MD by the Commission of Inquiry into the collision of two passenger vessels near Lamma Island in October 2012, the THB in May 2013 set up the Steering Committee on Systemic Reform of the MD (hereinafter referred to as the Steering Committee — Note 11) to advise and steer the Director of Marine to undertake a comprehensive systemic review (Note 12) and reform of the MD. A Task Force on Reform (Note 13) had been set up in the MD to support the work of the Steering Committee and to assist the Director of Marine to take forward the Committee's recommendations.

1.14 The Task Force on Reform, with the assistance of the Efficiency Unit, had conducted a two-phased organisational review between August 2013 and January 2015 to improve the MD's regulatory functions and business procedures on ship safety and navigational safety. After completion of the review, the MD started to review the operations of the GFD, which took up over 40% of both the manpower and resources of the department, with focus on financial controls and arrangements on procurement of government vessels. Accordingly, the Director of Marine had changed the reporting line of the GNCS to the Deputy Director of Marine (Special Duties) with effect from December 2015 to achieve better synergy in reviewing the actual workload and implementing various improvement proposals more efficiently and effectively. In early 2016, the reviews on the GNCS and MS commenced and additional resources were obtained for the GNCS to expedite the procurement process (see para. 2.19).

Note 11: *The Steering Committee was led by the Secretary for Transport and Housing and two lay members who had extensive administrative and management experience.*

Note 12: *The systemic review focused on three areas, namely: (a) operational issues such as safety standards and work practices; (b) manpower strategy and training; and (c) organisational structure and operational work process of the MD.*

Note 13: *The Task Force is headed by an Administrative Officer Staff Grade B (designated as Deputy Director of Marine (Special Duties)) and underpinned by a Senior Principal Executive Officer, an Assistant Director of Marine and a team of 19 non-directorate staff to provide professional and administrative support.*

Introduction

In July 2016, the whole GFD was put under the Deputy Director of Marine (Special Duties)'s purview to strengthen management oversight.

1.15 On manpower strategy and training matters, the Steering Committee noted that there were persistent manpower shortage and succession problems in the Marine Officer and SoS grades (Note 14). Despite the fact that the MD had implemented a series of stop-gap measures (see para. 2.19) to address the acute recruitment difficulties and manpower shortage of the two professional grades over the past few years, these measures were inadequate to resolve the manpower and succession problems of the two grades (see paras. 2.20 and 2.21). On the advice of the Steering Committee, the MD had been exploring ways to resolve the manpower problem of the two professional grades. In 2014, the MD commissioned a consultant to study how maritime authorities overseas tackled their recruitment and succession problems. In the light of the findings of the consultant, the Steering Committee strongly supported the creation of a new training or assistant rank through the conduct of a grade structure review for the two professional grades to offer long-term solutions to its manpower and succession problems. In May 2016, the MD sought the support of the Civil Service Bureau for the conduct of a grade structure review. On the invitation of the Civil Service Bureau in December 2016, the Standing Commission on Civil Service Salaries and Conditions of Service agreed to undertake the grade structure review and advised the MD to make a submission in this regard. In February 2017, the MD submitted its proposal for the grade structure review to the Standing Commission for its consideration.

Audit review

1.16 In 2006, the Audit Commission (Audit) completed a review of “Management of the government fleet”, the results of which were reported in Chapter 4 of the Director of Audit's Report No. 46 of March 2006. In April 2017, Audit commenced a review on the procurement and maintenance of government vessels by the MD, focusing on:

Note 14: *The two core professional grades in the MD are responsible for discharging the statutory functions relating to all navigational matters in the waters of Hong Kong and the safety standards of all classes and types of vessels. In the GNCS, the SoSs are responsible for the procurement of new vessels (see para. 2.17).*

- (a) procurement of government vessels (PART 2);
- (b) maintenance of government vessels (PART 3); and
- (c) management of maintenance materials (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

General response from the Government

1.17 The Secretary for Transport and Housing welcomes Audit's study into the procurement and maintenance of government vessels and agrees with the audit observations and recommendations. The Director of Marine also agrees with the audit recommendations.

1.18 The Director of Government Logistics has said that the Government Logistics Department (GLD) would stand ready to offer advice to the MD on its procurement and supply operations.

Acknowledgement

1.19 Audit would like to acknowledge with gratitude the assistance and full cooperation of the staff of the MD, GLD, HKPF and FSD during the course of the audit review.

PART 2: PROCUREMENT OF GOVERNMENT VESSELS

2.1 This PART examines the MD's work on the procurement of government vessels, focusing on the following issues:

- (a) planning for the procurement of new and replacement government vessels (paras. 2.2 to 2.8);
- (b) slow progress in implementing vessel procurement projects (paras. 2.9 to 2.32); and
- (c) frequent machine failure of two new vessels (paras. 2.33 to 2.35).

Planning for the procurement of new and replacement government vessels

2.2 The GFD is responsible for maintaining efficient marine transport services for all government departments. According to GFD Circular No. 10/2008 of 2008, the GFD would routinely examine the cost-effectiveness of existing government fleet, plan ahead for their replacement with new vessels and also liaise with user departments on any of their new requirements as follows:

- (a) ***Replacement of aged vessels.*** To plan for replacement, the GFD would carry out regular reviews to identify any existing vessel within three to five years from the end of its expected lifespan due for replacement (see Table 1). Usually not more than three years before the expiry of the expected lifespan, the MS (see para. 1.9) would arrange to compile a condition assessment report which included information on: (i) an assessment of the physical condition of the concerned vessel (covering its hull, machinery and electrical equipment) and the rectification required for the safe operation in its remaining lifespan; (ii) an evaluation of the average annual maintenance cost of the vessel for its remaining operating life; and (iii) an estimation of the average annual maintenance cost of a replacement vessel. The MS was tasked to advise user departments regarding the proposals on vessel replacement plan based on the information from the condition assessment reports;

Table 1**Expected lifespan of vessels of different hull types**

Hull type	Expected lifespan (Year)
Steel	20
Aluminum	15
Glass-reinforced plastic	15
Rubber	8

Source: MD records

- (b) ***Procurement of new vessels.*** User departments would be required to submit full justifications for acquiring new vessel(s) for their operational needs to the GNCS with the support endorsement of their respective policy bureaux. The GNCS would follow up on the necessary action in liaison with the user department concerned on the intended procurement of new vessel(s). The MS was required to give an estimate for the average annual maintenance cost of the new vessel(s); and
- (c) ***Five-year rolling plan.*** The GFD would compile a five-year rolling plan on procuring new or replacement government vessels for submission to the SCOGC in April or May each year for its consideration.

The duration for acquiring new vessels generally takes three to five years.

Ageing of major government vessels

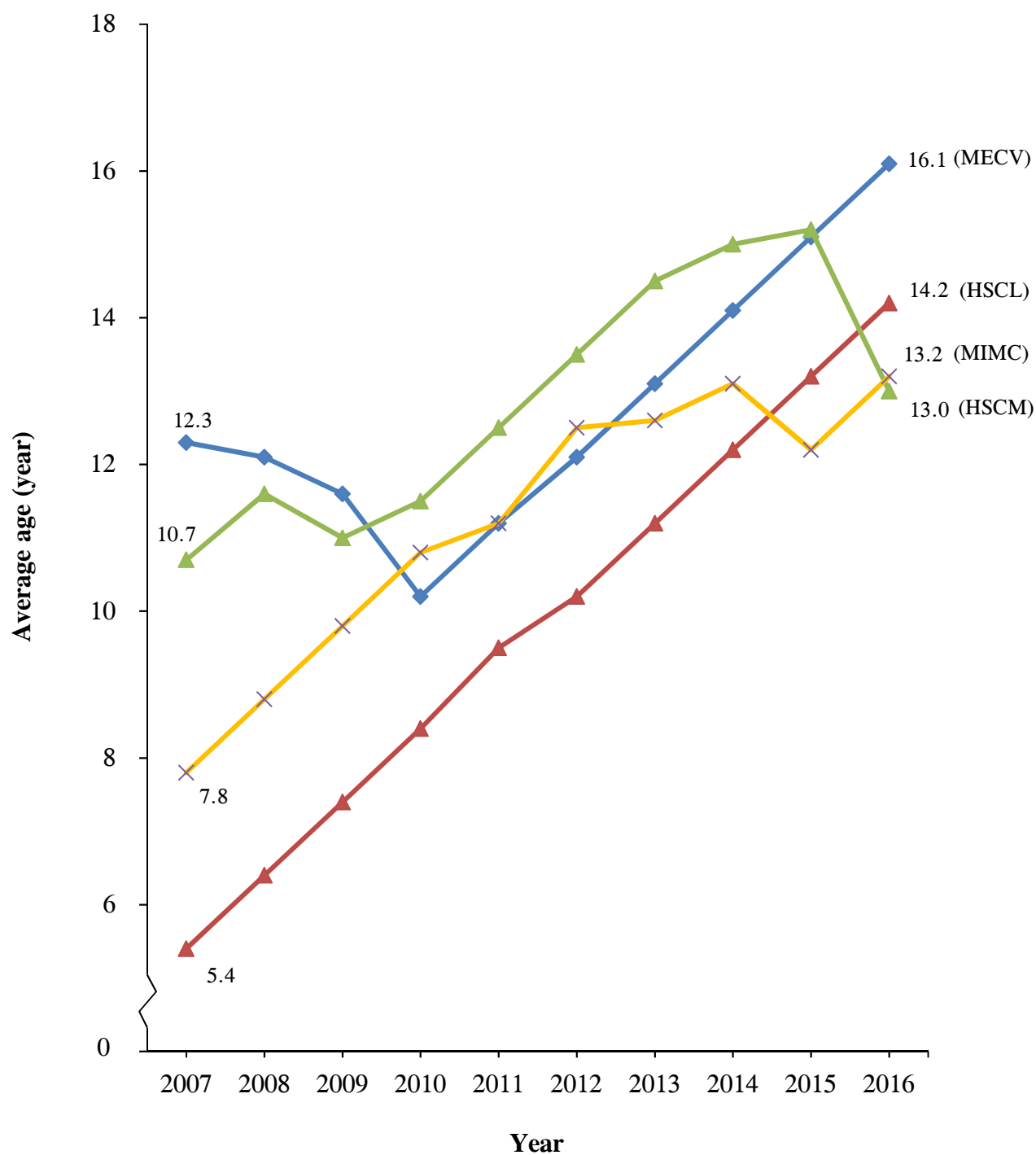
2.3 Audit analysis revealed that the average ages of four major classes of government vessels (Note 15) in service had increased significantly in the past 10 years from 2007 to 2016 (see Figure 1) as follows:

- (a) ***Major mechanised vessel (MECV).*** The average age of MECVs increased by 30.9% from 12.3 years in 2007 to 16.1 years in 2016. As at 31 March 2017, there were 94 MECVs, of which 42 were steel hulled with expected lifespan of 20 years and 52 were aluminum or glass-reinforced plastic hulled with expected lifespan of 15 years;
- (b) ***Minor mechanised vessel (MIMC).*** The average age of MIMCs increased by 69.2% from 7.8 years in 2007 to 13.2 years in 2016. As at 31 March 2017, there were 21 MIMCs and all of which were aluminum or glass-reinforced plastic hulled with expected lifespan of 15 years;
- (c) ***High-speed craft (large type — HSCL).*** The average age of HSCLs increased by 163% from 5.4 years in 2007 to 14.2 years in 2016. As at 31 March 2017, there were 13 HSCLs and all of which were aluminum or glass-reinforced plastic hulled with expected lifespan of 15 years; and
- (d) ***High-speed craft (medium type — HSCM).*** The average age of HSCMs increased by 21.5% from 10.7 years in 2007 to 13 years in 2016. As at 31 March 2017, there were 59 HSCMs and all of which were aluminum or glass-reinforced plastic hulled with expected lifespan of 15 years.

Note 15: *According to the MD, these four classes of vessels would incur higher maintenance expenditure and need closer monitoring and attention.*

Figure 1

Average ages of four major classes of vessels in the government fleet
(2007 to 2016)



Source: Audit analysis of MD records

Operation of major government vessels beyond their expected lifespans

2.4 Audit further analysed the ages of the four major classes of vessels against their expected lifespans. Audit found that of the 187 mechanised vessels and high-speed craft in service as at 31 March 2017, 76 (41 %) vessels had exceeded their expected lifespans by 1 to 12 years (see Table 2). Comparing with the position in March 2012 when only 33 (18%) of 183 such vessels were operating beyond their expected lifespans, the situation had deteriorated.

Table 2

**Analysis of major government vessels
serving beyond their expected lifespans
(31 March 2017)**

Service year beyond expected lifespan (Year)	Vessel class				Total (Number)
	MECV	MIMC	HSCL	HSCM	
	(Number)				
1 to <5	25	2	4	12	43
5 to 12 (Note)	13	6	0	14	33
Total	38	8	4	26	76

Source: Audit analysis of MD records

Note: The average number of service year beyond expected lifespan was 7.4 years.

Five-year rolling plan/10-year replacement plan not prepared until December 2016

2.5 In response to Audit's requests for examining the five-year rolling plans specified in GFD Circular No. 10/2008 (see para. 2.2), the MD in August and September 2017 said that:

- (a) since the issuance of GFD Circular No. 10/2008 in 2008, its application had been under review. Setting up a rigid mechanism for replacing government vessels simply according to their expected lifespans might not necessarily serve well the purpose of meeting the operational needs of the user departments, or fulfilling the cost-effectiveness of fully utilising individual vessels. While there was no specifically defined five-year rolling plan, the MD was progressing with the replacement projects according to user departments' requirements and making reference to the vessels' expected lifespans as one of the considerations in advising user departments on the replacement schedule of their vessels. The review of GFD Circular No. 10/2008 would take into account the experience gained from the recent reform measures undertaken by the GFD in respect of procurement, maintenance and consultation with individual user department on the timing and strategy on the procurement of new and replacement vessels; and
- (b) replacement projects had been hindered by a serious shortage of professional officers in the GNCS from 2009 to 2014. Adhering to a rolling procurement plan made at that time might not be reflecting a realistic programme for the user departments. Nevertheless, following the recommendation of the 2016 audit review on "Procurement and maintenance of fire services equipment" (as reported in Chapter 3 of the Director of Audit's Report No. 67 of October 2016) which covered the FSD's vessels, the MD had started to work out with major user departments a tentative 10-year vessel replacement plan since December 2016.

2.6 According to the July 2017 vessel replacement plan provided by the MD, 54 (71%) of the 76 vessels serving beyond their expected lifespans (see Table 2 of para. 2.4) had been included in the replacement plan. For the 22 vessels not covered by the July 2017 replacement plan, Audit noted that:

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- (a) the MD had not conducted condition assessments (see para. 2.2(a)) for 2 vessels, i.e. one year and six years respectively after passing their expected lifespans (Note 16); and
- (b) while the MD had conducted condition assessments for the remaining 20 vessels, there were inadequate follow-up actions on the assessment results for 18 vessels, as follows:
 - (i) 8 vessels (5 belonging to the Agriculture, Fisheries and Conservation Department (AFCD) and the other 3 to the MD) had been advised by the MS 5 months to 7.5 years ago that they should be replaced, but up to July 2017 they were still in service;
 - (ii) according to the assessment results 3 to 7.5 years ago, 6 vessels could remain in service for another 2 to 3 years subject to further assessments. However, further assessments had not been carried out since then; and
 - (iii) for the remaining 4 assessed vessels, the MS had not advised the concerned user departments whether they should be replaced or required further assessment.

2.7 Timely replacement of aged vessels is important for operational effectiveness and efficiency. In its request for funding from the THB to outsource the project design and management work of vessel procurement projects in 2013 (see para. 1.8), the MD stated that if the procurement projects could not be processed in time, they might result in: (a) over-budget due to increase in shipbuilding costs

Note 16: *In September and October 2017, the MD informed Audit that: (a) the two vessels were specialised vessels for pollution control and mainly put on stand-by mode for emergency readiness, i.e. oil pollution at sea. While the two vessels were generally maintained in good working condition due to their operational modes, the MD would carry out condition assessments during their coming preventive services; and (b) the MD was mindful that condition assessment was one of the measures to monitor a vessel's safe operating condition. The MD would also take into account the need to conduct such an assessment based on the actual condition observed during preventive services and running repairs in line with the value-for-money principle.*

(see paras. 2.9 and 2.10); and (b) significant increase in maintenance costs and extra downtime. An aged vessel is also not desirable for the smooth operation of the user department. In this connection, Audit noted that the Security Bureau wrote to the THB in August 2013 expressing concern over the delay in vessel replacement/procurement projects which could hamper the operational efficiency of the law enforcement agencies in responding to emergency incidents. The THB reassured the Security Bureau that measures had been taken to expedite the procurement process by providing additional resources to the MD to employ consultants for project management work, and to create time-limited posts to complete the outstanding and new anticipated projects.

2.8 In light of the ageing trend of government vessels, the MD needs to improve its overall planning for the procurement of new and replacement vessels, including:

- (a) expediting action to complete the review of GFD Circular No. 10/2008 (see para. 2.5(a)) regarding its requirement on compiling a five-year rolling plan; and
- (b) closely monitoring the safety of aged vessels by conducting condition assessments in a timely manner and in consultation with user departments, taking prompt follow-up actions on the assessment results.

Slow progress in implementing vessel procurement projects

2.9 As at 31 August 2017, the MD was managing 25 ongoing procurement projects for 90 vessels of the four major classes (see para. 2.3), eight of which were approved by the FC and the remaining 17 projects were approved by the Legislative Council in the context of the Appropriation Bill (i.e. they were included in the annual draft estimates of the General Revenue Account) or by the Financial Secretary under delegated authority in accordance with the Public Finance Ordinance (Cap. 2). Audit analysis revealed that five FC approved projects could not meet their target dates of vessel delivery (with delays ranging from 5 months to 4 years up to August 2017) as stated in the relevant FC papers (see Table 3). As a result of the delays, additional commitments totalling \$33.2 million (14% in excess of the approved funding) were required to cater for the increase in construction costs of the 8 vessels involved in four of these five projects.

Table 3

**Target vessel delivery dates not met in
five FC approved vessel procurement projects
(31 August 2017)**

Item	Vessel procurement project	Original expected delivery date	Status as at 31 August 2017
1	In January 2012, the FC approved funding of \$19.6 million for the Correctional Services Department to replace a vessel for conveying persons in custody of high security grading, which was expected to reach the end of its serviceable life in 2013.	Aug 2013	Contract awarded in August 2017 and shipbuilding in progress for expected delivery in February 2019 (see item 6 of Table 6 in para. 2.24)
2	In April 2012, the FC approved funding of \$17.1 million for the Customs & Excise Department (C&ED) to replace a speed craft which had been in service since 2003 and sustained damage beyond economic repair during an anti-smuggling operation in 2010.	Jan 2014	Tender evaluation in progress and contract to be awarded in October 2017 (see item 2 of Table 6 in para. 2.24)
3	In June 2012, the FC approved funding of \$85 million for the FSD to replace an aluminum-hulled fireboat (with expected lifespan of 15 years — see Table 1 in para. 2.2(a)) which had been in service since 1990.	Sep 2014	Tender evaluation in progress and contract to be awarded in November 2017
4	In May 2013, the FC approved funding of \$114 million for the HKPF to replace five aluminum-hulled speedboats which had been in service since 1999, including one which had been damaged beyond economic repair in 2012.	Mar 2016	Tender documents under preparation (Note)
5	In January 2014, the FC approved funding of \$46.4 million for the MD to replace four vessels which had been in service since 1995.	Mar 2017	Contract awarded in June 2016 and shipbuilding in progress for expected delivery in November 2017

Source: Audit analysis of MD records

Note: According to the MD, the technical specifications were finalised and it was awaiting the HKPF's advice on the tender approach.

2.10 Of the 17 vessel procurement projects approved in the context of the Appropriation Bill or by the Financial Secretary (see para. 2.9), seven were approved before 2013-14. Audit found that the progress of three of them was particularly slow, i.e. they were still in the tender stage up to 31 August 2017, some five years after funding approval (see Table 4). As a result of the delays, additional commitments totalling \$58.77 million (37% in excess of the approved funding) were required to cater for the increase in construction costs of the 19 vessels involved in these seven projects.

Table 4
Delays in implementing vessel procurement projects
with funding approval before 2013-14
(31 August 2017)

Item	Vessel procurement project	Year of funding approval	Status as at 31 August 2017
1	Provision of \$9.9 million for the replacement of one launch of the ImmD which had been in service since 1992	2010-11	Shipbuilding in progress (per contract awarded in June 2016)
2	Provision of \$9.7 million for the replacement of a vessel of the MD which had been in service since 1995	2011-12	Tender evaluation in progress
3	Provision of \$21 million for the procurement of three new speed craft for the HKPF's vessel interception operation	2011-12	Tender invitation in progress (with tender closing date in December 2017)
4	Provision of \$64 million for the replacement of eight speed craft of the HKPF which had been in service since 1997 or 1998	2011-12	Tender invitation in progress (with tender closing date in October 2017 — see item 1 of Table 6 in para. 2.24)

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Table 4 (Cont'd)

Item	Vessel procurement project	Year of funding approval	Status as at 31 August 2017
5	Provision of \$16 million for the replacement of two diving support speedboats of the FSD which had been in service since 2000	2012-13	Shipbuilding in progress (per contract awarded in May 2017 — see item 5 of Table 6 in para. 2.24)
6	Provision of \$10 million for the procurement of one new patrol vessel of the AFCD	2012-13	Shipbuilding in progress (per contract awarded in January 2017 — see item 4 of Table 6 in para. 2.24)
7	Provision of \$29.9 million (Note) for the replacement of three vessels of the MD which had been in service since 1993 or 1994	2012-13	Shipbuilding in progress (per contract awarded in March 2017 — see item 3 of Table 6 in para. 2.24)

Source: *Audit analysis of MD records*

Note: *As a result of the delay, the approved funding of 2012-13 was reallocated for other uses. New funding of \$44.6 million for the project was approved in the 2016-17 Estimates.*

2.11 Audit examination of the MD's records revealed the following factors contributing to the delays in implementing vessel procurement projects:

- (a) long time taken to review the marking scheme for tender assessment (see paras. 2.12 to 2.16);
- (b) shortage of SoSs (see paras. 2.17 to 2.22);
- (c) slow progress in outsourcing project management work to clear backlog (see paras. 2.23 to 2.27); and
- (d) discrepancies in tender documents (see paras. 2.28 and 2.29).

***Long time taken to review
the marking scheme for tender assessment***

2.12 It had been the practice of the MD to use a marking scheme for assessing tenders of a vessel procurement project with value exceeding \$1.43 million. In approving the award of a contract for vessel procurement in December 2009, the Central Tender Board (CTB) noted a provision in the tender evaluation sheet that the MD would exercise discretion to accept a tender which did not provide sufficient information for assessment under the Marking Stage. While the MD explained the circumstances under which such discretion would be exercised, the CTB was concerned that the arrangement was not made known to tenderers (as the tender evaluation sheet was an internal document). The CTB requested the MD to refine the relevant provision of the marking scheme in consultation with the Department of Justice (DoJ).

2.13 ***Projects postponed during the review.*** The GNCS was tasked to follow up on the review of the marking scheme. It took 10 months (from December 2009 to mid-October 2010) to draft a revised marking scheme for the HKPF's procurement project of 11 speed craft. During the period from October 2010 to April 2011, the GNCS sought a few rounds of comments on the marking scheme from the DoJ. In the course of consulting the DoJ, the GNCS pointed out that the revised marking scheme was intended to be used for all types of vessels. From May 2011 onwards, the GNCS continued to consult relevant parties (i.e. the HKPF, Financial Services and the Treasury Bureau (FSTB), CTB and DoJ) over different time periods and revise the marking scheme in light of their comments. In April 2012, the FSTB commented that a standard marking scheme for all types of vessels would be complicated and inappropriate given the variation of vessels' main characteristics. The GNCS was advised to submit the marking scheme representing the specific vessel type for approval. In October 2012, the CTB approved the revised marking scheme for the HKPF's speed craft procurement project (see Appendix C for a chronology of

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events of the tender marking scheme review). During the almost three-year period (from December 2009 to October 2012), 9 projects (Note 17) for the procurement of 29 vessels (including items 1 to 3 of Table 3 in para. 2.9 and items 1 to 4 of Table 4 in para. 2.10) with total approved funding of \$263.7 million were postponed for periods ranging from 4 months to 2.8 years.

2.14 Audit examined the MD's records to ascertain how the progress of the GNCS's work on revising the marking scheme had been monitored by the MD's management. Audit found that the GNCS started reporting the progress to the Government Dockyard weekly management meeting (which was chaired by the Assistant Director of the GFD) in August 2010. In September 2010, the GNCS reported that the revised marking scheme was expected to be approved by the CTB in February 2011. While the expected approval date of the revised marking scheme was subsequently not met, there was no record showing reporting/discussion at the management meetings on the likely impact (e.g. the number of procurement projects affected and the extent of delays) and any possible measures to mitigate the impact (such as reassessing the need for using marking schemes for the pending procurement projects). According to the SPRs, departments may consider the use of a marking scheme for tender evaluation where the quality of the service/product to be procured is of paramount importance. In this connection, Audit noted that in December 2010, the DoJ suggested that the MD should review the need for using a marking scheme. There was no record to show that the MD had responded to DoJ's suggestion. In the event, the GNCS conducted a tendering exercise for the procurement of 3 lighters without the use of a marking scheme in December 2012. The GNCS only used marking schemes for 3 projects after the CTB's approval of 2012, i.e. the 11 speed craft project of the HKPF (see para. 2.13), and two projects for other types of vessels after obtaining the GLD Tender Board's approval for the relevant marking schemes in 2014 (see Note 7 to para. 1.7(b)). In August 2014, the FSTB issued a circular

Note 17: *According to a "Report of review of manpower of GNCS" finalised by the MD in May 2013, since the review of the tender marking scheme in December 2009, all new vessel procurement projects that required a marking scheme had been postponed until 3 October 2012 (the date of the CTB's approval of the revised marking scheme). Up to 19 April 2013, there were a total of 13 outstanding projects (see para. 2.23) for 37 vessels, including 4 projects (for a total of 8 vessels) with funding approval between 4 October 2012 and 19 April 2013. In other words, 9 (13 less 4) projects for 29 (37 less 8) vessels were postponed until 3 October 2012 because of the review of the tender marking scheme. As at 31 August 2017, 2 of the 9 delayed projects had been completed.*

reminding bureaux/departments to avoid excessive use of marking scheme for tender assessment.

2.15 Audit also requested the MD to provide records of its senior management's monitoring of the GNCS's work on reviewing the marking scheme from 2010 to 2012, such as the Corporate Team Weekly Meeting which was attended by directorate officers of the MD. However, the MD informed Audit in August 2017 that no minutes of the Corporate Team meetings had been kept during the said period. As such, Audit was unable to ascertain whether the MD's senior management had been timeously informed of the delay in nine vessel procurement projects (see para. 2.13) caused by the long time taken in reviewing the marking scheme and had given any direction to the GNCS in this regard. In September 2017, the MD informed Audit that the situation had been improved since May 2014. Written notes of the Corporate Team meetings were prepared to record the deliberations of the meetings. Besides, to strengthen the management oversight of the GFD, the Director of Marine and Deputy Director of Marine (Special Duties) had attended the Government Dockyard management meetings since February 2016 on a regular basis.

2.16 Audit notes the MD's recent efforts to improve the documentation of important meetings and to strengthen the management oversight of the GFD's work. In Audit's view, the MD needs to sustain these improvement measures taken to ensure the timely delivery of vessel procurement projects.

Shortage of SoSs

2.17 **Recruitment difficulties.** The SoSs in the GNCS play an important role in the procurement of government vessels. They act as the marine engineer and naval architect for the MD on the construction of new vessels (Note 18). The MD has been experiencing difficulties in recruiting SoSs to fill the vacancies in the department. Since the lifting of the civil service recruitment freeze in 2007, the MD conducted

Note 18: *Main duties and responsibilities of SoSs in the GNCS include: (a) conducting feasibility studies of user operational requirements, advising user departments on technical and cost issues, and preparing SCOGC papers, specifications and tender documents; (b) evaluating tenders and making recommendations; (c) supervising design and construction of new vessels; (d) accepting vessels upon their delivery; and (e) liaising with user departments regarding modification of existing vessels.*

8 open recruitment exercises for SoS posts up to 2012. The number of SoSs successfully recruited in each exercise averaged 2.5 whereas the target numbers of recruits ranged from 2 to 9.

2.18 According to the “Final Report of the Steering Committee on Systemic Reform of the Marine Department” published in April 2016 (see para. 1.13), the supply of home-grown trained seafarers had always been very limited because there was a general lack of interest amongst young people to work on board ocean-going vessels. Besides, the maritime industry was a highly global business and shipping companies in the private sector were more flexible to address their manpower problems by offering a competitive remuneration package and recruiting employees from all over the world. Moreover, the professional qualifications required for entry to the SoS grade tended to be stringent (Note 19) which also led to the manpower shortage and succession problems (Note 20) in the MD.

2.19 *Stop-gap measures.* Five recruitment exercises of SoSs had been conducted between 2013 and January 2017. The MD had implemented some stop-gap measures in the recruitment exercises conducted since 2014, including: (a) relaxation of requirements on language proficiency and working experience; (b) granting of incremental credit for working experience; and (c) enhancing the publicity of the recruitment exercises. However, the average number of SoSs successfully recruited in each exercise was only 3.2 whereas the target numbers of recruits ranged from 7 to 10. For the GNCS, the MD obtained approval in September 2013 to create three time-limited SoS posts for the period from 2014-15 to 2017-18 to speed up the clearance of vessel procurement project backlog accumulated from December 2009 to 2013 (see para. 2.13). In November 2016, the MD obtained further time-limited resources for creation of one Senior SoS and two Assistant Ship Inspectors for five years from 2017-18 to 2021-22 to further speed up the clearance of the procurement backlog.

Note 19: *At the entry rank, candidates for the SoS grade must possess a relevant degree (e.g. in mechanical/marine engineering or nautical studies) and must have worked on board ocean-going vessels at designated responsible positions for the required length of sea service or accumulated relevant experience in the naval architectural field.*

Note 20: *For example, the average age of the new intakes for the recruitment exercises from 2007 to 2012 was 44.3 at the time of appointment.*

2.20 **Manpower situation.** Notwithstanding the implementation of the stop-gap measures, the number of vacancies in the SoS grade in the MD continued to increase from 5 (i.e. 9.3% of the establishment of 54 posts) as of April 2013 to 11 (i.e. 20% of the establishment of 55 posts) as of March 2017. Over this period, the GNCS continued to carry 1 to 3 vacancies (see Table 5). In June 2013 and March 2015, the MD informed relevant user departments that there would be delays in the vessel procurement projects due to the shortage of SoS grade staff and other priorities of the department. In 2017, the Task Force on Reform of the MD (see para. 1.13) conducted a review of the workload and manpower of the GNCS and recommended extending the three time-limited SoS posts for four years until 31 March 2022.

Table 5

Staffing position of SoS grade in the GNCS

SoS grade in the GNCS	Position as at 31 March				
	2013	2014	2015	2016	2017
	(Number)				
Permanent establishment (a)	4	4	4	4	4
Time-limited post endorsed for creation (b)	0	3	3	3	4
Total (c)	4	7	7	7	8
Civil service staff (d)	3	1	2	3	5
Non-civil service contract terms staff (e)	0	4	2	3	1
Vacancy (f) = (c) – (d) – (e) (Note)	1	2	3	1	2

Source: MD records

Note: In September 2017, the MD informed Audit that in view of the shortage of suitable SoS candidates to fill the vacancies, it had redeployed resources to create one Chief Supplies Officer and one Supplies Officer posts under the Task Force on Reform starting from February 2016 to provide expert advice to the officers in the GNCS on supplies and procurement matters. In November 2016, the MD obtained further time-limited resources to extend the two Supplies Officer grade staff posts for the period from 2017-18 to 2021-22.

2.21 *Succession problem.* According to the Steering Committee Report, the MD was also facing critical succession problem in the SoS grade. The average age of SoS grade staff was 52.2 as at 30 April 2013 and 52.1 as at 31 March 2017. Of the 47 SoSs as at March 2016, 33 (70%) would reach the normal retirement age in ten years' time. The Steering Committee considered that the MD should continue to implement the stop-gap measures that had already been rolled out and identify more practicable stop-gap measures for recruiting suitable candidates including the option of recruiting experienced professionals to the senior ranks. As regards the succession problem of the SoS grade staff, the Steering Committee strongly supported the creation of a new training or assistant rank through embarking on a grade structure review. To follow up on the recommendations of the Steering Committee, the MD had been working with the Civil Service Bureau through the conduct of a grade structure review of the SoS and the Marine Officer grades (see para. 1.15), which was in progress as of August 2017.

2.22 In Audit's view, the MD needs to expedite the implementation of the Steering Committee's recommendations in addressing the manpower shortage and succession problems of SoS grade staff to speed up the clearance of the procurement backlog.

Slow progress in outsourcing project management work to clear backlog

2.23 With the addition of 4 new projects after the approval of the revised marking scheme in October 2012, there were a total of 13 outstanding procurement projects (see Note 17 to para. 2.13) (costing over \$1.43 million each) up to April 2013. As another measure to clear the backlog of vessel procurement projects (see para. 2.19), the MD obtained funding of \$35.44 million from the THB in October 2013 to engage consultants from 2014-15 to 2016-17 to manage 10 projects for the procurement of 26 vessels. The nature of consultancy services would include carrying out conceptual design and preparing technical specifications prior to the award of shipbuilding contracts, and providing management services after the award of shipbuilding contracts.

2.24 However, up to August 2017, the MD only engaged consultants to assist in the management of 6 procurement projects of 16 vessels (see Table 6):

- (a) for 2 projects, the consultants were required to provide services both before and after the award of shipbuilding contracts; and
- (b) for the remaining 4 projects, the consultants were required to provide services after the award of shipbuilding contracts, i.e. MD in-house staff carried out the conceptual design and prepared the technical specifications.

Table 6

**Six vessel procurement projects managed by consultants
(August 2017)**

Project	Consultancy services		Tender invitation date for shipbuilding contract	
	Conceptual design and technical specifications	Management of shipbuilding contract	Expected	Actual
1. Replacement of eight speed craft of the HKPF (see item 4 of Table 4 in para. 2.10)	Yes	Yes (Note 1)	May 2015	April 2017 (tender closing in October 2017)
2. Replacement of a speed craft of the C&ED (see item 2 of Table 3 in para. 2.9)	Yes	Yes (Note 1)	June 2015	October 2016 (Note 2)
3. Replacement of three vessels of the MD (see item 7 of Table 4 in para. 2.10)	No	Yes	May 2015	July 2016 (contract awarded in March 2017)
4. Procurement of a patrol vessel of the AFCD (see item 6 of Table 4 in para. 2.10)	No	Yes	June 2015	January 2016 (contract awarded in January 2017)

Procurement of government vessels

Table 6 (Cont'd)

Project	Consultancy services		Tender invitation date for shipbuilding contract	
	Conceptual design and technical specifications	Management of shipbuilding contract	Expected	Actual
5. Replacement of two diving support speedboats of the FSD (see item 5 of Table 4 in para. 2.10)	No	Yes	June 2015	September 2016 (contract awarded in May 2017)
6. Replacement of a vessel of the Correctional Services Department (see item 1 of Table 3 in para. 2.9)	No	Yes	June 2015	December 2016 (contract awarded in August 2017)

Source: Audit analysis of MD records

Note 1: According to the MD, the consultancy service contracts for the management of shipbuilding contracts for the HKPF and C&ED were expected to be awarded in August 2018 and October 2017 respectively.

Note 2: According to the MD, the shipbuilding contract was awarded on 10 October 2017.

Remarks: As at August 2017, the status of the four procurement projects for which consultants had not been engaged was as follows: (a) for three projects, tender exercises for shipbuilding contracts had been arranged including one with contract to be awarded shortly, one under tender evaluation stage, and one pending tender closing; and (b) for the remaining project, invitation of tenders for the shipbuilding contract was pending the HKPF's advice on the tender approach.

2.25 According to the funding submission to the THB of 2013, the MD expected that with the outsourcing arrangement, tenders for the 6 shipbuilding contracts would

be invited in May or June 2015. However, as shown in Table 6, the expected tender invitation dates were not met in all six contracts, i.e. seven months to 2 years behind schedule.

2.26 For the two projects which the consultants were responsible for the conceptual design and technical specifications (see items 1 and 2 of Table 6), tenders for the consultancy services were invited in May 2015, about 10 months later than the expected tender invitation date of August 2014 as stated in the funding submission to the THB. In February 2016, the HKPF (one of the user departments) informed the MD of the following inadequacies of the consultancy services it received:

- (a) the tender specification prepared by the consultant for the eight speed craft resembled the features of the petrol craft in an earlier procurement exercise and it included features not required by the HKPF;
- (b) the consultant did not have technical staff stationed in Hong Kong to facilitate discussion; and
- (c) the consultancy service could not speed up the vessel procurement process.

In September and October 2017, the MD informed Audit that the outsourced project mentioned above was the first pilot project and with the experience gained, the ensuing outsourced projects were able to achieve the intended purpose in an effective manner.

2.27 Up to August 2017, of the backlog of 13 procurement projects with funding approval obtained before April 2013 (see para. 2.23), only 3 projects had been completed. Of the 10 outstanding projects (see items 1 to 3 in Table 3 of para. 2.9 and all seven items in Table 4 of para. 2.10), 5 were still in the tender stage. Audit considers that the MD needs to expedite action to clear the backlog. In this connection, the MD needs to speed up the outsourcing of project management work to consultants.

Discrepancies in tender documents

2.28 In examining a delayed vessel procurement project of the MD (see item 2 of Table 4 in para. 2.10), Audit noted that the delay was partly attributable to the discrepancies found in the tender documents (see Case 1 for details).

Case 1

Project delay due to discrepancies found in tender documents

1. In 2011-12, the MD obtained funding of \$9.7 million for replacing an aged vessel which had been in service since 1995. Due to the need to review the marking scheme (see paras. 2.12 and 2.13) and the shortage of SoSs (see paras. 2.17 to 2.20), tender preparation for the project was deferred until December 2015.

2. **Discrepancies found.** Tenders for the procurement contract were invited in March 2016 and a tender notice was gazetted on the same day. Upon close of tender in May 2016, five offers were received. During the tender evaluation process in August 2016, the GNCS found that there were discrepancies between the tender notice and the tender document in relation to the overall length and breadth of the vessel (e.g. the overall length was specified as not less than 15 metres (m) in the tender notice but as 14 to 15 m in the mandatory requirements of the tender document).

3. In September 2016, the MD sought legal advice from the DoJ on whether it could award a contract to a tenderer which conformed with the length requirement in the tender document but not the gazetted tender notice. In October 2016, the MD noted that a tenderer must conform to the essential requirements as set out in the tender notice and the tender document in order to be awarded the contract.

4. **Cancellation of tender.** In December 2016, the MD sought approval from the GLD Tender Board for cancellation of the tender. While granting the approval, the Board was of the view that the cancellation could have been avoided had the MD exercised due diligence in the preparation of the tender notice and the tender document. In April 2017, the procurement contract was re-tendered with the tender closing date in July 2017, i.e. the project was delayed by one year compared with the first tender closing date of May 2016.

Source: MD records

2.29 In light of the findings in Case 1, Audit examined another MD's vessel procurement project which was completed in March 2017 (see Case 2). Audit found that there was similar problem of discrepancies in the tender documents. Although the progress of the project had not been affected as a result, the recurrence of similar discrepancies is a cause of concern. There is a need for the MD to step up the checking of the accuracy and consistency of tender documents.

Case 2

Another project with discrepancies found in tender documents

1. In November 2013, the MD obtained funding of \$12 million for replacing two patrol vessels which had been in service since June 1994 and March 1996 respectively, i.e. they had been operating beyond the expected lifespan of 15 years.

2. ***Discrepancies found.*** Tenders for the supply of the two vessels were invited in July 2014 and a tender notice was gazetted on the same day. Prior to the close of tender in October 2014, a shipbuilding company found several discrepancies within the tender document in relation to the specifications of the hull of the vessels, their breadth and number of seats (e.g. the General Technical Requirements stated that the maximum breadth of the vessel was 2.4 m whereas the General Essential Requirements stated that the required breadth was not more than 4.2 m) and sought clarification from the GNCS in September 2014. After advising the shipbuilding company, the GNCS also revised the tender document posted on the MD's website. However, the Gazette Notice was not revised. The tender was closed in October 2014 but no offer was received. The procurement contract was re-tendered in August 2015. The contract was subsequently awarded in March 2016 and the vessels were delivered in March 2017.

Source: MD records

Delay in implementing a vessel procurement project due to change of shipbuilding contractor

2.30 In 2005, the FC approved funding of \$60 million for the HKPF to procure 23 divisional fast patrol craft as part of its versatile maritime policing response. According to the FC paper, the expected commissioning dates would be March 2008 for 17 vessels and March 2009 for the remaining 6 vessels. In December 2006, the MD on behalf of the HKPF awarded a contract for the procurement of the 23 vessels by 4 batches at a total sum of \$37.2 million to a shipbuilding contractor (Contractor A). The order of the second, third and fourth batches would be individually subject to the successful performance of the previous batch of vessels at the end of a 2-month trial period after vessel delivery and acceptance.

Procurement of government vessels

2.31 The first two batches of 6 vessels each were delivered in December 2007 and November 2009 respectively. However, due to a contractual dispute between the MD and Contractor A, the MD decided not to order the last two batches of vessels under the 2006 contract but awarded a new contract for the procurement of the remaining 11 vessels to another contractor in 2013. The 11 vessels were subsequently delivered in February 2016. In the event, the expected commissioning dates as stated in the FC paper (see para. 2.30) were not met for 17 (6 plus 11) vessels.

2.32 The contractual dispute between the MD and Contractor A is yet to be resolved. In order not to prejudice the ongoing dispute resolution process, Audit does not make any comment in relation thereto in this Audit Report.

Frequent machine failure of two new vessels

2.33 In November 2012, the MD obtained funding of \$11 million for the replacement of two of its patrol launches. In March 2014, a shipbuilding contract was awarded at a sum of \$9.54 million to a contractor (Contractor B). The two vessels were delivered in February 2015 and formally accepted by the MD after completion of the necessary acceptance tests (e.g. the official sea trial). During the warranty period from February 2015 to February 2016, the following defects were found in one of the two new patrol launches:

- (a) abnormal shutdown of the generator set;
- (b) frequent shutdowns of the outboard engines; and
- (c) defects in relation to the radar, navigation light and alarm.

2.34 By the time of expiry of the warranty period in February 2016, the problem of the generator set had not been fixed. According to Contractor B, it was still waiting for the delivery of the spare parts as the workers of the spare part supplier were on

strike in November and December of 2015 (Note 21). After completion of the repair work for the generator set in April 2016, the defects in relation to the radar, navigation light and alarm recurred. The defects were only rectified in November 2016 and March 2017.

2.35 As a result of repair works for the abovementioned defects, the downtime of the patrol launch from February 2015 to March 2017 recorded in the Government Dockyard was 126 days. In addition, the launch also underwent repair at Contractor B's shipyard from February to April 2016 which caused a downtime of 70 days. The total downtime of 196 days (27% of a 2-year period) appears excessive for a new vessel. As for the second patrol launch which also experienced problems with its generator set and one of its outboard engines mainly after the warranty period, its downtime was 22.5 days during the warranty period and 103 days in the year immediately after the warranty period. Up to August 2017, there was no record to show that the MD had conducted a review on the excessive downtime of the two new vessels. In Audit's view, the MD needs to carry out a review in this regard with a view to preventing recurrence of similar problems.

Audit recommendations

2.36 **Audit has *recommended* that the Director of Marine should:**

- (a) **improve the overall planning for the procurement of new and replacement government vessels, including:**
 - (i) **expediting action to complete the review of GFD Circular No. 10/2008 regarding its requirement on compiling a five-year rolling plan; and**
 - (ii) **closely monitoring the safety of aged vessels by conducting condition assessments in a timely manner and in consultation with user departments, taking prompt follow-up actions on the assessment results;**

Note 21: *The MD informed Audit in August 2017 that the GNCS had obtained from Contractor B limited warranty for the generator set for three additional months from May to August 2016.*

Procurement of government vessels

- (b) **sustain the improvement measures taken in monitoring the GFD's work to ensure the timely delivery of vessel procurement projects;**
- (c) **expedite action to clear the backlog of vessel procurement projects (see para. 2.27), including:**
 - (i) **implementing the Steering Committee's recommendations in addressing the manpower shortage and succession problems of SoS grade staff; and**
 - (ii) **speeding up the outsourcing of project management work to consultants;**
- (d) **step up the checking of the accuracy and consistency of tender documents; and**
- (e) **carry out a review on the long downtime of the two new vessels delivered in February 2015 (see paras. 2.33 to 2.35) with a view to preventing recurrence of similar problems.**

Response from the Government

2.37 The Director of Marine agrees with the audit recommendations. She has said that:

- (a) the MD has strengthened the governance of the GNCS and rolled out a series of measures to speed up vessel procurement projects since December 2015. For example, the MD has deployed Supplies Officer grade staff to provide expert advice to the GNCS, provided extra professional grade staff to expedite the clearance of the procurement backlog, and commenced the conduct of the grade structure review for the two professional grades to address the recruitment and succession problems in the long run; and
- (b) looking forward, the MD will sustain its effort to provide professional support to government departments for the procurement of new vessels.

PART 3: MAINTENANCE OF GOVERNMENT VESSELS

3.1 This PART examines the MD's work on the maintenance of government vessels, focusing on:

- (a) availability of government vessels to users (paras. 3.3 to 3.6);
- (b) management of downtime of government vessels (paras. 3.7 to 3.13); and
- (c) management of maintenance contracts (paras. 3.14 to 3.25).

Organisation of vessel maintenance work

3.2 According to its Controlling Officer's Report (COR), the MD aims to provide cost-effective maintenance services to the user departments. The MS (see para. 1.9) of the MD is headed by a Senior Maintenance Manager and comprises three maintenance teams. While preventive service (see para. 1.10(b)) is performed regularly in the Government Dockyard, running repair (see para. 1.10(c)) is carried out as and when necessary both inside and outside the Government Dockyard. The MD has outsourced some 90% of the vessel maintenance work. According to the MD, the remaining in-house maintenance work relating to workshop services and urgent minor repairs is carried out by Works Supervisor, Senior Artisan and Artisan grades staff, totalling 65 as at March 2017 (Note 22). Among them, 50 worked in the Government Dockyard, i.e. 47 in ten specialised workshops and three performed urgent repair work. The remaining 15 staff provided repair services at five regional forward bases of the Marine Police (Note 23).

Note 22: *Of the MS's establishment of 70 Works Supervisor, Senior Artisan and Artisan grades staff, 65 were deployed to carry out in-house maintenance work while the remaining 5 were responsible for monitoring outsourced maintenance work.*

Note 23: *The five regional forward bases of the Marine Police are located in Sai Kung, Tai Lam Chung, Ma Liu Shui, Sai Wan Ho and Aberdeen.*

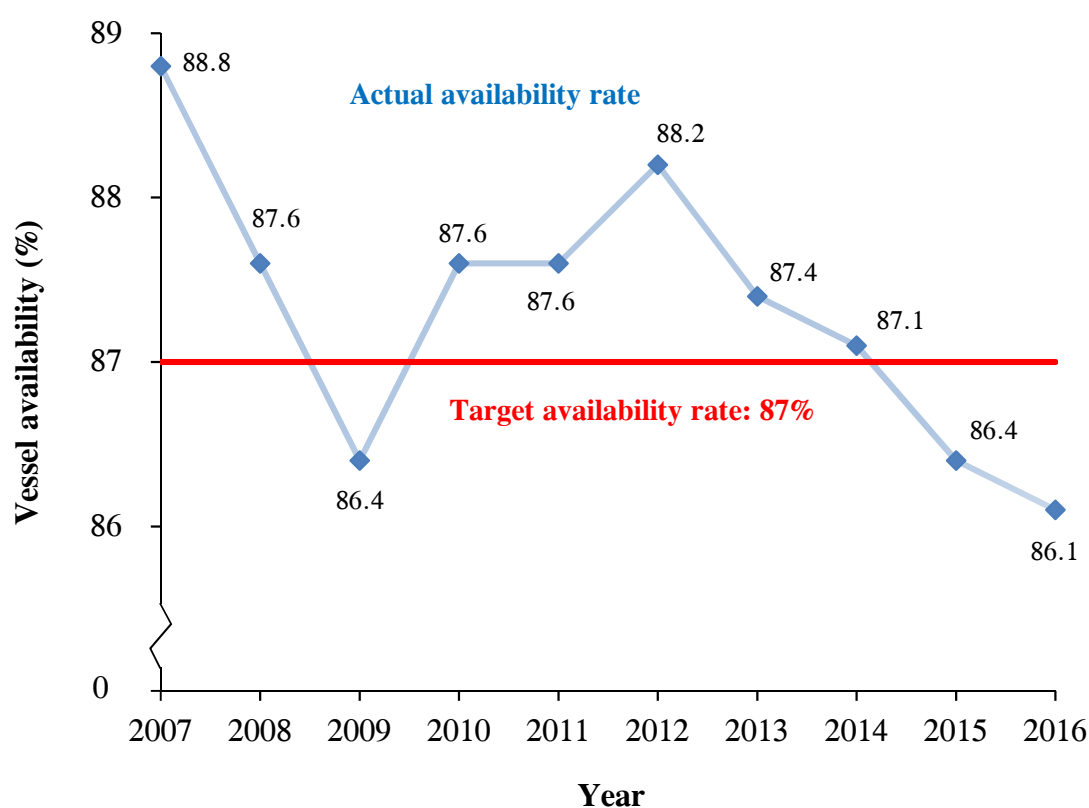
Availability of government vessels to users

Vessel availability rate on a decreasing trend

3.3 The MD's work on the maintenance of government vessels is important to support the work of various user departments, especially the disciplined services departments in carrying out law enforcement and emergency duties. The MD has set a performance target at 87% in its COR to monitor vessel availability to all users. As shown in Figure 2, the availability rates of government vessels as reported by the MD decreased from 88.8% in 2007 to 86.1% in 2016. For three years in 2009, 2015 and 2016, the availability rates were below the target of 87%, ranging from 86.1% to 86.4%.

Figure 2

Availability rates of government vessels
(2007 to 2016)



Source: MD records

3.4 Audit noted that the MD had also reported in an annual report entitled “Port of Hong Kong Statistical Tables” the availability rates of MECVs and HSCLs (see para. 2.3) of user departments. The reported availability rates of these two classes of vessels for six major user departments from 2012 to 2016 are summarised in Table 7. It can be seen that the target availability rate was not met in three years for both the HKPF and ImmD and in two years for the AFCD and the MD. The decreasing vessel availability rates for user departments in general, and non-attainment of the target vessel availability rate for the HKPF and ImmD (Note 24) in particular warrant the MD’s attention as their operational efficiency could be adversely affected.

Table 7

**Availability rates of MECVs and HSCLs for six major user departments
(2012 to 2016)**

Year	User department					
	HKPF	MD	FSD	AFCD	C&ED	ImmD
2012	87.1%	89.7%	88.0%	90.6%	88.9%	85.9%
2013	87.0%	86.9%	89.2%	90.0%	88.5%	85.8%
2014	85.6%	86.6%	88.1%	93.8%	88.5%	88.4%
2015	84.0% (Note)	88.9%	87.1%	85.3%	87.4%	86.8%
2016	84.8% (Note)	87.9%	83.9% (Note)	82.2% (Note)	87.4%	87.0%

Source: MD records

Note: In October 2017, the MD informed Audit that the low availability rates for the three user departments’ vessels were partly due to the downtime for running repairs as a result of accidents (i.e. 291 days in 2015 and 206 days in 2016 for the HKPF, 176 days for the FSD and 30 days for the AFCD). However, based on information provided by the MD, with the exception of the FSD, the target availability rate of 87% was still not met for the HKPF and AFCD in 2015 and/or 2016 after excluding the downtime due to accidents in calculating the actual availability rates.

Remarks: Shaded figures represent availability rates below the target of 87%.

Note 24: In September 2017, the MD informed Audit that the availability rate was affected by the unique fleet operating profile of these two user departments.

Inadequacies in reporting vessel availability rates

3.5 *Not all classes of vessels covered in reporting availability rates.* While the MD stated in its COR that the target vessel availability rate was set for all users, Audit found that the reported availability rates in fact only covered MECVs and HSCLs, two of the four major classes of vessels (see para. 2.3). For 3 of the 14 user departments which did not have any MECV and HSCL (see Appendix B), the reported vessel availability rates did not reflect their situation. For 6 of the 14 user departments, their MIMCs and/or HSCMs totalling 80 vessels were not covered in the reported vessel availability rates. The current practice of reporting the vessel availability rates without any explanatory note may cause misunderstanding to users of the COR. The MD needs to make improvement in this regard.

3.6 *Methodology in calculating vessel availability rates not explained in CORs.* According to the MD, the vessel availability rate was calculated using the following formula:

$$\frac{(365 \text{ days} \times \text{number of MECVs and HSCLs} - \text{total downtime (days)} \\ \text{for maintenance and repair of MECVs and HSCLs in a year})}{(365 \text{ days} \times \text{number of MECVs and HSCLs})} \times 100\%$$

According to the MD's quality manual of 2016 provided to Audit on 28 July 2017 (see an extract at Appendix D), the downtime for carrying out maintenance and repair both inside and outside the Government Dockyard would be recorded for working out the vessel availability rates. However, Audit's sample check of the Arrival and Completion Form (A&C Form — Note 25) used by the MD for recording the downtime revealed that the downtime for repair carried out outside the Government Dockyard (including those carried out in the five regional forward bases of the Marine Police — see Note 23 to para. 3.2) was not always recorded. Upon enquiry, the MD provided Audit in August 2017 with an internal circular of 2012 and an updated quality manual of 2017 which stated that only the downtime for carrying out

Note 25: *An A&C Form is used by the MD to record the arrival time of a vessel at the Government Dockyard for maintenance/repair services and the completion time of the related work which can also serve as a log sheet for recording the vessel downtime for maintenance/repair services. Audit sample checked 40 A&C Forms of November 2016 used for recording repair work outside the Government Dockyard and found that only 9 had recorded both the date and time of commencing and completion of the repair work.*

maintenance and repair inside the Government Dockyard would be taken into account in calculating the vessel availability rate. In response to Audit's further enquiry, the MD in August and October 2017 said that:

- (a) excluding the downtime of maintenance and repair outside the Government Dockyard had been the established practice for long even though this might not have been set out clearly in the former issues of the manual;
- (b) the reason for excluding the downtime outside the Government Dockyard was that the vessels were still under the control and operation of the user departments; and
- (c) the quality manual was revised on 16 August 2017. According to the 2017 quality manual, there was no requirement to record downtime for repair outside the Government Dockyard.

However, Audit noted that some of the repair work outside the Government Dockyard was related to deferred maintenance which was beyond the control of user departments, i.e. a vessel could be released from the Government Dockyard before the completion of some maintenance/repair work (e.g. pending the arrival of components) which would be followed up outside the Government Dockyard after arrival of the components. Moreover, from the users' point of view, vessels under maintenance/repair are not available for their use irrespective of where the maintenance/repair services are rendered. Audit also noted that the basis of reporting the performance of the MD's maintenance services had not been explained in the CORs for information of relevant stakeholders. In Audit's view, the MD needs to consult relevant stakeholders (including user departments and the THB) on the current practice of calculating the vessel availability rates without taking into account the downtime for repair outside the Government Dockyard and provide appropriate explanatory note in the COR if it is decided after the consultation to continue with such practice.

Management of downtime of government vessels

3.7 The downtime of government vessels as recorded in the A&C Forms (see Note 25 to para. 3.6) is inputted into the GFIS for generation of a monthly vessel availability report for management information. Based on the GFIS records and

Maintenance of government vessels

information provided by the MD, Audit analysed the downtime of four major classes of government vessels from 2012 to 2016. The results are summarised in Table 8.

Table 8
Downtime of four major classes of government vessels
(2012 to 2016)

Year	Downtime (Number of days)			Number of vessels at year end
	For preventive service (a)	For running repair (b)	Total (a) + (b)	
2012	4,190 (64 %)	2,393 (36 %)	6,583 (100 %)	183
2013	4,014 (50 %)	3,967 (50 %)	7,981 (100 %)	182
2014	4,022 (50 %)	3,966 (50 %)	7,988 (100 %)	183
2015	4,182 (54 %)	3,565 (46 %)	7,747 (100 %)	183
2016	4,518 (55 %)	3,683 (45 %)	8,201 (100 %)	187
Increase from 2012 to 2016 (%)	7.8%	53.9%	24.6%	2.2%

Source: Audit analysis of MD records

3.8 As shown in Table 8, while the total number of vessels increased by 2.2% from 2012 to 2016, the total downtime increased by 24.6%. The average downtime per vessel had increased from 36 (6,583 ÷ 183) days in 2012 by 22% to 44 (8,201 ÷ 187) days in 2016. The increase in total downtime is mainly attributable to the increase in running repair of 53.9% whereas preventive service only increased by 7.8% over the same period.

3.9 In response to Audit's enquiry, in August 2017 the MD said that:

- (a) the main reason for the increase in downtime was the ageing problem of the government vessels. Their operating parts required extensive maintenance and even replacement. However, spare parts required might not be available. The lead time in awaiting delivery of such parts would cause additional downtime. Similarly, some machines and control systems on board the vessels might have been phased out over the years. Modification of the systems would have to be studied; and
- (b) with a view to counteracting the ageing effect of the vessels, such as maintaining their service speed, preventive service had been enhanced which also caused extra downtime.

Audit understands that the increase in downtime has to be seen in the context of an ageing government fleet. However, the MD needs to critically examine if there were other factors contributing to the increase in downtime. In this connection, Audit found that there was room for improvement in managing the preventive service and running repair work as illustrated in paragraphs 3.10 to 3.13.

Preventive maintenance scheduling

3.10 Every 12 to 18 months, some 100 vessels will dock at the Government Dockyard for preventive service. Due to the limited dry-docking spaces (only 10 ship repairing sheds for the large mechanised vessels to carry out superstructure repair and/or painting work) and other docking facilities, the MD has to schedule the maintenance work to ensure the smooth operation of the Government Dockyard. If preventive service is properly planned, the downtime waiting for docking resources can be minimised. At the beginning of each year, the MD provides a maintenance schedule to each user department showing the start date and proposed working days required for preventive service (i.e. the budgeted downtime) of each of the specified vessels in the schedule. The scope of maintenance work is drawn up based on the defect list provided by the user department and the maintenance staff's pre-docking inspections (see para. 1.10(a)) of the vessels concerned.

3.11 According to the MD's quality manual, the progress of the maintenance service is closely monitored to minimise downtime by re-allocating docking resources. Based on the progress status of those vessels under maintenance, the number of vessels

Maintenance of government vessels

returning to the Government Dockyard for preventive service in the next quarter or their scheduled docking dates may be adjusted (e.g. user departments' requests for suiting their operational needs). If more time is spent on the scheduled maintenance than budgeted, the extra downtime and the underlying reasons will be recorded and inputted into the GFIS. Upon Audit's request, the MD provided an analysis of the extra downtime for preventive service of four major classes of vessels from 2012 to 2016 (see Table 9).

Table 9
Analysis of extra downtime
for preventive service of four major classes of vessels
(2012 to 2016)

Major reason	Extra downtime (Number of days)				
	2012	2013	2014	2015	2016
Extra work not covered in service contract	13	20	77	102	183
Waiting for spare parts	3	46	64	38	95
Bad weather	15	17	11	11	44
Interference of dockyard facilities/unavailability of dry-berth	3	6	3	7	37
Crew staff for dock & sea trial not available (including crew of user departments)	13	9	10	9	36
Dock/sea-trial defect	7	13	16	1	26
Slow work progress of contractor	1	6	8	13	4
Others (Note)	—	17	37	15	32
Total	55	134	226	196	457
Budgeted downtime	3,987	3,384	3,070	2,448	3,590

Source: MD records

Note: Examples were extra days for dimension measurements, remedial hull painting work, and material warranty claims to suppliers.

Remarks: Vessels with preventive services completed within the budgeted downtime were excluded from the above analysis.

3.12 ***Need to minimise extra downtime.*** Extra downtime is disruptive to the normal operation of the user departments and should be minimised as far as possible. As shown in Table 9, the total extra downtime increased by sevenfold from 55 days in 2012 to 457 days in 2016. The MD needs to look into the contributing factors to see whether there is room for improvement. In this connection, Audit has the following observations:

- (a) ***Extra work not covered in service contract (183 days).*** This has caused delays to the maintenance work of 32 vessels by 1 to 17 days each (averaging 5.7 days) in 2016. As the scope of maintenance in the contracts is determined by the MS based on the defect lists provided by the user departments and the pre-docking inspections of the vessels (see para. 1.10(a)), the increase in downtime due to extra work suggests that there may be room for improvement in conducting vessel inspection. Audit understands that some defects may be found after a vessel is opened up for inspection during preventive service. However, extra work after the award of a contract may entail a contract variation (with possible time and cost implications) which should be kept to a minimum wherever practicable;
- (b) ***Waiting for spare parts (95 days).*** A total of 13 vessels were delayed for this reason by 1 to 24 days each (averaging 7.3 days). There is a need to review the adequacy of spare parts planning and management;
- (c) ***Interference of dockyard facilities/unavailability of dry-berth (37 days).*** This has caused delays to 9 vessels by 1 to 9 days each (averaging 4.1 days). The situation calls for a review of the scheduling arrangements; and
- (d) ***Crew staff for dock and sea trial not available (36 days).*** A total of 17 vessels were delayed by 1 to 7 days each (averaging 2.1 days). Audit understands that there might be times when some trials could not be conducted due to public holidays and unavailability of crew staff of user departments who might be deployed for emergency duties. However, for those cases with long delay, the MD needs to explore ways to improve the coordination between the crew staff and maintenance staff.

Running repair

3.13 Running repair of vessels due to accident, damage, machinery breakdown or malfunctioning is carried out as and when required. The MD has put in place procedures for monitoring the downtime for running repair, i.e. requiring the maintenance teams to provide monthly progress reports to the Senior Maintenance Manager of the MS for running repair jobs exceeding 3 months. However, apart from monitoring the downtime, there is also a need to review those running repair cases occurring shortly after preventive service to see if there are lessons to be learnt. Based on the GFIS records as at 25 July 2017, there were five running repair cases (each lasting 5 days or more) occurring within about 3 months of preventive service. Case 3 is a case in point.

Case 3

Flooding of a high-speed craft of the HKPF shortly after preventive service

1. On 30 June 2017, a high-speed craft of the HKPF berthed at one of its operational bases was found to have sustained serious flooding of the engine, battery, steering and cockpit compartments with the stern of the craft submerged. The craft was subsequently towed back to the Government Dockyard for inspection and repair. In September 2017, the MD sent a copy of its initial investigation report to the HKPF for comments.

Audit comments

2. According to the MD's records, the flooded craft had been in service since 2004. It had undergone preventive service at the Government Dockyard in the past three years (from 2015 to 2017). The latest preventive service lasted for 36.75 days (from 27 March to 2 May 2017). In other words, the flooding incident occurred in about 2 months after the preventive service which was an unusual case requiring further investigation. The MD, in collaboration with the HKPF, needs to complete the investigation as soon as possible to see whether there are lessons to be learnt for preventing recurrence of similar problem.

Source: MD and HKPF records

Management of maintenance contracts

3.14 The MD has maintained a list of two groups of pre-approved maintenance service providers for invitation of tenders/quotations for its maintenance jobs, one group for job value up to \$50,000 and the other group for jobs of any value. For admission into the MD's pre-approved maintenance service provider list, a service provider: (a) must be a practising shipbuilder or ship repairer with a pre-requisite number of years of experience in the business; (b) must have adequate machines and tools for the relevant trades; (c) must have supervisors in the relevant trades to be based at the Government Dockyard; and (d) must have sufficient number of directly employed qualified technicians in the related trades. As of August 2017, the MD had 45 pre-approved maintenance service providers in six trades (e.g. engine repair).

3.15 The MD lets out its maintenance contracts on the following basis:

- (a) **Term contracts.** Term contracts are awarded to maintenance contractors for providing specific types of maintenance service (e.g. engine maintenance) over a contract period of one to two years. During the contract period, the contractors are required to provide the services as and when required, and at the contract rates; and
- (b) **One-off contracts.** For one-off contracts, the MD has to invite tenders/quotations each time a maintenance service is required. A one-off contract may be used for providing preventive service of a particular vessel or small-scale urgent repair service.

3.16 The number of maintenance contracts and estimated contract values for the past five financial years (2012-13 to 2016-17) are shown in Table 10.

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Table 10

**Number of maintenance contracts and estimated contract values
(2012-13 to 2016-17)**

Financial Year	Term contract			One-off contract			Total (\$ million)
	(No.)	(\$ million)	(%)	(No.)	(\$ million)	(%)	
2012-13	32	24.1	28%	3,301	63.2	72%	87.3
2013-14	30	25.5	23%	3,582	85.0	77%	110.5
2014-15	39	28.5	26%	3,982	81.6	74%	110.1
2015-16	31	31.1	25%	3,793	94.0	75%	125.1
2016-17	33	29.1	17%	3,671	144.3 (Note)	83%	173.4

Source: MD records

Note: The increase in estimated contract value in 2016-17 was mainly due to the increase in the number of major vessels receiving preventive service, i.e. 144 in 2016 compared with 112 and 113 in 2014 and 2015 respectively.

3.17 Guidelines on procurement and contract management. According to the SPRs, it is the Government policy to procure stores and services through fair and competitive procedures. The SPRs have stipulated that:

- (a) purchases of similar services should be consolidated for reducing administrative cost and obtaining discounts through bulk purchase contracts; and
- (b) for procurement with limited competition in past exercises, Controlling Officers should explore measures to enhance competition and satisfy themselves that the tendering or consultants selection strategy to attract new bidders is effective.

In addition, according to “User Guide to Contract Management” issued by the Efficiency Unit, contract size is an important factor that affects the interest of potential

bidders and departments should consider bundling logically related services into a single, sizeable contract to reduce the cost of contract administration and make it more attractive to potential bidders.

Need to enhance competition in the procurement of maintenance services

3.18 In 2016-17, the MD had 33 term contracts at a total estimated contract value of \$29.1 million all awarded by quotations. Among the 33 term contracts, Audit noted that 23 (70%) were each awarded to the only bidder, indicating that there had been limited competition in the procurement exercises. In July 2017, the FSTB expressed similar concern when commenting on the MD's management of one of these term contracts (see para. 3.24(b)). As invitations to bid had been sent to 15 to 31 maintenance service providers in each of these procurement exercises, there is a need to explore other measures to make the contracts more attractive to the potential bidders to enhance competition.

3.19 ***Measures taken to lengthen the duration of one-year term contracts.*** Of the 33 term contracts in 2016-17, 16 (48%) were one-year contracts (for 3 consecutive terms in 15 cases and for 2 consecutive terms in one case). According to the Efficiency Unit's report "A General Guide to Outsourcing" of 2008, "Departments should determine the optimum scope of outsourcing from the point of view of both the department and the potential service providers. Surveys of departments and service providers have identified the loss of economy, efficiency and effectiveness in letting contracts that are too small and have short contract duration". Audit noted that the MD had commenced a review of the term contracts' duration since January 2017. Up to August 2017, 21 out of 25 term contracts had been awarded with a two-year term. Among these 21 two-year term contracts, 8 were one-year contracts, 5 were 1.5-year contracts and 8 were 2-year contracts in their respective preceding terms.

3.20 ***Need to consider bundling of similar services in a single contract.*** Audit's further examination of the 16 one-year term contracts (see para. 3.19) revealed that 9 (56%) were for providing related services:

- (a) 6 (37%) contracts were for the repair and maintenance of engines of police vessels/speed craft (in particular two contracts were for the maintenance of outboard engines of the same maker and other onboard equipment); and

Maintenance of government vessels

- (b) 3 (19%) contracts were for the docking and undocking of government vessels.

Audit noted that these 9 contracts were of small values, ranging from \$0.49 million to \$1.4 million. The MD needs to consider bundling related maintenance services into reasonably sizeable contracts to reduce the cost of contract administration and make them more attractive to potential bidders whilst minimising the risk of over-reliance on a particular bidder for the required maintenance services.

Need to enhance job order and payment control under term contracts

3.21 *Long outstanding payments.* According to the MD's laid-down procedures, when maintenance work is required under a term contract, the responsible inspector should issue a job order to the contractor and seek his supervisor's approval before commencement of the work. After completion of work, the responsible inspector should forward the contractor's invoice to the Administration Branch (formerly the Accounting Services Section) for vetting and processing payment. In 2014, in the course of renewing a term contract for the maintenance and repair of five HKPF vessels in 2014-15, the MD was informed by the contractor that payments totalling \$1.68 million for 98 work items completed under four preceding contract terms from 2010 to 2014 were still outstanding.

3.22 The MD's subsequent investigation revealed that the incident was caused by the failure on the part of the subject inspector to submit:

- (a) the relevant job orders to his supervisor for approval before asking the contractor to carry out the maintenance and repair work; and
- (b) the relevant invoices received from the contractor to the Accounting Services Section for processing payment as he found that there was insufficient balance in the approved contract value to cover the payments required.

3.23 After obtaining confirmation from the HKPF that all 98 work items had been completed to its satisfaction and advice from a law enforcement agency that there was no pursuable case after its investigation of the incident, the MD sought the

FSTB's approval in May 2017 to increase the contract values of two expired term contracts for settling the relevant outstanding payments. The MD also informed the FSTB that the following measures had been introduced to enhance the management of term contracts:

- (a) bi-weekly review of all term contracts would be conducted by a designated officer at Maintenance Manager rank on any work item in the GFIS without job orders to ensure issue of job orders in reasonable time;
- (b) the Government Dockyard officers at Chief Technical Officer rank had been reminded to closely monitor spending under term contracts to avoid actual payment exceeding the budget sum;
- (c) the GFIS was enhanced to assist the management in monitoring the actual expenditure against the relevant term contracts, e.g. an e-mail would be sent out to all staff concerned when the total commitment of a term contract had met 80% and 90% of its total contract value;
- (d) a new circular was issued in April 2016 to alert all MS inspectors on the control and monitoring of vessel maintenance expenditure;
- (e) all work orders without job orders in the GFIS would be brought to the attention of the MS management in every two-week interval for follow-up actions; and
- (f) all invoices issued by term contractors should be submitted to the Administration, Tender and Security Services Unit of the Administration Branch centrally.

3.24 When granting approval to the MD's proposed increase in contract values in July 2017, the FSTB also advised that:

- (a) in view of the severity of the problems revealed, the MD should closely monitor its procurement and payment mechanism, and implement robust measures to rectify any malpractice, so as to prevent similar incidents from occurring again; and

Maintenance of government vessels

- (b) noting that there had been limited competitions in the past procurement exercises of the subject contract, the MD should explore ways to enhance competition in future procurement exercises (see para. 3.18). In this connection, it was noted that the MD would:
 - (i) refine the method of estimating the amount of procurement and consult user departments in the process so that more precise projection could be drawn up as far as possible;
 - (ii) critically review whether it was more appropriate to use tender procedures (instead of quotation procedures — see para. 3.18) in future; and
 - (iii) try to consolidate similar term contracts for maintenance/repair of vessels into one single contract when opportunities arose, with an aim of achieving economies of scale.

3.25 In Audit's view, the MD needs to closely monitor the implementation of the new measures introduced (see para. 3.23) to tighten job order and payment control under maintenance term contracts.

Audit recommendations

3.26 **Audit has *recommended* that the Director of Marine should:**

- (a) **closely monitor the decreasing trend in vessel availability rates and take effective measures to achieve the target rate of 87%;**
- (b) **in consultation with relevant stakeholders (including user departments and the THB), explore if there are better ways to report vessel availability rates in the COR, including:**
 - (i) **expanding the scope of reporting to cover all four major classes of vessels;**

- (ii) **reviewing the current practice of calculating the vessel availability rates without taking into account the downtime for repair outside the Government Dockyard; and**
 - (iii) **providing explanatory notes in the COR in case of any limitation in the scope of reporting vessel availability rates (such as classes of vessels and downtime excluded from the calculation of the reported rates);**
- (c) **closely monitor the increasing trend in downtime and take effective measures to minimise the extra downtime for preventive service, such as:**
 - (i) **improving the pre-docking inspection of vessels to ensure all necessary maintenance and repair work requirements are incorporated in the maintenance contracts as far as possible;**
 - (ii) **improving material planning and management to minimise waiting time for spare parts;**
 - (iii) **improving the scheduling arrangement to minimise interference of dockyard facilities/unavailability of dry-berth for maintenance work; and**
 - (iv) **improving the coordination between the crew staff of user departments and the maintenance staff to ensure timely conduct of dock and sea trials;**
- (d) **review running repair cases occurring shortly after preventive service to see whether there are lessons to be learnt (see para. 3.13);**
- (e) **continue to enhance competition in the procurement exercises of vessel maintenance services, such as:**
 - (i) **sustaining the efforts to review the duration of one-year term contracts with a view to enhancing their viability to attract bidders; and**

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- (ii) **considering bundling related maintenance services into reasonably sizable contracts to reduce the cost of contract administration and make them more attractive to potential bidders where appropriate; and**
- (f) **closely monitor the implementation of the new measures introduced (see para. 3.23) to tighten job order and payment control under maintenance term contracts.**

Response from the Government

3.27 The Director of Marine agrees with the audit recommendations. She has said that:

- (a) the MD will continue to seek improvement in providing maintenance services for government vessels;
- (b) in consultation with relevant parties, the MD will enhance the presentation of vessel availability in the COR; and
- (c) in order to further enhance competition in the procurement of vessel maintenance services, the duration of contracts will be reviewed and further bundling of contracts will be explored.

PART 4: MANAGEMENT OF MAINTENANCE MATERIALS

4.1 This PART examines the MD's management of maintenance materials, including spare parts for government vessels and the Government Dockyard's facilities. Some of the materials used/stored in the Government Dockyard are controlled under the Dangerous Goods Ordinance (Cap. 295). According to Section 3 of the Dangerous Goods Ordinance, the provisions of the Ordinance do not apply to the Government. Nevertheless, the MD is committed to minimising potential hazards and risks, and ensuring that all its staff and workers work in a safe and healthy environment.

Stock management

4.2 It is the MD's practice to provide maintenance materials for use of its in-house staff and contractors in carrying out maintenance/repair work. The Supplies Services Unit (SSU) of the Finance Section (see Appendix A) is responsible for the procurement of maintenance materials. In the past three financial years from 2014-15 to 2016-17, the MD spent, on average, \$132.2 million a year on procuring maintenance materials.

4.3 Maintenance materials (including repairable items taken out from vessels which can be reused after repair) are kept in the main store, 8 minor stores and 3 container stores of the Government Dockyard. The MD uses the GFIS to maintain information about maintenance materials (e.g. part description, quantity, price and date of receipt and issue) for stock management purposes. Table 11 shows the year-end stock values of maintenance materials for the past five financial years from 2012-13 to 2016-17.

Table 11

**Year-end stock values of maintenance materials
(2012-13 to 2016-17)**

Financial year	Stock value as at 31 March		
	Purchased and repaired item	Repairable item pending repair	Total
	(\$ million)		
2012-13	233.9	5.0	238.9
2013-14	218.1	9.0	227.1
2014-15	232.5	12.4	244.9
2015-16	248.9	11.9	260.8
2016-17	258.5	15.5	274.0 (Note)
Average	238.4	10.8	249.2

Source: MD records

Note: There were some 17,000 stock items as at 31 March 2017.

4.4 **Stock management guidelines.** To enhance stock management of the Government Dockyard, the GFD issued a circular in 2008 (currently in force) which laid down the following requirements:

- (a) reviewing regularly the optimum/minimum level of spare sets of engines and major components or equipment kept in the main store of the Government Dockyard; and
- (b) stepping up stock review and stocktaking exercise to identify and minimise obsolete/dormant and slow-moving items.

Need to take timely follow-up action on obsolete/dormant stocks

4.5 After a stock review in July 2013, the SSU identified 8,023 items of slow-moving stock (i.e. those without movement for over five years) with a total value of \$54.6 million. In April 2015, the SSU informed relevant sections in the MD that it intended to review the 8,023 slow-moving items by phases, with the first phase covering 547 items (including 50 items with value above \$50,000 each). In January 2017, the Assistant Director of the GFD raised concern (after his visit to the Government Dockyard storehouse) that some spare parts were very old, broken and unserviceable. The SSU then suggested that the MS should assign an experienced inspector to conduct a joint inspection on the slow-moving stock items. In its e-mail to the MS of January 2017, the SSU said that while new spare parts were procured for future maintenance of new vessels, outdated spare parts were not always disposed of together with the replaced vessels (Note 26). As a result, more and more spare parts had been accumulated but the storage spaces could not be expanded to accommodate more spare parts in a short time.

4.6 *Audit examination.* For a comparison of the current position of slow-moving stock with that in 2013 (see para. 4.5), Audit requested the MD to extract relevant information from the GFIS for analysis. Of 16,473 stock items held by the Government Dockyard as at 30 June 2017, 8,412 were slow-moving items (5% up from 8,023 in 2013) with a total value of \$73 million (34% up from \$54.6 million in 2013). An analysis of these slow-moving items shows that 2,128 items with a total value of \$10.5 million had been kept for more than 20 years, i.e. longer than the expected lifespans of all types of vessels in the existing government fleet (see Table 12).

Note 26: From 2012 to 2016, a total of 61 vessels had been disposed of.

Table 12**Analysis of slow-moving stock items
(30 June 2017)**

Period without movement (Note)	Number of stock items	Amount	
(Year)	(Number)	(\$ million)	(%)
> 5 to 20	6,284	62.5	86%
> 20	2,128	10.5	14%
Total	8,412	73.0	100%

Source: Audit analysis of MD records

Note: The period is counted from the date of last movement to 30 June 2017.

4.7 Upon Audit's enquiries in July and September 2017, the MD said that:

- (a) the review of slow-moving stock items required technical knowledge and involved the SSU, Material and Planning Management Unit and MS. Out of the 547 items identified in 2013, 68 items were disposed of in July 2016;
- (b) it was necessary for some spare parts to be kept longer than 20 years (see para. 4.6) because it was not uncommon for a government vessel to remain in service after its expected lifespan if the vessel was well maintained. The manufacturers of the vessels might cease producing the relevant spare parts. Moreover, some spare parts could be modified to be used in other government vessels;
- (c) the Task Force on Reform (see para. 1.13) was aware of the problem of slow-moving stock items but follow-up action could only be taken starting from January 2017 (see para. 4.5) because there was a need to prioritise reform work of the GFD and the need to identify expertise to undertake the task; and

- (d) in April 2017, a working group was formed to carry out a review of the slow-moving stocks. To speed up the review process, it was considered necessary to involve additional manpower in the review for sorting out the spare parts for various types of government vessels. In mid-July 2017, the MD employed a Technical Adviser (with marine engineering background) on contract terms to review the slow-moving stock items. Judging from the complexity of the process, the MD aimed to complete the review in about 12 to 15 months, subject to a progress review in 6-month time, i.e. January 2018.

4.8 Audit noted the MD's recent actions to review the remaining 7,476 (8,023 less 547 — see para. 4.7(a)) slow-moving stock items identified in 2013. However, the delay of some 4 years before taking follow-up action on such items is unsatisfactory as any obsolete/dormant stock could not be disposed of in a timely manner to save storage space and realise any resalable value where commercial disposal is applicable. Moreover, the increase in slow-moving stock from 8,023 items in 2013 to 8,412 items as of June 2017 indicates that the MD needs to step up stock review to identify obsolete/dormant and slow-moving stock items.

Deficiencies of the GFIS for stock management purposes

4.9 The GFIS was commissioned in 1994 and enhanced twice in 1999 and 2015 (Note 27). The GFIS aims to provide an integrated operation platform operating under a system of web-based applications for the Government Dockyard to manage its physical assets, plan maintenance activities and initiate the processes of maintenance/spare part procurement for all government vessels and Government Dockyard plant facilities. The GFIS provides a repository of up-to-date information that facilitates the real-time retrieval of required information by the users and it can also be used to monitor and control budgets as well as expenditures for management over vessel maintenance, and assess the need for replacing a vessel.

4.10 However, Audit found that some intended benefits of the GFIS could not be realised despite the system enhancements in 1999 and 2015, as follows:

Note 27: *In addition to stock management, the GFIS was also used to coordinate maintenance activities and support services. The system enhancement in 2015 cost \$8.5 million.*

Management of maintenance materials

- (a) ***Stock re-order level.*** The GFIS was designed to generate the re-order level of a stock item to remind relevant MD staff to initiate replenishment process. However, Audit found that as at 30 June 2017, the stock levels of 1,979 inventory items were below their re-order levels indicated in the GFIS. In response to Audit's enquiry, the MD said that the re-order levels generated by the GFIS could not fully reflect the current stock replenishment practice of the Government Dockyard which had to take account of many factors, e.g. the consumption rates, frequencies of use, different maintenance cycles of various types of machinery, whether they were critical for certain vessel(s), re-order lead time, and whether the items were covered under bulk purchase contract(s) or not. The stock replenishment practice was still under review and the GFIS might need fine-tuning at suitable juncture; and
- (b) ***Use of barcodes.*** The GFIS was designed to support the use of barcode identification technology to facilitate the monitoring of spare parts distribution and consumption, and automatic updating of inventory level. While the GFIS could generate barcodes for inventory items in the Government Dockyard stores, Audit found that they could not be used to automate the stock management operations. According to the MD, while there was limitation of scanning barcode into the GFIS to record the receipt and issue of stocks having regard to the existing workflow of stock movement at this stage, the possibility of adopting barcode scanning technology in receipt and issue of stocks to automate the processes would be covered in the review on the SSU to be conducted by the Task Force on Reform in the last quarter of 2017.

4.11 In Audit's view, the MD needs to take prompt actions to enhance the functions of the GFIS to ensure that it can support the Government Dockyard in effectively managing the vast stock of maintenance materials with an aggregate value of over \$200 million.

Audit recommendations

4.12 **Audit has recommended that the Director of Marine should:**

- (a) **step up stock review to identify slow-moving stock items and take timely follow-up actions to dispose of any obsolete/dormant stock; and**

- (b) **take prompt action to enhance the functions of the GFIS (see para. 4.10) to ensure that it can support the Government Dockyard in effectively managing its vast stock of maintenance materials.**

Response from the Government

4.13 The Director of Marine agrees with the audit recommendations. She has said that the MD will speed up the disposal of obsolete/dormant stock and enhance the functions of the GFIS in order to improve the stock management system in the GFD.

Management of dangerous goods

4.14 ***Dangerous goods used and stored in the Government Dockyard.*** In the course of repairing or maintaining government vessels, the MD's in-house staff and contractors are required to handle dangerous goods controlled under the Dangerous Goods Ordinance, as follows:

- (a) ***Diesel and petrol.*** Diesel and petrol are classified as Category 5 dangerous goods which give off inflammable vapour. To minimise fire risk, vessels undergoing maintenance/repair in the Government Dockyard are required to empty their fuel tanks first. Their fuel will be conveyed to approved stores of the Government Dockyard for temporary storage (i.e. diesel is pumped into the underground bulk storage of the Fuel and Oil Store and petrol in portable containers are stored in a dangerous goods store) and subsequent refuelling the vessels after completion of the maintenance/repair work;
- (b) ***Oxygen and acetylene gas cylinders.*** Oxygen and acetylene cylinders are classified as Category 2 dangerous goods containing compressed gas. The maintenance contractors bring along their own oxygen and acetylene cylinders for welding and cutting of metal. According to the MD, several vessels may require hull plating renewal at the same time and use of a large number of oxygen and acetylene cylinders is inevitable; and
- (c) ***Paints and thinner.*** Paints and thinner are also classified as Category 5 dangerous goods which give off inflammable vapour. For major vessel

Management of maintenance materials

maintenance, large quantities of paints are required especially for painting the hull. According to the MD, most vessels consume 300 litres of paints for hull painting and up to 900 litres for a few large vessels. The maintenance contractors could request the Government Dockyard to provide the required quantity of paints and thinner. After vetting and approval of the requests, the contractors could draw out the paints and thinner from the Government Dockyard's dangerous goods stores.

4.15 According to Section 6 of the Dangerous Goods Ordinance, no person shall manufacture, store, convey or use any dangerous goods except under and in accordance with a licence granted by the FSD under the Ordinance. The Dangerous Goods (General) Regulations (Cap. 295B) provide for some exemptions from such licensing requirement for the storage and conveyance of Categories 2 and 5 dangerous goods as shown in Table 13.

Table 13

Maximum storage and conveyance quantity of three types of dangerous goods exempted from licensing requirement

Dangerous goods	Maximum exempted quantity
Diesel and petrol	20 litres for petrol and 2,500 litres for diesel
Oxygen and acetylene cylinders	Two cylinders each for oxygen or acetylene
Paints and thinner	250 litres for paints and 20 litres for thinner

Source: Dangerous Goods (General) Regulations

4.16 While the provisions of the Dangerous Goods Ordinance do not apply to the Government, the MD has obtained the FSD's approvals on the quantities of the dangerous goods kept in its 10 dangerous goods stores (see Appendix E for details). According to the FSD, all dangerous goods not in use shall be returned to designated dangerous goods stores for safe storage.

4.17 In 2016, the MD commissioned a consultant to conduct a pre-feasibility study of the modernisation of the Government Dockyard. In its “Final User Interview and Site Study Report” of April 2017 and draft “Report of Best Practices, New Technologies and Equipment” of May 2017, the consultant pointed out the following issues in the MD’s management of dangerous goods in the Government Dockyard:

- (a) ***Handling of diesel and petrol.*** While vessels should dock in the Government Dockyard with a minimum quantity of fuel in the boat, in practice, it was not the case. The existing arrangement was that diesel was unloaded from vessels to tanks of 2,500 litres each which were mounted on a trawler and conveyed to the Fuel and Oil Store (see para. 4.14(a)). Petrol was unloaded to containers of 200 litres each for transfer to the dangerous goods store. As the Fuel and Oil Store for diesel and the designated dangerous goods store for petrol were away from the docking area and the defueling area, there was a long travelling distance for the transfer of fuels (see Appendix F for a layout plan of the Government Dockyard). Manual handling of petrol and diesel further increased the possibility of accidents;
- (b) ***Storage of oxygen and acetylene cylinders.*** Notwithstanding that five dangerous good stores (see Appendix E) were provided for storage of oxygen and acetylene cylinders, the actual utilisation of these stores was low probably because of the long distance between the boat repair sheds and the dangerous goods stores. It was noted that cylinders had not been returned to the approved dangerous goods stores but stayed overnight at the boat repair sheds (Note 28); and
- (c) ***Storage of paints and thinner.*** Similar to the oxygen and acetylene cylinders, three dangerous goods stores were designated for storage of

Note 28: *In October 2017, the MD informed Audit that according to its understanding, there were no explicit stipulations in the Dangerous Goods Ordinance not allowing oxygen and acetylene cylinders to stay overnight. In fact, Occupational Safety and Health Administration under the Department of Labour of the United States Government explicitly stated that the oxy-acetylene cylinders: (i) in the general work industry were not considered to be in storage when they were either “in use” or “connected for use”, and (ii) in the construction industry were considered to be in use when it was reasonably anticipated that gas be drawn from the cylinder within 24 hours. In this regard, the MD had liaised with the FSD and Labour Department for their advice. Considering that there would be clearer interpretations of the related Regulations, the Government Dockyard was prepared to better use the dangerous goods stores in accordance with the safety requirements.*

paints and thinner. However, they were also far away from the boat repair sheds which caused inconvenience to the maintenance contractors. This led to inefficiency in operation and discouraged the return of unused paints and thinner to the designated stores after daily operation.

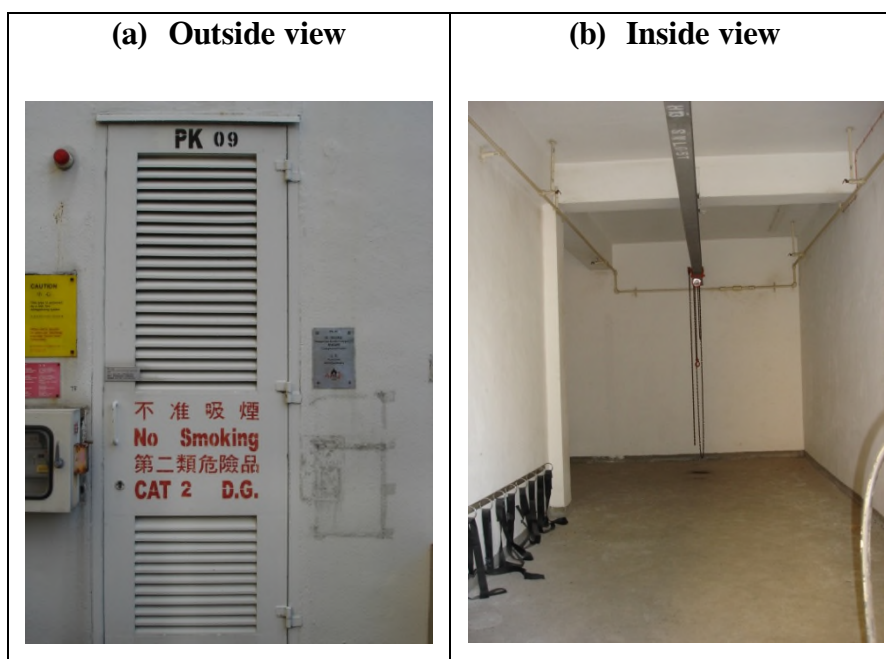
4.18 For a better understanding of the scale of the abovementioned issues in management of dangerous goods, Audit examined the relevant operation records provided by the MD and noted the following issues:

- (a) ***Handling of diesel and petrol.*** According to the MD, user departments had been advised to keep the quantity of fuel in a vessel to the minimum before it entered the Government Dockyard for service, although there might be practical difficulties to comply with the requirement in some cases, e.g. vessels returning to the Government Dockyard for unscheduled running repairs. Moreover, vessels of the law enforcement agencies needed to carry a certain quantity of petrol for operational reasons. In 2016, 39 petrol-fuelled vessels arrived at the Government Dockyard for maintenance service (comprising 18 for preventive service and 21 for running repair). Their fuel tanks (with storage capacity ranging from 200 to 1,300 litres) were 68% full on average. In one extreme case, a vessel was full-tanked (i.e. 500 litres) when it arrived at the Government Dockyard. As a result, the Government Dockyard had to handle large quantity of petrol unloaded from these vessels;
- (b) ***Storage of oxygen and acetylene cylinders.*** According to the GFD (Government Dockyard) Safety Management Manual, maintenance contractors should keep their number of gas cylinders at a minimum and gas cylinders in excess of the exempted quantities should be kept in the specified dangerous goods stores. However, Audit found that the MD had not tracked the quantities of oxygen and acetylene cylinders stored/used by the maintenance contractors in the Government Dockyard to facilitate its monitoring of the compliance with the Safety Management Manual requirements. Audit inspections around 5 p.m. (towards the end of the normal operation hours of the Dockyard) on 16 August 2017 revealed that three major dangerous goods stores designated for the storage of the two types of cylinders were empty (see Photograph 2(b) for an example), indicating that the consultant's observed practice of gas cylinders not returning to the designated stores after daily operation had continued (see para. 4.17(b)). There is a need to devise, in consultation with the FSD,

a feasible and safe work practice for returning surplus gas cylinders, if any, to the approved dangerous goods stores when they are not in-use; and

Photographs 2(a) and (b)

Acetylene cylinder not found in the largest approved dangerous goods store



Source: Photographs taken by Audit staff on 16 August 2017

- (c) **Storage of paints and thinner.** Audit examination of the MD's stock records revealed that on 81 days during January to July 2017, about 15,800 litres of paints and 3,360 litres of thinner were issued to the maintenance contractors for painting work of 117 vessels on 246 occasions (averaging 64 litres of paints and 14 litres of thinner on each occasion). According to the MD, the entire painting operation might take about 10 days depending on various factors such as vessel size, weather and humidity. On five occasions (see Table 14) with the largest quantities of both paints and thinner issued, there was no record to show that the unused paints/thinner had been returned to the dangerous goods stores after daily operation. The MD may consider issuing paints and thinner to meet the contractors' actual daily operation needs to minimise the safety hazards of unused paints/thinner (if any) not returning to the approved dangerous goods stores.

Table 14**Five occasions with the largest quantities of both paints and thinner issued**

Date of issue	Vessel	Quantity of paints issued (Litre)	Quantity of thinner issued (Litre)
13.2.2017	A	579	124
8.5.2017	B	540	80
3.7.2017	C	545	65
6.4.2017	D	520	88
21.6.2017	E	399	114

Source: Audit analysis of MD records

4.19 Audit noted that in March 2017 the MD engaged another consultant to provide advice on how the Government Dockyard could better manage the dangerous goods to meet both its operational needs and the requirements of the Dangerous Goods Ordinance and its Regulations. The study was targeted for completion around the first quarter of 2018. Between August and October 2017, the MD also informed Audit that:

- (a) taking the opportunity of recent renovation of the drenching system at the Fuel and Oil Store, the MD had requested the Electrical and Mechanical Services Department and the Architectural Services Department to explore the feasibility of installing a shore reception facility at the quay side which would allow direct transfer of petrol from vessels to the storage tanks. The MD had also reminded user departments to keep minimum fuel on board before sending their vessels to the Government Dockyard. The MD had been consulting the FSD to develop a permit-to-work system to enhance the safety for fuel transfer in the Government Dockyard; and
- (b) as regards the storage issue of oxygen and acetylene cylinders, the MD had reviewed the situation and taken improvement measures including stepping up safety patrols at the contractors' work sites, requiring them to keep records of the number of oxygen and acetylene cylinders in use and in

storage (Note 29), and encouraging them to store any spare gas cylinders in the designated dangerous goods stores. In addition, the GFIS would be utilised to better monitor, control and manage the number of gas cylinders used by the contractors in the Government Dockyard. In order to further enhance safety operation, the MD was actively liaising with the FSD and Labour Department to improve the handling procedures of gas cylinders as well as petrol/diesel.

4.20 While the MD should continue with the improved measures already rolled out, the MD needs to implement additional interim measures to minimise the safety hazards. For example, the MD needs to closely monitor the compliance with the Safety Management Manual requirements on the storage of dangerous goods and consider issuing paints and thinner to contractors based on their actual daily operational needs.

Audit recommendations

4.21 **Audit has *recommended* that the Director of Marine should:**

- (a) **closely monitor the progress of the ongoing consultancy study and feasibility study to develop long-term measures for further improving the management of dangerous goods in the Government Dockyard; and**
- (b) **implement additional interim measures to minimise the safety hazards in the Government Dockyard, such as closely monitoring the compliance with the Safety Management Manual requirements on the storage of dangerous goods and considering the issue of paints and thinner to contractors based on their actual daily operational needs.**

Note 29: *According to the MD, as at 30 August 2017, there were 27 cylinders each of oxygen and acetylene held by its maintenance contractors.*

Response from the Government

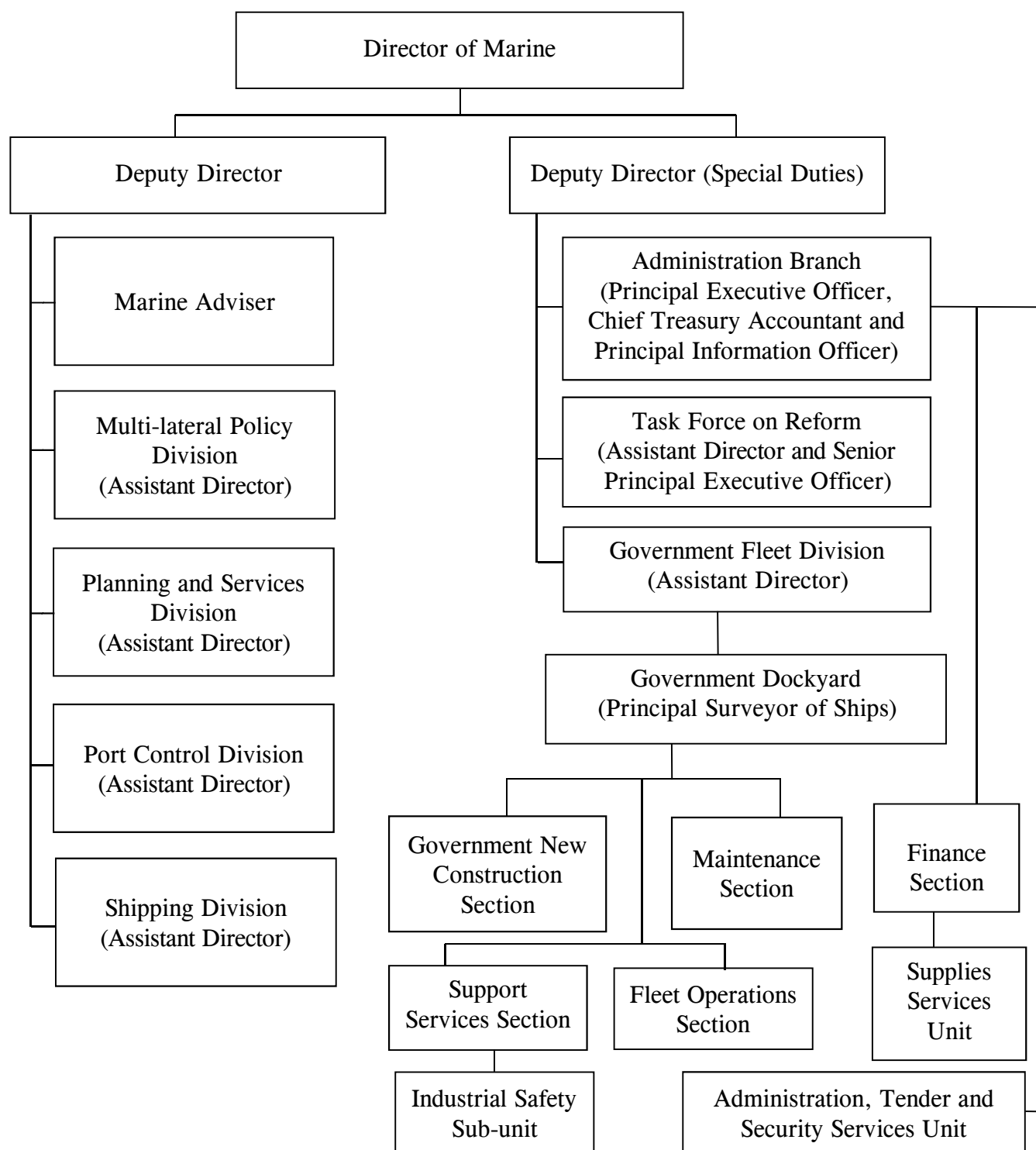
4.22 The Director of Marine agrees with the audit recommendations. She has said that:

- (a) the MD attaches great importance to industrial safety at the Government Dockyard; and
- (b) apart from commissioning a consultancy study to develop long-term measures for improving the management of dangerous goods in the Government Dockyard, the MD has obtained additional manpower resources to upgrade the Industrial Safety Sub-unit to an Industrial Safety Unit and put it under the purview of the Support Services Section. The Industrial Safety Manager who is the Unit Head of the Industrial Safety Unit assumed the post in October 2017.

4.23 The Director of Fire Services generally agrees with the audit recommendations in paragraph 4.21. He has said that:

- (a) all dangerous goods not in use (such as gas cylinders — see para. 4.18(b)) should be returned to the approved dangerous goods stores of relevant type for safe storage; and
- (b) as the MD is devising a safety management system and mitigation measures to control the process of diesel and petrol transfer in the Government Dockyard (see para. 4.19(a)), the FSD will provide assistance to the MD by giving fire safety advice on the use of appropriate container and conveyance process.

**Marine Department:
Organisation chart (extract)
(31 March 2017)**



Source: MD records

Appendix B
(paras. 1.5 and 3.5 refer)

**Government fleet of vessels
(31 March 2017)**

Department	Mechanised vessel		High-speed craft		Lighter	Dinghy/ inflatable boat	Beach craft/raft	Total
	MECV	MIMC	HSCL	HSCM				
	(Number)							
Leisure and Cultural Services Department						1	540	541
Hong Kong Police Force	36	6	10	43	6	9	17	127
Marine Department	25	2		5	21	4	1	58
Fire Services Department	9	5		2	1	16	9	42
Agriculture, Fisheries and Conservation Department	3	5		7		10		25
Customs and Excise Department	7		3	2		2	7	21
Civil Aid Service						11		11
Immigration Department	7							7
Water Supplies Department		3				4		7
Civil Engineering and Development Department	3							3
Correctional Services Department	2							2
Environmental Protection Department	1					1		2
Department of Health	1							1
Auxiliary Medical Service						1		1
Total	94	21	13	59	28	59	574	848

Legend: MECV = Major mechanised vessel MIMC = Minor mechanised vessel
 HSCL = High-speed craft (large type) HSCM = High-speed craft (medium type)

Source: MD records

**A chronology of events
of the tender marking scheme review**

Date	Event
December 2009	The CTB advised that the MD should conduct a review of the tender making scheme in consultation with the DoJ.
October 2010	The MD submitted a revised marking scheme for the DoJ's comments in the context of a procurement project for 11 speed craft of the HKPF (Note 1).
December 2010	The DoJ suggested that the MD should review the need for using a marking scheme. Since then, there were continuous exchanges of views and meetings between the MD and the DoJ. Subsequently, the discussion focused on how to standardise and trim the number of quality criteria in the marking scheme.
April 2011	The DoJ finalised and issued comments on the draft marking scheme to the MD, after a few earlier rounds of review and a meeting.
May 2011	With the DoJ's comments and corresponding amendments made on the draft, the revised marking scheme was submitted to the FSTB for comments before formal submission of the tender for the HKPF's speed craft for the CTB's approval. The FSTB later advised the MD that items in the marking scheme should be supported by measurable evaluation criteria. The MD then discussed with the HKPF on the FSTB's requirements and further revised the marking scheme.
July 2011	The further revised draft marking scheme was passed to the FSTB for comments.
August 2011	The FSTB advised the MD that some criteria for awarding marks on quality items should be more specific and accurate. The MD subsequently worked with the HKPF on the FSTB's comments. The FSTB gave further comments on the draft marking scheme and the mandatory requirements to the MD. The MD was further requested to consider adopting the life cycle cost approach in the price assessment stage (Note 2).
October 2011	Further to internal discussions and discussions with the HKPF, another version of the revised marking scheme was submitted to the FSTB for comments.

Appendix C
(Cont'd)
(para. 2.13 refers)

Date	Event
November 2011	The FSTB advised that the MD could put forward the revised marking scheme for the CTB's approval. To ensure that the revised marking scheme was legally in order, the MD sent the revised draft for the DoJ's comments. Apart from changes on the revised marking scheme, the DoJ also commented on other parts of the tender documents of the HKPF's speed craft project.
December 2011	The DoJ completed its review and issued to the MD its comments on the revised draft marking scheme.
January 2012	The revised marking scheme was sent to the FSTB.
February 2012	The DoJ proposed further textual changes to the marking scheme to align it with the rest of the tender documents. In the light of these changes, the MD sent another revised version of the marking scheme to the FSTB for approval.
April 2012	A meeting was held with the FSTB and it was concluded that the marking scheme for specific vessel type could be submitted for the CTB's approval instead of one standard marking scheme to cover all projects with due regard to the uniqueness of individual vessel characteristics.
May 2012	The FSTB requested the draft marking scheme of the HKPF's speed craft project be submitted for their preview and comments. On the basis of the FSTB's further comments, the further revised version came up eventually.
August 2012	The FSTB sent the price assessment criteria adopted for the supply of vehicles to the MD for reference. As a result, the MD revised the marking scheme again and a complete set of tender documents was sent to the DoJ for comments.
September 2012	The tender documents for the HKPF's speed craft project with the revised marking scheme cleared by the DoJ were formally submitted to the CTB for approval.
October 2012	The marking scheme for the HKPF's speed craft project was finally approved by the CTB.

Appendix C
(Cont'd)
(para. 2.13 refers)

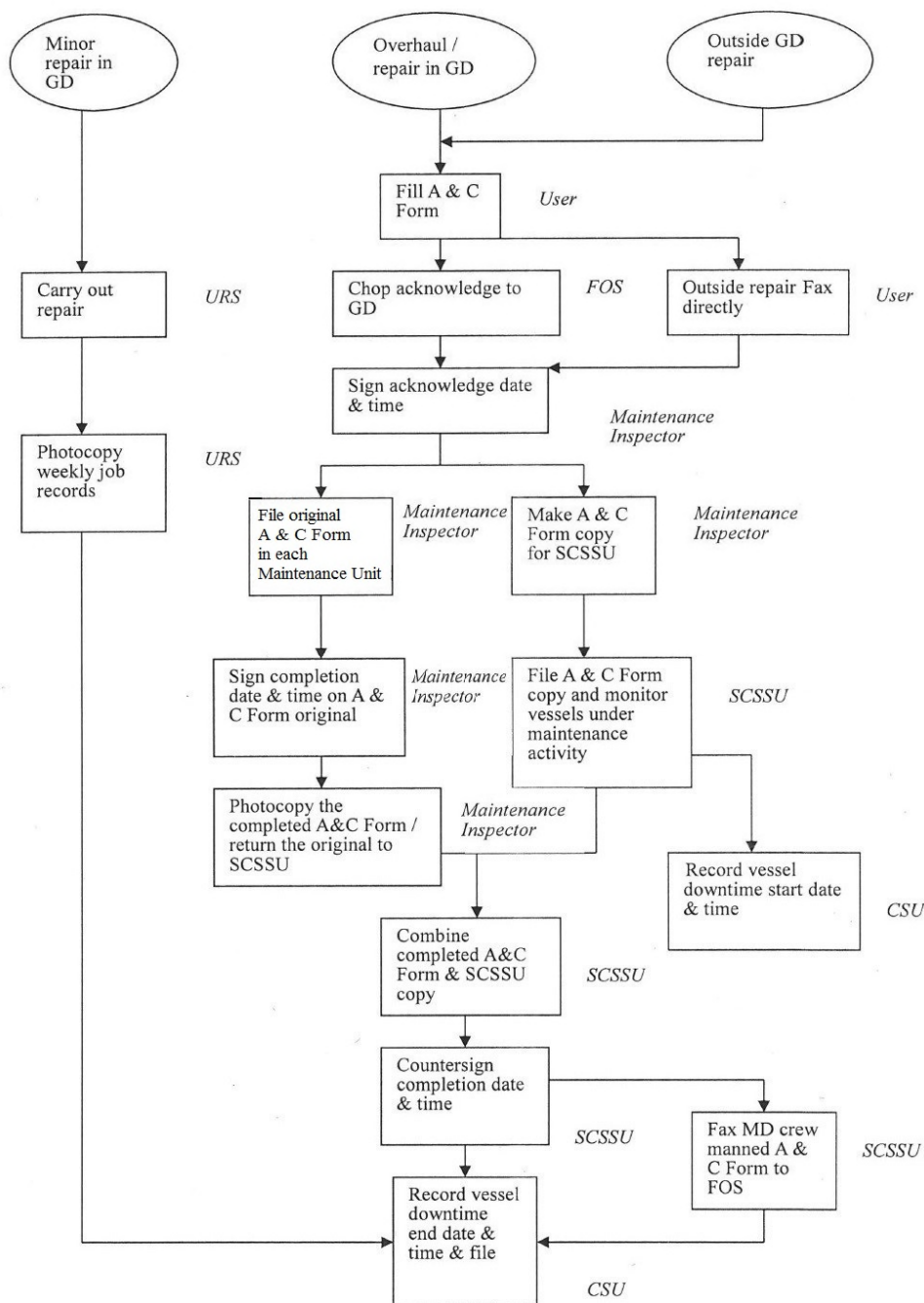
Date	Event
November 2012	The approved marking scheme was standardised to cover projects for speedboats with high performance engines. After obtaining the CTB's approval for its use for speedboats, the new marking scheme was applied to the tender for 11 speed craft with high performance engines for the HKPF in March 2013. For the tenders of two other projects, i.e. two catamaran speedboats for MD and a steel vessel for the ImmD in September 2013 and April 2014 respectively, relevant marking schemes were used after obtaining the GLD Tender Board's approval in 2014.
August 2014	The new marking scheme was used until FSTB Circular Memorandum No. 8/2014 was issued in August 2014 to remind bureaux/departments to avoid excessive use of marking scheme. The MD had stopped using marking scheme for new construction projects since then.

Source: MD records

Note 1: According to the MD, it would facilitate the consideration by the DoJ of the revised marking scheme through an actual vessel procurement project.

Note 2: According to the MD, considering that it was a totally new idea, the MD took some time to study and evaluate the idea and its implication prior to applying it to the marking scheme in order to ensure that the tender evaluation could be conducted in a pragmatic, feasible, accurate and fair manner.

Marine Department's quality manual of 2016 (extract)



Existing A&C Form Flow Chart as on May 2004

Legend: CSU = Clerical Services Unit FOS = Fleet Operations Section
GD = Government Dockyard URS = Urgent Repair Squad
SCSSU = Scheduling Coordination and Seatrial Sub-unit

Source: MD records

Appendix E
(paras. 4.16 and
4.17(b) refer)

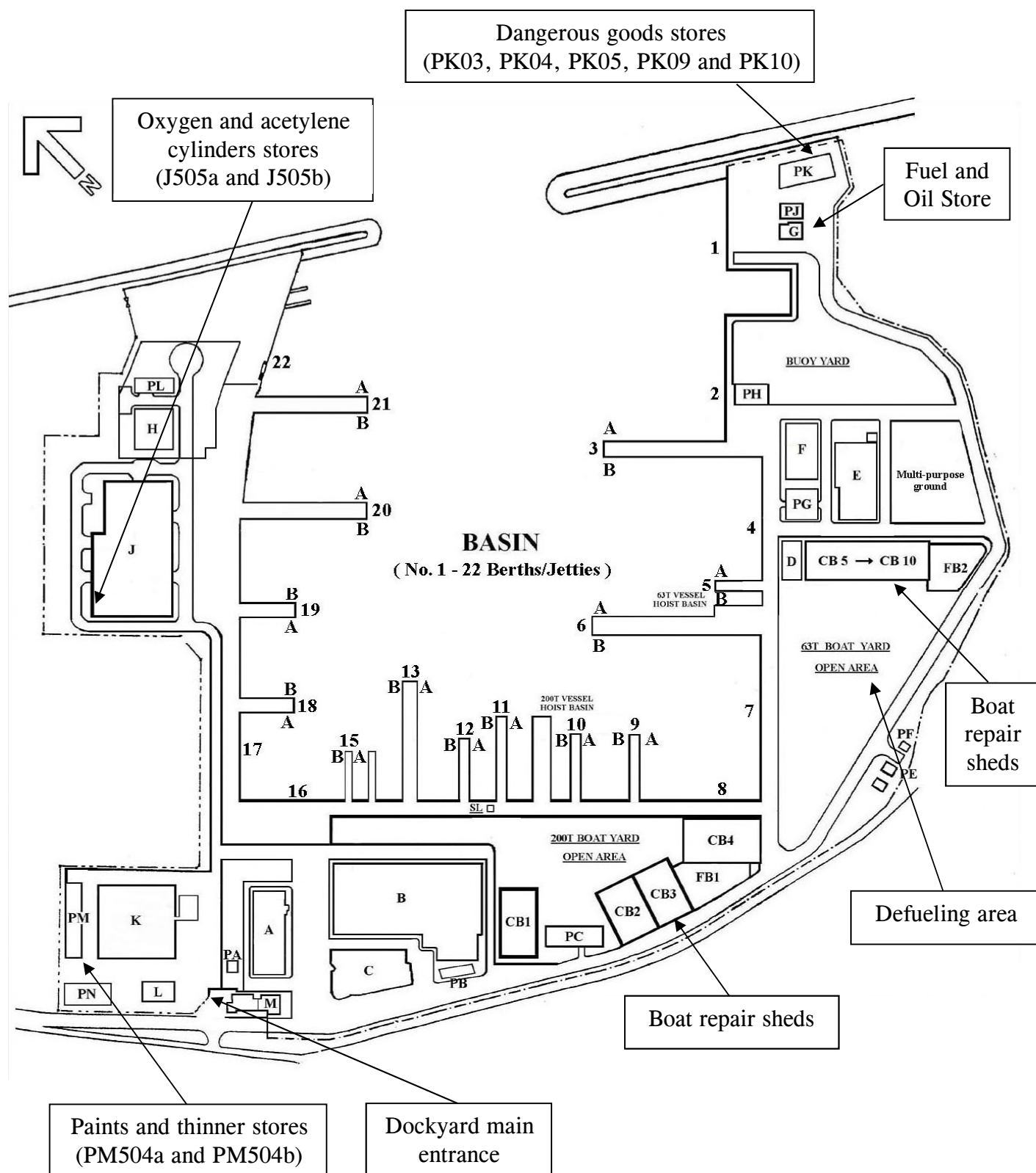
**Approved storage quantities of dangerous goods
at the Government Dockyard
(30 June 2017)**

Store (Note)	Dangerous goods stored	FSD approved quantities	Date of FSD's approval
<i>Diesel and petrol</i>			
Fuel and Oil Store	Diesel and petrol	120,000 litres of diesel 20,000 litres of petrol	February 1997 and December 1999
PK10	Petrol	7,000 litres	October 2013
<i>Oxygen and acetylene cylinders</i>			
PK04	Oxygen cylinder	8 × 65 kilograms/cylinder	July 1995
PK05	Oxygen cylinder	8 × 65 kilograms/cylinder	July 1995
PK09	Acetylene cylinder	40 × 65 kilograms/cylinder	October 1995
J505a	Oxygen cylinder	6 × 6.8 cubic metres/cylinder	January 2001
J505b	Acetylene cylinder	4 × 6.2 cubic metres/cylinder	January 2001
<i>Paints and thinner</i>			
PK03	Paints and thinner	6,000 × 5 litres/tin of paint 400 × 5 litres/tin of thinner	December 2009
PM504a	Paints and thinner	21,083 litres	November 1999
PM504b	Paints and thinner	21,000 litres	

Source: MD records

Note: Locations of the dangerous goods stores are shown in the layout plan of the Government Dockyard in Appendix F.

Layout plan of the Government Dockyard



Source: MD records

Acronyms and abbreviations

A&C Form	Arrival and Completion Form
AFCD	Agriculture, Fisheries and Conservation Department
Audit	Audit Commission
C&ED	Customs and Excise Department
COR	Controlling Officer's Report
CTB	Central Tender Board
DoJ	Department of Justice
FC	Finance Committee
FSD	Fire Services Department
FSTB	Financial Services and the Treasury Bureau
GFD	Government Fleet Division
GFIS	Government Fleet Information System
GLD	Government Logistics Department
GNCS	Government New Construction Section
HKPF	Hong Kong Police Force
HSCL	High-speed craft (large type)
HSCM	High-speed craft (medium type)
ImmD	Immigration Department
MD	Marine Department
MECV	Major mechanised vessel
MIMC	Minor mechanised vessel
MS	Maintenance Section
m	metres
SCOGC	Standing Committee on Government Craft
SoS	Surveyor of Ships
SPRs	Stores and Procurement Regulations
SSU	Supplies Services Unit
THB	Transport and Housing Bureau

CHAPTER 3

**Food and Health Bureau
Hospital Authority**

**Hospital Authority's management of
public hospital projects**

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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HOSPITAL AUTHORITY'S MANAGEMENT OF PUBLIC HOSPITAL PROJECTS

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HOSPITAL AUTHORITY'S MANAGEMENT OF PUBLIC HOSPITAL PROJECTS

Executive Summary

1. The Hospital Authority (HA) is a statutory body established under the Hospital Authority Ordinance (Cap. 113) to manage and establish public hospitals in Hong Kong. The Food and Health Bureau (FHB) is the policy bureau responsible for the overall health policies in Hong Kong including the development of public hospitals. As of September 2017, the HA managed 42 public hospitals and institutions (providing a total of about 28,000 beds) to provide public hospital services grouped under seven clusters. According to the HA, these hospital buildings covered a total floor area of 2.7 million square metres (m²) and 59% of the floor area had been in use for more than 30 years. To sustain the provision of public hospital services, the HA has initiated and undertaken public hospital projects with a view to achieving the objectives of: (a) meeting growing demand for healthcare services; (b) modernising the physical facilities of public hospitals; and (c) making the buildings safer.

2. Public hospital projects are broadly classified into two categories: (a) major hospital projects (each costing over \$75 million) which include the construction of new hospitals or the redevelopment/expansion of existing hospitals; and (b) minor hospital projects (each costing \$75 million or below) in existing hospitals to improve the conditions and environment of ageing facilities and to enhance their service capacity. During the 5-year period from 2012-13 to 2016-17, six major hospital projects had been completed. The funding approved by the Legislative Council's Finance Committee (FC) (i.e. Approved Project Estimate (APE)) of these projects totalled \$12.5 billion and ranged from \$590.5 million to \$3,910.9 million. The 2016 Policy Address announced a 10-year Hospital Development Plan costing \$200 billion to meet new demand and improve existing services. For minor hospital projects, in December 2013, the FC approved a one-off grant of \$13 billion to the HA for carrying out minor works projects over a 10-year period starting from 2014-15, subject to a financial ceiling of \$75 million for each individual works item. For the 3-year period from 2014-15 to 2016-17, the HA initiated a total of 1,092 minor works projects and, as of March 2017, the total expenditure was \$3.3 billion.

Executive Summary

3. The Audit Commission (Audit) has recently conducted a review to examine the HA's management of public hospital projects with a view to identifying room for improvement. The review examined two major public hospital projects completed during the past 5 years (see para. 2) and minor hospital projects. For major hospital projects, Audit selected: (a) the Redevelopment of Caritas Medical Centre (Phase 2) (hereinafter referred to as "CMC Phase 2") for review of its project management in view of its APE having increased significantly by over 40% (see para. 5); and (b) North Lantau Hospital (Phase 1) (hereinafter referred to as "NLTH Phase 1") for review of its commissioning of facilities because facilities of this new hospital have not been fully commissioned three years after its commencement of operation in September 2013.

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

4. CMC, managed under the HA's Kowloon West Cluster, is an acute general hospital (with around 1,200 beds as of October 2017) providing a full range of medical services mainly to residents of the Sham Shui Po District. It commenced operation in 1964 and its hospital blocks had over the years become old, dilapidated and sub-standard. The Government decided to redevelop CMC in two phases. Phase 1 redevelopment was completed in 2002. CMC Phase 2 commenced in 2007 and was substantially completed in October 2015. The Phase 2 project mainly included the demolition of four hospital blocks, construction of a new hospital block to accommodate 260 rehabilitation beds, ambulatory care and clinical support facilities, a rehabilitation garden, car parks and access roads, and refurbishment of another block to accommodate administrative functions. The HA acted as the works agent for the project and engaged four consultants for the design, tender preparation and contract administration of the project (paras. 2.2 to 2.5).

5. ***Increase in project cost and delay in project completion.*** In May 2007, the FC approved funding of \$1,218.1 million for implementing CMC Phase 2. The FHB informed the FC that the new hospital block and the rehabilitation garden would be completed by August 2011 and March 2012 respectively. The HA planned to implement CMC Phase 2 under a single works contract with a total construction period of 56 months. In July 2007, the HA invited tenders, but the bids of all five conforming tenders received were 47% to 56% higher than the original estimate, resulting in the HA cancelling the tender exercise in November 2007. In June 2011, the FHB resubmitted a funding application and the FC approved increasing the APE

Executive Summary

of CMC Phase 2 by \$501.5 million (41 %) from \$1,218.1 million to \$1,719.6 million, mainly due to the increase in construction costs and higher provision for price adjustment. In the event, the new hospital block and the rehabilitation garden under CMC Phase 2 were substantially completed in November 2013 and October 2015 respectively, 27 months and 43 months later than the original target completion dates for which the FC was informed in 2007 (paras. 2.6 to 2.8).

6. ***Need to enhance the accuracy of cost estimate.*** According to the FHB and the HA, one of the reasons for the higher-than-expected prices of all conforming tenders received by the HA at its first tender exercise conducted in 2007 was that the HA's project consultants might not have adequately gauged the rapid upsurge in construction prices and fully reflected the prevailing market sentiments in the project cost estimate. There is a need for the HA to take measures to ensure that the project cost is estimated as accurately as possible (paras. 2.8 to 2.10).

7. ***Need to enhance vetting of consultants' design and contract strategy.*** Owing to the higher-than-expected tender prices, from November 2007 to October 2008, the HA and its consultants conducted a design review (2008 Design Review) with a view to identifying savings in respect of the project design, project specifications and contract strategy. The 2008 Design Review identified cost savings of at least \$236 million (19% of the original APE of \$1,218.1 million) and improved competitiveness of tenders by revising the building design and the contract strategy (i.e. splitting the works into three (instead of one) works contracts). In Audit's view, the HA needs to take measures to enhance the vetting of its consultants' design and contract strategy (paras. 2.8 and 2.11 to 2.14).

8. ***Room for improvement in the HA's site investigations and coordination work.*** During June 2009 to August 2013, after conducting a tender exercise for each contract, the HA awarded three contracts to three contractors respectively for implementing the works under CMC Phase 2 at a total contract sum of \$1,570.2 million. There is scope for the HA to conduct more thorough site investigations and strengthen the coordination between works and medical staff, as revealed by: (a) an Extension of Time (EOT) of 174 days was granted to a contractor due to the additional time needed to revise the design and divert the planned works arising from the discovery of underground cables and pipes not indicated in the related utility records; and (b) an EOT of 20 days was granted to the contractor for works suspension on 20 occasions upon urgent requests of medical staff due to the noise and vibrations of the construction on eye-surgery operations being conducted

Executive Summary

at nearby hospital buildings. These incidents might have been avoided as, according to the HA, the appointments for eye-surgery operations were made on average one to two months ahead of time (paras. 2.17 to 2.22).

9. ***Need to step up efforts to ensure construction site safety and reporting of all site accidents.*** Audit examination found that the accident frequency rate during the construction period of one of the three contracts for implementing CMC Phase 2 was 0.92 reportable accident per 100,000 man-hours worked, which was significantly higher than the limit of 0.5 stipulated by the HA and the limit of 0.6 adopted by the Development Bureau (DEVB) for government works projects. Audit noted that three reportable accidents which occurred during the construction period involving three workers employed respectively by three sub-contractors of the contractor were not reported to the HA and its consultant. There is a need for the HA to step up efforts to ensure safety of construction sites and reporting of all site accidents (paras. 2.28, 2.29 and 2.32 to 2.34).

10. ***Need to review HA guidelines for assessing a contractor's site safety performance.*** For public works projects carried out by government works departments, the related DEVB's Technical Circular requires that a contractor's overall site safety performance should be rated as "Very Poor" if any 1 of the 5 prescribed events (e.g. failure to revoke a suspension notice issued by the Labour Department within 14 days after it was issued) occurs. However, Audit noted that the HA's guidelines for assessing contractors' performance on site safety had not stipulated any prescribed events which would trigger giving an adverse overall safety rating to a contractor (paras. 2.37 and 2.38).

Commissioning of facilities of the North Lantau Hospital (Phase 1)

11. According to the FHB, NLTH was developed to meet the long-term demand for hospital services on Lantau Island. It would be developed in two phases. In January 2010, the FC approved funding of \$2,482 million for the construction of NLTH Phase 1 to provide a public hospital (including an accident and emergency department, 180 beds and specialist out-patient clinics). Upon the full development of the North Lantau New Town, the Government would provide an additional 170 beds under the Phase 2 development in a site adjacent to the Phase 1 development. The construction works of NLTH Phase 1 were substantially completed in

Executive Summary

December 2012 and the hospital commenced operation in September 2013 under the management of the HA's Kowloon West Cluster (paras. 3.2 and 3.3).

12. ***Commissioning of some medical services later than the proposed dates.***

In November and December 2011, the HA management respectively informed the HA's Medical Services Development Committee (MSDC) and the HA Board that NLTH Phase 1 would start to provide service in phases from the third quarter of 2013 and migrate to full service in the third quarter of 2016. Audit examination found that 5 types of medical services at NLTH Phase 1 (namely, 24-hour accident and emergency service, day rehabilitation centre, specialist out-patient clinics on orthopaedics and traumatology and surgery, day surgery centre and 20 in-patient beds) were commissioned later than the respective commissioning dates as proposed by the HA management to the HA's MSDC in 2011. Furthermore, as of June 2017, some medical services had not yet been commissioned at the hospital, including: (a) specialist out-patient services for gynaecology and paediatrics (proposed for commissioning in the third quarter of 2014); (b) 20 day-beds for day-surgery patients (proposed for commissioning in the first quarter of 2014); and (c) a total of 120 in-patient beds (proposed for commissioning by the third quarter of 2016). According to the HA, the key constraints for commissioning of medical services at NLTH Phase 1 were attributed to manpower shortage and competing needs across the HA (paras. 3.4, 3.5, 3.8 and 3.13).

13. ***Need to keep under review anticipated timeline for commissioning medical services and report progress to HA Board/Committees and FHB.***

After commissioning of the operation of NLTH Phase 1 in September 2013, the HA management reported annually to the HA Board and quarterly to the FHB the medical services that had already been commissioned at the hospital. However, information on the anticipated timeline for commissioning the remaining medical services at NLTH Phase 1 (see para. 12) had not been provided to the HA Board and the FHB (para. 3.15).

14. ***Hospital building not fully utilised.*** In December 2012, a total floor area of 13,729 m² was constructed for the hospital building of NLTH Phase 1. Audit analysis found that, as of June 2017, 2,867 m² (21% of the total area of 13,729 m²) of the hospital building were vacant or had not been utilised for the intended functions. These 2,867 m² comprised 2,204 m² for wards, 466 m² for canteen and kitchen area and 197 m² for the day surgery centre (paras. 3.21 and 3.22).

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15. ***Under-utilisation of medical equipment.*** Since the commissioning of NLTH Phase 1 in 2013, the HA had procured 10 major medical equipment items (each costing \$1 million or above) at a total cost of \$32.7 million. Audit noted that the utilisation of 7 of the 10 major medical equipment items in 2016 was below 60% of the expected utilisation (ranging from 6% to 58%). Audit also noted that, as of June 2017, the HA had not yet put into use some other medical equipment items (each costing less than \$1 million) at NLTH Phase 1 since their procurement, and the warranty periods of all such items had already expired (paras. 3.30 to 3.34).

Management of minor hospital projects

16. ***High proportion of unplanned minor works projects.*** For the 3-year period from 2014-15 to 2016-17, the HA initiated a total of 1,092 minor works projects incurring a total expenditure of \$3.3 billion. According to the HA's internal guidelines, at least 90% of the new minor works projects initiated during a financial year should be planned projects included in the relevant 3-year rolling plan approved by the HA's Chief Executive. However, Audit examination found that, during 2014-15 to 2016-17, only 64% to 77% of the new minor works projects initiated each year had been included in the relevant approved 3-year rolling plan, falling short of the HA's 90% target (paras. 4.3 to 4.6).

17. ***Need to report survey results of building condition of public hospitals.*** Audit found that the HA's seven clusters were responsible for conducting building condition surveys of public hospitals on an annual basis, but the clusters had not provided the survey results to the HA's Chief Executive for vetting and approval of the 3-year rolling plan for minor works projects (para. 4.8).

18. ***Need to closely monitor works progress.*** In December 2013, the FHB informed the FC that the HA could annually initiate around 500 new minor works projects over the 10-year period from 2014-15 to 2023-24 (i.e. totally 5,000 projects in 10-year time). However, Audit noted that only 1,092 projects were initiated in the 3-year period from 2014-15 to 2016-17, representing an average of 364 projects per year (i.e. 73% of 500 projects). Audit also noted that, as of August 2017 (i.e. after passage of about 3.4 years of the 10-year period), only 62 (12% of the HA's estimate of 500) wards had been renovated, and 9 (17% of the HA's estimate of 52) electrical installations and 13 (4% of the HA's estimate of 364) lifts had been upgraded (paras. 4.2, 4.11 and 4.12).

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19. ***Delay in completing works orders and need to enhance management of minor works.*** Audit examination of 654 works orders issued to HA minor-works contractors in 2015-16 and 2016-17 found that there were delays in completing 303 (46%) of the 654 orders. For one case with the longest delay of 17 months among the 654 works orders, Audit noted that the additional time was required for variation orders issued, design changes of an electrical system by the HA after works commencement and late handover of works site by the HA. This case shows that there is scope for the HA to take measures to enhance the planning and implementation of works orders (paras. 4.16 to 4.18).

20. ***Better use of technology to effectively monitor project implementation.*** Audit noted that the HA's information system could not provide comprehensive management information for effectively monitoring the implementation of minor works projects (e.g. information on the progress in implementing works orders). According to the HA: (a) due to the limitations of the information system, the HA staff primarily process works orders manually; and (b) it planned to launch a new information system in April 2018 with a view to maintaining and providing more comprehensive information of works orders related to minor works projects (paras. 4.31 to 4.33).

Audit recommendations

21. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has recommended that the Chief Executive, HA should:**

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

- (a) when implementing hospital projects in future:**
 - (i) take measures to ensure that the project cost is estimated as accurately as possible (para. 2.15(a));**
 - (ii) take measures to enhance the vetting of the HA consultants' design and contract strategy (para. 2.15(b));**

Executive Summary

- (iii) **conduct more thorough site investigations with a view to identifying unrecorded utilities as far as possible, particularly for those projects involving redevelopment of old hospital buildings and at critical works locations (para. 2.25(a)(i));**
- (iv) **strengthen the coordination between works and medical staff on the scheduling and interfacing of construction works and medical operations at nearby hospital buildings (para. 2.25(a)(ii)); and**
- (v) **step up efforts to ensure safety of construction sites and reporting of all site accidents with a view to minimising site accident rate (para. 2.43(a)(i) and (ii));**
- (b) **conduct a review of the HA's guidelines for assessing contractors' performance on site safety, making reference to the related government requirements (e.g. stipulating a list of prescribed events that would trigger giving an adverse overall safety rating to a contractor) (para. 2.43(b));**

Commissioning of facilities of the North Lantau Hospital (Phase 1)

- (c) **regarding NLTH Phase 1 and major hospital projects to be implemented in future:**
 - (i) **keep track of the medical service demand of residents at the related districts, and commission the planned medical services of the completed hospital projects in a timely manner to meet the demand as soon as practicable (para. 3.17(a)); and**
 - (ii) **regularly report to the HA Board (or its relevant Committees) and the FHB the progress of commissioning the medical services vis-à-vis the anticipated timeline for monitoring purpose (para. 3.17(b));**
- (d) **before the vacant areas at NLTH Phase 1 could be utilised, explore measures to put such areas into gainful uses in the interim period (para. 3.28(a));**

Executive Summary

- (e) for areas temporarily used for other unintended functions (e.g. storage) at NLTH Phase 1, review whether such areas could be put into better alternative use (para. 3.28(b));
- (f) for medical equipment not put into use since their procurement, take measures to put them into gainful use (para. 3.35(b));
- (g) when implementing hospital projects in future, take measures to ensure that the procurement programme for medical equipment dovetails with the commissioning of the related medical services as far as possible (para. 3.35(c));

Management of minor hospital projects

- (h) strengthen the planning of minor works projects to meet the HA's 90% planning target (para. 4.9(a));
- (i) monitor the ageing conditions of public hospital buildings and take measures to ensure that the survey results of the building condition of public hospitals are reported to the HA's Chief Executive for vetting and approval of the 3-year rolling plans (para. 4.9(b));
- (j) closely monitor the progress of minor works projects to ensure timely completion and take measures to initiate more projects to improve the conditions of the HA's ageing facilities (para. 4.27(a));
- (k) take measures to enhance the planning and implementation of works orders, including the finalisation of works design before commencement of works and the timely handover of works sites (para. 4.27(b)); and
- (l) take measures to ensure that the HA's new information system is timely launched, and to better use technology to generate comprehensive management information for monitoring the implementation progress of minor works projects and the related works orders (para. 4.37(a)).

Executive Summary

22. Audit has also *recommended* that the Secretary for Food and Health should keep under review the HA's commissioning of all medical services at completed hospital projects with a view to meeting the demand for public hospital services (para. 3.18).

Response from the Hospital Authority and the Government

23. The Chief Executive, HA and the Secretary for Food and Health agree with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 The Hospital Authority (HA — Note 1) is a statutory body established under the Hospital Authority Ordinance (Cap. 113) to provide public hospital services in Hong Kong. Under the Ordinance, the HA's functions include managing and establishing public hospitals, and advising the Government of the needs of the public for hospital services and of the resources required to meet those needs.

1.3 As of September 2017, the HA managed 42 public hospitals and institutions (providing a total of about 28,000 beds) to provide public hospital services grouped under the HA's seven clusters (see Appendix A). According to the HA, these hospital buildings covered a total floor area of 2.7 million square metres (m²) and 59% of the floor area had been in use for more than 30 years (see Appendix B).

1.4 Owing to the ageing population in Hong Kong, there has been an increasing demand for healthcare services. According to the HA, physical facilities of its hospitals have a profound influence on the capacity, capability, workflow and efficiency of its hospital services, and such facilities also affect the HA's ability to meet future healthcare demands and accommodate the introduction of new services and technologies. To sustain the provision of public hospital services, the HA has initiated and undertaken public hospital projects with a view to achieving the following objectives:

Note 1: *The HA is governed by the HA Board, the members of which are appointed by the Chief Executive of the Hong Kong Special Administrative Region. As of June 2017, the HA Board consisted of 28 members, comprising 24 non-official members (including the Chairman), 3 public officers (i.e. Permanent Secretary for Food and Health (Health), Director of Health and Deputy Secretary for Financial Services and the Treasury (Treasury)) and 1 principal officer (i.e. the HA's Chief Executive). In general, the HA Board meets 12 times a year.*

Introduction

- (a) meeting growing demand for healthcare services;
- (b) modernising the physical facilities of public hospitals; and
- (c) making the buildings safer.

1.5 The HA will take into account various factors when planning and developing public hospital projects, including future population growth and ageing in the region, demand for healthcare services, overall provision of healthcare services in various clusters of the HA, and development of public and private healthcare services. Public hospital projects are broadly classified into two categories, namely major hospital projects and minor hospital projects.

Major hospital projects

1.6 According to the HA, a hospital project costing over \$75 million is classified as a major hospital project which includes the construction of a new hospital or the redevelopment/expansion of an existing hospital. Upon identifying the need for major hospital projects, the Food and Health Bureau (FHB), being the policy bureau responsible for the overall health policies in Hong Kong including the development of public hospitals, would take the lead in consulting the stakeholders (e.g. the related District Councils and the Panel on Health Services of the Legislative Council (LegCo)) and in seeking funding approval from LegCo Finance Committee (FC) for implementing the projects under the Capital Works Reserve Fund (CWRF — Note 2). The HA acts as the works agent of major hospital projects constructed on non-government land. The Architectural Services Department (ArchSD) acts as the works agent of major hospital projects constructed on government land.

Note 2: *The CWRF was established with effect from April 1982 by a LegCo resolution in January 1982 for financing public works projects and acquisition of land.*

1.7 In his Policy Address of January 2016, the Chief Executive of the Hong Kong Special Administrative Region announced that, to meet new demand and improve existing services, a 10-year Hospital Development Plan costing \$200 billion would be implemented. The Government has worked with the HA to devise the Plan which includes the construction of a new hospital and the redevelopment/expansion of 11 existing hospitals to provide some 5,000 additional public hospital beds and over 90 new operating theatres. Apart from the 10-year Hospital Development Plan, the HA is also implementing three major hospital projects (see Appendix C).

1.8 During the 5-year period from 2012-13 to 2016-17, six major hospital projects had been completed (see Table 1). The FC's approved funding (i.e. Approved Project Estimate (APE)) of these projects ranged from \$590.5 million to \$3,910.9 million. The APE of all these projects remained unchanged except for the project of the Redevelopment of Caritas Medical Centre (Phase 2) (hereinafter referred to as "CMC Phase 2"). The APE of CMC Phase 2 increased by \$501.5 million (41%) from \$1,218.1 million to \$1,719.6 million.

Table 1

**Major hospital projects completed
(2012-13 to 2016-17)**

Project	Works completion date	APE (\$ million)	Actual expenditure as of June 2017 (Note 1) (\$ million)
(A) New hospital projects			
1. Tin Shui Wai Hospital	Jul 2016	3,910.9	2,751.6
2. North Lantau Hospital (Phase 1)	Dec 2012	2,482.0	1,911.6
(B) Hospital redevelopment/expansion projects			
1. Reprovisioning of Yaumatei Specialist Clinic at Queen Elizabeth Hospital	Aug 2016	1,891.6	1,410.9
2. Redevelopment of Yan Chai Hospital	Apr 2016	590.5	537.3
3. CMC Phase 2	Oct 2015	1,719.6 (Note 2)	1,589.9
4. Expansion of Tseung Kwan O Hospital	Nov 2013	1,944.9	1,475.6
Total		12,539.5	9,676.9

Source: HA and ArchSD records

Note 1: As of June 2017, of the 6 major hospital projects, the accounts for the construction works of 2 projects (North Lantau Hospital (Phase 1) and Expansion of Tseung Kwan O Hospital) had been finalised. The accounts of the furniture and equipment items of all the 6 projects had not been finalised.

Note 2: In May 2007, the FC approved funding of \$1,218.1 million for the project. In June 2011, the FC approved increasing the APE of the project by \$501.5 million (41%) from \$1,218.1 million to \$1,719.6 million.

Minor hospital projects

1.9 The HA carries out minor works projects (i.e. each costing \$75 million or below) in existing hospitals to improve the conditions and environment of ageing facilities and to enhance their service capacity. In December 2013, the FC approved a one-off grant of \$13 billion to the HA for carrying out minor works projects over a 10-year period starting from 2014-15, subject to a financial ceiling of \$75 million for each individual works item. For the 3-year period from 2014-15 to 2016-17, the HA initiated a total of 1,092 minor works projects and, as of March 2017, the total expenditure was \$3.3 billion.

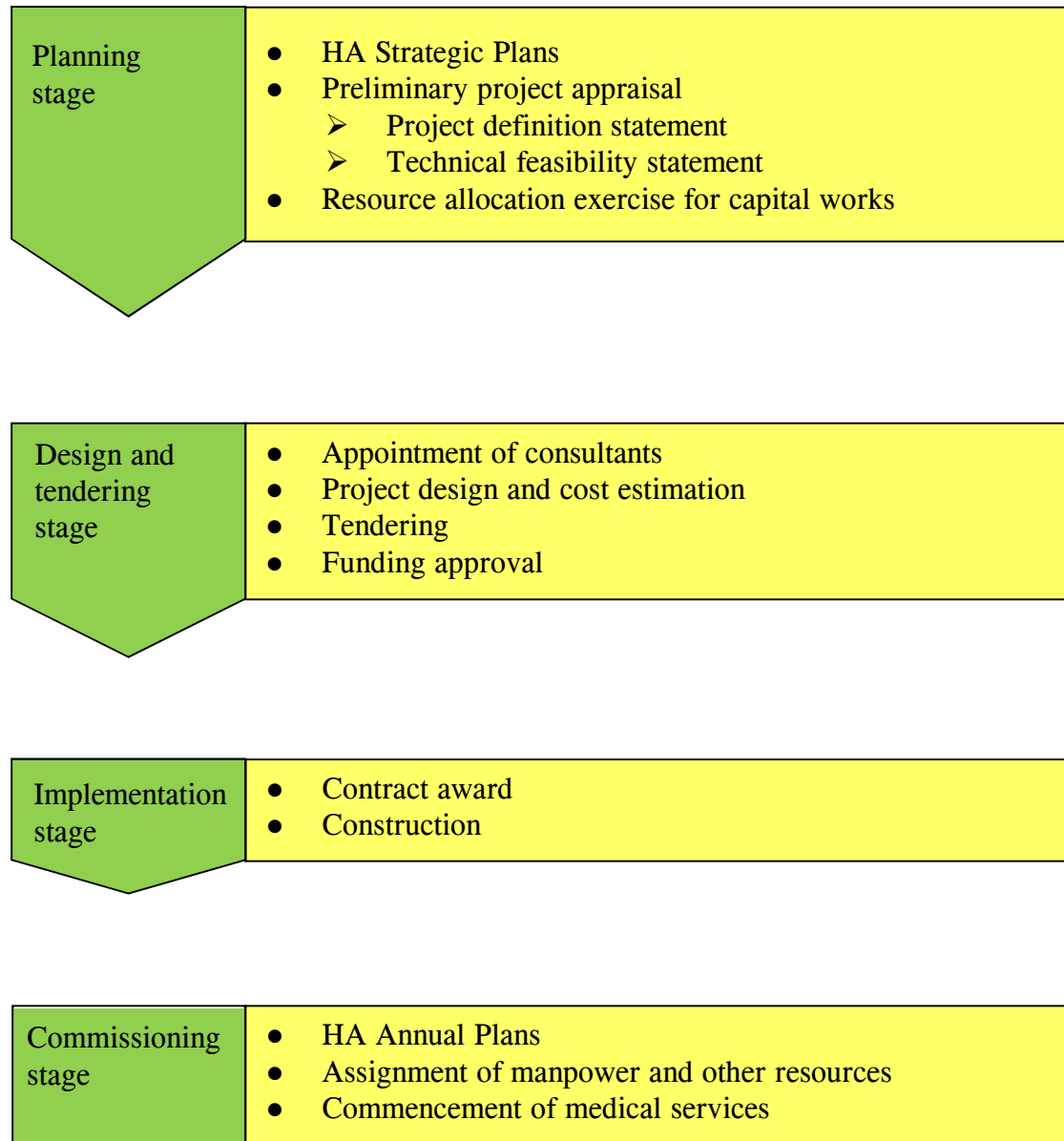
HA's management and governance of hospital projects

1.10 The Capital Planning Department under the Strategy and Planning Division of the HA is responsible for the management of public hospital projects. The HA's Cluster Services Division and seven clusters are responsible for the commissioning of facilities upon the completion of public hospital projects. As of June 2017, the HA's Capital Planning Department had 89 staff (68 professional/technical staff and 21 administrative staff). Appendix A shows an extract of the HA's organisation chart.

1.11 The development of a major public hospital project mainly involves four key stages, namely planning stage, design and tendering stage, implementation stage and commissioning stage. Figure 1 shows the key stages of major hospital projects. For minor hospital projects, the development mainly involves the preparation and approval of a 3-year rolling plan (see para. 4.4) and the implementation of minor works by the HA's contractors (see para. 4.15).

Figure 1

Key stages of major hospital projects



Source: HA records

1.12 The HA's governance on the planning and implementation of public hospital projects is primarily effected through a three-tier mechanism, as follows:

- (a) **HA management.** For each major hospital project, a Project Steering Committee (Note 3) is set up to steer the project implementation, monitor the works progress and financial position, and endorse the project design. As regards minor hospital projects, the Quarterly Review Meeting (Note 4) is convened to monitor the overall works progress and financial position of the projects;
- (b) **HA Board and Committees.** For major hospital projects, the HA management provides summary reports to the HA's Supporting Services Development Committee (Note 5) relating to the project progress and up-to-date cost estimates on a quarterly basis. As regards minor hospital projects, the HA management submits the audited financial statements on the use of the one-off grant (see para. 1.9) to the HA Board for approval on an annual basis; and
- (c) **Government level.** For major hospital projects, the HA provides summary reports to the FHB relating to the project progress on a monthly basis. For each minor hospital project, the HA submits to the FHB information on the project scope, objectives and estimated costs for approval before works commencement.

Note 3: *A Project Steering Committee is chaired by the Hospital Chief Executive of the concerned public hospital or the Director of the HA's Strategy and Planning Division, and comprises the related Cluster Chief Executive (or representatives from the related HA cluster) and representatives from the Hospital Governing Committee (or its parent organisation), the Strategy and Planning Division, the FHB and the ArchSD.*

Note 4: *The Quarterly Review Meeting is chaired by the Director of the HA's Strategy and Planning Division, and attended by representatives from seven HA clusters and the Capital Planning Department.*

Note 5: *The Supporting Services Development Committee is established by the HA Board under the Hospital Authority Ordinance. It is chaired by an HA Board member and comprises 14 other members. The Committee's functions include reviewing and advising the HA Board on the implementation and monitoring of the HA's hospital projects. In general, the Committee meets 4 times a year.*

Audit review

1.13 In April 2017, the Audit Commission (Audit) commenced a review to examine the HA's management of two major public hospital projects (namely CMC Phase 2 and the North Lantau Hospital (Phase 1) — hereinafter referred to as “NLTH Phase 1”) and minor hospital projects. Audit selected CMC Phase 2 for review of its project management in view of its APE having increased significantly by over 40% (see Table 1 in para. 1.8). NLTH Phase 1 was selected for review of its commissioning of facilities because facilities of this new hospital have not been fully commissioned three years after its commencement of operation in September 2013. The two projects were selected to identify any lessons to be learned in managing major public hospital projects.

1.14 The review focuses on the following areas:

- (a) project management of the Redevelopment of Caritas Medical Centre (Phase 2) (PART 2);
- (b) commissioning of facilities of the North Lantau Hospital (Phase 1) (PART 3); and
- (c) management of minor hospital projects (PART 4).

Audit has found room for improvement in the above areas, and has made a number of recommendations to address the issues.

Acknowledgement

1.15 Audit would like to acknowledge with gratitude the full cooperation of the staff of the FHB, the Development Bureau (DEVB), the HA, the ArchSD, the Labour Department (LD) and the Electrical and Mechanical Services Trading Fund (EMSTF) during the course of the audit review.

PART 2: PROJECT MANAGEMENT OF THE REDEVELOPMENT OF CARITAS MEDICAL CENTRE (PHASE 2)

2.1 This PART examines the HA's work in the project management of CMC Phase 2, focusing on:

- (a) project planning (see paras. 2.8 to 2.16);
- (b) project implementation (see paras. 2.17 to 2.26);
- (c) construction site safety (see paras. 2.27 to 2.45); and
- (d) construction defects (see paras. 2.46 to 2.53).

Redevelopment of Caritas Medical Centre

2.2 CMC, managed under the HA's Kowloon West Cluster (Note 6), is an acute general hospital (with around 1,200 beds as of October 2017) providing a full range of medical services mainly to residents of the Sham Shui Po District. The medical services provided include 24-hour accident and emergency services, in-patient beds, out-patient clinics, rehabilitation and community care services.

2.3 CMC commenced operation in 1964 and its hospital blocks had over the years become old, dilapidated and sub-standard. The Government decided to redevelop CMC in two phases to meet the present-day standard of an acute general hospital and the increase in service demand. Phase 1 redevelopment was completed in 2002 (Note 7).

Note 6: *As of October 2017, the HA's Kowloon West Cluster managed five public hospitals, namely the Princess Margaret Hospital, CMC, the Yan Chai Hospital, NLTH Phase 1 and the Kwai Chung Hospital.*

Note 7: *The works mainly involved the demolition of two sub-standard hospital blocks for the construction of a new block (namely the Wai Shun Block) to accommodate medical facilities including in-patient wards, an accident and emergency department, an intensive care unit and operating theatres.*

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

2.4 CMC Phase 2 commenced in 2007 and was substantially completed in October 2015. According to the paper submitted to the LegCo Public Works Subcommittee in April 2007, the Phase 2 project mainly included the demolition of four hospital blocks, construction of a new hospital block, a rehabilitation garden and external works, and refurbishment of another block (Note 8). Details are as follows:

- (a) demolition of an old hospital block (namely the Wai Ming Block) for the construction of a new ambulatory and rehabilitation block on the same site to accommodate 260 rehabilitation beds, ambulatory care and clinical support facilities;
- (b) demolition of another three hospital blocks (namely the Wai Tak Block, the Wai On Block and the Wai Yan Block) for the construction of external works (e.g. a rehabilitation garden, car parks and access roads);
- (c) refurbishment of the Wai Oi Block to accommodate administrative functions (e.g. a training and conference centre, security and transport services, and a maintenance department) reprovisioned from the old hospital blocks; and
- (d) construction of Link Bridges A and B, a walkway and a lift tower to facilitate commuting by hospital staff, patients and the general public.

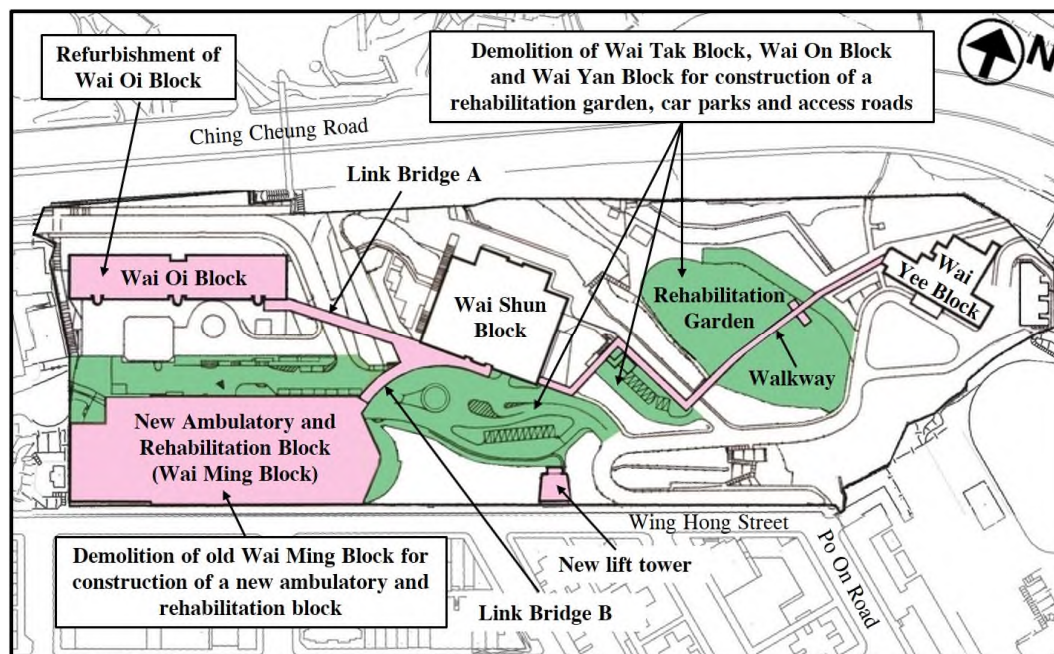
Figure 2 shows the layout plan of CMC Phase 2.

Note 8: *CMC had 7 blocks after the completion of Phase 1 redevelopment. Except for the Wai Shun Block (constructed under Phase 1 in 2002) and another block (renovated in 1993), the other 5 blocks had been used for a long time. Phase 2 redevelopment involved the redevelopment/refurbishment of all these 5 blocks.*

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

Figure 2

Layout plan of CMC Phase 2



Legend: New and refurbished hospital blocks and other structures
 External works

Source: HA records

Remarks: As of October 2017, CMC had a total of 1,206 beds, comprising 752 beds in the Wai Shun Block, 280 beds in the Wai Ming Block and 174 beds in the Wai Yee Block.

Roles of FHB and HA in project administration

2.5 The FHB was mainly responsible for seeking funding approval from the FC for implementing CMC Phase 2 and keeping track of the project progress through summary reports provided by the HA (see para. 1.12(c)). The HA acted as the works agent for the project as the hospital was constructed on non-government land (Note 9) (see para. 1.6). The HA engaged four consultants (Note 10) for the design, tender preparation and contract administration of the project.

Increase in project cost and delay in project completion

2.6 In May 2007, the FC approved funding of \$1,218.1 million (Note 11) for implementing CMC Phase 2. The FHB informed the FC that the new Wai Ming Block and the rehabilitation garden would be completed by August 2011 and March 2012 respectively. In June 2011, the FHB resubmitted a funding application and the FC approved increasing the APE of the project by \$501.5 million (41%) from \$1,218.1 million to \$1,719.6 million (mainly due to the increase in construction costs and higher provision for price adjustment (Note 12)). The FHB informed the FC that the new Wai Ming Block and the rehabilitation garden would be completed by September 2013 and mid-2014 respectively.

2.7 In the event, the new Wai Ming Block and the rehabilitation garden were substantially completed in November 2013 and October 2015 respectively, 27 months and 43 months later than the original target completion dates for which the FC was informed in 2007 (or 2 months and 16 months later than the revised target completion

Note 9: *The concerned land lots were granted to Caritas Hong Kong (the parent organisation of CMC) as private treaty grants.*

Note 10: *The four consultants were engaged to provide consultancy services in CMC Phase 2 relating to the architectural, civil and structural engineering, building services and quantity surveying aspects respectively.*

Note 11: *Caritas Hong Kong, the parent organisation of CMC, had undertaken to contribute \$50 million towards the total project cost.*

Note 12: *The additional funding of \$501.5 million comprised \$358.5 million for increase in construction costs, \$10 million for additional external works and \$136.1 million for higher provision for price adjustment, with the cost increase having been offset by a saving of \$3.1 million due to the reduced extent of decanting works.*

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

dates for which the FC was informed in 2011) (see para. 2.6). Photographs 1 and 2 show the new Wai Ming Block and the rehabilitation garden.

Photograph 1

The new Wai Ming Block



Source: HA records

Photograph 2

Rehabilitation garden



Source: HA records

Project planning

2.8 In early 2007, the HA planned to implement CMC Phase 2 under a single works contract with a total construction period of 56 months. After the FC's funding approval in May 2007 (see para. 2.6), in July 2007, the HA invited tenders for carrying out the works. In November 2007, as the bids of all five conforming tenders were 47% (\$508 million) to 56% (\$600 million) higher than the original estimate of \$1,070 million and the potential of significantly lowering the tender price was limited, the HA cancelled the tender exercise.

Need to enhance the accuracy of cost estimate

2.9 In April 2009, the FHB and the HA informed the LegCo Panel on Health Services that the higher-than-expected tender price of the project was due to the following reasons:

- (a) ***Rapid price inflation in 2007.*** The costs of construction had been escalating since early 2007 as a result of sharp and unexpected increase in the prices of major construction materials;
- (b) ***Marking-up of tender prices by tenderers.*** Under a highly inflationary market situation at the time of conducting the tender exercise in 2007, the tenderers considered that the price-fluctuation allowance in the 56-month single works contract (see para. 2.8) was inadequate and they built in additional premium in their tenders to cover inflation risks over the long contract period; and
- (c) ***Under-estimation of project cost by HA's consultants.*** The HA's project consultants might not have adequately gauged the rapid upsurge in construction prices and fully reflected the prevailing market sentiments in the project cost estimate.

2.10 According to the HA:

- (a) regarding the under-estimation of project cost by its consultants (see para. 2.9(c)):
 - (i) the HA has not instigated any penalty measures on its consultants because the HA considered that the construction market conditions from mid-2007 to 2009 were exceptional; and
 - (ii) the exceptional market conditions might be demonstrated by the fact that the Government sought the FC's approval in November 2008 for increasing the APEs (up to 54% increase) of 35 public works projects due to upsurge in construction costs; and
- (b) since 2007, the HA has taken various measures to achieve good value for money and enhance the accuracy of project cost estimates, including
 - (i) in December 2013, the HA developed cost benchmarks for different types of hospital facilities; and
 - (ii) in July 2014, the HA promulgated cost control guidelines for major hospital projects managed by the HA.

In Audit's view, when implementing hospital projects in future, the HA needs to take measures to ensure that the project cost is estimated as accurately as possible.

Need to enhance vetting of consultants' design and contract strategy

2.11 After cancellation of the tender exercise in 2007 (see para. 2.8), from November 2007 to October 2008, the HA and its consultants conducted a design review (2008 Design Review) with a view to identifying savings in respect of the project design, project specifications and contract strategy. In the event, the 2008 Design Review identified cost savings of at least \$236 million (19% of the original APE of \$1,218.1 million). The details of cost savings are shown in Table 2. According to the HA, the cost savings identified in the 2008 Design Review materialised during the subsequent re-tendering exercises conducted between 2009 and 2013 (see para. 2.17).

Project management of the Redevelopment of Caritas Medical Centre (Phase 2)

Table 2

Cost savings identified in 2008 Design Review

Aspect	Key revision	Cost savings materialised
(a) Project design	<ul style="list-style-type: none">Reducing construction floor area of new Wai Ming BlockReducing size of rehabilitation garden	\$145 million
(b) Project specifications	<ul style="list-style-type: none">Replacing wall and floor finishes by cheaper alternativesDeleting escalators for out-patient department	\$91 million
(c) Contract strategy	<ul style="list-style-type: none">Relaxing qualification requirements of main contractor and sub-contractorsAdjusting contract packaging	No estimation by HA
Total		\$236 million

Source: HA records

2.12 In April 2009, the FHB and the HA informed the LegCo Panel on Health Services that, in view of the higher-than-expected tender price (see para. 2.8), they decided to take the following remedial actions:

- (a) ***Adopting a more compact building form.*** The construction floor area of the new Wai Ming Block had been reduced by 5,100 m² (Note 13) from 59,100 m² to 54,000 m² and the number of storeys reduced from 15 to 12. According to the FHB and the HA, the updated design enhanced the area efficiency of the redeveloped hospital block while the original scope of the redevelopment project (see para. 2.4) could be maintained; and

Note 13: *The reduced 5,100 m² covered car parking areas (2,900 m²), engineering plant rooms and building services pipe ducts (1,800 m²), and lift lobbies, staircases and corridors (400 m²).*

- (b) ***Splitting into smaller works contracts.*** To enhance the competitiveness of tenders and minimise the likelihood of tenderers building in additional premium for extensive contract periods, the redevelopment works would be split into three works contracts (instead of a single works contract — see para. 2.8), namely: (i) Foundation Contract; (ii) Main Building Works Contract; and (iii) Remaining Works Contract. In addition, the decanting works necessary for demolition of the old hospital blocks and the refurbishment works of the Wai Oi Block would be carried out by an HA term contractor (Note 14).

2.13 Audit noted that the 2008 Design Review identified significant cost savings and improved competitiveness of tenders by revising the building design and the contract strategy (see paras. 2.11 and 2.12). According to the HA, in May 2016, it engaged an international expert team to carry out a consultancy study on the planning efficiency of local and overseas hospitals.

2.14 In Audit's view, when implementing hospital projects in future, the HA needs to take measures to enhance the vetting of its consultants' design and contract strategy.

Audit recommendations

2.15 **Audit has *recommended* that the Chief Executive, HA should, when implementing hospital projects in future:**

- (a) **take measures to ensure that the project cost is estimated as accurately as possible; and**
- (b) **take measures to enhance the vetting of the HA consultants' design and contract strategy.**

Note 14: *The decanting works commenced in July 2009 and were completed in February 2010, and refurbishment works commenced in June 2012 and were completed in June 2015.*

Response from the Hospital Authority

2.16 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that the HA will continue to identify appropriate new initiatives to be undertaken with a view to ensuring that no budget problem is encountered in its major hospital projects, as has been the case in the past 10 years.

Project Implementation

2.17 During June 2009 to August 2013, after conducting a tender exercise for each contract, the HA awarded the three contracts (see para. 2.12(b)) to three contractors respectively for implementing the works under CMC Phase 2 at a total contract sum of \$1,570.2 million. Audit examination found that the Extension of Time (EOT) granted under one of the three contracts revealed room for improvement in the HA's site investigations and coordination work (see paras. 2.18 to 2.22).

Need to conduct more thorough site investigations

2.18 Audit noted that, for a contract for implementing CMC Phase 2:

- (a) during the construction stage, underground electricity cables obstructing certain construction works were discovered by the contractor. According to the HA, the cables had not been indicated in the related utility records and the HA consultants and the contractor subsequently took action to revise the design for relocating the works involved, causing delay to the contractor's works. In the event, an EOT of 80 days was granted to the contractor; and
- (b) during the connection of a stormwater pipe into a public manhole, an underground gas pipe obstructing the pipe connection works was discovered by the contractor. According to the HA, the gas pipe had not been indicated in the related utility records and the contractor subsequently took action to divert the gas pipe, causing delay to the contractor's works. In the event, an EOT of 94 days was granted to the contractor.

2.19 Audit noted that a total EOT of 174 (80 + 94) days was granted to the contractor due to clash of works with unrecorded utilities. As a result, it took a longer time to complete the related construction works. In August 2017, the HA informed Audit that:

- (a) the contractor had relied on the utility records from utility companies collected during the design stage and the underground utility surveys carried by the HA's consultants for planning its construction works. In order not to adversely affect the prevailing traffic flow and hospital operation, further site investigations (e.g. trial trench works) were only arranged during the construction stage;
- (b) having reviewed the delays caused by underground utilities, the HA considered that additional site investigations could be conducted during the early stage of construction works (such as conducting on-site visual inspection for estimating the possible alignment of unrecorded utilities, carrying out utility diversion works in advance when obstruction was found and diversion was inevitable, and carrying out site investigations in advance to reveal the underground condition at the critical works locations); and
- (c) the additional site investigations in (b) above would have cost implications and might cause possible disruptions to the prevailing traffic flow and hospital operation, which should be carefully weighed against the potential benefits of carrying out additional site investigations.

2.20 While noting the HA's explanations above, in Audit's view, when implementing hospital projects in future, particularly for those projects involving redevelopment of old hospital buildings and at critical works locations, there is scope for the HA to conduct more thorough site investigations with a view to identifying unrecorded utilities as far as possible.

Need to strengthen coordination work

2.21 Audit also noted that, for the same contract in paragraph 2.18, works were suspended on 20 occasions upon urgent requests of medical staff due to the noise and vibrations of the construction on eye-surgery operations being conducted at nearby hospital buildings. According to the HA, the noise and vibrations caused by the related construction works were within the statutory and contractual requirements. In the event, an EOT of 20 days was granted to the contractor.

2.22 In August 2017, the HA informed Audit that the appointments for eye-surgery operations were made on average one to two months ahead of time. Therefore, the 20 occasions of eye-surgery operations were known in advance. In Audit's view, when implementing hospital projects in future, there is scope for the HA to strengthen the coordination between works and medical staff on the scheduling and interfacing of construction works and medical operations at nearby hospital buildings (e.g. requesting works suspension at an earlier time or exploring alternative locations for the conduct of operations). There are also merits for the HA to explore the feasibility of specifying more stringent noise and vibration limits in future hospital works contracts affecting medical operations at nearby hospital buildings during the construction works with a view to minimising the impact of works-induced noise and vibrations on nearby hospital buildings.

Need to complete assessment of EOT claims within a reasonable time

2.23 During March 2015 to January 2016, a contractor for implementing CMC Phase 2 made 8 EOT claims for reasons other than inclement weather for the related works. Audit noted that, up to July 2017, the assessments of these claims had not been completed. According to the HA:

- (a) regarding 2 EOT claims (involving 160 days in total) submitted by the contractor in March 2015 and December 2015 respectively, the contractor had not provided supplementary information as requested by the HA consultant in April 2016; and

- (b) regarding the remaining 6 EOT claims (involving 297 days in total) submitted by the contractor during December 2015 to January 2016, the contractor provided supplementary information in June 2017 as requested by the HA consultant in April 2016. In July 2017, the HA consultant requested the contractor to provide further supplementary information.

2.24 According to the contract provisions, the HA consultant shall within a reasonable time determine, grant and notify in writing the EOT, and if the contractor fails to submit information requested by the HA consultant, he shall consider granting EOT based on the information available to him. As of July 2017, about 1.5 to 2.5 years after the contractor's submission of EOT claims, the claims were still under assessment. In Audit's view, the HA needs to take measures to ensure that the assessment of EOT claims is completed within a reasonable time period.

Audit recommendations

2.25 **Audit has *recommended* that the Chief Executive, HA should:**

- (a) **when implementing hospital projects in future:**
 - (i) **conduct more thorough site investigations with a view to identifying unrecorded utilities as far as possible, particularly for those projects involving redevelopment of old hospital buildings and at critical works locations;**
 - (ii) **strengthen the coordination between works and medical staff on the scheduling and interfacing of construction works and medical operations at nearby hospital buildings; and**
 - (iii) **explore the feasibility of specifying more stringent noise and vibration limits in hospital works contracts affecting medical operations at nearby hospital buildings during the construction works; and**
- (b) **take measures to ensure that the assessment of EOT claims is completed within a reasonable time period.**

Response from the Hospital Authority

2.26 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) provisions regarding identification of unrecorded underground utilities and specification of noise and vibration limits have been and will continue to be incorporated in the HA's construction contracts as appropriate, for example:
 - (i) for the Expansion of the Hong Kong Red Cross Blood Transfusion Service Headquarters, the results and recommendations of a consultancy study conducted by a local university in June 2011 regarding construction-induced vibrations were incorporated as contractual requirements; and
 - (ii) for the foundation and associated works contract awarded in May 2016 for the Redevelopment of Kwong Wah Hospital, the contractor had been required to expose by hand-digging, verify and divert as necessary all existing underground utilities before commencement of foundation works; and
- (b) the HA will review the relevant provisions in its construction contracts and consultancy agreements to see whether appropriate measures can be incorporated to ensure early completion of EOT assessments.

Construction site safety

2.27 According to the HA:

- (a) it is committed to protecting the safety of its staff, patients, visitors, works agents, contractors and key stakeholders who work in or have access to the capital works projects managed by the HA; and
- (b) it views the safety records of its construction sites very seriously, and the aim is for all the sites to achieve zero fatal accident at all times and minimise site accident rate.

2.28 In April 2012, the HA stipulated a limit on accident frequency rate at 0.5 reportable accident (Note 15) per 100,000 man-hours worked. This limit is applicable to each HA's works project. According to the HA, with a view to driving for better safety performance, its limit on accident frequency rate is more stringent than the limit of 0.6 reportable accident per 100,000 man-hours worked adopted by the DEVB for public works projects carried out by the Government.

Need to step up efforts to ensure construction site safety

2.29 Audit noted that, during the construction period of the three contracts for implementing CMC Phase 2, the accident frequency rates of two contractors (being 0.38 and 0.41 reportable accident per 100,000 man-hours worked) were within the HA's limit of 0.5. The accident frequency rate of the remaining contractor of 0.92 reportable accident per 100,000 man-hours worked was significantly higher than the HA's limit. It was also considerably higher than the limit adopted by the DEVB for government works projects (see para. 2.28). During the eight quarters of the 2-year construction period, the contractor's accident frequency rates of two quarters (i.e. 0 and 0.47 reportable accident per 100,000 man-hours worked in the first and fourth quarters respectively) were below the HA's limit of 0.5, whereas the rates of the other six quarters (ranging from 0.53 to 1.47) were above the HA's limit. Audit noted that, during the construction period, various safety-related events of the contractor took place, including:

- (a) 21 reportable accidents occurred involving a total of 2,556 days of sick leave (Note 16) being granted to the injured workers, with sick leave granted in each accident ranging from 7 to 349 days (Note 17);
- (b) on the next day after a falling-from-height accident causing multiple rib fractures of a construction worker occurred in April 2013, the LD issued a

Note 15: *According to the HA, the number of reportable accidents refers to the number of workers involved in fatal cases or injury with incapacity for more than three days.*

Note 16: *Two of the 21 reportable accidents were related to two workers employed respectively by two sub-contractors of the contractor. The HA informed Audit in October 2017 that it did not maintain information related to the number of days of sick leave being granted to the two workers.*

Note 17: *According to the HA, no fatal case occurred during the construction period.*

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suspension notice under the Occupational Safety and Health Ordinance (Cap. 509) requesting the contractor to immediately suspend the related construction works to alleviate the imminent safety risks. The suspension notice was revoked by the LD 22 days after the issue of the notice, and the contractor resumed the construction works concerned; and

- (c) another four incidents, all concerning falling objects (e.g. wooden log and concrete debris) from height and affecting the general public and hospital operations, occurred during April to July 2013. No person was injured in these incidents.

2.30 According to the HA, it had taken various remedial actions since April 2013 with a view to minimising recurrence of similar accidents in the contract, including:

- (a) reminding the contractor to conduct site safety inspections on a weekly basis, and to submit accident reports and review safety measures immediately after the occurrence of each accident; and
- (b) requesting the HA consultant to assign a building professional to conduct regular site visits and closely monitor the safety performance of the contractor.

2.31 However, Audit noted that, even after the HA's remedial actions mentioned above, the accident frequency rate still reached 0.99 reportable accident per 100,000 man-hours worked during July to August 2013 and exceeded the HA's limit of 0.5 (and also the DEVB's limit of 0.6). In October 2017, the HA informed Audit that:

- (a) it had taken various measures over the years to enhance construction site safety, including:
 - (i) in February 2014, the HA engaged a consultant specialised in construction site safety to conduct a review on the safety performance of the HA's capital works contracts;

- (ii) since June 2015, the HA had stipulated in construction contracts the requirement to conduct regular safety audits by independent registered safety auditors; and
 - (iii) in September 2016 and July 2017, the HA organised training courses on effective safety management for its executive staff on hospital projects to enhance their safety awareness and culture; and
- (b) in 2016, the HA achieved zero fatal accidents and an overall accident frequency rate of 0.31 reportable accident per 100,000 man-hours worked at its construction sites.

2.32 In Audit's view, when implementing hospital projects, the HA needs to step up efforts to ensure safety of construction sites with a view to minimising site accident rate.

Need to strengthen measures to ensure reporting of all site accidents

2.33 According to the contract provisions, the contractor with high accident frequency rate (see para. 2.29) shall submit a monthly report for consideration by the HA and its consultants at the meeting of the Site Safety and Environmental Management Committee (SSEMC — Note 18). The monthly report should include all accidents involving death or personal injury irrespective of severity or damages to properties in or adjacent to the construction site. However, according to the LD's records, Audit noted that three reportable accidents which occurred during the construction period involving three workers employed respectively by three sub-contractors of the contractor were not included in the pertinent monthly reports submitted to the SSEMC (Note 19).

Note 18: *The SSEMC was chaired by an HA consultant and included representatives from the CMC staff, the HA and the pertinent contractors. The Committee held meetings at monthly intervals.*

Note 19: *Under the Employees' Compensation Ordinance (Cap. 282), notice of any accident which results in death, total or partial incapacity of an employee shall be given to the LD by an employer within a specified time after the accident. The three sub-contractors of the contractor respectively gave the LD a notice of the corresponding accident.*

2.34 Audit noted that the SSEMC's functions included reviewing accident frequency rates and statistics of a contractor and its sub-contractors, and establishing safe working provisions and procedures. Any under-reporting of site accidents would undermine the SSEMC's performance of its functions. In Audit's view, when implementing hospital projects in future, the HA needs to strengthen measures to ensure that contractors report all site accidents to the HA and its consultants.

***Need to review HA guidelines
for assessing a contractor's site safety performance***

2.35 According to the HA's Capital Works Procedural Manual, performance reports of a contractor are prepared generally on a quarterly basis to assess the performance of the contractor in 10 aspects including site safety (Note 20). In a quarterly performance report, each aspect is given 1 of the 5 ratings, namely "Very Good", "Good", "Satisfactory", "Poor" or "Very Poor", and an overall performance rating will be given for the performance report.

2.36 According to the HA, a contractor's performance is assessed based on its "Guidance Notes for Completion of Contractors' Performance Reports". Under the Guidance Notes, the site safety performance of a contractor is assessed under 6 safety sub-aspects (Note 21). An overall safety rating will be given based on the assessment results of these 6 sub-aspects.

Note 20: *The other 9 aspects are workmanship, progress, environmental pollution control, organisation, general obligations, industry awareness, resources, design and attendance to emergency. A "Very Poor" rating in workmanship, progress, site safety or environmental pollution control will result in an "Adverse" performance report.*

Note 21: *The 6 sub-aspects are:*

- (a) Provision of maintenance of plant;*
- (b) Provision and maintenance of working environment;*
- (c) Provision of information, instruction and training;*
- (d) Provision and implementation of safe systems of work;*
- (e) Employment of safety officer/supervisor; and*
- (f) Site accident record.*

2.37 In this connection, it is relevant to note that, for public works projects carried out by government works departments, the related DEVB's Technical Circular (Note 22) requires that a contractor's overall site safety performance should be rated as "Very Poor" if any 1 of the 5 following prescribed events occurs:

- (a) failure to revoke a suspension notice issued by the LD within 14 days after it was issued;
- (b) repeated non-compliance with safety procedures despite warnings given by site supervision staff and the LD, and failure to rectify the situation within a reasonable time;
- (c) more than 2 improvement notices and/or suspension notices were issued by the LD to the contractor within the performance reporting period in respect of separate incidents or safety inspections;
- (d) any suspension of works ordered by site supervision staff under the relevant contract provisions on grounds of site safety; and
- (e) failure to rectify within a reasonable time any situation of imminent danger identified by an independent registered safety auditor and/or site supervision staff.

2.38 Audit noted that the overall safety rating of an HA contractor is based on the assessment results of 6 sub-aspects (see para. 2.36). The HA's guidelines had not stipulated any prescribed events which would trigger giving an adverse overall safety rating to a contractor. As the prescribed events in the DEVB's Technical Circular may also be applicable to the HA's contractors, there is merit for the HA to consider stipulating such prescribed events for assessing the overall safety rating of its contractors in future.

Note 22: *The related requirements are stipulated in Works Bureau Technical Circular No. 26/2000 on "Score Card for Assessment for Site Safety Performance" issued by the then Works Bureau in September 2000, and updated by the then Environment, Transport and Works Bureau in February 2007 and the DEVB in November 2012. The site safety performance of government works contractors is also assessed under the same 6 sub-aspects in the HA guidelines (see Note 21 to para. 2.36).*

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2.39 In Audit's view, to enhance the assessment of contractors' performance on site safety, the HA needs to conduct a review on its guidelines, making reference to the related government requirements (e.g. stipulating a list of prescribed events that would trigger giving an adverse overall safety rating to a contractor).

Accident statistics not regularly reported to HA Board/Committees

2.40 During the 5-year period from 2012-13 to 2016-17, the HA management had only reported the accident statistics of its hospital projects to the HA's Capital Works Subcommittee (Note 23) on two occasions:

- (a) in August 2012, reporting the overall accident rate per 1,000 workers from 2007 to 2011; and
- (b) in November 2016, reporting the accident statistics from November 2013 to October 2016, including number of fatalities, average accident frequency rate and suspension notices issued by the LD.

2.41 Audit noted that:

- (a) the HA management had not reported the related accident statistics during January 2012 to October 2013 to the HA Board or the above Subcommittee; and
- (b) contractors' safety performance (including comparison of the actual accident frequency rates against the HA's accident limit) was not regularly reported to the HA Board or the above Subcommittee for monitoring purpose. In this connection, Audit noted that the DEVB published the accident statistics of government works departments on an annual basis.

Note 23: *In March 2012, the HA's Supporting Services Development Committee (see Note 5 to para. 1.12(b)) established the Capital Works Subcommittee. It is chaired by a member of the Committee and comprises 8 other members. The Subcommittee's functions include advising and making recommendations to the Committee on the planning, implementation and monitoring of the HA's major hospital projects. In general, the Subcommittee meets 4 times a year.*

2.42 In Audit's view, when implementing hospital projects in future, the HA management needs to report the accident statistics regularly to the HA Board/its relevant Committees and publish them for enhancing transparency and public accountability.

Audit recommendations

2.43 Audit has *recommended* that the Chief Executive, HA should:

- (a) **when implementing hospital projects in future:**
 - (i) **step up efforts to ensure safety of construction sites with a view to minimising site accident rate;**
 - (ii) **strengthen measures to ensure that contractors report all site accidents to the HA and its consultants; and**
 - (iii) **report the accident statistics regularly to the HA Board/its relevant Committees, and publish them for enhancing transparency and public accountability; and**
- (b) **conduct a review of the HA's guidelines for assessing contractors' performance on site safety, making reference to the related government requirements (e.g. stipulating a list of prescribed events that would trigger giving an adverse overall safety rating to a contractor).**

Response from the Hospital Authority and the Government

2.44 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) the HA will continue to identify appropriate measures to be taken for further safety enhancements, including measures to ensure that its contractors report all site accidents to the HA and its consultants;

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- (b) the HA will report and publish its accident statistics regularly in future; and
- (c) in October 2017, the HA concluded a review initiated in May 2016 on its performance appraisal system in order to align with the corresponding practices adopted by government works departments.

2.45 The Secretary for Development concurs with the audit recommendations for the HA to enhance its safety management system and the assessment of contractors' performance on site safety.

Construction defects

2.46 Under the three contracts for CMC Phase 2:

- (a) the maintenance period is 12 months counting from the date of substantial completion of a works section, and all the maintenance works shall be carried out by the pertinent contractor at their own expense during the maintenance period or within 14 days after its expiry;
- (b) the HA consultants may require the pertinent contractor to make good any defects or other faults identified within the maintenance period, and the contractor shall carry out such works within the maintenance period or as soon as practicable thereafter;
- (c) if the pertinent contractor fails to carry out any defect rectification works, the HA shall be entitled, after giving a reasonable written notice to the contractor, to have such works carried out by its own workers or by other contractors, and the HA shall be entitled to recover from the contractor the expenditure incurred; and
- (d) upon expiry of the maintenance period, and when all the outstanding and defect rectification works have been completed, the HA consultants shall issue a maintenance certificate to the pertinent contractor.

Delay in rectification of construction defects

2.47 According to the HA, of the three contracts for implementing CMC Phase 2:

- (a) for one contract, no construction defect was identified; and
- (b) for the other two contracts, as of 30 June 2017, 247 defect items (2.4% of a total 10,091 items) remained outstanding although the corresponding maintenance periods had already lapsed. The outstanding defect items were mainly related to water seepage, building works and electrical and mechanical (E&M) works.

2.48 In July 2017, the HA informed Audit that the outstanding defects had not been timely rectified due to various reasons, including:

- (a) adequate resources had not been deployed by the pertinent contractors during the respective maintenance periods;
- (b) only limited access had been provided for the pertinent contractors to carry out defect rectification works because of the existing hospital operations;
- (c) it was difficult to identify the sources of water seepage (a major type of construction defects); and
- (d) although some replacement items were of small monetary value, it required a long time for the manufacturing and delivery processes.

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2.49 In Audit's view, it is less than satisfactory that, as of June 2017, 8 months and 3 years after expiry of the respective maintenance periods of the two contracts, the defect rectification works were still outstanding. In October 2017, the HA informed Audit that it had put in place various measures over the years for quality assurance of construction works, including:

- (a) in November 2014, the HA initiated a pilot scheme on the direct employment of resident site staff to help retain expertise in the quality supervision of hospital projects;
- (b) in June 2016, the HA initiated a programme of quality assurance audits conducted by in-house cross-team project staff; and
- (c) in May 2017, the HA promulgated the Resident Site Staff Handbook to align quality-supervision practices at different construction sites.

2.50 Audit considers that the HA needs to step up measures to ensure that the outstanding defects under the two contracts are rectified as soon as possible. When implementing a hospital project in future, the HA also needs to take measures to ensure that all defect rectification works are completed in a timely manner.

Need to conduct thorough investigations to identify hidden construction defects posing safety risks

2.51 Furthermore, in March 2017, a piece of square-shaped loose concrete (with sides of about 300 millimetres and a thickness of about 10 millimetres) was found falling from the ceiling of a structure. No person was nearby the structure and there was no injury during the incident. According to the investigation report of the contractor concerned, the loose concrete was considered as a hidden construction defect and therefore had not been identified beforehand. In the same month, at the request of CMC staff, the contractor attempted and could not identify other hidden construction defects. Audit considers that, when implementing a hospital project in future, the HA needs to conduct thorough investigations before commissioning of the related hospital facilities with a view to identifying all the construction defects posing safety risks to hospital users.

Audit recommendations

- 2.52 **Audit has *recommended* that the Chief Executive, HA should:**
- (a) **step up measures to ensure that the outstanding defects under the contracts of CMC Phase 2 are rectified as soon as possible; and**
 - (b) **when implementing a hospital project in future:**
 - (i) **take measures to ensure that all defect rectification works are completed in a timely manner; and**
 - (ii) **conduct thorough investigations before commissioning of the related hospital facilities with a view to identifying all the construction defects posing safety risks to hospital users.**

Response from the Hospital Authority

- 2.53 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:
- (a) as of end September 2017, all except 9 defect items under the contracts of CMC Phase 2 had been rectified. The 9 outstanding defect items will be rectified by end October 2017; and
 - (b) the HA will continue to identify appropriate measures to be taken for further quality assurance of construction works in order to minimise the need for defect rectification works after works completion.

PART 3: COMMISSIONING OF FACILITIES OF THE NORTH LANTAU HOSPITAL (PHASE 1)

3.1 This PART examines the HA's work in commissioning of facilities of NLTH Phase 1, focusing on:

- (a) commissioning of medical services (see paras. 3.4 to 3.20);
- (b) utilisation of hospital building (see paras. 3.21 to 3.29); and
- (c) utilisation of medical equipment (see paras. 3.30 to 3.36).

North Lantau Hospital

3.2 In December 2009, the FHB informed the LegCo Public Works Subcommittee that:

- (a) **NLTH.** In accordance with the general planning standard, an acute hospital would be planned for a district when the population of the district reached 200,000. The FHB decided to develop a new hospital in North Lantau before the population in the district reached the relevant level under the general planning standard:
 - (i) to cope with the projected population growth of the Lantau Island from 100,000 in 2006 to 123,100 by 2015 and further to around 220,000 upon the full development of North Lantau New Town in the long term; and
 - (ii) having considered that the Hong Kong International Airport and some major tourist facilities are situated in North Lantau.

NLTH would be developed in two phases (see (b) and (c) below);

Commissioning of facilities of the North Lantau Hospital (Phase 1)

- (b) **Phase 1.** It would be a government project to provide a public hospital (including an accident and emergency department, 180 beds and specialist out-patient clinics), which would be sufficient to meet the demand for public hospital services for the projected population of 123,100 on Lantau Island by 2015. The estimated annual recurrent expenditure arising from this project was \$300 million. Construction works for the Phase 1 development were planned for completion in December 2012; and
- (c) **Phase 2.** To meet the long-term demand for hospital services on Lantau Island upon the full development of the North Lantau New Town, the Government would provide an additional 170 beds under the Phase 2 development in a site adjacent to the Phase 1 development (Note 24).

3.3 In January 2010, the FC approved funding of \$2,482 million (comprising \$2,082 million for works and \$400 million for furniture and equipment items) for the construction of NLTH Phase 1 (Note 25). The ArchSD was responsible for the construction of NLTH Phase 1 as it is located on government land (see para. 1.6). In December 2012, the construction works were substantially completed (Note 26). In September 2013, the hospital commenced operation under the management of the HA's Kowloon West Cluster (see Note 6 to para. 2.2). NLTH Phase 1 comprises one hospital building block (see Photograph 3). The HA's work in commissioning the facilities of NLTH Phase 1 is shown in paragraphs 3.4 to 3.36. Audit has found room for improvement in the HA's related work.

Note 24: *The Government would explore the introduction of public-private-partnership for the private sector to provide other medical facilities and services in the available area in addition to the 170 beds provided by the Government. In the event that the above partnership arrangement would not materialise for the Phase 2 development, the Government would still proceed with the Phase 2 development in due course as a government project.*

Note 25: *According to the FHB's paper seeking funding approval from the FC, the unit construction cost was considered reasonable as compared with other similar hospital projects.*

Note 26: *Up to June 2017, the total expenditure was \$1,911.6 million (comprising \$1,737.1 million for building works and \$174.5 million for furniture and equipment items).*

Commissioning of facilities of the North Lantau Hospital (Phase 1)

Photograph 3

North Lantau Hospital (Phase 1)



Source: HA records

Commissioning of medical services

3.4 In November 2011, the HA management informed the HA's Medical Services Development Committee (MSDC — Note 27) that:

- (a) in view of the tight medical and nursing manpower in the next few years, medical services at NLTH Phase 1 would be introduced in phases, tying in with the supply of manpower and making reference to the graduating seasons of medical and nursing students. A service timeline for commissioning medical services in phases (from the third quarter of 2013 to full operation in the third quarter of 2016) at NLTH Phase 1 was proposed;

Note 27: *The MSDC is established by the HA Board under the Hospital Authority Ordinance. It is chaired by an HA Board member and comprises 13 other members. The functions of the Committee include advising and making recommendations to the HA Board on the directions relating to the development of public hospitals and related services. In general, the Committee meets 6 times a year.*

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- (b) NLTH Phase 1 would need to have 650 staff (comprising 62 doctors, 174 nurses, 83 allied health professionals (Note 28) and 331 supporting staff) to deliver its medical services when in full operation (Note 29);
- (c) in view of the tension in the supply of doctors and nurses at that time, a proactive recruitment plan for doctors, nurses and allied health professionals was crucial to guarantee that the services of NLTH Phase 1 could be up and running upon its phased commissioning. All the channels would be considered for proactively recruiting the required manpower for delivering the planned services for the phased commissioning of NLTH Phase 1, including part-time employment, special honorarium scheme and overseas recruitment; and
- (d) it was estimated that NLTH Phase 1 would require an annual budget of about \$500 million when in full operation (Note 30). The HA was in the process of securing a bid under the Government's Resource Allocation Exercise to support the operating cost of NLTH Phase 1, and recurrent funding support from the Government would need to be secured before commissioning of the hospital.

The MSDC noted the above-mentioned commissioning plan of NLTH Phase 1.

Note 28: *Allied health professionals included physiotherapists, occupational therapists and speech therapists.*

Note 29: *According to the HA, the manpower of 650 staff was estimated on the basis of:*

- (a) *scope of service provision (especially for the need to cope with disasters);*
- (b) *minimum number of staff to cover the required service hours (including the staff needed for shift duties at the accident and emergency department); and*
- (c) *reference with the manpower provision for various services in other public hospitals.*

Note 30: *According to the HA, the annual recurrent expenditure of \$300 million (see para. 3.2(b)) provided to LegCo in December 2009 was a rough estimation based on the latest cost data at that time. In 2011, the hospital management estimated that an annual recurrent expenditure of \$476 million (comprising \$311 million for personal emoluments and \$165 million for other recurrent costs) would be required for full operation of NLTH Phase 1.*

Commissioning of facilities of the North Lantau Hospital (Phase 1)

3.5 In December 2011, the HA Board noted that NLTH Phase 1 would start to provide service in phases from the third quarter of 2013 and migrate to full service in the third quarter of 2016 (via the submission of a progress report on the items discussed at the meeting of the MSDC held in November 2011).

3.6 In April 2013, the HA management informed the HA Board of the service scope of NLTH Phase 1 in 2013-14, the related challenges and way forward, including:

- (a) the hospital would commence certain medical services (Note 31) in September 2013 to tie in with the graduation seasons of medical and nursing students, and to allow sufficient time for team building and staff orientation. The HA would commission the remaining medical services in phases in subsequent years subject to resources available under the prevailing mechanisms;
- (b) the difficulties in recruiting junior frontline staff to the hospital were manageable, as there was reasonably convenient transportation to Tung Chung, and good supply of working population (particularly for junior positions) was expected in the district; and
- (c) the HA management was optimistic on the recruitment of staff for the hospital in view of the encouraging responses in staff briefing forums and recruitment exercises. Job rotation of medical staff within the Kowloon West Cluster would be arranged for training opportunity and exposure to different frontline settings.

3.7 As mentioned in paragraphs 3.4 to 3.6, the HA management informed the HA Board and its MSDC the proposal for commissioning the medical services in phases in NLTH Phase 1. Table 3 shows a comparison of the service timeline as proposed to the MSDC in 2011 and the actual commissioning dates of key medical services at NLTH Phase 1.

Note 31: *The medical services included accident and emergency services, general out-patient services, specialist out-patient services for medicine and psychiatrics, and community care services.*

**Commissioning of facilities of
the North Lantau Hospital (Phase 1)**

Table 3

**Proposed and actual commissioning dates of
key medical services at NLTH Phase 1**

Key medical service	Commissioning date	
	Proposed to HA's MSDC in 2011	Actual
(A) Accident and emergency department		
(i) 8-hour service	3rd quarter of 2013	September 2013
(ii) 24-hour service	1st quarter of 2014	September 2014
(B) General out-patient clinic	3rd quarter of 2013	September 2013
(C) Community care services	3rd quarter of 2013	September 2013
(D) Day rehabilitation centre	1st quarter of 2014	September 2014
(E) Specialist out-patient clinics		
(i) Medicine, psychiatrics	3rd quarter of 2013	September 2013
(ii) Orthopaedics and traumatology, surgery	3rd quarter of 2013	September 2014
(iii) Gynaecology, paediatrics	3rd quarter of 2014	Not yet commissioned as of June 2017
(F) Day surgery centre with 20 day-beds		
(i) Day surgery centre	1st quarter of 2014	October 2014
(ii) 20 day-beds	1st quarter of 2014	Not yet commissioned as of June 2017
(G) Wards for in-patients (160 beds in total)		
(i) 20 beds	1st quarter of 2014	September 2014 (for 40 beds)
(ii) Another 40 beds	3rd quarter of 2014	
(iii) Another 20 beds	3rd quarter of 2015	Not yet commissioned as of June 2017 (for 120 beds)
(iv) Another 40 beds (Note)	4th quarter of 2015	
(v) Another 40 beds (Note)	3rd quarter of 2016	

Legend: Shaded boxes indicate commissioning of medical services later than the respective commissioning dates as proposed by the HA management to the HA's MSDC in 2011.

Source: HA records

Note: According to the HA management's proposal to the MSDC in 2011, the actual provision of these 80 (40+40) in-patient beds would be dependent on the service needs at the prevailing time.

Commissioning of facilities of the North Lantau Hospital (Phase 1)

Commissioning of some medical services later than the proposed dates

3.8 As shown in Table 3, the 24-hour accident and emergency service (item (A)(ii)), the day rehabilitation centre (item (D)), the specialist out-patient clinics on orthopaedics and traumatology and surgery (item (E)(ii)), the day surgery centre (item (F)(i)) and 20 in-patient beds (item (G)(i)) of NLTH Phase 1 were commissioned later than the respective commissioning dates as proposed by the HA management to the HA's MSDC in 2011. While the HA management informed the HA Board and the MSDC that it proposed to commission all medical services in the third quarter of 2016, as of June 2017, some medical services had not yet been commissioned at the hospital, including:

- (a) specialist out-patient services for gynaecology and paediatrics (proposed for commissioning in the third quarter of 2014 — see item (E)(iii));
- (b) 20 day-beds for day-surgery patients (proposed for commissioning in the first quarter of 2014 — see item (F)(ii)); and
- (c) a total of 120 in-patient beds (proposed for commissioning by the third quarter of 2016 — see item (G)(ii) to (v)).

3.9 Audit noted that, according to the results of the 2016 Population By-census conducted by the Census and Statistics Department, the actual population of the Lantau Island was about 123,300 in 2016, which was very close to the population forecast of 123,100 by the FHB in 2009 when seeking funding approval from LegCo for NLTH Phase 1 project (see para. 3.2(b)). According to the FHB's paper submitted to LegCo in 2009, the Lantau population of about 123,000 would require a public hospital of 180 beds in order to meet their demand for public hospital services. However, as of June 2017, only 40 beds (22% of the planned 180 beds) were commissioned at NLTH Phase 1 to provide public hospital services for the 123,000 Lantau residents.

3.10 According to the HA, Lantau residents requiring medical services not yet provided by NLTH Phase 1 have primarily been referred to other public hospitals managed by the HA's Kowloon West Cluster for treatment (Note 32). The majority of Lantau residents had been referred to the HA's Princess Margaret Hospital (PMH) — about 27 kilometres from NLTH involving travelling time of about 25 minutes by private car/taxi or about 50 minutes by public transport) for treatment.

3.11 According to HA records, as of 30 June 2017, 1,044 Lantau residents and 899 Lantau children had made appointments for specialist out-patient services for gynaecology and paediatrics respectively at the PMH, as these services had not yet been provided at NLTH Phase 1 (Note 33). In this connection, Audit noted that a LegCo member and some members of the Islands District Council had indicated on various occasions in 2017 that the patient transfer and referral arrangements from NLTH Phase 1 to PMH involved long travelling time and hence caused inconvenience to Lantau residents.

3.12 Audit noted that, in April 2013, the HA management informed the HA Board that it was optimistic on the staff recruitment for the phased commissioning of NLTH Phase 1 in 2013-14 in view of the encouraging responses in staff briefing forums and recruitment exercises (see para. 3.6(c)). In the event, as of 31 March 2017, only 397 staff were deployed to the hospital for providing the commissioned medical services. The 397 staff comprised 245 staff deployed through

Note 32: *According to the HA:*

- (a) *it organises the provision of medical services on a cluster approach by grouping its medical facilities and services together to form a network within a cluster in ensuring that patients will receive a continuum of medical care within the same cluster and throughout their episode of illness;*
- (b) *apart from achieving integration and collaboration among various clinical services within a cluster, the cluster arrangement also serves to ensure cost-effective use of resources within the same cluster; and*
- (c) *medical needs of Lantau residents are addressed by NLTH Phase 1 and the Princess Margaret Hospital together with other hospitals and facilities of the HA's Kowloon West Cluster.*

Note 33: *According to the HA, in June 2017, a daily average of 154 Lantau residents were receiving in-patient medical services in the PMH (being the only acute tertiary hospital in the Kowloon West Cluster), of which a daily average of 143 Lantau residents were admitted due to complexity of their clinical situation requiring medical treatment in an acute tertiary hospital.*

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internal transfer within the HA and 152 staff recruited from external sources, representing 61% of the 650 staff required for the full operation of the hospital (see Appendix D).

3.13 During May to September 2017, the HA informed Audit that:

- (a) for all the HA's service initiatives, including the phased commissioning of medical services at NLTH Phase 1, the key constraints for commissioning of the service initiatives were attributed to two key factors (i.e. manpower shortage and competing needs across the HA — see Appendix E for details). As a result, only some of the service initiatives would be allocated with the necessary resources (including manpower) for implementation; and
- (b) patient's convenience was not the only factor for consideration in setting up hospital or specialist out-patient services. Patients might also choose to seek services at public hospitals in other districts for various reasons (e.g. proximity to workplace). Nonetheless, certain groups of patients might benefit more from medical services in the vicinity of their residential locations (e.g. general out-patient service, community elderly service and community psychiatric service). The priority in establishing these services had reflected a balance among various factors, including patients' convenience and cost-effectiveness.

3.14 In Audit's view, regarding NLTH Phase 1 and major hospital projects to be implemented in future, the HA needs to keep track of the medical service demand of residents at the related districts and commission the planned medical services of the completed hospital projects (including NLTH Phase 1) to meet the demand as soon as practicable.

Need to keep under review anticipated timeline for commissioning medical services and report progress to HA Board/Committees and FHB

3.15 As indicated in paragraphs 3.4 and 3.5, in 2011, the HA management informed the HA Board and its MSDC the proposal for commissioning the medical services in phases in NLTH Phase 1, and the manpower needed to deliver all the medical services. Audit noted that, after commissioning of the operation of the hospital in September 2013, the HA management reported annually to the HA Board

and quarterly to the FHB the medical services that had already been commissioned at the hospital. However, Audit found that information on the anticipated timeline for commissioning the remaining medical services at NLTH Phase 1 (see para. 3.8(a) to (c)) had not been provided to the HA Board and the FHB.

3.16 In Audit's view, the HA management needs to regularly report the progress of commissioning the remaining medical services at NLTH Phase 1 against its anticipated timeline to the HA Board (or its relevant Committees) and the FHB. Moreover, when implementing major hospital projects in future, the HA management needs to keep under review the anticipated timeline for commissioning medical services and regularly report to the HA Board (or its relevant Committees) and the FHB the progress vis-à-vis the anticipated timeline for monitoring purpose. The FHB also needs to keep under review the HA's commissioning of all medical services at completed hospital projects with a view to meeting the demand for public hospital services.

Audit recommendations

3.17 **Audit has *recommended* that the Chief Executive, HA should, regarding NLTH Phase 1 and major hospital projects to be implemented in future:**

- (a) **keep track of the medical service demand of residents at the related districts, and commission the planned medical services of the completed hospital projects (including NLTH Phase 1) in a timely manner to meet the demand as soon as practicable; and**
- (b) **keep under review the anticipated timeline for commissioning all medical services at completed hospital projects (including NLTH Phase 1), and regularly report to the HA Board (or its relevant Committees) and the FHB the progress of commissioning the medical services vis-à-vis the anticipated timeline for monitoring purpose.**

3.18 **Audit has *recommended* that the Secretary for Food and Health should keep under review the HA's commissioning of all medical services at completed hospital projects with a view to meeting the demand for public hospital services.**

Response from the Hospital Authority and the Government

3.19 The Chief Executive, HA has said that the HA agrees with the audit recommendations in paragraphs 3.17 and 3.18. He has also said that:

- (a) the HA will continue to keep track of the medical service demand of the completed hospital projects (including NLTH Phase 1) by analysing the service utilisation of residents in the respective catchment areas of the cluster hospitals. This information will be used to formulate appropriate service opening plan of the completed hospital projects (including NLTH Phase 1) in the HA's annual planning exercise;
- (b) the HA will review the anticipated timeline for the phased opening of NLTH Phase 1 and hospital projects to be completed in future by anticipating the realistic competing needs, assessing related manpower supply and adjusting the proposed timeline at different stages of their phased opening. The updated proposal together with the overall progress of the service opening of NLTH Phase 1 and hospital projects to be completed in future will be separately reported to the HA Board or its relevant Committees (including the FHB representative serving at the HA Board/Committees) at regular intervals; and
- (c) apart from the existing reporting mechanism on the phased opening of medical services at completed hospital projects to the HA Board or its relevant Committees (including the FHB representative serving at the HA Board/Committees) and the quarterly reports to the FHB, the HA will additionally report the remaining facilities/services yet to be opened so as to keep the FHB abreast of the overall progress of the service commissioning.

3.20 The Secretary for Food and Health agrees with the audit recommendation in paragraph 3.18. She has also said that:

- (a) the HA reports to the FHB the progress of its major capital works projects and commissioning of medical services in hospital projects through various channels (e.g. through the FHB's monthly meetings with the HA and the HA's quarterly progress review reports to the FHB). Ad-hoc meetings would also be held where necessary on the commissioning of services in completed hospital projects. For example, the FHB and the HA have worked closely and held ad-hoc meetings on the planned commissioning of services at the Hong Kong Children's Hospital in 2018;
- (b) regarding NLTH Phase 1, although there is no regular report from the HA specifically on the commissioning of the remaining medical services, the FHB has maintained close liaison with the HA, and both parties have jointly considered the planning of the remaining services at NLTH Phase 1 and its Phase 2 development (see para. 3.2(c)) in view of the rising demand for medical services in the district arising from the proposed Tung Chung New Town Extension project; and
- (c) the FHB will, in consultation with the HA, consider how the communication and reporting mechanism regarding the progress of commissioning of services at completed hospital projects can be regularised and enhanced.

Utilisation of hospital building

3.21 In December 2012, the construction works for NLTH Phase 1 were substantially completed. A total floor area of 13,729 m² was constructed for the hospital building.

Hospital building not fully utilised

3.22 As indicated in paragraph 3.8, certain medical services at NLTH Phase 1 were not commissioned as of June 2017. As a result, the hospital building was not fully utilised. Audit analysis found that, as of June 2017, 2,867 m² (21% of the total area of 13,729 m²) of the hospital building were vacant or had not been utilised for the intended functions. These 2,867 m² comprised 2,204 m² for wards, 466 m² for canteen and kitchen area, and 197 m² for the day surgery centre.

Commissioning of facilities of the North Lantau Hospital (Phase 1)

3.23 Audit's site visit to NLTH Phase 1 on 30 June 2017 found that, for wards and the day surgery centre, some of the areas were vacant or used for temporary storage (see Photographs 4 and 5).

Photograph 4

A vacant ward area



Source: Photograph taken by Audit staff on 30 June 2017

Photograph 5

A ward area used for temporary storage



Source: Photograph taken by Audit staff on 30 June 2017

3.24 Audit also noted that the HA had made gainful use of a ward area at NLTH Phase 1 of about 112 m² (4% of the total area of 2,867 m² which were vacant or had not been utilised for the intended functions) temporarily as a gymnasium for physiotherapy patients (see Photograph 6). In October 2017, the HA informed Audit that, in addition to using the vacant ward area temporarily as rehabilitation areas, other vacant ward areas were also being used temporarily as staff training venue for the hospital and the HA's Head Office. In Audit's view, for the remaining vacant areas, the HA needs to explore measures to put such areas into gainful uses in the interim period. For areas temporarily used for other unintended functions (e.g. storage), the HA also needs to review whether such areas could be put into better alternative use.

Photograph 6

A ward temporarily used as a gymnasium



Source: Photograph taken by Audit staff on 30 June 2017

3.25 As regards the area earmarked for canteen and kitchen (see Photograph 7), Audit noted that, in August 2013, the HA conducted a tender exercise to invite caterers to bid for the provision of canteen service for NLTH Phase 1 but no tender was returned in that exercise. Up to August 2017, the HA had not conducted any further tender exercise for the service.

Photograph 7

Vacant canteen and kitchen area



Source: Photograph taken by Audit staff on 30 June 2017

3.26 In August 2017, the HA informed Audit that:

- (a) in the 2013 tender exercise, the potential canteen operators considered that the canteen at NLTH Phase 1 was not a viable business owing to the operation scale, projected sales volume, capital investment and geographic location; and
- (b) since 2015, as an interim measure, the hospital management had arranged an operator to provide cafeteria services to provide meals, light refreshment and beverages to the general public and hospital staff.

3.27 According to the HA, catering service has always been an important part of a public hospital. In Audit's view, given that various medical services (e.g. 24-hour accident and emergency service and day rehabilitation centre — see Table 3 in para. 3.7) have been provided to the general public at NLTH Phase 1 since the last tender exercise in August 2013 and the increase of its staff from 164 in September 2013 to 397 in March 2017, the HA needs to revisit the feasibility of providing the canteen service. Before the canteen and kitchen area could be used for the intended purpose, the HA also needs to explore measures to put the area into gainful uses in the interim period.

Audit recommendations

- 3.28 **Audit has *recommended* that the Chief Executive, HA should:**
- (a) **before the vacant areas at NLTH Phase 1 could be utilised, explore measures to put such areas into gainful uses in the interim period;**
 - (b) **for areas temporarily used for other unintended functions (e.g. storage) at NLTH Phase 1, review whether such areas could be put into better alternative use; and**
 - (c) **revisit the feasibility of providing the canteen service at NLTH Phase 1, and before the canteen and kitchen area could be used for the intended purpose, explore measures to put the area into gainful uses in the interim period.**

Response from the Hospital Authority

- 3.29 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:
- (a) the HA will continue to explore measures to put the unused areas at NLTH Phase 1 into gainful use where practicable, such as for organising staff/patient activities in the interim period before such areas could be utilised;
 - (b) the use of some vacant areas for storage is on a temporary basis, and the areas will be cleared upon the implementation of the measures in (a) above or the phased opening of new wards in NLTH Phase 1 targeted in 2018-19 and thereafter; and
 - (c) further to the unsuccessful tender exercise for the provision of canteen service at NLTH Phase 1 in 2013, the HA's Kowloon West Cluster will conduct another tender exercise in the fourth quarter of 2017.

Utilisation of medical equipment

3.30 Before utilising the funding approved by the FC (see para. 3.3) for procurement of major medical equipment (i.e. costing \$1 million or above per equipment item), the HA needs to seek the FHB's approval and provide the justifications, including the expected utilisation (e.g. in terms of the number of examinations to be conducted) of the equipment. Moreover, HA hospitals are required to record the actual utilisation of each major medical equipment item and report the results to its cluster management. For example, the management of NLTH Phase 1 needs to report the actual utilisation of its major medical equipment to the HA's Kowloon West Cluster Technology Committee (Note 34).

Under-utilisation of medical equipment

3.31 Since the commissioning of NLTH Phase 1 in 2013, the HA had procured 10 major medical equipment items at a total cost of \$32.7 million for use at the hospital. The utilisation of the 10 equipment items in 2016 is shown in Table 4.

Note 34: *The Committee is chaired by the Hospital Chief Executive of a public hospital managed by the Kowloon West Cluster and comprises hospital end-users and management staff from the same cluster. The Committee usually holds meetings on an annual basis. If the actual utilisation of a major medical equipment is lower than the expected utilisation, the responsible hospitals are required to provide justifications to the Committee.*

**Commissioning of facilities of
the North Lantau Hospital (Phase 1)**

Table 4

**Utilisation of major medical equipment at NLTH Phase 1
(2016)**

Equipment item (Note)	Unit cost (a) (\$ million)	Expected utilisation per year (b)	Actual utilisation in 2016 (c)	Utilisation rate $(d) = \frac{(c)}{(b)} \times 100\%$
1. Mobile C-arm X-ray Machine	1.4	110	7	6 %
2. Computed Radiography System	2.2	5,000	502	10 %
3. Fluoro/Angiographic Unit	6.9	825	182	22 %
4. Prescription Dispensing System	3.1	79,500	34,635	44 %
5. Anaesthetic Clinical Information System	3.0	2,500	1,154	46 %
6. Ultrasound Scanner	1.5	2,200	1,171	53 %
7. Automatic Tablet Dispensing and Packaging System	2.6	116,480	67,287	58 %
8. Computed Tomography System	7.0	6,000	6,618	110 %
9. Digital Radiography System (for accident and emergency department)	2.5	20,000	24,131	121 %
10. Digital Radiography System	2.5	9,000	25,115	279 %
Total	32.7			

Source: Audit analysis of HA records

Note: Of the 10 major medical equipment items:

- (a) 7 items were for the conduct of medical examinations (i.e. items 1, 2, 3, 6, 8, 9 and 10) and their utilisation was measured in terms of the number of examinations conducted;
- (b) 2 items were for the dispensing of medicines (i.e. item 4 (utilisation measured in terms of the number of prescriptions handled) and item 7 (utilisation measured in terms of the number of pouches of medicines packed)); and
- (c) the remaining 1 item was for the storage of clinical information (i.e. item 5) and its utilisation was measured in terms of the number of clinical cases handled.

Commissioning of facilities of the North Lantau Hospital (Phase 1)

3.32 As shown in Table 4, the utilisation of 7 (70%) of the 10 major medical equipment items was below 60% of the expected utilisation, ranging from 6% to 58%. In August and September 2017, the HA informed Audit that:

- (a) regarding the 7 major medical equipment items for the conduct of medical examinations (see item (a) of Note to Table 4), they were mainly used for in-patients and x-ray screening services in operating theatres, and were essential for the provision of existing medical services at NLTH Phase 1; and
- (b) patients outside the catchment areas of NLTH Phase 1 had been referred from other hospitals of the Kowloon West Cluster for utilising the medical equipment at the hospital. The utilisation of the above 7 equipment items would be expected to further increase upon the full commissioning of medical services at NLTH Phase 1.

In Audit's view, the HA needs to strengthen measures to further improve the utilisation of medical equipment in the interim period.

3.33 Moreover, apart from some major medical equipment, Audit noted that, as of June 2017, the HA had not yet put into use some other medical equipment (costing less than \$1 million) at NLTH Phase 1 since their procurement (see Table 5).

Table 5
Medical equipment not put into use since procurement
(June 2017)

Item	Date of purchase	Quantity	Unit cost	Useful life	Warranty period
(1) Electric bed (see Photograph 8)	Oct 2013	42	\$15,214	10 years	2 years
(2) Wheelchair (see Photograph 8)	Apr 2013	10	\$945	5 years	1 year
(3) Blood pressure monitor (see Photograph 9)	Nov 2013	14	\$10,400	7 years	1 year
(4) Stand for laundry bag (see Photograph 9)	Jun 2013	20	\$2,545	7 years	1.5 year

Source: HA records

Photograph 8

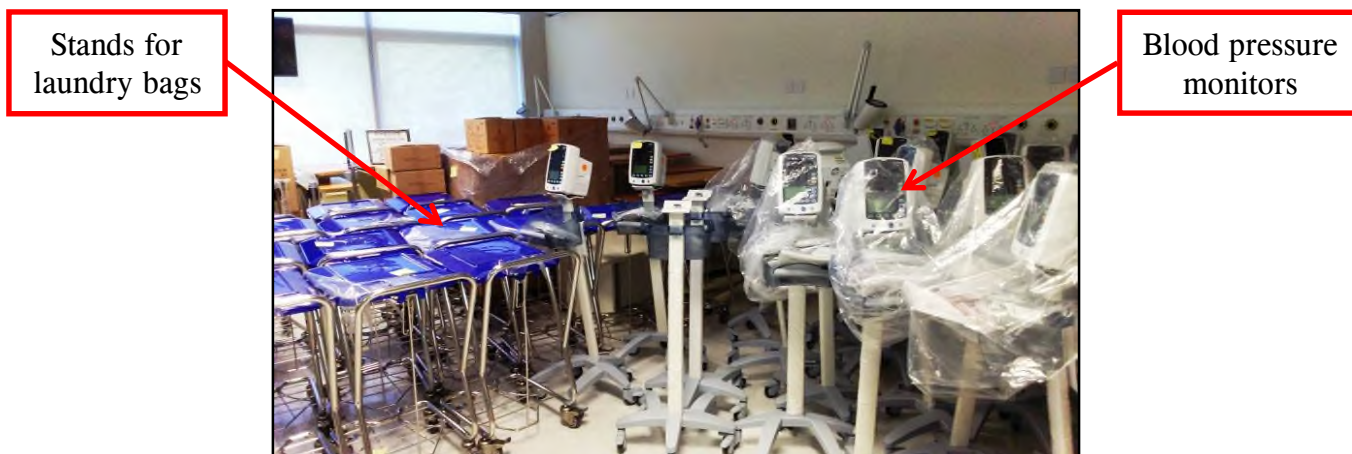
Electric beds and wheelchairs not put into use since procurement



Source: Photograph taken by Audit staff on 30 June 2017

Photograph 9

**Blood pressure monitors and stands for laundry bags
not put into use since procurement**



Source: Photograph taken by Audit staff on 30 June 2017

Commissioning of facilities of the North Lantau Hospital (Phase 1)

3.34 Audit noted that, as of August 2017, the warranty periods of all the medical equipment (see Table 5 in para. 3.33) had already expired. In September 2017, the HA informed Audit that some of the not-in-use equipment items were required for possible mass-casualty incidents, patients requiring contact precautions and back-up during repair and maintenance of other similar items. In Audit's view, the HA needs to take measures to put such medical equipment into gainful use. When implementing hospital projects in future, the HA needs to take measures to ensure that the procurement programme for medical equipment dovetails with the commissioning of the related medical services as far as possible.

Audit recommendations

3.35 Audit has *recommended* that the Chief Executive, HA should:

- (a) **for medical equipment already put into use, strengthen measures to further improve their utilisation in the interim period before the full commissioning of medical services at NLTH Phase 1;**
- (b) **for medical equipment not put into use since their procurement, take measures to put them into gainful use; and**
- (c) **when implementing hospital projects in future, take measures to ensure that the procurement programme for medical equipment dovetails with the commissioning of the related medical services as far as possible.**

Response from the Hospital Authority

3.36 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) apart from measures taken to refer appropriate patients to NLTH Phase 1 for treatment, the HA will examine referring patients residing in the HA's Kowloon West Cluster to the hospital to better utilise the spare capacity of the in-use medical equipment and to speed up patients' access to service before the full commissioning of medical service at the hospital;
- (b) for medical equipment not put into use since their procurement, the HA anticipates that the equipment will be fully utilised under the service proposal for 2018-19 when additional beds will be commissioned; and
- (c) when implementing hospital projects in future, the HA will formulate a procurement plan for specific medical equipment items to dovetail with the commissioning of new beds under the Government's Resource Allocation Exercise. For medical equipment items with common specification across different service areas, the HA will critically evaluate the benefits of bulk purchase against possible obsolescence, post-warranty maintenance and contingency back-up.

PART 4: MANAGEMENT OF MINOR HOSPITAL PROJECTS

4.1 This PART examines the HA's work in the management of minor hospital projects, focusing on:

- (a) project planning (see paras. 4.2 to 4.10);
- (b) project implementation (see paras. 4.11 to 4.29); and
- (c) information management and performance reporting (see paras. 4.30 to 4.38).

Project planning

4.2 In December 2013, the FC approved a one-off grant of \$13 billion under the CWRP to the HA for carrying out minor works projects (each costing \$75 million or below) starting from 2014-15. In seeking the funding approval, the FHB informed the FC that:

- (a) the one-off grant would replace a prevailing block vote under the CWRP (Note 35) to provide sufficient resources and allow more flexible planning for the HA to implement planned improvement works programmes in an intensive manner over the 10-year period from 2014-15 to 2023-24;
- (b) the HA could annually initiate around 500 new minor works projects (i.e. totally 5,000 projects in 10-year time), and the projects were grouped into five categories for implementation (Note 36); and

Note 35: *The CWRP block vote provided funding for the HA to carry out minor works projects on a lump-sum basis annually. According to the FHB, expenditure of the ongoing minor works projects initiated before 2014-15 under the CWRP block vote would be funded by the new one-off grant effective from 2014-15.*

Note 36: *The five categories are: (a) facility rejuvenation; (b) capacity enhancement; (c) safe engineering; (d) universal accessibility; and (e) regular maintenance works and preparatory works for major hospital projects.*

- (c) the HA would invest funds which would not be immediately required in low-risk investments while ensuring the provision of adequate liquid funds for meeting expenditure requirements. The one-off grant of \$13 billion plus the estimated investment income of \$1.9 billion (i.e. \$14.9 billion in total) was expected to be able to support the HA's minor works for about 10 years.

4.3 For the 3-year period from 2014-15 to 2016-17, the HA initiated a total of 1,092 minor works projects incurring a total expenditure of \$3,315 million (see Table 6).

Table 6

**Number of minor works projects initiated and expenditure incurred
(2014-15 to 2016-17)**

Year	Minor works projects initiated (No.)	Expenditure incurred on minor works (as of March 2017) (\$ million)
2014-15	424	890
2015-16	323	1,200
2016-17	345	1,225
Total	1,092 (Note 1)	3,315 (Note 2)

Source: HA records

Note 1: There were 1,036 (95% of 1,092) minor works projects initiated for HA hospitals and 56 (5%) projects for HA clinics.

Note 2: A sum of \$916 million (28% of \$3,315 million) was incurred for the ongoing minor works projects initiated before 2014-15 under the CWRP block vote and funded by the one-off grant (see Note 35 to para. 4.2(a)).

Remarks: As of March 2017, the balance of the one-off grant was \$10.7 billion (the original \$13 billion plus investment income of \$1 billion minus expenditure of \$3.3 billion).

High proportion of unplanned minor works projects

4.4 According to the HA, the general workflow for planning of its minor works projects is as follows:

- (a) in August each year, the HA's seven clusters would each submit a tentative list of minor works projects for the current and the next two financial years ("tentative 3-year rolling plan") to the Strategy and Planning Division for vetting;
- (b) in March next year, based on the HA's internal budget allocation, the clusters' tentative 3-year rolling plan would be amended accordingly and the HA's Chief Executive would approve the 3-year rolling plan;
- (c) for the injection of new minor works projects not included in the approved 3-year rolling plan, the HA's clusters should submit these injected projects to the Strategy and Planning Division for review. The Division would then seek the approval of the HA's Chief Executive if the projects are considered necessary; and
- (d) before commencement of a minor works project, the HA would submit a standard form providing information on the project scope, objectives and estimated costs to the FHB for approval.

4.5 According to the HA's internal guidelines, at least 90% of the new minor works projects initiated during a financial year should be planned projects included in the relevant approved 3-year rolling plan (Note 37). If the percentage is below 90%, the HA's concerned clusters should make greater efforts in properly planning their minor works projects. However, Audit examination found that, during 2014-15 to 2016-17, unplanned projects (i.e. projects not in the relevant approved 3-year rolling plan) accounted for 23% to 36% of the new projects initiated each year (see Table 7).

Note 37: *According to the HA, with a view to ensuring that the HA's clusters properly plan their minor works projects in a timely manner, at least 90% of the new projects initiated during a financial year should be planned projects included in the 3-year rolling plan approved in March of the year preceding the last financial year. For example, for 2016-17, of 345 new minor works projects initiated, 247 projects were included in the 3-year rolling plan approved in March 2015, representing 72% of the total number of projects initiated in 2016-17 (see Table 7).*

Table 7

**Planned and unplanned minor works projects
(2014-15 to 2016-17)**

Particulars	2014-15	2015-16	2016-17
(a) No. of planned minor works projects under the HA's relevant approved 3-year rolling plan	1,003	1,373	1,488
(b) No. of planned projects not selected for implementation	731	1,123	1,241
(c) No. of planned projects selected for implementation [(c) = (a) – (b)]	272 (64%)	250 (77%)	247 (72%)
(d) No. of unplanned projects initiated during the year	152 (36%)	73 (23%)	98 (28%)
(e) Total no. of new projects initiated during the year [(e) = (c) + (d)]	424 (100%)	323 (100%)	345 (100%)

Source: Audit analysis of HA records

4.6 As shown in Table 7, only 64% to 77% of the new minor works projects initiated each year had been included in the relevant approved 3-year rolling plan, falling short of the HA's 90% target. According to the HA, some projects had to be deferred or deleted due to technical constraints and unavailability of sites, or some projects were injected to cater for changes in operational needs. In Audit's view, the HA needs to strengthen the planning of minor works projects to meet the HA's 90% target.

Need to report survey results of building condition of public hospitals

4.7 In October 2013, when seeking the support from the LegCo Panel on Health Services for the one-off grant of \$13 billion for the HA to carry out minor works projects, the HA said that:

- (a) the conditions of the HA's ageing buildings would require particular attention, as they would have significant impact on the health and safety of their occupants and on the daily operation of public hospitals in the delivery of quality medical services to the community. Public hospitals were particularly prone to accelerated deterioration due to their constantly heavy utilisation. As a result, many of the HA's ageing facilities were in unsatisfactory conditions; and
- (b) it would conduct a yearly review on the conditions of the structures and facilities of public hospitals. Based on the review outcome, each HA cluster would determine the order of priority and the amount of funding for implementation of various minor maintenance and improvements works in the coming three years.

4.8 Audit noted that the HA's seven clusters were responsible for conducting building condition surveys of public hospitals on an annual basis, but the clusters had not provided the survey results to the Strategy and Planning Division and the HA's Chief Executive for vetting and approval of the 3-year rolling plan for minor works projects (see para. 4.4(a) and (b)). In Audit's view, the HA needs to monitor the ageing conditions of public hospital buildings (see para. 1.3 and Appendix B) and take measures to ensure that the survey results of the building condition of public hospitals are reported to the HA's Chief Executive for vetting and approval of the 3-year rolling plans.

Audit recommendations

4.9 **Audit has *recommended* that the Chief Executive, HA should:**

- (a) **strengthen the planning of minor works projects to meet the HA's 90% planning target; and**
- (b) **monitor the ageing conditions of public hospital buildings and take measures to ensure that the survey results of the building condition of public hospitals are reported to the HA's Chief Executive for vetting and approval of the 3-year rolling plans.**

Response from the Hospital Authority

4.10 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) unplanned projects will be kept to a minimum, but those due to certain unforeseen circumstances (e.g. sudden surge in service demand rendering it impossible for works area to be handed over to works contractors) are unavoidable; and
- (b) the HA will review its internal guidelines for future planning of minor works projects, including the requirement to report the survey results of the building condition to the HA's senior management in future.

Project implementation

4.11 According to the FHB's paper submitted to the FC in 2013, the HA had estimated the works to be implemented under minor works projects funded by the one-off grant over a 10-year period from 2014-15 to 2023-24. The HA's progress in implementing the minor works as of August 2017 is shown in Table 8.

Management of minor hospital projects

Table 8

**Implementation progress of minor works
(August 2017)**

Category	Minor works estimated to be implemented over 10 years (as FC was informed in 2013)	Works completed (as of August 2017)	Percentage $(c) = \frac{(b)}{(a)} \times 100\%$
	(a)	(b)	
(1) Facility rejuvenation	Renovating 500 wards	62 wards renovated	12 %
(2) Capacity enhancement	Providing 800 additional beds	253 additional beds provided	32 %
(3) Safe engineering	(i) Upgrading electrical installations in 16 hospitals (involving 52 electrical installations — Note)	(i) Electrical installations upgraded in 3 hospitals (involving 9 installations)	19 % (17 % in terms of electrical installations)
	(ii) Upgrading lifts in 33 hospitals (involving 364 lifts — Note)	(ii) Lifts upgraded in 4 hospitals (involving 13 lifts)	12 % (4 % in terms of lifts)
(4) Universal accessibility (for enhancing facilities for pedestrians and disabled persons)	No specific target	66 projects completed (in 32 hospitals and 5 clinics)	Not applicable
(5) Regular maintenance works and preparatory works for major hospital projects	No specific target	522 projects completed	Not applicable

Source: Audit analysis of HA records

Note: The number of electrical installations and lifts to be upgraded was not included in the FHB's paper submitted to the FC in 2013.

Need to closely monitor works progress

4.12 In December 2013, the FHB informed the FC that the HA could annually initiate around 500 new minor works projects (see para. 4.2(b)). However, Audit noted that only 1,092 projects (see Table 6 in para. 4.3) were initiated in the 3-year period from 2014-15 to 2016-17, representing an average of 364 projects per year (i.e. 73% of 500 projects). Audit also noted that, as of August 2017, after passage of about 3.4 years (34%) of the 10-year period:

- (a) while the HA had estimated to renovate 500 wards over the 10 years, only 62 wards (12%) had been completed (see item (1) in Table 8 of para. 4.11);
- (b) while the HA had estimated to upgrade 52 electrical installations in 16 hospitals over the 10 years, only 9 (17% of 52) electrical installations in 3 (19% of 16) hospitals had been upgraded (see item (3)(i) in Table 8 of para. 4.11); and
- (c) while the HA had estimated to upgrade 364 lifts in 33 hospitals over the 10 years, only 13 (4% of 364) lifts in 4 (12% of 33) hospitals had been upgraded (see item (3)(ii) in Table 8 of para. 4.11).

4.13 In June 2017, the HA informed Audit that the initiation of 500 new minor works projects annually was an estimated average. The actual number of projects initiated depended on factors including clinical requirements, operational needs and cash flow projection of future financial years.

4.14 In Audit's view, the HA needs to closely monitor the progress of minor works projects and take measures to initiate more projects to improve the conditions of the HA's ageing facilities.

Delay in completing works orders

4.15 For carrying out minor works projects, the HA generally adopts the following arrangements:

- (a) ***Projects with a value of \$30 million or below.*** The HA has appointed 4 term contractors (TCs — generally under a 3-year term contract), 4 term maintenance surveyors (TMSs) and 4 term quantity surveyors (TQSs) (both TMS and TQS under a 5-year term consultancy) for carrying out these projects (Note 38). In general, the projects are carried out by the TC responsible for the related cluster area. The works of each TC are monitored by a TMS and a TQS. A TMS also undertakes design work and issues works orders to the TC, and a TQS is also responsible for cost control, contract payment and preparation of final accounts of the projects;
- (b) ***Projects with a value of more than \$30 million and not exceeding \$75 million.*** The HA conducts an exercise to engage a consultant and contractor for carrying out each of these projects (hereinafter referred to as “other minor-works contractors”); and
- (c) ***E&M works.*** Apart from the above arrangements, the HA has signed a 5-year service contract with the EMSTF (Note 39) for engaging the EMSTF to carry out certain E&M works in a minor works project where appropriate.

Note 38: *Of the 4 TCs, 3 are each responsible for carrying out minor works projects (with a value of \$30 million or below) in 2 HA clusters (namely, the Hong Kong East and Hong Kong West Clusters, the Kowloon Central and Kowloon East Clusters, or the New Territories East and New Territories West Clusters), and the remaining TC is responsible for the minor works projects in the Kowloon West Cluster. The same division of responsibilities applies for the 4 TMSs and 4 TQSs.*

Note 39: *The EMSTF was set up in August 1996 under the Trading Funds Ordinance (Cap. 430) to manage and account for the operation of certain services of the Electrical and Mechanical Services Department. The services provided by the EMSTF include operation and maintenance of electrical, mechanical, electronic and building services systems and equipment.*

4.16 Depending on the nature of a minor works project, the HA or TMS may issue works order(s) to a TC and other minor-works contractors for carrying out the required works, and the HA may request the EMSTF to carry out E&M works under the same project. Each works order specifies the “Date due for completion” (hereinafter referred to as “expected works completion date”). Up to August 2017, for the 323 minor works projects initiated in 2015-16 and the 345 projects initiated in 2016-17, Audit noted that 624 and 480 works orders (i.e. a total of 1,104 works orders — Note 40) had been issued respectively. Table 9 shows the implementation progress of these works orders.

Table 9

**Implementation progress of works orders
(August 2017)**

Works delay (Time lapse between expected and actual works completion dates)	No. of works orders issued		Total (c) = (a) + (b)
	Works completed (a)	Works in progress (Note 1) (b)	
No delay	324	27	351 (32 %)
> 0 to ≤ 3 months	117	26	143
> 3 to ≤ 6 months	69	34	103
> 6 to ≤ 12 months	28	27	55
> 12 to ≤ 17 months	2	0	2
Sub-total	540	114	654 (Note 2)
The HA was unable to provide the information (Note 3)			450 (41 %)
Total			1,104 (100 %)

Source: Audit analysis of HA records

Note 40: In April 2017, Audit requested the HA to provide details of the works orders for the minor works projects initiated in 2014-15, 2015-16 and 2016-17. According to the HA, due to the lack of an information system for processing of works orders (see also paras. 4.31 to 4.33), it was only able to manually retrieve the 1,104 works orders initiated in 2015-16 and 2016-17 for Audit analysis.

Table 9 (Cont'd)

Note 1: As of August 2017, works under 114 works orders were in progress. The works delays are counted up to 31 August 2017. For those works orders with expected works completion dates after that date, the works are regarded as having “No delay”.

Note 2: The 654 works orders related to 400 minor works projects.

Note 3: In April 2017, Audit requested the HA to provide details of the 1,104 works orders issued for minor works projects initiated in 2015-16 and 2016-17, including the estimated works values and expected and actual works completion dates. According to the HA, due to the lack of an information system for processing of works orders (see also paras. 4.31 to 4.33), it was only able to manually retrieve the relevant details of 654 (but not the 450) works orders for Audit analysis.

4.17 Delay in completing works orders. Audit noted that there were delays in completing 303 (27%) of the 1,104 works orders (or 46% of the 654 orders with information provided by the HA). In this connection, Audit noted that 219 (72% of the 303) works orders having delay were carried out by TCs, and the progress of works orders carried out by 2 TCs was less than satisfactory (Note 41). In Audit’s view, the HA needs to strengthen measures to monitor the progress of minor works orders to ensure their timely completion.

4.18 Need to enhance management of minor works. Case 1 shows that there is room for improvement in the HA’s management of minor works orders as revealed by Audit examination of a works order with delay of 17 months (being the longest delay among the works orders in Table 9 in para. 4.16).

Note 41: *An adverse performance report had been issued to a TC in the fourth quarter of 2016 and another TC in the first quarter of 2017 due to their “Very Poor” performance on works progress. While the contractors’ overall performance rating was rated as “Satisfactory” in subsequent periods up to June 2017, the corresponding performance reports still indicated that the progress of some minor works projects had lagged behind the works programme due to factors such as poor site monitoring, shortage of labour and late delivery of materials.*

Case 1

A minor works order with long delay in completion

1. The works order was issued to a TC in November 2015 with the expected works completion date of February 2016. The works involved renovating the physiotherapy department and upgrading the dilapidated building conditions at the Grantham Hospital. In the event, the required works were completed in July 2017, 17 months later than the original target date.

2. Audit noted that the delay was due to variation orders issued (accounting for 8 months), disturbance to works progress due to design changes of an electrical system by the HA after commencement of works (accounting for another 8 months), and late handover of works site by the HA (accounting for another 1 month).

Audit comments

3. In Audit's view, the HA needs to take measures to enhance the planning and implementation of works orders, including the finalisation of works design before commencement of works and the timely handover of works sites.

Source: HA records

Need to set a target time for finalising accounts of minor works projects

4.19 Under the HA's minor works contracts:

- (a) the account of a minor works project shall be finalised within the time limit stipulated for steps under the account-finalisation process (Note 42), and final payment for the project shall be made upon account finalisation; and
- (b) the maintenance period is 12 months counting from the date of substantial works completion, and all the outstanding works and construction defects shall be carried out by a contractor at his own expense within the maintenance period.

4.20 According to the HA, if the finalised value of a minor works project is less than the APE, the difference would be regarded as savings which would be deployed for use in other minor works projects, and early finalisation of accounts could facilitate planning of future projects. Under the HA's practice, after the expiry of the 12-month maintenance period of a minor works project, it would submit a standard form to the FHB containing details such as the actual dates of works completion and account finalisation as well as the finalised expenditure.

4.21 According to the HA, as of March 2017, of the 1,092 minor works projects initiated during 2014-15 to 2016-17, 693 projects had been completed. As the HA did not maintain readily available information on the progress of finalising the accounts of individual completed projects, Audit examined the FHB's records on the

Note 42: *The HA's minor works contracts have stipulated time limits for the concerned parties to prepare, assess and agree the final accounts of minor works projects:*

- (a) *30 days (counting from the issue date of certificate of works completion) for a contractor to submit the final bill to a TMS;*
- (b) *45 days for the TMS to provide the contractor with assessment on the final bill based on the advice of the TQS;*
- (c) *14 days for the contractor to provide substantiation on disagreed items and to submit the revised final bill;*
- (d) *14 days for the TMS to provide the contractor with final assessment on the revised final bill based on the advice of the TQS; and*
- (e) *14 days for the contractor to agree with the TMS's final assessment.*

standard forms relating to 132 completed projects submitted by the HA to ascertain the progress up to June 2017. Audit found that the time taken to finalise the accounts of the 132 minor works projects varied considerably, ranging between less than 1 month and up to 18 months (see Table 10).

Table 10

**Progress of finalising accounts of 132 minor works projects
(June 2017)**

Time lapse between actual works completion date and account finalisation date	No. of projects (a)	Total APE (b) (\$ million)	Total finalised value (c) (\$ million)	Saving (d) = (b) – (c) (\$ million)
≤ 6 months	63 (48%)	149.3	133.2	16.1 (37%)
> 6 to ≤ 12 months	29 (22%)	73.4	53.5	19.9 (45%)
> 12 to ≤ 18 months	40 (30%)	123.8	115.9	7.9 (18%)
Total	132 (100%)	346.5	302.6	43.9 (100%)

Source: Audit analysis of FHB records

4.22 As shown in Table 10, the accounts of 69 (52% of the 132) minor works projects were finalised more than 6 months (with 40 of them more than 12 months) after the actual date of works completion. If their project accounts could be finalised earlier, the related saving, being unused funding, would not be locked-up and could be deployed for use in other projects in a timely manner (see para. 4.20).

4.23 In August 2017, the HA informed Audit that:

- (a) the actual duration for finalising the accounts of minor works projects would depend on various factors including the time taken for submission of final bills by TCs, verification of final bills and agreement on further substantiation provided by TCs; and

Management of minor hospital projects

- (b) for simple cases, it was possible that the accounts of minor works projects could be finalised within 2 to 3 months after works completion. However, for complicated cases, it was not uncommon that it might take longer to finalise the related accounts.

4.24 As early finalisation of accounts would enable timely deployment of savings for use in other minor works projects (see para. 4.20), Audit considers that the HA needs to set a target time for finalising the accounts of minor works projects and endeavour to meet the target time.

4.25 Moreover, Audit noted that the service contract between the HA and the EMSTF (see para. 4.15(c)) only specified that the accounts of E&M works should be finalised as soon as possible without stipulating a definite time limit for the purpose. In this connection, Audit noted that, of the 69 minor works projects having accounts finalised more than 6 months after the actual date of works completion (see Table 10 in para. 4.21), 24 (35%) projects related to E&M works carried out by the EMSTF.

4.26 In Audit's view, for more effective monitoring of the progress of the account-finalisation work, there are merits for the HA to explore with the EMSTF the possibility of stipulating under the service contract a definite time limit for finalising accounts of E&M works in minor works projects after works completion.

Audit recommendations

4.27 **Audit has *recommended* that the Chief Executive, HA should:**

- (a) **closely monitor the progress of minor works projects to ensure timely completion and take measures to initiate more projects to improve the conditions of the HA's ageing facilities;**
- (b) **take measures to enhance the planning and implementation of works orders, including the finalisation of works design before commencement of works and the timely handover of works sites;**
- (c) **set a target time for finalising the accounts of minor works projects and endeavour to meet the target time; and**

- (d) **in collaboration with the Director of Electrical and Mechanical Services, explore the possibility of stipulating under the EMSTF service contract a definite time limit for finalising accounts of E&M works in minor works projects after works completion.**

Response from the Hospital Authority and the Government

4.28 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) following the FC's approval of the one-off grant of \$13 billion for minor works projects in December 2013, the HA put in place a work plan for the delivery of committed targets over the 10-year period from 2014-15 to 2023-24, against which the progress has been regularly monitored in the HA's Quarterly Review Meeting (see para. 1.12(a)); and
- (b) as the information system for processing of works orders will be launched in early 2018, the HA will be in a better position to exercise closer monitoring of minor works projects, but certain flexibility is required to be allowed having regard to the nature of minor works projects in hospital settings.

4.29 The Director of Electrical and Mechanical Services agrees with the audit recommendation in paragraph 4.27(d).

Information management and performance reporting

4.30 According to the HA, it has maintained an information system (known as "Computing System of Project Planning and Execution") primarily for the preparation of standard forms to be submitted to the FHB for the initiation, cost variation and finalisation of minor works projects. The information system also maintains the related financial data such as expenditure allocated and incurred by each HA's cluster under the one-off grant.

Better use of technology to effectively monitor project implementation

4.31 Audit noted that the HA's information system could not provide comprehensive management information for effectively monitoring the implementation of minor works projects, including information on:

- (a) the progress in implementing works orders (e.g. management reports of all the works orders having works delay);
- (b) the assessment progress of EOT claims and imposition of liquidated damages (e.g. management reports of all EOT claims not yet assessed after a long time period); and
- (c) the progress of finalising the accounts of completed projects (e.g. management reports of all completed projects with accounts not yet finalised long time after works completion).

4.32 According to the HA, due to the limitations of the information system, the HA staff primarily process works orders manually and retrieve the related information by accessing individual case files containing the works orders.

4.33 Audit noted that the HA planned to launch a new information system in April 2018 with a view to maintaining and providing more comprehensive information of works orders related to minor works projects. In Audit's view, the HA needs to take measures to ensure that the new information system is timely launched, and to better use technology to generate comprehensive management information for monitoring the implementation progress of minor works projects and the related works orders.

***Progress of works implementation and account finalisation
not reported to HA Board/Committees***

4.34 In December 2013, when seeking funding approval, the FHB informed the FC that the HA would submit the following information to LegCo on an annual basis to ensure transparency and accountability on the use of the one-off grant for minor works projects:

- (a) a full list of planned minor works projects to be funded by the one-off grant in the following financial year;
- (b) reports on the key minor works projects implemented and the actual expenditure in the past financial year, as well as key minor works projects planned to be implemented and the forecast expenditure under the one-off grant in the coming year; and
- (c) audited financial statements on the use of the one-off grant.

In February 2016 and February 2017, the HA submitted the above information to LegCo relating to the use of the one-off grant in 2014-15 and 2015-16 respectively.

4.35 The HA management had submitted regular reports to the HA Board and its relevant Committees on the progress of implementing minor works projects mainly relating to the financial aspects (e.g. overall expenditure patterns and cash balance of the one-off grant for minor works projects). For example:

- (a) for the HA Board, the audited financial statements on the use of the one-off grant were submitted for its approval on an annual basis; and
- (b) for the HA's Capital Works Subcommittee (see Note 23 to para. 2.40), financial reports relating to the overall expenditure incurred on the 5 works categories (see Note 36 to para. 4.2(b)) and the cash balance of the one-off grant were submitted for information on a quarterly basis.

Management of minor hospital projects

4.36 Audit noted that management information on the progress of and the delays encountered in the implementation of minor works projects (see para. 4.16) and the finalisation of accounts of the projects (see para. 4.21) had not been reported to the HA Board or its Committees. For transparency, accountability and monitoring purpose, the HA management needs to consider reporting regularly such information to the HA Board and its relevant Committees.

Audit recommendations

4.37 Audit has *recommended* that the Chief Executive, HA should:

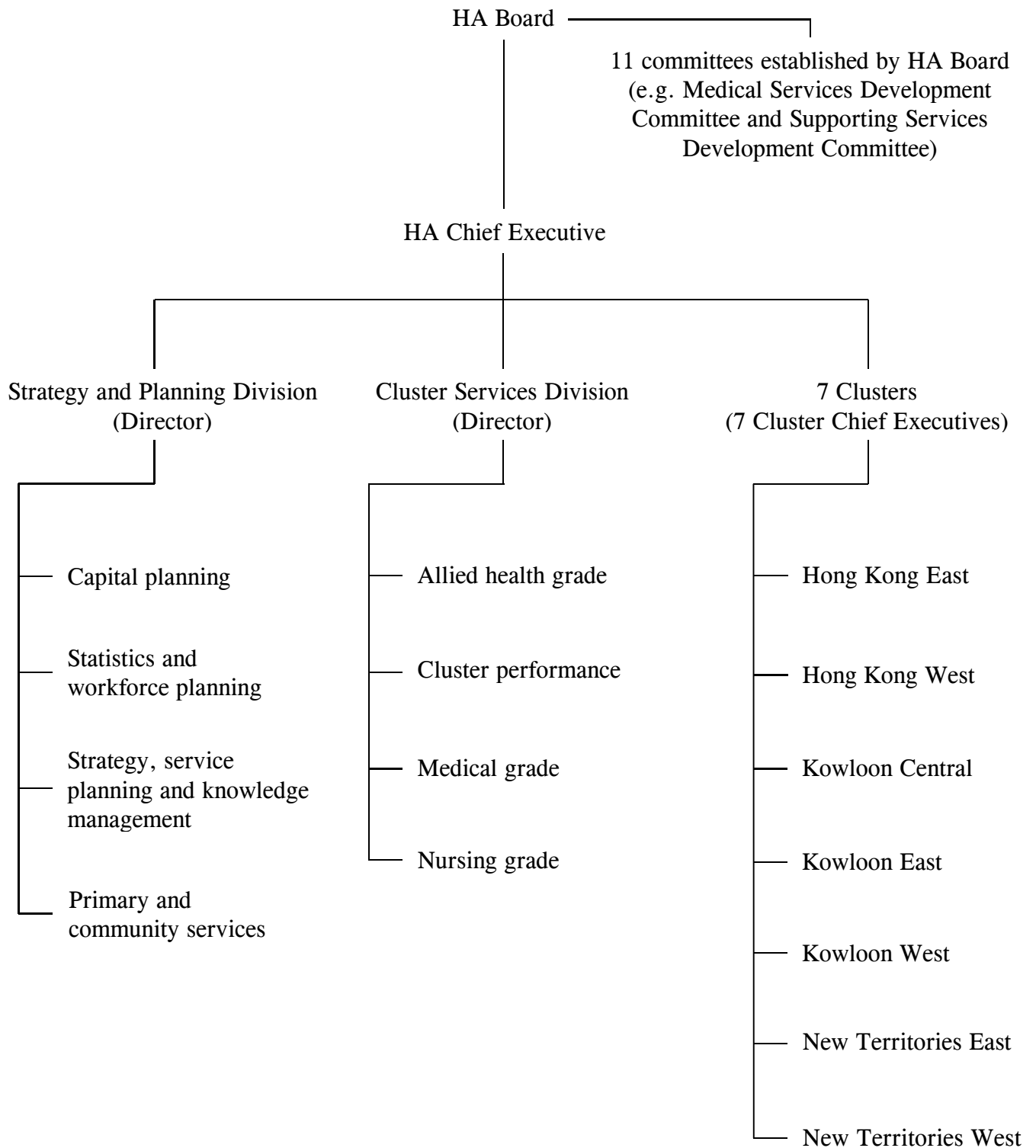
- (a) **take measures to ensure that the HA's new information system is timely launched, and to better use technology to generate comprehensive management information for monitoring the implementation progress of minor works projects and the related works orders; and**
- (b) **consider reporting regularly the information relating to the implementation progress (including delays encountered) of minor works projects and the finalisation of accounts of the projects to the HA Board and its relevant Committees to facilitate their monitoring of the progress of minor works projects.**

Response from the Hospital Authority

4.38 The Chief Executive, HA has said that the HA agrees with the audit recommendations. He has also said that:

- (a) following a consultancy study conducted in May 2015 to review the processing of works orders for minor works projects, the HA has initiated the development of a new information system for end-to-end processing of works orders, and the new system is planned to be put into operation in early 2018; and
- (b) the implementation progress of minor works projects, including the status of account finalisation, will be regularly reported to the HA's Supporting Services Development Committee in future.

**Hospital Authority:
Organisation chart (extract)
(September 2017)**



Source: HA records

**Ageing analysis of floor areas of HA's hospital buildings
(September 2017)**

Length of time since building completion (Year)	Floor area (m²)
≤ 10	186,460 (7%)
> 10 to ≤ 20	221,410 (8%)
> 20 to ≤ 30	702,360 (26%)
> 30 to ≤ 40	528,700 (19%)
> 40 to ≤ 50	356,000 (13%)
> 50 to ≤ 60	295,970 (11%)
> 60	423,600 (16%)
Total	2,714,500 (100%)

1,604,270 m²
(59%)

Source: Audit analysis of HA records

Appendix C
(para. 1.7 refers)

**HA's major hospital projects under planning or in progress
(August 2017)**

Project	Estimated additional bed (No.)	Estimated additional operating theatre (No.)	Tentative completion date	Status	
				Under planning	Works in progress
(A) Major hospital projects included in 10-year Hospital Development Plan					
1. Expansion of Haven of Hope Hospital	160	—	2021		✓
2. Extension of Operating Theatre Block for Tuen Mun Hospital	—	9	2021	✓	
3. Expansion of United Christian Hospital	560	5	2023		✓
4. New Acute Hospital at Kai Tak Development Area	2,400	37	2024	✓	
5. Expansion of North District Hospital	600	—	2024	✓	
6. Expansion of Lai King Building in Princess Margaret Hospital	400	—	2024	✓	
7. Redevelopment of Kwai Chung Hospital	80	—	2024	✓	
8. Redevelopment of Our Lady of Maryknoll Hospital	16	—	2024	✓	
9. Redevelopment of Queen Mary Hospital (Phase 1)	—	14	2024		✓
10. Redevelopment of Grantham Hospital (Phase 1)	—	3	2024	✓	
11. Redevelopment of Kwong Wah Hospital	350	10	2025		✓
12. Redevelopment of Prince of Wales Hospital (Phase 2, Stage 1)	450	16	2027	✓	
Total	5,016	94	—	—	—
(B) Major hospital projects not included in 10-year Hospital Development Plan					
1. Hong Kong Children’s Hospital	468	12	2017		✓
2. Refurbishment of Hong Kong Buddhist Hospital	130	—	2019		✓
3. Expansion of the Hong Kong Red Cross Blood Transfusion Service Headquarters	For improving blood-transfusion facilities		2020		✓
Total	598	12	—	—	—

Source: FHB and HA records

Appendix D
(para. 3.12 refers)

**Planned and actual manpower provision at
North Lantau Hospital (Phase 1)**

Medical services	No. of staff					
	Planned for full operation		Actual (as of March 2017)		Difference	
	(a)		(b)		(c) = (b) – (a)	
	Prof. staff	Support staff	Prof. staff	Support staff	Prof. staff	Support staff
(A) Accident and emergency	70	15	61	16	(9)	1
(B) General out-patient clinic	11	12	9	12	(2)	0
(C) Community care services	9	2	5	1	(4)	(1)
(D) Day rehabilitation centre	28	23	23	17	(5)	(6)
(E) Specialist out-patient clinics	23	19	11	14	(12)	(5)
(F) Day surgery centre	21	19	11	16	(10)	(3)
(G) Wards for in-patients	83	51	26	16	(57)	(35)
(H) Miscellaneous						
(i) Hospital administration (e.g. medical records and facility management)	7	157	4	75	(3)	(82)
(ii) Radiology	26	17	21	16	(5)	(1)
(iii) Pharmacy	28	14	18	7	(10)	(7)
(iv) Pathology	13	2	13	5	0	3
Sub-total	319	331	202	195	(117)	(136)
Total	650		397 (Note)		(253)	

Source: Audit analysis of HA records

Note: Of these 397 staff, 245 staff had been deployed through internal transfer within the HA and 152 staff recruited from external sources.

Remarks: “Prof. staff” referred to clinical professional staff including doctors, nurses and allied health professionals. “Support staff” referred to supporting staff (e.g. hospital administrators, patient care assistants and executive assistants) for effective operation of the hospitals.

**Key factors affecting commissioning of medical services at
North Lantau Hospital (Phase 1)**

The HA informed Audit during May to September 2017 that the following two key factors would affect the commissioning of medical services at NLTH Phase 1.

(A) Manpower shortage (especially for clinical professional staff)

1. There were multiple contributing factors leading to the persisting manpower shortage of healthcare professionals in Hong Kong which could be traced back to the economic downturn since the late 1990s.
2. Due to the adverse economic condition in the aftermath of Severe Acute Respiratory Syndrome epidemic, student intake of the two medical schools in Hong Kong was reduced from 301 to 280 in 2003 and to 250 in 2005, and then increased to 320 in 2009 and to 420 since 2012. In terms of the number of local medical graduating interns available for recruitment by the HA, the annual number was reduced from 301 to 280 in 2009 to 250 in 2011 and then increased to 320 in 2015. The HA expected that 420 medical graduates would be available for recruitment by the HA in 2018.
3. There had been a reduction in the number of nursing graduates since 1999. With the government policy of upgrading basic nursing education to degree level for enhancing the quality of healthcare services, majority of HA nursing schools (except the nursing school at Queen Elizabeth Hospital) had ceased student intake to the HA nursing programmes since July 1999. In 2009, the number of places for nursing programmes was increased from 550 to 590 at degree level and from 110 to 160 at associate degree level. In 2003, the student intake for physiotherapists, occupational therapists and radiographers was reduced, and the number had been increased gradually since 2012.
4. The HA had been adopting a multi-faceted approach to attract and retain staff, and managed to achieve steady growth of manpower including doctors, nurses and allied health professionals in the past years. However, with the accumulative effect over the years, the severe manpower shortage had become one of the major constraining factors confining the pace and extent of the healthcare service expansion to cope with the escalating demand in public healthcare services.

(B) Competing needs across the HA

1. As a publicly-funded organisation, the HA was accountable to the Government through the Secretary for Food and Health, who formulated the overall health policy for Hong Kong. The HA's strategic plans served as the over-arching frameworks for HA staff to align their priorities and efforts with the corporate directions and strategies in a consistent way. These strategic plans had also prospectively guided the HA's annual planning process and submissions to the Government under the annual Resource Allocation Exercise. Following the HA's corporate strategic directions, there were a large number of service initiatives competing through the annual planning process for the limited available resources (including manpower) on a year-on-year basis.
2. The HA's prioritisation of service proposals was carried out with reference to its strategic priorities and service directions, operational readiness of various service programmes, and the Government's healthcare priorities. The new initiatives and service programmes would have to undergo a process of resource bidding, prioritisation and allocation. It was an integrated and rolling process, and had linked up the Resource Allocation Exercise with other resource bidding exercises for non-recurrent funding. Hence, the HA had a structured annual planning exercise to achieve the following objectives:
 - (a) deploying resources effectively and in a focused manner that was targeted at service priorities set out in the HA's strategic plans;
 - (b) deciding on and prioritising service provisions for the coming year;
 - (c) ensuring a fair and transparent internal resource allocation system; and
 - (d) ensuring that an effective mechanism was in place to monitor the implementation and progress of the approved programmes.
3. New services and initiatives to be implemented in the ensuing financial year had been set out in the HA's annual plans. During the HA's annual planning exercise, inputs from clinical specialties, hospital clusters and the HA's Head Office were gathered under a structured framework for systematic review and prioritisation, taking into account various factors such as the baseline services in different clusters, the healthcare needs of the population in different localities, the Government's policy initiatives, the availability of manpower and the prevailing situation of the infrastructure under the phased completion of new hospital facilities. With limited resources (including manpower), there were practical needs to prioritise various service initiatives critically and realistically.

Appendix E
(Cont'd)
(para. 3.13(a) refers)

4. In the planning process for service commissioning of NLTH Phase 1, the key considerations within the Kowloon West Cluster were service needs, community expectation, readiness of medical services and availability of resources (including manpower). Furthermore, to ensure patient safety and smooth operation, services of new hospitals would be commissioned in phases. The priority service areas for service opening at NLTH Phase 1 in 2013-14 included accident and emergency service, medicine and psychiatrics specialist out-patient services, relocation of the Tung Chung General Out-patient Clinic, community outreach services and allied health services.
5. Similar to the HA's other service programmes, the plan for commissioning new services at NLTH Phase 1 needed to go through the annual planning process, which was part of the Resource Allocation Exercise. As the overall public hospital service demand exceeded the resource (including manpower) availability in terms of both quantity and quality, the service commissioning proposal of NLTH Phase 1 would have to compete with other service enhancement initiatives, and only a portion of the annual planning initiatives would be allocated with the necessary resources (including manpower) to implement the programmes. With the changing circumstances and the uncertainties involved, the HA would examine the service commissioning initiatives of NLTH Phase 1 on a year-by-year basis.

Source: HA records

Acronyms and abbreviations

APE	Approved Project Estimate
ArchSD	Architectural Services Department
Audit	Audit Commission
CMC	Caritas Medical Centre
CWRF	Capital Works Reserve Fund
DEVB	Development Bureau
EMSTF	Electrical and Mechanical Services Trading Fund
EOT	Extension of Time
E&M	Electrical and mechanical
FC	Finance Committee
FHB	Food and Health Bureau
HA	Hospital Authority
LD	Labour Department
LegCo	Legislative Council
MSDC	Medical Services Development Committee
m ²	Square metres
NLTH	North Lantau Hospital
PMH	Princess Margaret Hospital
SSEMC	Site Safety and Environmental Management Committee
TC	Term contractor
TMS	Term maintenance surveyor
TQS	Term quantity surveyor

CHAPTER 4

Transport and Housing Bureau Transport Department

Regulation of non-franchised bus and school private light bus services

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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REGULATION OF NON-FRANCHISED BUS AND SCHOOL PRIVATE LIGHT BUS SERVICES

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REGULATION OF NON-FRANCHISED BUS AND SCHOOL PRIVATE LIGHT BUS SERVICES

Executive Summary

1. Public transport services are closely related to the daily life of the public. In 2016, over 12 million passenger trips (representing 90% of the total passenger trips) per day were made through different public transport services in Hong Kong. It is the Government's transport policy to maintain a balanced public transport system with coordination among different modes including railway, franchised buses, public light buses, non-franchised buses (NFBs) and taxis. NFBs play a supplementary role in the public transport system through relieving the demand for franchised bus and green minibus services during peak hours, and providing services to specific passenger groups (e.g. tour groups, hotel guests and students) when the regular public transport services cannot provide appropriate services. In accordance with the Road Traffic Ordinance (RTO — Cap. 374) and the Public Bus Services Ordinance (Cap. 230), there are eight main types of public NFB services (e.g. student service and residents' service) which are intended for use for hire or reward and four types of private NFB services which are free of charge except those for disabled persons and students. Apart from NFBs, school private light buses (SPLBs) are also allowed under the RTO to solely provide student service. As at 31 December 2016, there were 7,043 public NFBs, 651 private NFBs and 1,966 SPLBs. The operation of NFB and SPLB services is regulated by the Transport Department (TD) through the Passenger Service Licence (PSL) system under the RTO and its subsidiary legislation. The Audit Commission (Audit) has recently conducted a review to examine the TD's work in regulating NFB and SPLB services.

Administration of licensing requirements

2. *PSL system.* PSLs authorise licensees to operate vehicles to provide passenger services whereas Passenger Service Licence Certificates (PSLCs) are issued to vehicles operating under the PSLs. A PSL holder is also required to obtain from the TD individual service endorsement(s) for the specific type(s) of service and approval of individual route(s) for regular services (i.e. with fixed schedules and

Executive Summary

routes). In 2016, the TD processed 24,897 licence applications for NFBs and SPLBs, of which 20,894 (84%) were related to PSLs or PSLCs (paras. 1.7, 2.5 and 2.19).

3. ***Measures to coordinate the change in NFB services with demand.*** In 2004, in light of the unhealthy competition with other public transport modes arising from an excessive supply of NFB services, the Transport Advisory Committee (TAC) recommended that the Government should coordinate the change in NFB services with demand in a more effective manner. In January 2005, the Legislative Council (LegCo) Panel on Transport was informed that a package of measures would be implemented to ensure that new NFB services and vehicles would only be approved when there was justified demand, including stringent vetting of NFB applications and requiring PSL applicants to source vehicles from the existing fleet in the market for a period of six months (i.e. the sourcing requirement) (paras. 1.9(a) and 2.7).

4. ***Need to review the implementation of the sourcing requirement.*** According to the Government, although it is not appropriate to impose a cap on the NFB fleet, the sourcing requirement is important for the proper control over NFB operations whilst ensuring the service demand is met. Since the implementation of the sourcing requirement in April 2005, no application for additional public NFBs which involved a net increase in the total number of NFBs had been approved. The number of public NFBs had in fact decreased by 169 (2%) from 7,212 in 2004 to 7,043 in 2016, although the number of private NFBs had increased by 158 (32%) from 493 in 2004 to 651 in 2016, primarily because the sourcing requirement has been relaxed since 2007 with exemption granted to charitable organisations and educational institutions (paras. 2.7(c), 2.10 and 2.13). However, Audit noted that:

- (a) the sourcing requirement was implemented in accordance with the TD's internal guidelines which included a requirement not stated in the 2004 TAC review report and the 2005 LegCo Panel on Transport paper, i.e. an applicant who failed to source a second-hand NFB at the end of the six-month period would be asked to make further efforts to source vehicles from the existing fleet if the TD's annual survey revealed that there was no shortfall in supply of vehicles for NFB services and there were active transactions in the second-hand market (paras. 2.9 and 2.13);

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- (b) according to the TD's annual surveys, the utilisation rate of public NFBs had increased from 81 % in 2004 reaching its peak at 89 % in 2014 before slightly dropping to 86 % in 2016. The number of trips of NFB had increased by 40 % from 40,104 per day in 2004 to 55,970 per day in 2016, indicating service demand had increased (para. 2.11(a)); and
- (c) as regards the second-hand transactions of public NFBs, while the number of second-hand public NFB transfer cases increased from 53 in 2005 to a peak of 362 in 2012, it was generally on a decreasing trend thereafter, falling to 142 in 2016. The average transaction price of a second-hand public NFB had increased from \$0.3 million in 2005 by 200 % to \$0.9 million in 2016 whereas the average price for a new bus normally ranged from \$0.6 million to \$0.9 million (para. 2.11(b)).

In light of the above findings and having regard to the lapse of some 12 years, it is timely for the TD to conduct a review on the implementation of the sourcing requirement (para. 2.13).

5. ***Need to tighten vetting of supporting documents for PSL renewal applications.*** From 2014 to 2016, the TD processed 2,080 PSL renewal applications for public NFBs. To apply for PSL renewal and renewal of service endorsements, a PSL holder shall provide a service contract of any duration to justify the continued need for the service and at least one service contract for renewal of each service endorsement permitted under the PSL respectively. Audit examined 10 PSL renewals involving 41 service endorsements granted to existing PSL holders from 2014 to 2016 and noted that: (a) for 6 (15 %) service endorsements, the PSL holders had not submitted relevant service contracts but only declared that the NFBs would be deployed for the relevant services; and (b) for 26 (63 %) service endorsements, the service contracts submitted could not fully support the number of vehicles required, e.g. in one renewal of service endorsement granted to 76 NFBs, the service contract submitted showed that only 3 NFBs were required (para. 2.14).

6. ***Need to enforce the more stringent vetting requirement on renewal applications of expired PSLs.*** If a PSL holder does not renew his PSL upon the expiry date, the TD will issue a warning letter to inform him that the concerned PSL has been cancelled, and any application for PSL thereafter will be treated as a new application (i.e. requiring the submission of service contracts with at least six-month validity to justify the genuine long-term service need). Audit examined 20 expired

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PSL cases with warning letters issued in 2015 and 2016 and noted that in 11 (55%) cases, the PSL holders subsequently submitted applications for renewal of the expired PSLs. However, all 11 cases were not processed as new applications, contrary to the requirements set out in the warning letters (paras. 2.23 and 2.24).

7. ***Need to consider streamlining the licensing requirements of PSLCs.*** In 2016, there were 17,899 PSLC-related applications. Audit examination has revealed scope for streamlining the licensing requirements of PSLCs, which would simplify the TD's administrative work and facilitate the NFB trade (para. 2.25):

- (a) ***Need to consider merging the two types of PSLC.*** It has been the practice of the TD to issue two types of PSLC, namely the green PSLC for vehicles providing regular services according to a schedule of service and the red PSLC for vehicles providing non-regular services. However, the schedule of service requirement has been extended to all regular NFB services since 2005 and hence four types of public NFB service previously classified as non-regular have been required to operate in accordance with schedules of service for those parts of their services which are of a regular nature (e.g. hotel shuttle service). In other words, public NFBs issued with the red PSLC for these four types of service endorsement may be providing a mix of regular and non-regular services. There is merit to examine the feasibility of merging the two types of PSLC (para. 2.25(a)); and
- (b) ***Need to consider aligning the validity periods of PSLCs and related PSLs for NFB operators.*** At present, an NFB operator normally has to renew his PSL once every two years and the related PSLCs for his NFBs every year. As the main licensing controls over the NFB operation are laid down in the PSL and the application for which is subject to stringent vetting, the issue of a PSLC is based on the approved operation details in the related PSL. Hence, a more frequent renewal cycle of a PSLC than that of a PSL is not warranted. Having regard to the fact that there are over 9,000 PSLCs for NFBs, it is worthwhile to explore the feasibility of aligning the validity periods of PSLCs and related PSLs (para. 2.25(b)).

Regulatory controls over unauthorised operations

8. *Need to strengthen enforcement actions against unauthorised NFB operations.* In 2004, the TAC noted the problems of unauthorised NFB operations, i.e. providing services: (a) without valid service endorsements; or (b) not in accordance with PSL conditions (e.g. operating more trips than permitted and deviating from the approved routeings). Such activities could lead to traffic and environmental problems, and the third party insurance of the NFBs concerned might also be invalidated. The TAC then recommended that the Government should strengthen regulatory controls over NFB operations and enhance the efficiency and effectiveness of enforcement actions. According to the TD's annual surveys from 2004 to 2016, with the exception of residents' service, the number of NFBs suspected to be operating without suitable endorsements for five other types of public NFB services was generally on an increasing trend. There is a need to strengthen enforcement actions to address the issue (paras. 3.4, 3.8 and 3.11).

9. *Need to improve investigative work of the Regional Offices (ROs).* The TD's two ROs conduct investigative surveys on black spots proactively or upon receipt of a complaint or referral. If an unauthorised service detected by the ROs persists and is substantiated after further investigation by the NFB Enforcement Team, the case will be recommended to the Commissioner for Transport for holding an inquiry. Audit test check of the TD's records has revealed the following inadequacies in the ROs' investigative work (paras. 3.12 and 3.13):

- (a) *Inadequate on-board surveys.* While terminal surveys (i.e. observation at the terminal or approved stops) are effective in detecting overrun trips and operations without relevant endorsements, they are less effective than on-board surveys (i.e. taking a ride on the buses in question) in detecting routeing deviation and unauthorised intermediate stops. Audit examined 400 surveys conducted by the ROs from 2012 to 2017 and found that 371 (93%) were terminal surveys and the remaining 29 (7%) were on-board surveys. From April to May 2017, Audit performed 22 on-board surveys on residents' service routes selected on a risk-based approach and found that 21 (95%) of them had been operated with unauthorised stop(s) and/or routeing deviation. There is a need to use a risk-based approach to determine the mix of on-board and terminal surveys for detecting different types of unauthorised NFB operations (para. 3.14);

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- (b) ***Inadequate follow-up actions on investigative surveys.*** In 53 surveys with irregularities found by the ROs' contractors from 2010 to 2017, there had been omissions and delays in taking follow-up actions in 35 (66%) cases. For example, in 10 cases, no clarification letter was sent to the PSL holders and no follow-up survey was conducted to confirm cessation of unauthorised operations (para. 3.15(a));
 - (c) ***Inadequate follow-up actions on complaint cases.*** In 18 complaint cases from 2012 to 2016, the ROs issued letters to inform the operators concerned that complaints had been received and requested them to cease the unauthorised operations. However, the ROs had only conducted follow-up surveys to ascertain cessation of the unauthorised operations in 3 (17%) of the 18 complaint cases (para. 3.15(b)(ii)); and
 - (d) ***Inadequacies in ROs' record keeping.*** The ROs had not maintained a database of all unauthorised NFB services found and information on actions taken and progress, contrary to the internal guideline requirements. For better case management, there is a need to strictly enforce the laid-down requirements and consider making better use of technology in monitoring compliance (paras. 3.15 and 3.19).
10. ***Need to improve the efficiency and effectiveness of enforcement actions.*** The Commissioner for Transport may cancel, suspend or vary a PSL for substantiated inquiry cases. Audit examination of the records of 175 inquiries from January 2012 to mid-May 2017 (paras. 3.2(b) and 3.21) revealed the following issues:
- (a) ***Long time taken to complete inquiries.*** Of the 175 inquiries, 93 had been concluded and 82 were outstanding. Among the 93 concluded cases, 67 cases were sanctioned. For these 67 cases, the time taken from the date of recommending to the Commissioner for Transport for holding an inquiry to the date of implementing sanctions averaged 24 months (ranging from 13 to 46 months). Of the 82 outstanding cases, 20 (24%) had been pending for over 2 years. Audit sample checked 8 of the 82 outstanding cases and found that unauthorised operations had continued in all of them while inquiries were in progress. Given the relatively long processing time for inquiry and the considerable number of breaches of PSL conditions (e.g. failure to display the stipulated service signboards for half or more of their trips was found in 3,048 (52%) of 5,870 NFBs surveyed in 2016),

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there is a need to explore additional enforcement tools against common breaches of PSL conditions (paras. 3.7, 3.22, 3.23(a) and 3.28); and

- (b) ***Sanctions not implemented due to transfer of ownership of NFBs.*** There were 25 (27%) of a total of 93 concluded cases in which the offending PSL holders had avoided sanctions through transfer of ownership of NFBs. For example, in five inquiries on unauthorised services from 2011 to 2015, before the completion of the inquiry process, the ownership of three NFBs was transferred to other PSL holders (i.e. four companies with common director(s) and one individual being a shareholder of one of the companies) at \$1 each and the relevant PSLs under the inquiries were cancelled. As a result, no sanction could be imposed. There is a need to shorten the lead time in completing an investigation and inquiry to minimise the risk of transfer of vehicles, and explore feasible measures to plug the sanction avoidance loophole in the long run (paras. 3.23(b) and 3.25).

11. ***Need to improve the publicity of authorised NFB services.*** Publicity is important for protecting the public from inadvertently using unauthorised NFB services which may not be covered by insurance in the event of accidents, and enhancing public scrutiny of unauthorised operations (para. 3.34). Audit has found room for improvement, as follows:

- (a) ***Stop signs for residents' service.*** To educate the general public not to use unauthorised residents' services, the TD erected stop signs at approved bus stops for some residents' service routes. Audit found that in three selected districts, only 49 (49%) out of 101 authorised NFB stops were erected with these stop signs. Audit inspected 58 stop signs in 6 districts and found that 3 (5%) of them were with outdated information. Audit also found that stop signs were erected by some operators at unauthorised locations without the TD's approval (paras. 3.29 and 3.30); and
- (b) ***Publicising approved schedules of service.*** Currently, the TD publishes on its website operation details stipulated in the schedules of service of all approved residents' service and certain cross-boundary international passenger service. However, the TD has not published similar operation details for other types of regular service (e.g. hotel shuttle service). Audit found suspected cases of non-compliance with the schedules of service under hotel service and contract hire service (including operation without schedules of service, charging of separate route fare, overrun trips and

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unauthorised stopping points), highlighting the need to publicise approved schedules of service for easy identification by the general public (paras. 3.33 and 3.34).

Safety measures of student service vehicles

12. As at 31 December 2016, there were 5,238 student service vehicles, including 3,169 public NFBs and 103 private NFBs with student service endorsements, and 1,966 SPLBs. Notwithstanding the generally satisfactory safety records of student service vehicles, the Government considers it important to explore measures to further enhance their safety. Since 2008, the provision of escort service has become a mandatory requirement for all NFBs and SPLBs carrying kindergarten and primary school students. In 2007, legislative amendment was made to require all student service vehicles registered on or after 1 May 2009 to be equipped with safer seats, i.e. strong and closely spaced seats with high and energy-absorbing backs, to protect children in the event of a crash (paras. 1.9(d), 4.2, 4.3(b) and 4.5).

13. ***Implementation of the safer seat requirements.*** As at 24 July 2017 (some eight years after the safer seat requirements came into operation on 1 May 2009), 3,382 (64%) of 5,261 student service vehicles were fitted with safer seats. Through a normal replacement cycle, it may take up to some 6 years to phase out/replace the remaining 1,879 (36%) student service vehicles without safer seats. There is a need to explore measures to speed up the progress of phasing in student service vehicles with safer seats (para. 4.7).

14. ***Additional safety measures.*** After the implementation of safer seat requirements in 2009, some LegCo Members expressed concern on the adequacy of safety measures on student service vehicles and requested the TD to explore further means for the protection of the passengers of student service vehicles, particularly those at young ages. According to the TD's consultancy study report of 2013, while safer seats were effective in providing protection to occupants on student service vehicles regardless of occupant age and size, their benefit could be further enhanced by the following measures (paras. 4.8 and 4.9):

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- (a) ***Child restraint device (CRD).*** The use of appropriate restraint systems could provide better protection to passengers aged under 4.5 years or weighing 18 kilograms or less in cases involving lateral and side-impact crashes, rollovers and ejections (para. 4.9(b)); and
 - (b) ***Seat belt.*** Passengers should be better protected by seat belts in side-impact and rollout accidents than safer seats alone, provided that seat belts were properly worn. In terms of safety benefits, safer seats with lap-shoulder seat belts were rated as excellent while safer seats alone and safer seats with lap-belts as average. After taking into account other factors (such as cost estimates, operational considerations and implementation issues), the overall performance of safer seat alone option was as good as that of safer seat with a lap-shoulder belt option (paras. 4.8 and 4.14).
15. ***Developments locally and overseas.*** Audit noted the following developments which needed to be taken into account in considering additional measures for enhancing the safety of student service vehicles (para. 4.13):
- (a) ***CRD.*** In 2013, two Members of the LegCo Panel on Transport considered that CRD/seat belt requirements should be imposed on student service vehicles which regularly carried child passengers. Audit's Internet research revealed that the use of CRDs on school buses was recommended for improving the protection of younger children in the United States and Canada which had safer seat requirements similar to those of Hong Kong (paras. 4.11 and 4.12); and
 - (b) ***Seat belt.*** While there was no mandatory requirement on the use of seat belts in student service vehicles, Audit analysis of the TD's records revealed that of the 3,382 student service vehicles fitted with safer seats as of July 2017, 2,094 (62%) had in fact been fitted with both safer seats and seat belts. In a sample check of the TD's records of 30 student service vehicles fitted with both safer seats and seat belts, Audit found that all of them were equipped with lap-belts which according to the 2013 consultancy study report were inferior to lap-shoulder seat belts in reducing the risks of severe head and neck injuries in frontal crashes (paras. 4.16 and 4.17).

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16. *Unresolved issues.* According to the TD, there were a number of issues to be thoroughly considered and resolved before a decision could be taken on the types of measures to further enhance the safety of student service vehicles, including safety benefits, cost implications, technical, operational, implementation and legal issues, impact on trade and views of stakeholders. In Audit's view, the TD needs to consider conducting a survey of stakeholders (including the operators, schools and parents) to gauge their views, preference and willingness to pay for various possible enhancement options, and address operational and implementation issues that may arise (paras. 4.18, 4.19 and 4.21(b)).

Audit recommendations

17. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Commissioner for Transport should:**

- (a) **in consultation with the Secretary for Transport and Housing, conduct a review of the implementation of the sourcing requirement (para. 2.15(a));**
- (b) **uphold the supporting document requirements in processing PSL renewal applications (paras. 2.15(b), 2.15(c) and 2.29(c));**
- (c) **consider streamlining the licensing requirements of PSLCs (para. 2.29(d));**
- (d) **strengthen enforcement actions against unauthorised NFB operations, such as using a risk-based approach to determine the mix of on-board and terminal surveys for detecting different types of unauthorised NFB operations (para. 3.35(a));**
- (e) **improve the efficiency and effectiveness of the enforcement actions, including endeavouring to shorten the lead time in completing the investigation and inquiry process, and exploring feasible measures to plug the sanction avoidance loophole in the existing inquiry mechanism (para. 3.35(d));**

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- (f) **consider publicising approved schedules of service of all regular NFB services, in particular for hotel and contract hire services, for easy identification by the general public (para. 3.35(f));**
- (g) **explore measures to speed up the progress of phasing in student service vehicles with safer seats (para. 4.20(a)); and**
- (h) **continue to keep abreast of the latest developments in enhancing the safety of student service vehicles, and consider conducting a survey of stakeholders to gauge their views and willingness to pay for possible enhancement options and address operational and implementation issues that may arise (para. 4.20(b)).**

Response from the Government

18. The Government generally agrees with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Government's transport policy

1.2 Public transport services are closely related to the daily life of the public. In 2016, over 12 million passenger trips (representing 90% of the total passenger trips) per day were made through different public transport services in Hong Kong. It is the Government's transport policy (Note 1) to:

- (a) maintain a balanced public transport system with coordination among different modes; and
- (b) ensure the provision of safe, efficient and cost-effective public transport services to the community.

It is also the Government's policy that public transport services should be run by the private sector in accordance with commercial principles to enhance efficiency and cost-effectiveness.

1.3 The Third Comprehensive Transport Study of May 2000 has set out a hierarchy of the roles and positioning of different public transport services having regard to their relative efficiency and capacity. According to the Public Transport Strategy Study Report of June 2017, the roles and positioning of different public transport services as set out in the past decades remain the same today, namely:

Note 1: *The policy was first stated in "The White Paper on Transport Policy in Hong Kong" published in January 1990 and reaffirmed by the "Hong Kong Moving Ahead — A Transport Strategy for the Future" of October 1999, the Third Comprehensive Transport Study of May 2000, and the latest Public Transport Strategy Study Report of June 2017.*

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- (a) railway is at the top of the hierarchy as it operates on dedicated rail corridors and provides high-capacity, convenient and emission-free services;
- (b) among the public transport modes other than heavy rail, franchised buses are mass carriers with a high capacity and can be deployed more flexibly, and their service pattern can be adjusted within a relatively short period to meet changes in demand. They serve areas without direct railway access as well as provide feeder service connecting railway network and inter-district service. Light Rail also plays an important role in the public transport system in the Northwest New Territories on feeder services to West Rail and as rail-based transport in the area;
- (c) the role of public light buses (Note 2) is to provide supplementary feeder service and to serve areas with relatively lower passenger demand or where the use of high-capacity transport modes is not suitable;
- (d) non-franchised buses (NFBs) play a supplementary role in the public transport system through relieving the demand for franchised bus and green minibus services during peak hours, and through providing services for districts where the operations of franchised buses and green minibuses are not cost-effective. They provide tailor-made services for specific groups, such as students and tourists. Since October 1999, private light buses which also provide school transport services have been put under the Passenger Service Licence (PSL) system as NFBs (see paras. 1.6 and 1.7); and
- (e) taxis provide a personalised, point-to-point and more comfortable public transport service at a higher fare.

1.4 To make the hierarchy of the public transport modes effective, a high degree of inter-modal coordination is required. The Transport Department (TD) is the authority for administering the Road Traffic Ordinance (RTO — Cap. 374) and

Note 2: *There are two types of public light buses, i.e. the green minibuses which operate regular services with their routes, fares, vehicle allocation and timetable subject to the approval by the Transport Department and the red minibuses which are not required to operate on fixed routes or timetables, and can set their own fares.*

legislation for the regulation of public transport services (Note 3). An extract of the TD's organisation chart is at Appendix A.

Non-franchised buses

1.5 In accordance with the RTO and the Public Bus Services Ordinance (PBSO — Cap. 230), NFBs provide two broad categories of services, as follows:

- (a) ***Public NFB services.*** The RTO defines a public bus as a bus used or intended for use for hire or reward. There are eight main types of services provided by public NFBs (see Appendix B for a brief description of the eight types of services):
 - (i) tour service (administrative code A01);
 - (ii) hotel service (A02);
 - (iii) student service (A03);
 - (iv) employees' service (A04);
 - (v) international passenger service (A05);
 - (vi) residents' service (A06);
 - (vii) multiple transport service (A07 — Note 4); and
 - (viii) contract hire service (A08).

Note 3: *For example, the railway services are regulated under the Mass Transit Railway Ordinance (Cap. 556) while franchised public buses are regulated under the Public Bus Services Ordinance (Cap. 230).*

Note 4: *The TD has not granted approval for multiple transport service for years due to market changes.*

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Public NFBs may be licensed to operate one or more of the above services subject to the operators obtaining the corresponding service endorsements from the TD (see para. 1.7); and

- (b) ***Private NFB services.*** The RTO defines a private bus as a bus used or intended for the carriage of passengers free of charge except when providing a student service and/or a disabled persons' service. There are four types of services provided by private NFBs:
 - (i) student service (B01) for designated schools or school sponsoring bodies;
 - (ii) employees' service (B02);
 - (iii) disabled persons' service (B03); and
 - (iv) any other service (B04) approved by the Commissioner for Transport.

Private NFBs are subject to strict restrictions by way of registration of vehicles (e.g. a private NFB for student service must be registered in the name of an educational institution) and mode of operation (i.e. a private bus used for employees' service and any other service must not be used for hire or reward), with vehicle ownership mostly confined to the institutes or organisations requiring the services. Private NFBs may be licensed to provide one or more of the above four services subject to the operators obtaining the corresponding service endorsements from the TD (see para. 1.7).

School private light buses

1.6 Apart from NFBs, vehicles allowed under the RTO to provide student service include school private light buses (SPLBs) which have 19 seats or less (Note 5). Commonly known as nanny vans, most SPLBs are painted in yellow and

Note 5: *The RTO was amended in July 2017 to increase the maximum passenger seating capacity of light buses from 16 to 19.*

bear the signs (e.g. a continuous horizontal purple stripe — Note 6) in accordance with the Road Traffic (Construction and Maintenance of Vehicles) Regulations (Cap. 374A) for alerting road users in keeping a safe distance when the SPLB is travelling on the road and when young children are boarding and alighting (see Photograph 1). Unlike NFBs, SPLBs are solely for providing student service.

Photograph 1

An SPLB



Source: Photograph taken by staff of Audit Commission on 6 July 2017

Licensing and regulatory regime

1.7 The operation of NFB and SPLB services is regulated through the PSL system (Note 7) under the RTO and its subsidiary legislation. PSLs authorise licensees to operate vehicles (e.g. NFBs or SPLBs) to provide passenger services whereas Passenger Service Licence Certificates (PSLCs) are issued to vehicles operating under the PSLs. A PSL holder is also required to obtain from the TD individual service endorsement(s) for the specific type(s) of service (see para. 1.5) he/she intends to provide and seek the TD's approval of individual route(s) for regular

Note 6: *The requirements on the signs and the colour of the outside of the vehicle do not apply to SPLBs registered before 1 May 1997.*

Note 7: *In order to exercise better control over the use of SPLBs, the Road Traffic (Amendment) Ordinance was enacted in October 1999 to require SPLBs to operate under the PSL system. In addition to NFB and SPLB services, public light bus service is also regulated under the PSL system.*

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services (see para. 2.5). The numbers of registered vehicles, PSLs, PSLCs and service endorsements issued in respect of NFBs and SPLBs as at 31 December 2016 are shown in Table 1. According to the TD's annual survey (Note 8), the fleet utilisation rate of NFBs and SPLBs in 2016 was about 86%.

Table 1

**Numbers of registered vehicles, PSLs, PSLCs and service endorsements
(31 December 2016)**

Type of vehicles	Registered vehicle	PSL	PSLC	Service endorsement (Note 1)
Public NFB	7,043	1,287	8,769 (Note 2)	17,806
Private NFB	651	200	651	867
SPLB	1,966	705	1,966	1,966

Source: TD records

Note 1: As an NFB can be issued with more than one service endorsement, the number of service endorsements is larger than the number of registered vehicles. An SPLB can only have one service endorsement.

Note 2: There are two types of PSLC, one for vehicles providing regular services and the other for non-regular services (see para. 2.6). As a public NFB providing regular and non-regular services will be issued with separate PSLCs, the number of PSLCs is larger than the number of registered vehicles.

1.8 The Public Vehicles and Prosecution Section of the Administration and Licensing Branch (see Appendix A), in collaboration with the Urban Regional Offices

Note 8: *The TD commissions a consultant to undertake an annual survey to collect operational information and utilisation of NFBs. In view of the public concerns on demand and supply of school bus service, SPLBs have been included in the annual survey since 2015.*

and the New Territories Regional Offices (ROs — Note 9), administers the PSL system, including issuing PSLs and PSLCs and taking enforcement actions against vehicles governed by PSLs operating unauthorised services. The enforcement tools available under the RTO and PBSO against unauthorised NFB services and breaches of the PSL conditions include prosecution and inquiry (see para. 3.2(a) and (b)).

Measures to address the operational problems of NFBs and SPLBs

1.9 Over the years, there have been various operational problems related to NFBs and SPLBs, and the TD has introduced various measures to address these problems:

- (a) ***Measures to address the oversupply of NFBs.*** Between 1998 and 2003, the number of registered NFBs increased from 5,900 to 7,200, representing an increase of 22% whereas public transport patronage only increased by 2.7% from 11.1 million to 11.4 million passengers per day over the same period. As a result, NFB operators faced greater competition among themselves and they also competed more intensively with other public transport modes, in particular public light buses and taxis to obtain passenger share. The unhealthy competition arising from an excessive supply of NFB services was against the inter-modal coordination policy (see para. 1.4). After conducting a review and consulting the transport trade in 2004, the Transport Advisory Committee (TAC — Note 10) recommended that the Government should coordinate the change in NFB services with demand. Accordingly, the TD tightened the licensing regime so that new supply of NFB services and vehicles would only be approved when there was justified demand. In addition, PSL applicants are required to source NFBs from the existing fleet (i.e. the sourcing requirement);

Note 9: *The ROs are responsible for all transport matters within their respective areas. The two ROs are each headed by an Assistant Commissioner for Transport and supported by some 40 Transport Officer grade staff responsible for overseeing public transport matters.*

Note 10: *The TAC comprises 15 non-official members including the chairman and three ex-officio members, i.e. the Permanent Secretary for Transport and Housing (Transport) or his representative, the Commissioner for Transport and the Commissioner of Police or his representative. The TAC's function is to advise the Chief Executive-in-Council on transport matters including broad issues of transport policy with a view to improving the movement of both people and freight.*

- (b) ***Measures to address the unauthorised NFB services.*** The TAC's 2004 review also noted that as a result of the keen competition, some NFB operators had operated unauthorised NFB services, undermining the regular and legitimate transport services and causing traffic problems at some popular spots. The TAC recommended that the Government should strengthen regulatory controls over NFB operation and enhance the efficiency and effectiveness of enforcement actions. To facilitate better monitoring and enforcement against unauthorised NFB operations, schedules of service stipulating all relevant operation details have been extended since 2005 to all NFB services which are of a regular nature with the same origin and destination areas, and appropriate signs in a standardised format have to be displayed in all NFBs to indicate the service being operated. Figure 1 shows the specified format of signboard to be displayed when an NFB is operating an employees' service;

Figure 1

Service signboard of employees' service



Legend: * Indicates the minimum height of the characters

Source: TD records

- (c) ***Measures to address the inadequate provision of student service by NFBs.*** Due to the growing demand from the tourism industry and cross-boundary transport sector, the number of NFBs with student service endorsement decreased by 16% from 4,270 in 2004 to 3,577 in 2011. Meanwhile, the

number of SPLBs (not subject to the sourcing requirement — see (a) above) increased from 1,259 in 2011 to 1,899 in 2014. In 2012, the TD allowed an NFB operator in possession of student service endorsement to use all vehicles meeting the relevant requirements in its fleet for carriage of students upon application. While over 400 additional vehicles had since been granted student service endorsement through this measure, the number of NFBs with student service endorsement continued to decrease from 3,489 in 2012 to 3,286 in 2014. According to a survey conducted by the TD in 2014, about 70% of NFBs with student service endorsement were actually providing student service. On the other hand, the number of kindergarten and primary school students had increased by a total of around 25,000 during the four school years from 2011/12 to 2014/15 although the total student population had decreased by around 2,500 over the same period. The TD expected that there would remain considerable demand for school bus service in the coming years. In 2015, the TD exempted PSL applicants of private NFBs providing student services from the sourcing requirement (see (a) above) but the transport trade objected to a similar relaxation for public NFBs; and

- (d) *Measures to enhance the safety of student service vehicles.* The provision of escorts on student service vehicles can assist school children during boarding and alighting, and help monitor their behaviour when the vehicles are in motion. The mandatory escort requirement was introduced in 1997 for NFBs serving kindergarten and primary school students. The same requirement was extended to SPLBs serving kindergarten students in 2005 and primary school students in 2008. In 2007, legislative amendment was made to require all student service vehicles (NFBs with student service endorsement and SPLBs) registered on or after 1 May 2009 to install safer seats to reduce the risk of students being thrown out of their seats and the extent of their injuries in vehicle collisions.

Audit review

1.10 In 2008, the Audit Commission (Audit) completed a review of “Licensing of vehicles under the passenger service licence system” focusing on the provision of licensing services under the PSL system by the TD. The results were reported in Chapter 4 of the Director of Audit’s Report No. 50 of March 2008. The Government accepted the audit recommendations for implementation. In April 2017, Audit

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commenced a review to examine the TD's work in regulating NFB and SPLB services, focusing on:

- (a) administration of licensing requirements (PART 2);
- (b) regulatory controls over unauthorised operations (PART 3); and
- (c) safety measures of student service vehicles (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

Acknowledgement

1.11 Audit would like to acknowledge with gratitude the assistance and full cooperation of the staff of the TD during the course of the audit review.

PART 2: ADMINISTRATION OF LICENSING REQUIREMENTS

2.1 This PART examines the TD's work in administering the licensing requirements of NFBs and SPLBs, focusing on the:

- (a) measures to coordinate the change in non-franchised bus services with demand (paras. 2.7 to 2.14); and
- (b) processing of applications (paras. 2.18 to 2.28).

Passenger Service Licence system

2.2 ***Passenger Service Licence.*** The operation of NFB and SPLB service is regulated through PSLs issued by the Commissioner for Transport under section 27 of the RTO. In accordance with section 28 of the RTO, when considering any application for a PSL, the Commissioner for Transport shall take into account, in addition to any other matter which she considers relevant to the application:

- (a) any policy direction from the Chief Executive of the Hong Kong Special Administrative Region with respect to the provision of public transport services;
- (b) any limit in force under section 23 of the RTO on the number of vehicles that may be registered (Note 11);
- (c) the need for and the standard of the services to be provided by the applicant;
- (d) the level of service already provided or planned by other public transport operators; and

Note 11: *There is currently no limit in force under section 23 of the RTO on the number of NFBs that may be registered.*

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- (e) traffic conditions in the areas and on the roads where the services are to be provided.

2.3 ***Application requirements.*** Applicants for PSLs have to provide in their applications, amongst others, the following operation details:

- (a) the type of service proposed;
- (b) the route, area or educational institutions to be served;
- (c) the number and type of vehicles to be operated on the service;
- (d) the frequency and the period on each day during which the service shall be operated; and
- (e) proposed fares (if any).

They are also required to submit supporting documents such as service contracts or user group support letters (e.g. letters from educational institutions for PSL applications of SPLBs or student service endorsements of NFBs) to justify the need for the proposed services. The TD will examine the supporting documents to verify whether the service demand is substantiated when considering the applications.

2.4 ***PSL conditions.*** The issue of a PSL and the use of vehicles are subject to PSL conditions. Apart from specifying the approved operation details of each vehicle under the PSL (see para. 2.3(a) to (e)), PSL conditions also require a licensee to comply with certain operating requirements such as:

- (a) keeping operating and maintenance records for a specified period;
- (b) displaying a service signboard for the type of service permitted when the service is in operation; and
- (c) providing an escort when student service to kindergarten or primary school students is in operation.

In accordance with the Road Traffic (Public Service Vehicles) Regulations (Cap. 374D), a PSL may be issued for a period not exceeding five years and may be renewed for further periods of not more than five years each. In practice, the first issue of a new PSL is valid for one year and will be in general renewed for a period of two years for NFBs and one year for SPLBs upon expiry. A PSL is not transferable.

2.5 *Operation of regular services.* Among the eight types of services provided by public NFBs (see para. 1.5(a)), international passenger service and residents' service are issued with schedules of service stipulating all relevant operation details (such as fares, routings, operating hours, frequency, number and types of buses and stopping points) as approved by the Commissioner for Transport. With a view to facilitating better monitoring and enforcement against unauthorised operations, the schedule of service requirement has been extended to other four types of public NFB services including shuttle services provided under hotel service, student service for post-secondary educational institutions, employees' service and contract hire service which is regularly operated with the same origin and destination areas since 2005 (see para. 1.9(b)). As at June 2017, there were around 1,500 approved schedules of service (see Table 8 in para. 3.32).

2.6 *Passenger Service Licence Certificate.* The TD issues two types of PSLC, i.e. one for vehicles providing regular services according to a schedule of service approved by the TD such as residents' service and the other for vehicles providing non-regular services such as tour service. A PSLC is imprinted with the PSL number and the approved operation details of the vehicle, such as the types of service permitted. In accordance with the Road Traffic (Public Service Vehicles) Regulations:

- (a) every NFB or SPLB operating under a PSL shall display a PSLC on the left hand half of the vehicle's windscreen in a manner as to be visible from the front of the vehicle; and
- (b) a PSLC shall be valid for a period of 12 months or until the expiry of the PSL to which the PSLC relates, whichever is the sooner.

Measures to coordinate the change in non-franchised bus services with demand

2.7 In July 2004, to address the oversupply problem of NFBs, the TAC recommended that the Government should coordinate the change in NFB services with demand in a more effective manner (see para. 1.9(a)). In January 2005, the then Environment, Transport and Works Bureau (Note 12) informed the Legislative Council (LegCo) Panel on Transport that it would implement a package of measures based on the TAC's recommendations to ensure that new NFB services and vehicles would only be approved when there was justified demand. These measures included the following:

- (a) ***Stringent vetting of NFB applications and documentary requirements.*** To justify a PSL application related to new supply of NFBs (Note 13), an applicant had to provide relevant supporting documents, e.g. service contracts with validity period of six months or above, to prove the genuine long-term need for the proposed new services;
- (b) ***Single/restrictive service endorsements.*** New supply of vehicles applied for by new PSL applicants and existing operators should normally be granted with one type of service endorsement only. If the vehicle so applied for was sourced from the existing NFB fleet and would not entail a net increase in the total number of NFBs, such vehicle transferred among NFB operators (regardless of whether they were existing or new operators) should normally not be granted more than three service endorsements;
- (c) ***Sourcing vehicles from existing fleet.*** As a further step to contain the growth of total number of NFBs in the market, incentives would be provided to encourage PSL applicants to source vehicles from the existing fleet (which did not require replacement vehicles) in the market, in lieu of purchasing additional vehicles which would entail a net increase in

Note 12: *With the re-organisation of the policy bureaux effective from 1 July 2007, the transport-related policy responsibilities of the then Environment, Transport and Works Bureau were transferred to the Transport and Housing Bureau.*

Note 13: *New supply of NFB services and vehicles refers to applications for new PSLs from new applicants, applications for additional service endorsements and vehicles from existing operators, and applications for future renewal of the above PSLs and service endorsements.*

NFB fleet, to meet new service demand. Applicants who intended to purchase additional vehicles would be given a period of six months to try to source vehicles from the existing NFB fleet. Their applications would be processed as soon as they could source vehicles from the existing fleet or at the end of the period if they could not source such vehicles during the period. The length of the period would be kept under review to suit the changing circumstances; and

- (d) ***Imposing a cap on NFB fleet not appropriate.*** The then Environment, Transport and Works Bureau also informed the LegCo Panel on Transport that it was not appropriate to impose a cap on the NFB fleet because it would restrict the flexibility in meeting the genuine needs of some service sectors which might require additional vehicles to meet demand due to their special circumstances. It might also lead to undesirable speculative activities and thus generate premium for PSLs and NFB vehicles, increasing the cost of NFB services which would eventually be passed on to the passengers.

Implementation of the sourcing requirement

2.8 Through the PSL/PSLC application forms, the TD has advised applicants for additional NFBs that they would be given a period of six months to source vehicles from the existing NFB fleet in the market. For applicants who are able to acquire the required NFBs from the existing NFB fleet and the existing owners of the NFBs concerned agree not to purchase replacement vehicles, their applications will be processed immediately. For applicants who are unable to acquire the required NFBs from the existing fleet, their applications will be reviewed at the end of the six-month period instead of being processed as soon as possible as stated in the 2004 TAC review report and the 2005 LegCo Panel on Transport paper (see para. 2.7(c)).

2.9 ***Internal guideline requirements.*** The TD has laid down the following guidelines for staff in processing applications involving additional NFBs:

- (a) upon receipt of an application involving additional NFBs where the applicant has not purchased NFBs from the existing fleet, the TD will issue a notice requiring the applicant to hire or purchase NFBs from the existing fleet. According to the notice, an applicant may seek assistance from three of the five trade associations in the first month after receipt of the notice

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and place an advertisement in two Chinese newspapers every month to source or hire NFBs, or conduct open tenders in six months after receipt of the notice;

- (b) if the applicant fails to source a second-hand NFB at the end of the six-month period, he/she should explain with proof why he/she could not meet the requirement set out in the notice (see item (a) above). Nevertheless, the explanation provided by the applicant shall not necessarily render an approval for an additional NFB entailing a net increase in the NFB fleet. The following factors should be taken into account:
 - (i) the overall utilisation rate of the NFB fleet as observed through the TD's annual surveys (see Note 8 to para. 1.7);
 - (ii) the number of transfers of second-hand NFBs recorded in recent three months or longer period; and
 - (iii) the merits of individual case; and
- (c) if the utilisation survey reveals that there is no shortfall in supply of vehicles for NFB services and there are active transactions in the second-hand market, the applicant would be asked to make further efforts to source vehicles from the existing fleet.

2.10 Since the implementation of the sourcing requirement in April 2005, no application for additional public NFBs which involved a net increase in the total number of NFBs in the market had been approved (Note 14). According to the TD, applicants for additional public NFBs had either successfully sourced public NFBs from the existing fleet or stopped pursuing their applications for reasons unknown to the TD while some eligible organisations opted for private NFBs to serve their own needs. The number of public NFBs decreased by 169 (2%) from 7,212 in 2004 to 7,043 in 2016. For private NFBs, the sourcing requirement has been relaxed since

Note 14: *The only exception was in 2011 when the TD approved an application for reclassifying 14 private NFBs into public NFBs serving a post-secondary educational institution based on the individual merits of the case, resulting in a net increase of 14 public NFBs.*

2007 with exemption granted to charitable organisations which obtain government funding, lottery fund or donations to finance the capital costs of their vehicles and educational institutions (i.e. kindergartens, primary schools and secondary schools). Besides, such exemption has also been granted to other applications based on individual merits. As a result, the number of private NFBs had increased by 158 (32%) from 493 in 2004 to 651 in 2016.

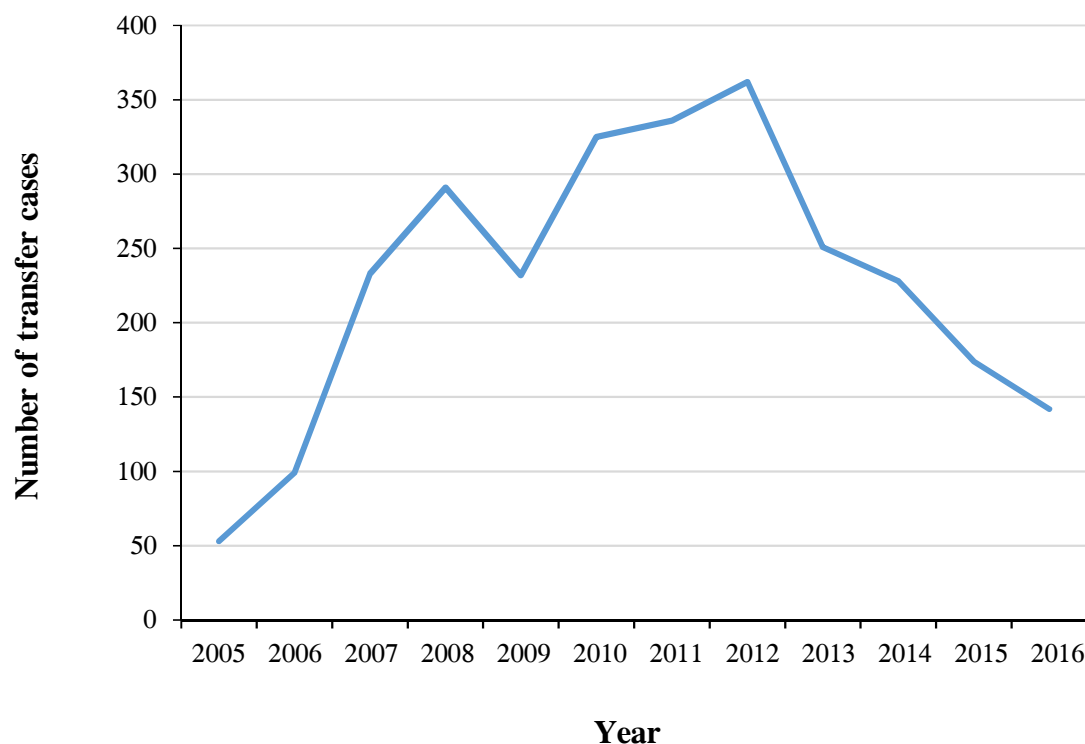
Changes in the public NFB market

2.11 Audit noted that since the implementation of the sourcing requirement in April 2005, there had been changes in the public NFB market, as follows:

- (a) ***Utilisation of public NFBs.*** According to the TD's annual surveys, the utilisation rate of public NFBs had increased from 81% in 2004 reaching its peak at 89% in 2014 before slightly dropping to 86% in 2016. By comparison, the utilisation rates of franchised buses operated by different companies (which did not have sourcing requirement) ranged from 88% to 93% in 2016. The increase in the utilisation rate was also reflected by the number of trips of NFB observed during the annual surveys which had increased by 40% from 40,104 per day in 2004 to 55,970 per day in 2016. Over the same period, the estimated number of passengers using public NFB services had also increased by 19% from 468,684 per day in 2004 to 559,113 per day in 2016;
- (b) ***Transactions of second-hand public NFBs.*** As shown in Figure 2, while the number of second-hand public NFB transfer cases increased from 53 in 2005 to a peak of 362 in 2012, it was generally on a decreasing trend thereafter, falling to 142 in 2016; and

Figure 2

**Number of second-hand public NFB transfer cases
(2005 to 2016)**



Source: TD records

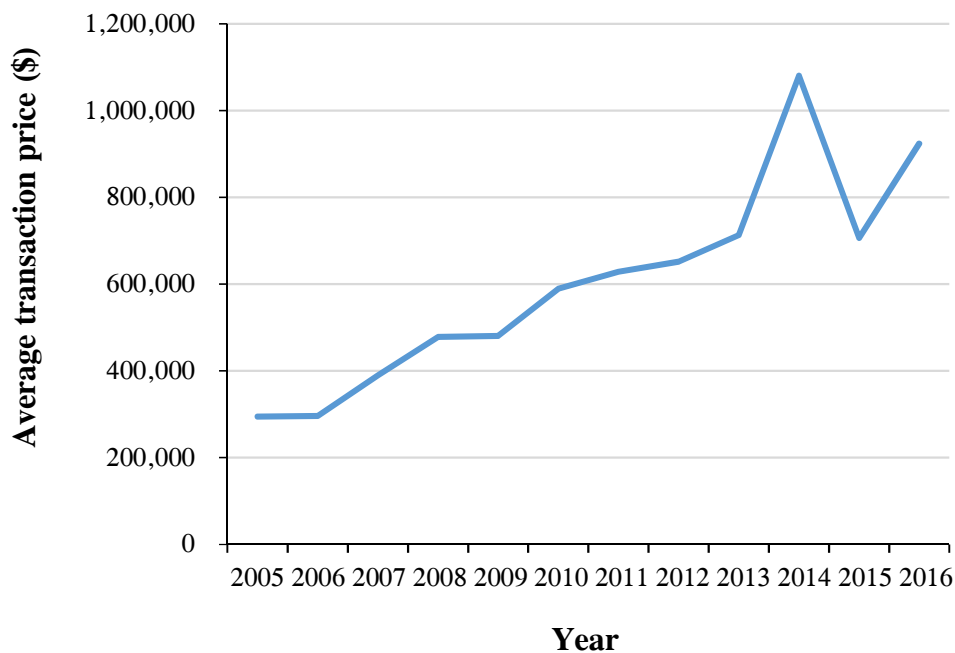
Remarks: The numbers of NFB transfer cases shown are those with transaction prices above \$100,000. Based on the records of the TD, the market value of a second-hand public NFB was usually not less than \$100,000 and those transactions with prices below \$100,000 might be between related parties. The numbers of transactions with prices equal to or below \$100,000 ranged from 39 to 304 a year.

- (c) **Transaction prices of second-hand public NFBs.** As shown in Figure 3, the average transaction price of a second-hand public NFB had increased from \$0.3 million in 2005 by 200% to \$0.9 million in 2016. Based on the TD's records, the average price for a new bus normally ranged from \$0.6 million (for a bus with about 30 seats) to \$0.9 million (for a bus with about 60 seats). Analysis of the 142 transactions in 2016 (see (b) above) showed that the transaction prices of 51 transactions (36%) were below \$0.5 million and 59 transactions (42%) ranged from \$0.5 million to

\$1 million. The remaining 32 (22%) transactions were above \$1 million (up to \$4.9 million each for two second-hand double deck NFBs). According to the TD, factors such as the prevailing economic condition and business prospect of the trade would affect the transaction volume and price.

Figure 3

**Average transaction prices of second-hand public NFBs
(2005 to 2016)**



Source: TD records

Remarks: Based on the records of the TD, the market value of a second-hand public NFB was usually not less than \$100,000. In calculating the average transaction price, to avoid skewed effect of those exceptionally low transaction prices, which might be transactions between related parties, only transactions at price above \$100,000 were counted.

Need to review the implementation of the sourcing requirement

2.12 According to the 2004 TAC review report and the 2005 LegCo Panel on Transport paper, the main measures to coordinate the change in NFB services with

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demand were stringent vetting of NFB applications and documentary requirements, and granting of single/restrictive service endorsements (see para. 2.7(a) and (b)). The sourcing requirement was a further administrative measure to encourage PSL applicants to source vehicles from the existing fleet and thus contain the growth of total number of NFBs in the market. There was no intention to impose a cap on the NFB fleet which would: (a) restrict the flexibility in meeting the genuine needs of some service sectors; and (b) lead to undesirable speculative activities and generate premium for PSLs and NFB vehicles which would eventually be passed on to the passengers (see para. 2.7(c) and (d)).

2.13 Audit understands that the sourcing requirement is important for the proper control over NFB operations whilst ensuring the service demand is met. Such requirement helps prevent excessive supply of NFB services in the market and minimise unhealthy competition in the NFB market and with other public transport modes. With the lapse of some 12 years after the implementation of the sourcing requirement in 2005 and in light of the changes in the NFB market over the years (see para. 2.11), it is timely for the TD to conduct a review to see if there is room for improvement. In this connection, there is a need to re-examine the TD's internal guideline requirement whereby applicants for additional NFBs would be asked to make further efforts to source vehicles from the existing fleet even after having done so for six months (see para. 2.9(c)). Such a requirement was not stated in the 2004 TAC review report and the 2005 LegCo Panel on Transport paper, and may not be flexible enough for some NFB operators in meeting genuine service needs.

Need to tighten vetting of supporting documents for PSL renewal applications

2.14 A PSL holder shall provide a service contract of any duration to justify the continued need for the service to support a PSL renewal application. For renewal of service endorsements, at least one service contract of any duration should be submitted for each type of service permitted under the PSL. The PSL renewal application may not be approved if a PSL holder is unable to provide the relevant supporting documents. From 2014 to 2016, the TD processed 2,080 PSL renewal applications for public NFBs. Audit examined 10 of these renewals (involving 41 service endorsements) granted to existing PSL holders during this period and noted that:

- (a) in 3 approved applications involving 9 service endorsements, the PSL holders concerned submitted service contracts to justify the continued need

for 3 contract hire service endorsements. For the remaining 6 (15%) of 41 endorsements relating to tour and hotel services, the PSL holders had not submitted relevant service contracts but only submitted letters declaring that the NFBs under the concerned PSLs would be deployed for such services. In September 2017, the TD informed Audit that the PSL holders in these 3 approved applications were also registered travel agents and that tour and hotel services were referred to as complementary services (i.e. serving similar clientele) in the 2004 TAC review report. However, according to the TAC report, endorsements for complementary services could be granted provided that the need for such endorsements could be justified. There is a need to uphold such supporting document requirement in processing PSL renewal applications; and

- (b) in 9 approved applications involving 39 service endorsements, the service contracts submitted by the PSL holders could not fully support the number of vehicles required under 26 (63%) of 41 service endorsements. For example, in one renewal of service endorsement granted to 76 NFBs, the service contract submitted by the PSL holder showed that only 3 NFBs were required. Audit noted that it had been the practice of the TD to require a PSL holder to submit at least one contract for each type of service. According to the TD, such arrangement provided flexibility for the PSL holders in vehicle deployment and meeting their operational needs. To strike a balance between providing reasonable flexibility for the NFB trade and maintaining effective regulation of the NFB services, the TD needs to consider tightening the requirements on service contracts provided for each service endorsement to justify the number of vehicles required.

Audit recommendations

2.15 Audit has *recommended* that the Commissioner for Transport should:

- (a) **in consultation with the Secretary for Transport and Housing, conduct a review of the implementation of the sourcing requirement, in particular in relation to the TD's internal guideline requirement on further sourcing when an applicant is unable to source an NFB from the existing fleet for six months;**

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- (b) **uphold the requirement on a PSL holder to submit a service contract or other relevant documents for supporting each service endorsement when applying for PSL renewal; and**
- (c) **consider tightening the requirements on service contracts provided for each service endorsement to justify the number of vehicles required.**

Response from the Government

2.16 The Commissioner for Transport agrees with the audit recommendations. She has said that the TD will:

- (a) conduct a review on the internal guidelines for the implementation of the sourcing requirement;
- (b) uphold the requirement on a PSL holder to submit a service contract or other relevant documents for supporting each service endorsement when applying for PSL renewal; and
- (c) consider drawing up a consistent approach in requiring a PSL holder to provide service contracts to justify the number of vehicles required under each service endorsement, taking into account the deployment flexibility of the NFB operation.

2.17 The Secretary for Transport and Housing agrees with the audit recommendation in paragraph 2.15(a). He has said that:

- (a) as set out in the report of the Public Transport Strategy Study released in June 2017, NFBs would continue to perform its role and positioning as a supplementary public transport facility, achieving the functions of:
 - (i) relieving demand on the franchised bus and green minibus services primarily during the peak hours; and
 - (ii) providing services to specific passenger groups (e.g. tour groups, hotel guests and students) when the regular public transport services cannot provide appropriate services;

- (b) the sourcing requirement has been put in place based on policy considerations for the purpose of exercising proper control over operation of NFBs while ensuring service demand is met. This helps prevent excessive supply of NFB services in the market and minimise unhealthy competition in the NFB market and with other public transport modes; and
- (c) the Transport and Housing Bureau (THB) agrees that the TD should review the implementation of the sourcing requirement, in particular the TD's internal guidelines on the "further sourcing" requirement when an applicant is unable to source an NFB from the existing fleet after the six-month period, whilst ensuring that the policy objective in (b) can continue to be met. In this regard, the TD will report the implementation of the sourcing requirement to the TAC in due course.

Processing of applications

2.18 The Public Vehicles Unit (PVU) under the Public Vehicles and Prosecution Section (see Appendix A and Note 15) is responsible for processing applications in relation to NFBs and SPLBs except those for cross-boundary international passenger service (Note 16), which are processed by the New Territories ROs direct. The PVU's work includes vetting applications and relevant supporting documents, clarifying with applicants on application details, seeking inputs from ROs on operation details (e.g. routeings, timetable and stopping points), issuing replies to applicants and handling the associated licensing matters. The PVU uses a number of registers to monitor the progress of applications (Note 17).

Note 15: *The PVU is headed by a Senior Executive Officer who is supported by a team of 30 staff. The PVU is responsible for processing licensing applications in relation to NFBs, light buses, hire cars and taxis.*

Note 16: *The cross-boundary international passenger service is a form of international passenger service which is regulated by a quota system jointly administered by the Hong Kong and Mainland authorities. The quota system aims at ensuring smooth traffic flow and safe operation at the control points.*

Note 17: *A number of registers are maintained for different types of service (e.g. one register is maintained for all applications relating to public NFBs operating residents' services). The registers may be electronic or paper-based (e.g. in the form of computer spreadsheets and physical log books).*

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2.19 The number of applications processed in 2016 totalled 24,897, of which 20,894 (84%) were related to PSLs or PSLCs (see Table 2). The remaining 4,003 (16%) applications were mainly for the replacement of vehicles, transfer of ownership of vehicles and display of advertisement on vehicles.

Table 2

**Number of PSL and PSLC related applications processed
(2016)**

Type of applications		Type of vehicles			Total
		Public NFB	Private NFB	SPLB	
PSL	First issue	74	16	47	137
	Renewal	701	80	626	1,407
	Others (Note)	619	32	800	1,451
PSLC	First issue	1,957	88	373	2,418
	Renewal	8,168	676	1,771	10,615
	Others (Note)	4,257	60	549	4,866
Total		15,776	952	4,166	20,894

17,899

Source: TD records

Note: These mainly include applications for the amendment, suspension and cancellation of PSLs and PSLCs.

Need to consider publicising the processing time for all types of new applications of NFBs and SPLBs through more channels

2.20 The TD has not advised applicants of the time it may take to process new applications (Note 18) in the relevant application forms except for the operation of new scheduled contract hire service (see para. 2.21). The TD has only publicised on the government portal (www.gov.hk) that an application for a PSL for operation of public NFB services can be processed in about six to eight weeks (Note 19). However, there is no mentioning whether the processing time of six to eight weeks is also applicable to new applications for private NFBs and SPLBs, and all four types of new applications for public NFBs (Note 20). According to the TD, the trade has been fully aware of the normal processing time of six to eight weeks for new applications through its regular meetings with trade representatives and the half-yearly bulletins issued to the trade. Based on an examination of 30 new applications (except those for operation of new scheduled contract hire service — see para. 2.21) in 2015 and 2016, Audit found that 6 (20%) applications were submitted less than six weeks before the intended commencement dates of the service as stated in the service contracts. In the event, 5 (83%) of the 6 applications were approved after the intended service commencement dates which might cause inconvenience to the service users. To facilitate better time planning by prospective applicants to meet their operation needs, the TD should consider publicising the estimated processing time for all types of new applications of public NFBs, private NFBs and SPLBs through more channels (e.g. the application forms).

Note 18: *The TD has stated in the relevant application forms and approval letters that a renewal application shall be submitted: (a) within four months and at least 14 days before the expiry date for the renewal of PSL and/or PSLC; (b) not less than three weeks before the expiry date for the renewal of scheduled contract hire service; and (c) at least two months before the expiry date for the renewal of other regular services.*

Note 19: *The actual processing time would depend on the complexity of each application. The general processing time for PSL applications for NFBs has been publicised on the government portal since 2011.*

Note 20: *The four types of new applications for public NFBs are: (a) application for a new PSL; (b) application for additional vehicles by a PSL holder; (c) application for additional endorsements of an existing NFB by a PSL holder; and (d) application for operation of a new regular service.*

Need to process applications involving operation of scheduled contract hire service in a timely manner

2.21 It is stated in the application forms that an application for operating a new scheduled contract hire service should be submitted at least 14 days prior to the service commencement. Audit analysed 90 such applications approved in 2016 and found that:

- (a) 76 (84%) applications had been submitted at least 14 days prior to the service commencement;
- (b) the TD took more than 14 days to process 64 (84% of the 76) applications (with an average processing time of 30 days and the longest one being 67 days); and
- (c) in 4 of the 64 applications, the TD granted approvals 7 to 31 days (averaging 19 days) after the intended service commencement dates.

2.22 Audit noted that the long processing time taken in some cases was because the PVU had to consult ROs and/or district traffic engineers on the operation details (e.g. the routeings and stopping points) proposed in the applications. However, as a majority of the applicants had submitted their applications within the time as advised by the TD, they would have a reasonable expectation that their applications could be processed in a timely manner. To better meet the applicants' expectation, the TD needs to explore possible measures to expedite the processing of applications for scheduled contract hire service once the applicants have submitted all necessary supporting documents.

Need to enforce the more stringent vetting requirement on renewal applications of expired PSLs

2.23 According to the 2004 TAC review report and the 2005 LegCo Panel on Transport paper, all NFB applications should be subject to stringent vetting to ensure that only services that are genuinely in demand are approved. However, to address the concerns of existing operators about the difficulties to secure future service contracts of sufficiently long period, the TD allows an existing operator to submit a contract of any duration for renewal of a PSL before its expiry. In case a service contract cannot be obtained before the PSL expires, the operator will be required to

submit a new application and provide a service contract with validity period of at least six months to prove the genuine long-term need for the service. Against the above background, the TD will issue a reminder letter to a PSL holder six weeks prior to the expiry of the PSL. If the PSL holder does not renew the concerned PSL upon the expiry date, a warning letter will be sent to inform the PSL holder that:

- (a) vehicles under the concerned PSL could no longer be deployed for provision of service; and
- (b) the concerned PSL has been cancelled upon the expiry date and any application for PSL thereafter will be treated as a new application and subject to a more stringent vetting (i.e. requiring the submission of service contracts with at least six-month validity to justify the genuine long-term service need).

2.24 In 2015 and 2016, a total of 83 warning letters were issued in respect of expired PSLs. Audit examined 20 (24%) of the 83 cases and noted that in 11 (55%) cases, the PSL holders subsequently submitted applications for renewal in 5 to 23 days after the expiry of PSLs. However, all 11 cases were not processed as new applications, contrary to the requirements set out in the warning letters (see para. 2.23(b)). The TD needs to uphold the more stringent vetting requirement on renewal applications of expired PSLs so as to encourage timely submission.

Need to consider streamlining the licensing requirements of PSLCs

2.25 In 2016, there were 17,899 PSLC-related applications (see Table 2 in para. 2.19), which accounted for 72% of all 24,897 applications processed by the PVU. Audit has noted that there is scope for streamlining the licensing requirements of PSLCs as follows:

- (a) ***Need to consider merging the two types of PSLC.*** The Road Traffic (Public Service Vehicles) Regulations require every vehicle operated under a PSL to display a PSLC. There is no stipulation on the format of the PSLC but it has been the practice since its inception that two types of PSLC i.e. green PSLC and red PSLC are issued for vehicles providing regular services and non-regular services respectively (see para. 2.6) for the sake of easy identification at the front of vehicles (see Figure 4) in line with the display of two types of PSL plate (see Figure 5) at the rear of vehicles in

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accordance with the Road Traffic (Public Service Vehicles) Regulations (Note 21). For public NFBs, green PSLCs are issued for residents' service, international passenger service and multiple transport service, and red PSLCs are issued for the other types of public NFB services (see Appendix B). However, the schedule of service requirement has been extended to all regular NFB services since 2005 (see para. 2.5) and hence four types of public NFB service previously classified as non-regular have been required to operate in accordance with schedules of service for those parts of their services which are of a regular nature, i.e. hotel shuttle service, student service for post-secondary educational institutions, employees' service and certain free shuttle service provided under contract hire service. In other words, public NFBs issued with the red PSLC for these four types of service endorsement may be providing a mix of regular and non-regular services. Under the circumstances, there is merit to examine the feasibility of merging the two types of PSLC which would simplify the TD's administrative work for the issue, renewal and amendment of PSLCs, and facilitate the NFB trade, especially those PSL holders who are issued with two types of PSLC for the same NFB (see Note 21); and

Note 21: *As at 31 December 2016, there were 1,726 public NFBs issued with two types of PSLC. As for private NFBs and SPLBs which only operate non-regular services, they are issued with the red PSLC.*

Figure 4

Two types of PSLC for display at the front of vehicles

Green PSLC for regular services

Red PSLC for non-regular services

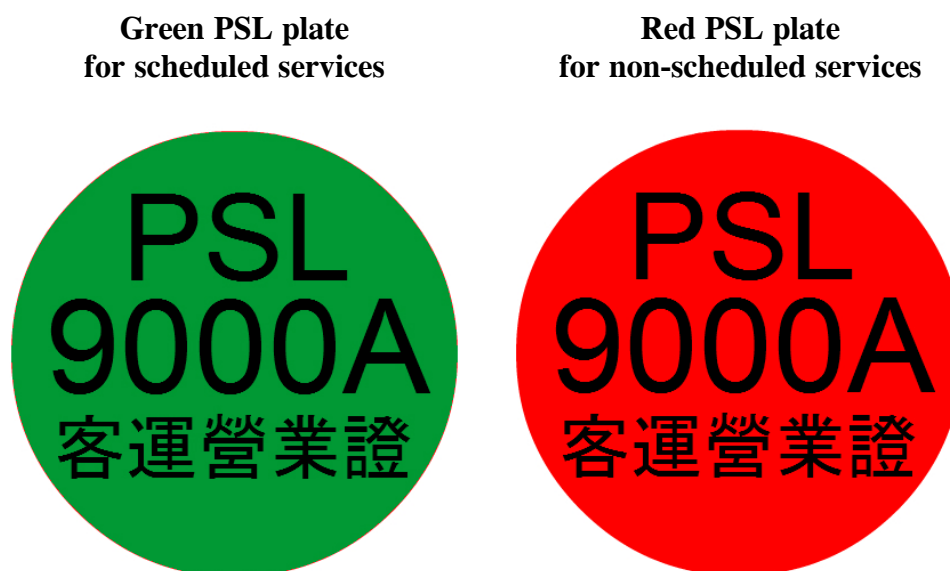
[illegible]

<div style="display: flex; justify-content: center; align-items: center;"> <div style="text-align: center; margin-right: 10px;"> <p>運輸署</p> </div> <div style="text-align: center;"> <p>TRANSPORT DEPARTMENT</p> </div> </div>	
<p>客運營業證證明書</p> <p>Passenger Service Licence Certificate</p>	
<p>2550133</p>	<div style="border: 1px solid black; height: 60px; width: 100%;"></div>
<p>車輛登記號碼</p> <p>Vehicle Registration Mark</p>	<div style="border: 1px solid black; height: 30px; width: 100%;"></div>
<p>屆滿日期</p> <p>Expiry Date</p>	<p>27/10/2017</p>
<p>營業性質</p> <p>Type of Service</p>	<p>A01,A08*****</p> <p>*****</p>
<p>限制事項代碼</p> <p>Restriction Codes:</p>	<p>*****</p> <p>*****</p> <p>*****</p> <p>*****</p> <p>*****</p> <p>*****</p> <p>*****</p> <p>*****</p>
<p>編號記錄</p> <p>Transaction</p>	<div style="display: flex; justify-content: space-between;"> <div> <p>核發日期</p> <p>Issued</p> </div> <div> <p>18/10/2016</p> </div> </div>

Source: TD records

Figure 5

PSL plates required to be displayed at the rear of vehicles



Source: TD records

- (b) ***Need to consider aligning the validity periods of PSLCs and related PSLs for NFB operators.*** At present, an NFB operator normally has to renew his PSL once every two years and the related PSLCs for his NFBs every year (Note 22). The shorter validity period of PSLCs has caused inconvenience to those operators who have a large fleet of NFBs as they may have to make multiple PSLC renewal applications every year. As shown in paragraphs 2.3 and 2.4, the main licensing controls over the NFB operation are laid down in the PSL, the application for which is subject to stringent vetting. The issue of a PSLC is based on the approved operation details in the related PSL and hence a more frequent renewal cycle of a PSLC than that of a PSL is not warranted. On the other hand, aligning the validity periods of a PSLC and its related PSL could simplify the TD's administrative work and facilitate the NFB trade. In this connection, Audit noted that in 2016, the NFB trade commissioned a consultancy study of the NFB services which also called for, among other things, aligning the validity periods of PSLCs and related PSLs. While Audit understands that

Note 22: *According to the current practice, the first issue of a new PSL is valid for one year and will be in general renewed for a period of two years for NFBs and one year for SPLBs upon expiry (see para. 2.4).*

such alignment may involve legislative amendment (see para. 2.6(b)), it is worthwhile to explore its feasibility having due regard to the fact that there are over 9,000 PSLCs for NFBs and the potential long-term benefits in terms of facilitating the NFB trade.

Need to improve the implementation of performance pledges for licensing services of NFBs and SPLBs

2.26 ***Performance pledges.*** The TD has promulgated three performance pledges to inform the public of the service standards and the performance targets for three types of licensing services involving NFBs and SPLBs. The achievement of the performance targets in 2015 and 2016 as reported by the TD on its website is shown in Table 3.

Table 3

**Achievement of performance targets
for licensing services involving NFBs and SPLBs
(2015 and 2016)**

Type of licensing services	Pledged processing time (working day)	Target	Actual achievement	
			2015	2016
Application for replacement of vehicle of private light buses, taxis, public light buses and hire cars	5	100 %	100 % (see para. 2.28(b))	100 %
Renewal of PSL/PSLC for private NFBs	7	100 %	100 %	100 %
Application for display of advertisements/marketing on NFBs, taxis and public light buses	7	100 %	100 %	100 % (see para. 2.28(b))

Source: TD records

Remarks: The performance targets for renewal of PSL/PSLC for private NFBs and application for display of advertisements/marketing on NFBs were set in response to a recommendation of the 2008 audit review (see para. 1.10).

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2.27 *Need to consider extending the coverage of the performance pledges.* According to the good practices promulgated in Civil Service Bureau (CSB) Circular No. 7/2009, performance pledges should cover all departmental services that have a public interface. However, the licensing services of NFBs and SPLBs covered in the three performance pledges only accounted for 2,069 (8%) of 24,897 licence applications for NFBs and SPLBs processed in 2016. According to the TD, there are difficulties in setting pledged processing times for PSL applications of public NFBs given that multiple service endorsements may be involved. However, the TD may consider extending the scope of the performance pledges to cover the less complex renewal cases (see para. 2.25(b)) of PSL/PSLC of SPLBs and PSLC of public NFBs, which accounted for 10,565 (42%) of 24,897 applications processed in 2016.

2.28 *Need to improve performance measurement.* Audit examination of the existing arrangements for measuring the achievement of the target processing time has revealed the following areas for improvement:

- (a) *Method of measuring the actual processing time.* According to the good practices promulgated in CSB Circular No. 7/2009, bureaux and departments have been advised to use end-to-end measurement for the whole process rather than covering part of it. However, it has been the practice of the TD to count the processing time of an application from the date of the receipt to the date of approval or, in the absence of such date, the issue date of approval letter. Audit sample checked 30 applications processed from 2015 to 2017 and found that the dates of approval were recorded for measuring the actual processing time in 15 cases. On average, it took 9 working days to issue the approval letters after the approval dates but such time would not be taken into account in determining whether the target processing times of 5 and 7 working days were achieved. In Audit's view, the TD needs to take measures to shorten the lead time for issuing approval letters and consider standardising the use of issue date of approval letters for measuring the achievement of the target processing time in line with the good practices promulgated by the CSB; and

- (b) ***Implementation of the prescribed measuring procedures.*** According to the TD's internal guidelines, a survey should be conducted (Note 23) to assess the achievement of the performance targets in meeting the pledged processing times. However, Audit noted that no survey had been conducted since 2014. Audit sample checked 26 applications processed in 2015 and 2016 and found that in two cases, the pledged processing times were not met and hence the reported 100% achievement of the pledged processing times (see Table 3 in para. 2.26) was not supported. The TD needs to take measures to improve the situation.

Audit recommendations

2.29 **Audit has recommended that the Commissioner for Transport should:**

- (a) **consider publicising the estimated processing time for all types of new applications of NFBs and SPLBs through more channels;**
- (b) **explore possible measures to expedite the processing of applications for scheduled contract hire service to meet the applicants' expectation;**
- (c) **uphold the more stringent vetting requirement on renewal applications of expired PSLs;**
- (d) **consider streamlining the licensing requirements of PSLCs, such as examining the feasibility of:**
 - (i) **merging the two types of PSLC for public NFBs; and**
 - (ii) **aligning the validity periods of PSLCs and related PSLs; and**
- (e) **improve the implementation of performance pledges for licensing services of NFBs and SPLBs, including:**

Note 23: *According to the TD's internal guidelines, the responsible officer should select one week in May and November with five full working days at the beginning of the year for conducting the survey. The processing times of various applications received within this week would be measured against the pledged processing times.*

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- (i) **considering the extension of the scope of the performance pledges to cover renewal cases of PSL/PSLC of SPLBs and PSLC of public NFBs;**
- (ii) **shortening the lead time for issuing approval letters and considering standardising the use of issue date of approval letters for measuring the achievement of the target processing time of licence applications of NFBs and SPLBs; and**
- (iii) **taking measures to ensure that the reported results of performance measurement are fully substantiated.**

Response from the Government

2.30 The Commissioner for Transport agrees with the audit recommendations. She has said that the TD will:

- (a) consider publicising the estimated processing time for all types of new applications of NFBs and SPLBs, if possible, through more channels;
- (b) expedite the processing of applications for scheduled contract hire service and better manage the applicants' expectation within available resources;
- (c) examine viable measures to uphold the more stringent vetting requirement on renewal applications of expired PSLs;
- (d) review the feasibility of merging the two types of PSLC for public NFBs;
- (e) examine the feasibility of extending the validity period of the PSLCs, and if it is considered appropriate to effect such a change, appropriate actions (such as by way of legislative amendments) would be taken to extend the validity of the PSLCs to tally with that of the PSLs; and
- (f) consider extending the scope of the performance pledges to cover renewal cases of PSL/PSLC of SPLBs and PSLC of public NFBs.

2.31 The Commissioner for Transport has also said that, in respect of the audit recommendations in paragraph 2.29(e)(ii) and (iii), the TD has already:

- (a) adopted the use of the date of approval letters for measuring the achievement of the target processing time. The time taken to prepare approval letters has also been compressed with a view to meeting the pledged processing time; and
- (b) taken measures in recording the processing time of all relevant applications electronically with a view to ensuring accurate reporting of the achievement of the pledged processing time. Therefore, the conduct of surveys to assess the achievement of performance targets will no longer be needed.

PART 3: REGULATORY CONTROLS OVER UNAUTHORISED OPERATIONS

3.1 This PART examines the TD's enforcement procedures and measures to address the problem of unauthorised operations, focusing on:

- (a) unauthorised non-franchised bus operations (paras. 3.4 to 3.11);
- (b) investigative work of the Regional Offices (paras. 3.12 to 3.19);
- (c) enforcement actions against unauthorised operations (paras. 3.20 to 3.28);
and
- (d) publicity on authorised non-franchised bus services (paras. 3.29 to 3.34).

Existing regulatory controls

3.2 ***Legislative measures.*** The NFB and SPLB operations are governed by the PBSO and RTO, as follows:

- (a) ***Prosecution.*** Section 52 of the RTO provides for the prosecution for carriage of passengers by an NFB or an SPLB without a PSL or in contravention of any conditions subject to which the vehicle licence was issued. The maximum penalties are a fine of \$5,000 and imprisonment for 3 months for a first conviction, and a fine of \$10,000 and imprisonment for 6 months for a second or subsequent conviction for the same offence. Separately, section 4(2) of the PBSO prohibits the operation of a public bus service without a franchise or unless the service is a type of authorised NFB services or approved by the Commissioner for Transport under section 27(4)(b) of the RTO. The maximum penalty for conviction of the offence is a fine of \$100,000. Since 2004, the TD has focused resources on taking enforcement actions against unauthorised operations by means of inquiry (see (b) below). Accordingly, there was no prosecution made in recent years;

- (b) ***Inquiry.*** Section 30 of the RTO stipulates that if the Commissioner for Transport has reasons to believe that an NFB or an SPLB has been used other than for the purpose authorised by the PSL, or any PSL condition or provision of the RTO has not been complied with, she may appoint a public officer to hold an inquiry. The Commissioner for Transport may cancel, suspend or vary a PSL for substantiated inquiry cases. From January 2012 to mid-May 2017, there were 175 inquiries (see para. 3.20); and
- (c) ***Fixed penalty.*** If an NFB or an SPLB is found picking up/setting down passengers within restriction zones or within designated bus stop areas, the Hong Kong Police Force (HKPF) may issue fixed penalty tickets to the concerned vehicle under sections 59 and 61 of the Road Traffic (Traffic Control) Regulations (Cap. 374G). According to the statistics provided by the HKPF, the numbers of fixed penalty tickets issued to NFBs and SPLBs were 1,111 and 822 in 2015 and 2016 respectively.

3.3 ***Administrative measures.*** In addition to the above legislative measures, the TD has put in place the following administrative measures to regulate NFB/SPLB operations:

- (a) issuing clarification/warning letters to instruct concerned PSL holders to cease unauthorised operations;
- (b) implementing traffic and transport management schemes including bus clearways, and prohibited and restricted zones to help eradicate unauthorised NFB/SPLB services. Since 2004, the TD has implemented 24 traffic and transport management schemes in various regions; and
- (c) improving parallel public transport services.

Unauthorised non-franchised bus operations

3.4 ***TAC's review.*** In 2004, the TAC (see para. 1.9(b)) noted the following problems of unauthorised NFB operations:

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- (a) ***Unauthorised services.*** Some NFBs had provided services without valid service endorsements, which would undermine the financial viability of other regular and legitimate transport services; and
- (b) ***Breaches of PSL conditions.*** Some NFB operators had provided services not in accordance with PSL conditions (e.g. operating more trips than permitted, deviating from the approved routings and picking up or setting down passengers at unapproved locations).

Such activities could lead to traffic and environmental problems. The third party insurance of the NFBs concerned might also be invalidated if the vehicle concerned was used for operating unauthorised services. In its 2004 review report, the TAC recommended that the Government should: (i) strengthen regulatory controls over NFB operations (such as extending the schedule of service requirement to all regular NFB services — see para. 2.5); and (ii) enhance the efficiency and effectiveness of enforcement actions (such as enhancing the identification system of NFB services to facilitate enforcement officers' monitoring and specifying some common breaches of PSL conditions as scheduled offences that would be subject to the fixed penalty ticketing system — see paras. 3.7 and 3.26 respectively).

3.5 *Enforcement actions of TD.* The TD will take enforcement actions against violations of PSL conditions. Examples of violations include unauthorised service trailing along franchised buses to pick up passengers, provision of services without appropriate service endorsement and deviation from approved schedule of service.

Need to strengthen enforcement actions against unauthorised NFB operations

3.6 *Annual surveys.* The TD conducts annual surveys of public NFBs (see Note 8 to para. 1.7) to collect operational information for the purpose of keeping track of the utilisation pattern of existing NFB fleet and services under various service endorsements. The results are also used to facilitate monitoring as well as understanding the implication of the regulatory and licensing measures on their operations. In general, the following information relating to the NFBs observed at various checkpoints is collected during an annual survey:

- (a) vehicle registration mark;

- (b) carrying capacity/seating capacity;
- (c) display of service signboard at the front of NFB when providing service;
- (d) display of PSL plate at the rear end of NFB;
- (e) time passing the checkpoint;
- (f) type of service provided; and
- (g) number of passengers on-board.

With a view to ensuring that accurate results can be obtained from the fieldwork, instructions are given to field workers to facilitate them to distinguish the types of service provided by the NFBs observed with reference to the characteristics of the NFBs and passengers on board. For example, an NFB observed to be displaying the name of a school and carrying mostly young children in school uniforms would be identified as providing student service, while one displaying the name of a company and carrying adults only would be classified as providing employees' service.

3.7 *Failure to display service signboards and PSL plates.* In line with the TAC's recommendation to enhance the identification system of NFB services to facilitate enforcement officers' monitoring, appropriate signboards in a standardised format should be displayed in all NFBs to indicate the types of service being operated (see para. 1.9(b)). The TD's annual surveys found cases of not displaying the stipulated service signboards and/or the PSL plates at the rear of NFBs. For example, of 5,870 NFBs surveyed in 2016:

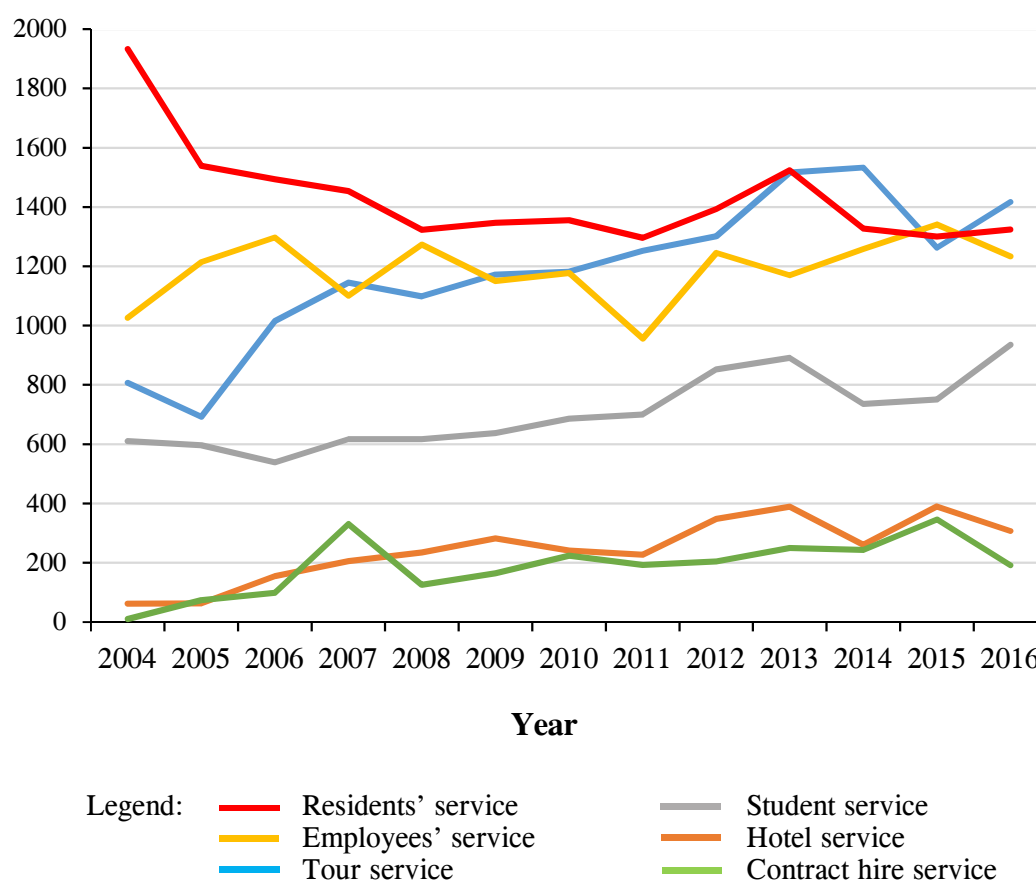
- (a) 3,048 (52%) NFBs were found not displaying the stipulated service signboards for half or more of their trips, contrary to the PSL conditions; and
- (b) 173 (3%) NFBs had not displayed the PSL plates at their rear, contrary to the requirement of the Road Traffic (Public Services Vehicles) Regulations (see para. 2.25(a)).

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3.8 *NFBs suspected to be operating without suitable endorsements.* Based on the characteristics of the NFBs and passengers on board (see para. 3.6), some NFBs were observed during the annual surveys to have operated various types of service without the corresponding service endorsements issued by the TD. As shown in Figure 6, with the exception of residents' service, the number of NFBs suspected to be operating without suitable endorsements for five other services was generally on an increasing trend. Audit's further analysis of the 2016 survey results showed that for residents' service, the number of NFBs suspected to be operating without the relevant endorsement was higher than the number of licensed ones (see Table 4).

Figure 6

Numbers of NFBs suspected to be operating without suitable endorsements found in surveys from 2004 to 2016



Source: TD records

Remarks: There was no observed unauthorised NFB operation for international passenger service. Most of the international passenger service was related to the cross-boundary international passenger service regulated under the quota system (see Note 16 to para. 2.18). The remaining international passenger service was related to free shuttle service to the Airport Express stations.

Table 4

**Comparison of the number of NFBs with and without
corresponding service endorsements in the 2016 survey**

Number of NFBs	Service type					
	Tour	Hotel	Student	Employees'	Residents'	Contract hire
(a) licensed with service endorsement	3,193	1,742	3,181	1,750	1,089	5,495
(b) licensed with service endorsement and observed in survey	2,008	213	2,591	909	621	1,640
(c) suspected to be operating without corresponding service endorsement	1,417	307	935	1,233	1,324	191

Source: TD records

Remarks: The same NFB could be operating different services and be recorded at different checkpoints during the survey period.

3.9 In September 2017 upon Audit's enquiry, the TD informed Audit that:

- (a) the numbers of NFBs suspected to be operating without suitable endorsements as reported in the surveys included those NFBs without displaying the stipulated service signboards or displaying service signboards without the relevant service endorsements;
- (b) failure to display a service signboard or a PSL plate did not necessarily mean that the service operated was indeed unauthorised. However, the survey information would help ascertain the possible number of breaches

Regulatory controls over unauthorised operations

of the PSL conditions or regulations for not displaying the service signboards or PSL plates respectively; and

- (c) the TD had requested NFB operators to comply with the requirements through regular trade meetings and half-yearly bulletins issued to the trade, and would closely monitor the situation and take necessary follow-up actions (such as issuing reminders and conducting follow-up surveys to ascertain the breaches with a view to taking enforcement actions) where appropriate.

3.10 **Public concerns.** From time to time, there were media reports about unauthorised NFB services. In February 2017, there was a media report alleging that of some 320 residents' service routes approved by the TD, the operating details of about 80 (25%) shown on the operators' websites or other websites did not tally with the approved schedules of service. In July 2017, the TD informed Audit that it had completed checking on 43 of the 80 alleged routes and found irregularities in 18 (42%) routes. Its checking on the remaining 37 routes would be completed in the next few months. In July 2017, another media report alleged that for a residents' service route in the New Territories, about one-fourth of some 2,000 scheduled trips per month were operating without the TD's approval. Subsequent to the TD's follow-up action, the management of the relevant residential development announced that it had ceased operating the unauthorised trips.

3.11 In light of the considerable number of breaches of PSL conditions and suspected unauthorised NFB operations as revealed in the TD's annual surveys (see paras. 3.7 and 3.8) and the public concerns (see para. 3.10), the TD needs to strengthen enforcement actions to address the issue and ensure that a balanced public transport system is maintained.

Investigative work of the Regional Offices

3.12 **Investigative and enforcement process.** In general, investigative surveys are conducted to ascertain that the services are unauthorised before initiating inquiries:

- (a) **Preliminary investigations by the ROs.** The two ROs of the TD (see Appendix A) are responsible for the daily monitoring of transport services on a district basis. The relevant ROs will mainly arrange

contractors' staff to conduct investigative surveys on black spots proactively or upon receipt of a complaint or referral. When an unauthorised operation is detected, the ROs will seek clarifications from the PSL holder and conduct follow-up survey(s) whenever deemed necessary. If the violation persists, the case will be referred to the NFB Enforcement Team (NFBET) under the Public Vehicles and Prosecution Section (see Appendix A) for further investigations;

- (b) ***Investigations by the NFBET.*** The NFBET conducts proactive surveys on unauthorised operations and follows up cases referred by the ROs. The investigation proceedings are similar to those of the ROs except that they are mainly carried out by TD in-house staff instead of the contractors' staff. If the unauthorised service is substantiated after surveys, the case will be reported to the NFB Operation and Enforcement Committee (see para. 3.17) and recommended to the Commissioner for Transport for holding an inquiry; and
- (c) ***Inquiry under section 30 of the RTO.*** The inquiry involves appointment of a directorate officer of the TD to conduct hearings and submit an investigation report to the Commissioner for Transport for a decision. If the PSL holder does not accept the decision, he/she may apply for a review of the decision by the Transport Tribunal.

Need to improve investigative work of the ROs

3.13 According to the TD's internal guidelines, in addition to conducting investigative surveys upon receipt of complaints and referrals, the ROs should carry out proactive checks on various black spots at regular intervals, and take proper follow-up actions upon detection of unauthorised services. Audit examination of the ROs' records has revealed inadequacies in their investigative work, as illustrated in paragraphs 3.14 to 3.16 below.

3.14 ***Inadequate on-board surveys.*** To confirm existence of unauthorised operations, investigative surveys are conducted by way of observation at the terminal or approved stops (terminal survey) or taking a ride on the buses in question (on-board survey). While terminal surveys are effective in detecting overrun trips (i.e. operating more trips than approved) and operations without relevant endorsements, they are less effective in detecting routeing deviation and unauthorised intermediate stops. Based

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on an examination of 400 surveys conducted by the ROs from 2012 to 2017, Audit noted that 371 (93%) were terminal surveys and the remaining 29 (7%) were on-board surveys (Note 24). Audit performed 22 on-board surveys on residents' service routes (Note 25) from April to May 2017 and found that 21 (95%) of them had not been operated in accordance with the approved schedules of service, suggesting that such irregularities were not uncommon (see Table 5). However, as a result of the limited number of on-board surveys conducted by the TD, these types of irregularities might not have been detected.

Table 5

Unauthorised operations of 21 residents' service routes

Nature of unauthorised operations	Number of routes
With both unauthorised stop(s) and routeing deviation (see Case 1 for an example)	18 (ranging from 1 to 10 unauthorised stops)
With unauthorised stop(s) but without routeing deviation	2 (ranging from 1 to 4 unauthorised stops)
With routeing deviation but without unauthorised stop	1
Total	21

Source: Audit on-board surveys from April to May 2017

Note 24: *Of the 29 on-board surveys, 21 were for monitoring regular services (i.e. checking if the operations were in accordance with the approved schedules of service), while the other 8 were for identifying unauthorised operations without the TD's approval. Deviations from approved routeings and unauthorised intermediate stops were found in 19 (90%) of the 21 service monitoring surveys.*

Note 25: *Audit selected the routes using a risk-based approach, i.e. after Internet research showing potential irregularities.*

Case 1

NFB operations with unauthorised stops and routeing deviation

1. The NFB residents' service selected for Audit examination was for the carriage of passengers to and from a residential development in Tuen Mun. According to the approved schedule of service, it had two intermediate set-down stops in Central and a terminal point in Admiralty.

2. In an on-board survey of the selected route conducted on 4 May 2017, Audit staff found that there was one additional unauthorised pick-up stop in Tuen Mun, and nine unauthorised set-down stops in Central, Admiralty, Wan Chai and Causeway Bay (i.e. a total of 10 unauthorised stops). The terminal point was also extended from Admiralty to Causeway Bay.

Audit comments

3. While the ROs performed terminal surveys in Tuen Mun and Central annually upon receiving route renewal application, the above irregularities had not been detected. In Audit's view, the ROs need to use a risk-based approach to determine the mix of on-board and terminal surveys for detecting different types of unauthorised NFB operations.

Source: TD records and Audit on-board survey on 4 May 2017

3.15 ***Inadequate follow-up actions on detected unauthorised operations.*** Preliminary findings/reports on unauthorised operations are prerequisite for further investigation leading to possible inquiries. When an unauthorised operation is detected, the ROs will conduct survey(s) and seek clarifications from the PSL holder. If the violation persists, the ROs will refer the case to the NFBET (see para. 3.12(a)). The ROs should maintain a database of all unauthorised NFB services found in the respective regions, recording, inter alia, the operation details of the unauthorised services and background information, such as sources of complaints, actions taken and progress. However, Audit noted the ROs had not maintained such database, contrary to the internal guideline requirements. The TD informed Audit in August 2017 that individual district teams in the ROs might keep their own records of follow-up actions on the unauthorised operations. The records kept might not be

Regulatory controls over unauthorised operations

systematic and updated regularly. Audit conducted case studies and found the following inadequacies in the ROs' follow-up actions:

- (a) ***Investigative surveys.*** In 53 surveys with irregularities found by the ROs' contractors during the surveys from 2010 to 2017, there had been omissions and delays in taking follow-up actions in 35 (66%) cases as summarised in Table 6; and

Table 6

ROs' omissions and delays in taking follow-up actions

Type of omissions/delays	Number of surveys
No clarification letter sent and no follow-up survey conducted to confirm cessation of the unauthorised operations (see para. 3.12(a))	10
Clarification letter sent but no follow-up survey conducted (see Case 2 for an example)	10 (Note 1)
Clarification letter sent but follow-up survey was not arranged in a timely manner	14 (Note 2)
Delay in sending clarification letter (Note 3)	1
Total	35

Source: Audit analysis of TD records

Note 1: According to the TD, for seven surveys conducted from February 2015 to January 2017 concerning an operator of three residents' service routes, a meeting was held in March 2017 to remind the operator to operate the services in accordance with the schedules of service and review the need for any service adjustment.

Note 2: According to the TD, the follow-up surveys were conducted 3 to 15 months after the clarification letters had been sent.

Note 3: The survey was conducted in March 2017. The clarification letter was not sent until July 2017 (4 months later) after Audit's enquiry in June 2017.

Case 2

Inadequate follow-up actions on detected unauthorised operations

1. In a spot check at a residents' service terminal conducted in 2010, the ROs found a service plate placed by a PSL holder and noticed the service operated might have unauthorised stops. The TD issued a clarification letter to the PSL holder. In his reply to the TD, the PSL holder did not provide any explanation about the unauthorised stops. No follow-up survey was conducted to ascertain the cessation of such irregularity.

2. In 2016, after a media report on unauthorised stops of this route, the TD conducted another round of surveys (i.e. on-board surveys) and came up with similar findings. While clarification letters and repeated reminders had been sent by the TD to the PSL holder, Audit's on-board surveys on 2 and 25 May 2017 found that the residents' service still had five to eight unauthorised stops.

Audit comments

3. The TD needs to tighten control to ensure that all preliminary findings/reports on unauthorised NFB operations are properly followed up in accordance with the laid-down procedures.

Source: TD records and Audit on-board surveys on 2 and 25 May 2017

- (b) **Complaint cases.** According to the TD, upon receipt of complaints, the ROs will first conduct investigative surveys to collect facts and provide an opportunity to the operators for explanations. When the unauthorised operations are established, the complaint cases will be referred to the NFBET, which will conduct another series of investigative surveys before taking further enforcement actions. In a test check of the TD's records, Audit noted that:
- (i) while the complaints were recorded in the Government's Integrated Call Centre system which would automatically send an alert message to the supervisory staff if a reply was not issued to the complainant within 21 days, the case officers of the ROs only

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recorded the actions taken and progress of selected complaint cases on unauthorised operations for reporting to the NFB Operation and Enforcement Committee (see para. 3.17), rendering it difficult for the supervisory staff to monitor the progress of all complaint cases; and

- (ii) in 18 complaint cases from 2012 to 2016, the ROs issued letters to inform the operators concerned that complaints had been received and requested them to cease the unauthorised operations. However, the ROs had only conducted follow-up surveys to ascertain cessation of the unauthorised operations in 3 (17%) of the 18 complaint cases.

3.16 The inadequacies in the ROs' follow-up actions noted above were also reflected in the small number of cases referred to the NFBET for further enforcement actions (i.e. 12 cases in total since 2012). In Audit's view, the TD needs to tighten control to ensure that all preliminary findings/reports on unauthorised NFB operations are properly followed up in accordance with the laid-down procedures.

Need to improve record keeping for better case management

3.17 To improve the coordination of different branches/offices on NFB related issues, the TD has set up the NFB Operation and Enforcement Committee (Note 26) to provide a regular forum for the discussion of policy issues, operations, and progress of enforcement actions against unauthorised NFB operations. The TD's internal guidelines require the keeping of the following enforcement records and statistics to support the work of the Committee:

- (a) the ROs are responsible for keeping enforcement records at the regional level which include the number of clarification/warning letters issued to PSL holders who are found having operated unauthorised services. The NFBET may coordinate inputs from the ROs from time to time in order to maintain the overall enforcement records and statistics;

Note 26: *The Committee is chaired by the Assistant Commissioner (Bus & Railway) and includes representatives from the Bus and Railway Branch (see Appendix A), ROs and NFBET. In general, the Committee meeting is held half-yearly.*

- (b) the ROs shall maintain a database of all unauthorised operations found, including the operation details of such services, actions taken and progress of the cases, and provide monthly updates of newly identified unauthorised services as well as information of those ceased to the NFBET for coordination;
- (c) the NFBET is responsible for maintaining proper management information in respect of various enforcement statistics, including the summon actions on NFB traffic offences taken by the HKPF, progress of inquiries, Transport Tribunal hearings, etc. with an objective to monitoring the progress of enforcement actions; and
- (d) the NFBET shall compile all cases referred by the ROs for discussion at the NFB Operation and Enforcement Committee meeting. The main roles and functions of the Committee are to review the enforcement progress of unauthorised NFB services and to determine the priority of cases for enforcement.

3.18 *Inadequacies in ROs' record keeping.* As mentioned in paragraph 3.15, the ROs' records of unauthorised operations might not be systematically maintained and regularly updated. Hence, the ROs did not provide monthly updates to the NFBET for coordination. For enforcement records such as the number of clarification/warning letters issued, while the NFBET requested the ROs' inputs from 2012 to 2015, it did not do the same from 2016 to June 2017 (Note 27). Hence, the results were not reported to the Committee. While there is no laid-down requirement to report these statistics to the Committee, in the absence of such information, the Committee might not have a comprehensive picture of the unauthorised operations in the territory and the effectiveness of enforcement actions.

3.19 In September 2017, in response to Audit's enquiry, the TD said that while it would be more desirable if comprehensive enforcement statistics had been provided to the Committee, the Committee was still aware of the progress of enforcement actions through other management information, such as updates on the progress of

Note 27: *According to the ROs' records, the number of clarification letters sent to PSL holders on unauthorised operations reached its peak of 274 in 2013, decreasing to some 100 a year in 2015 and 2016.*

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inquiries by the NFBET (including cases referred by the ROs) and briefing of selected complaint cases on unauthorised services by the ROs (see para. 3.15(b)(i)). However, for better case management, Audit considers that the TD needs to strictly enforce the laid-down requirements on maintaining management information and statistics, and consider making better use of technology in monitoring compliance and case progress.

Enforcement actions against unauthorised operations

3.20 The NFBET will initiate an inquiry (see para. 3.12(c)) on a PSL holder when sufficient evidence is collected on unauthorised operations. If the unauthorised operations and/or breaches of PSL conditions are established and the Commissioner for Transport has accepted the inquiry report, the TD will issue a pre-sanction letter to notify the PSL holder of the result of the inquiry. The PSL holder may, within 14 days of being notified, reply in writing to the TD indicating whether he/she would like to provide further information for the consideration of the Commissioner for Transport who will take into account a basket of factors including but not limited to the seriousness and history of the non-compliance before making a decision on the imposition of sanction. Table 7 shows the number of inquiries from January 2012 to mid-May 2017 in relation to NFBs and SPLBs.

Table 7

**Number of inquiries against NFBs and SPLBs
(January 2012 to mid-May 2017)**

Number	2012	2013	2014	2015	2016	2017 (up to 12 May)	Total
Inquiries initiated in the year	32	40	25	39	34	5	175 (Note 1)
Cases concluded	32	33	15	13	0	0	93
Cases with sanctions implemented/to be implemented (Note 2)	18	26	12	11	0	0	67
Cases in which no sanction could be implemented (Note 3)	14	7	3	2	0	0	26

Source: Audit analysis of TD records

Note 1: Of the 175 inquiries, 40 were related to SPLBs. These 40 cases were mainly concerned with providing student services to educational institutions without the Commissioner for Transport's prior permission. Sanctions were implemented on 24 out of 26 concluded SPLB cases.

Note 2: The sanctions imposed/to be imposed ranged from suspension of PSLCs for 7 days to 8 months of the NFBs/SPLBs concerned.

Note 3: No sanction could be implemented in 26 cases due to: (a) cancellation of PSLs in 25 cases (see para. 3.23(b)); and (b) passing away of the PSL holder before hearing in 1 case.

3.21 According to the TD, the objectives of imposing sanctions are to: (a) achieve a just and fair disposal of the inquiry cases in accordance with the law; (b) preserve the integrity of the TD's licensing system of public service vehicles; (c) convey a proper message to operators to comply with statutory legislations and PSL conditions; and (d) give a message to the public and other public transport operators that the Government has a mechanism to deter unauthorised services. Audit examination of the inquiry records from January 2012 to mid-May 2017 revealed room for improvement, as illustrated in paragraphs 3.22 to 3.28.

Need to improve the efficiency and effectiveness of enforcement actions

3.22 ***Long time taken to complete inquiries.*** Of the 175 inquiries from January 2012 to mid-May 2017, Audit noted that:

- (a) among the 93 concluded cases, 67 cases were sanctioned. For these 67 cases, the time taken from the date of recommending to the Commissioner for Transport for holding an inquiry to the date of implementing sanctions averaged 24 months (ranging from 13 to 46 months). This was 1.4 times longer than the average time of 10 months found in the 2008 audit review (Note 28); and
- (b) of the 82 outstanding cases, 20 (24%) had been pending for over 2 years.

Audit selected 18 of the 93 concluded cases to further analyse the time taken on investigative surveys, and noted that the NFBET took on average four months to complete the surveys before recommending a case to the Commissioner for Transport for holding an inquiry. Taken together, it took on average 28 months (4 months on surveys plus 24 months on inquiry) from identifying the unauthorised operations to imposing sanctions on the operators.

3.23 Audit noted the following issues in relation to the lengthy inquiry process:

- (a) ***Continuation of unauthorised operations while inquiries were in progress.*** To ascertain whether a PSL holder had ceased the unauthorised service in the course of an inquiry, Audit conducted a sample check of 8 of the 82 outstanding cases. Audit found that unauthorised operations had continued in all of them; and
- (b) ***Sanctions not implemented due to transfer of ownership of NFBs.*** There were 25 (27% of a total of 93) concluded cases (see Table 7 in para. 3.20)

Note 28: *To ensure a like-with-like comparison with the findings in the 2008 audit review (see para. 1.10), any deferment of sanction implementation due to appeals to the Transport Tribunal was excluded, i.e. the sanction implementation date proposed by the TD was used in the calculation.*

in which the offending PSL holders had avoided sanctions through transfer of ownership of NFBs (Note 29). Case 3 is an example.

Case 3

Avoidance of sanctions by transfer of ownership of NFBs

1. From 2011 to 2015, there were five inquiries on unauthorised services between the New Territories West and Hong Kong Island, in which the PSL holders involved operated successively a residents' service route with a fleet of three NFBs. For the first inquiry in 2011, when the proposed sanction was pending the Commissioner for Transport's endorsement, the PSL holder concerned (Company A) applied to the TD for transferring the ownership of all three NFBs in its fleet at \$1 each to Company B, which would also take over the operation of the residents' service route. In May 2011, the transfer of NFBs and change of service operator were approved by the TD. The PSL of Company A was cancelled and the sanction could not be implemented.

2. Subsequently, four more inquiries were initiated on the unauthorised services. Similarly, before the completion of the inquiry process, the ownership of all three NFBs was transferred to other PSL holders (Note) at \$1 each and the relevant PSLs under the inquiries were cancelled. As a result, no sanction could be imposed.

Audit comments

3. This case highlighted a loophole in the existing enforcement mechanism whereby sanctions could be avoided by repeated transfers of ownership of vehicles with the unauthorised services remaining in operation.

Source: TD records

Note: Of the five PSL holders, one was an individual and four were companies. Company searches showed that the four companies had common director(s). The individual was also a shareholder of one of the companies.

Note 29: *Under the current enforcement mechanism, when there is a change of ownership of the vehicle to be sanctioned before the sanction starts, the penalty would be imposed on another bus of the concerned PSL holder's fleet. However, if the PSL holder does not have any other vehicle, the PSL will be cancelled and no sanction can be implemented.*

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3.24 In the 2008 audit review, Audit had expressed similar concern about the problem of avoidance of sanctions by transfer of ownership of vehicles mentioned in paragraph 3.23(b) and recommended that the TD should review the effectiveness of the sanction. In order to achieve sufficient deterrent effect, the TD has subsequently imposed heavier sanctions on repeated offenders. However, such sanctions could still be avoided by transfer of ownership of vehicles.

3.25 In 2015, the TD informed the THB that the loophole could only be exploited by small NFB operators with just one vehicle but not the large operators as sanctions could still be meted out to other vehicles in their fleet (see Note 29 to para. 3.23(b)). However, Audit noted that of the 25 sanction cases for which sanctions could not be implemented (see para. 3.23(b)), 20 cases involved the transfer of their whole NFB fleets (with 2 to 25 NFBs), indicating that even large NFB operators might exploit the loophole. The TD's annual survey of 2016 showed that 1,236 (96%) of the 1,287 NFB operators held 1 to 25 NFBs in their fleets. In September 2017, the TD informed Audit that it would not be an easy task to plug the loophole. Legal issues (such as property rights of the PSL holders in respect of the concerned buses) would have to be considered if the Government was to:

- (a) impose restrictions on the transfer of vehicles before completion of an inquiry; or
- (b) impose penalty on a transferred NFB when there was a decision to impose sanction after inquiry.

In Audit's view, the TD should adopt both short and long term measures to improve the efficiency and effectiveness of enforcement actions, such as endeavouring to shorten the lead time in completing an investigation and inquiry to minimise the risk of transfer of vehicles during the lengthy enforcement process (see para. 3.22), and exploring feasible measures to plug the sanction avoidance loophole in the long run.

Need to explore more efficient measures for tackling common breaches of PSL conditions

3.26 In 2004, the TAC recommended using a fixed penalty ticketing system instead of the complex and time-consuming inquiry process to streamline the enforcement procedures for common breaches of PSL conditions (see para. 3.4), such as failure to display the service signboards on NFBs. In the 2008 audit review,

Audit urged the TD to expedite implementation of the TAC's recommendation. In this connection, the TD had obtained legal view from the Department of Justice that legislative amendment would be required to implement such proposal.

3.27 While some unauthorised operations (e.g. NFBs picking up or setting down passengers at unauthorised stops) may provide convenience to the passengers, they may also cause inconvenience to the general public as they could lead to traffic congestion and environmental problems. In the absence of an efficient enforcement measure, Audit noted that the problem of non-compliance with PSL conditions had persisted. For example, as reflected by the TD's 2016 annual survey, 52% of the 5,870 NFBs surveyed were found not displaying the stipulated service signboards for half or more of their trips, contrary to the PSL conditions (see para. 3.7). Moreover, based on Audit's on-board surveys, 21 (95%) of 22 residents' service routes were not operated in accordance with the approved schedules of service (see para. 3.14).

3.28 In September 2017, the TD informed Audit that it had further deliberated the effectiveness of the proposed fixed penalty ticketing system, as follows:

- (a) the deterrent effect of the fixed penalty ticketing in combating breaches of PSL conditions might be limited as it would be difficult to prove most breaches on the spot (Note 30); and
- (b) in terms of financial loss to the PSL holders, the impact of fixed penalty would also be limited because it would only penalise the driver instead of the PSL holder even after a penalty ticket had been issued. On the contrary, if the case had gone through the inquiry path, once the non-compliance with PSL conditions was confirmed, the PSLCs of the respective vehicles could

Note 30: *According to the TD, when an NFB picks up passengers at an unauthorised stop under regular service, it may argue that it is in fact operating a non-regular service for that particular trip (since a considerable number of NFBs operate both regular and non-regular services), rendering it extremely difficult if not impossible for the enforcement officer to issue a penalty ticket on the spot. It is even more difficult for fixed penalty tickets to be issued for cases involving unauthorised services, since enforcement officers cannot ascertain the types of service that the NFBs are providing on the spot (i.e. it is not uncommon for incorrect display of service signboards, while this does not necessarily mean that the service is unauthorised).*

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be suspended, cancelled or varied. During the suspension period, the concerned vehicles would be prohibited from providing any service.

However, given the relatively long processing time for an inquiry and the considerable number of breaches of PSL conditions, there is a need to explore additional enforcement tools against common breaches of PSL conditions.

Publicity on authorised non-franchised bus services

3.29 *Stop signs for residents' service.* According to the TD, between 1998 and 2003, the number of unauthorised residents' service rose rapidly, resulting in congestion on main roads in the central business districts, especially in the evening peak hours. To address the problem, the TD had taken some measures to regulate the operation of residents' service. To educate the general public not to use unauthorised residents' services, the TD erected stop signs (see Photograph 2 for an example) at approved bus stops for some residents' service routes in the urban area (e.g. Central, Causeway Bay, Wan Chai and Tsim Sha Tsui) and the New Territories (e.g. Sha Tin and Yuen Long) (Note 31). Up to August 2017, there were 113 stop signs for residents' service in the territory, of which 82 (73%) were erected on Hong Kong Island and in Kowloon.

Note 31: *The TD published a leaflet titled "Don't patronise unauthorised non-franchised bus service" in November 2003 to facilitate passengers in identifying approved residents' service. According to the leaflet, the TD would continue to erect such stop signs in other areas.*

Photograph 2

A stop sign for an NFB residents' service



Source: Photograph taken by Audit staff on 29 June 2017

3.30 In September 2016, there was a media report that the information displayed on some stop signs was outdated. In response to Audit's enquiry, the TD said that all the updating work carried out by the Highways Department at the request of the TD had been completed in April 2017. Audit's site inspections from May to August 2017 found the following inadequacies in managing the stop signs for NFBs:

- (a) **TD's stop signs.** Audit compared the approved schedules of service and the list of stop signs provided by the TD for three selected districts (i.e. Tsim Sha Tsui, Wan Chai and Tuen Mun) and noted that the TD had not erected stop signs for all approved bus stops (i.e. only 49 stop signs (49%) out of 101 authorised NFB stops were erected). Audit also inspected 58 stop signs in 6 districts and found that 3 (5%) of them were still with outdated information; and
- (b) **Operators' stop signs.** Audit conducted site inspections in areas adjacent to Tsuen Wan railway station (being one of the hot spots as NFB stops) in August 2017 and found 15 stop signs erected thereon by some operators for various types of regular services (including hotel service, employees'


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service and residents' service by public or private NFB operators — see Photograph 3 for examples). These stop signs had different designs from the one prescribed by the TD. According to the TD, no approval had been granted to erecting such stop signs. Audit compared the information on these stop signs with the schedules of service approved by the TD and noted that two routes were not authorised to stop at Tsuen Wan railway station (Note 32). The TD needs to take necessary actions against those operators who have erected stop signs on public streets without the TD's approval, especially those signs erected at unauthorised locations which could cause confusion to the public.

Photograph 3

Stop signs erected by operators on a public street adjacent to Tsuen Wan railway station



Legend:  Stop signs erected by operators

Source: Photograph taken by Audit staff on 17 August 2017

Note 32: One of the 15 stop signs was erected by a private NFB operator. While a private NFB service is not issued with a schedule of service stipulating details such as stopping points, a private NFB operator has to apply to the TD for erecting stop signs.

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3.31 In August 2017, the TD informed Audit that it would conduct a review on the need for the provision of residents' service stop signs with due regard to their functions, prevalence of illegal activities of residents' service, and the enforcement arrangement. Pending the result of the review, the TD needs to take measures to keep the information displayed on the authorised stop signs up-to-date.

3.32 ***Publicising approved schedules of service.*** To facilitate better monitoring and enforcement against unauthorised operations, schedules of service stipulating all relevant operation details have been extended since 2005 to shuttle services provided under hotel service, student service of tertiary educational institutions, employees' service and contract hire service which are of a regular nature with the same origin and destination areas (see para. 2.5). As at June 2017, there were around 1,500 approved schedules of service (see Table 8).

Table 8

**Number of approved schedules of service
(June 2017)**

Type of services	Number of approved schedules of service
Hotel service	32
Student service	17
Employees' service	381
International passenger service	750
Residents' service	322
Contract hire service	29
Total	1,531

Source: TD records

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3.33 Currently, the TD publishes on its website operation details (e.g. routeings, stopping points, operating period and fare table) stipulated in the schedules of service of all approved residents' service and certain cross-boundary international passenger service (Note 33). However, the TD has not published similar operation details for other types of regular service. In this connection, Audit noted the following suspected cases of non-compliance with the schedules of service under hotel service and contract hire service:

- (a) ***Operation without schedules of service.*** Audit research and site visits found two cases of suspected regular services without approved schedules of service, i.e. a hotel service on Hong Kong Island and a scheduled contract hire service (i.e. a free shuttle service to and from a shopping mall) in Kowloon;
- (b) ***Charging of separate route fare.*** According to the schedules of service for 30 of the 32 hotel routes (see Table 8 in para. 3.32), collection of separate fare was not allowed. Audit research of the hotel websites revealed that separate fare was charged for 2 (7% of the 30) routes. For the 29 contract hire services (see Table 8 in para. 3.32) which according to the RTO shall not charge separate fare, Audit noted that in 7 (24%) cases, spending receipt was required to redeem a shuttle bus ticket. It is not clear as to whether such arrangement constitutes charging of separate fare which is defined in the PBSO as “a payment made by a person entitling him to be carried as a passenger in a bus notwithstanding that it is made in consideration of other matters in addition to the journey and irrespective of the person by or to whom it is made”; and
- (c) ***Overrun trips and unauthorised stopping points.*** Audit research of the 32 hotel websites also revealed that there might be overrun trips and/or unauthorised stops in 5 (16%) cases.

Note 33: *The TD only publishes on its website operation details of six designated routes of the short-haul cross-boundary coach service to Lok Ma Chau Control Point and the Lok Ma Chau – Huanggang Cross-boundary Shuttle Bus Service. The remaining cross-boundary coach service is long-haul service to various parts of the Mainland via different control points. According to the TD, the schedules of service for long-haul cross-boundary coach service only show routeings and stopping points within Hong Kong boundary and therefore it may not be meaningful to publish such operation details on its website.*

3.34 The suspected non-compliance cases noted above highlight the need to publicise approved schedules of service, in particular for hotel and contract hire services, for easy identification by the general public. This is important for protecting them from inadvertently using such unauthorised services which may not be covered by insurance in the event of accidents, and also enhancing public scrutiny of unauthorised operations.

Audit recommendations

3.35 Audit has *recommended* that the Commissioner for Transport should **strengthen enforcement actions against unauthorised NFB operations**. In particular, the Commissioner for Transport should:

Investigative work of the ROs

- (a) **use a risk-based approach to determine the mix of on-board and terminal surveys for detecting different types of unauthorised NFB operations;**
- (b) **tighten control to ensure that all preliminary findings/reports on unauthorised NFB operations are properly followed up in accordance with the laid-down procedures;**
- (c) **strictly enforce the laid-down requirements on maintaining management information and statistics for better case management, and consider making better use of technology in monitoring compliance and case progress;**

Enforcement actions against unauthorised operations

- (d) **improve the efficiency and effectiveness of the enforcement actions, including:**
 - (i) **endeavouring to shorten the lead time in completing the investigation and inquiry process;**

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- (ii) **exploring feasible measures to plug the loophole in the existing inquiry mechanism whereby an offending PSL holder can avoid sanctions by transfer of ownership of vehicles; and**
- (iii) **exploring additional enforcement tools for tackling common breaches of PSL conditions;**

Publicity of authorised NFB services

- (e) **complete the review on the need for the provision of stop signs for residents' service as soon as possible and in the interim:**
 - (i) **take measures to keep the information displayed on the authorised stop signs up-to-date; and**
 - (ii) **take necessary actions against those operators who have erected stop signs without the TD's approval; and**
- (f) **consider publicising approved schedules of service of all regular NFB services, in particular for hotel and contract hire services, for easy identification by the general public.**

Response from the Government

3.36 The Commissioner for Transport agrees with the audit recommendations. She has said that the TD will:

- (a) **consider conducting more on-board surveys to check compliance of NFB operators in respect of scheduled routeings and stopping points;**
- (b) **put in place a mechanism to monitor that findings on unauthorised NFB operations are properly followed up, and to provide management information and statistics for better case management;**
- (c) **endeavour to speed up the investigation and inquiry process within resources constraints;**

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- (d) explore the feasibility of introducing measures to prevent the offending PSL holders to avoid sanctions by transfer of ownership of their vehicles, with due regard to legal complication on the property rights of PSL holders in respect of the concerned buses;
- (e) explore the feasibility and applicability of additional enforcement tools for tackling common breaches of PSL conditions in consultation with the Department of Justice and the HKPF;
- (f) conduct a review on the need for the provision of stop signs for residents' service with due regard to their functions and maintenance, and prevalence of illegal activities;
- (g) during the interim, keep the information on the authorised stop signs up-to-date and take actions against unauthorised stop signs that caused safety problem or serious obstruction; and
- (h) consider publicising approved schedules of service, in particular for hotel and contract hire services, for easy identification by the general public.

PART 4: SAFETY MEASURES OF STUDENT SERVICE VEHICLES

4.1 According to its Controlling Officer's Report, the TD aims to promote road safety through the efficient regulation of vehicles and drivers. The work of the TD in this regard includes promoting safer vehicles through reviewing and updating the relevant regulations and safety standards, and examining and implementing measures to enhance road safety through legislation, publicity and use of technology. This PART examines the TD's work to further enhance the safety of student service vehicles, focusing on:

- (a) implementation of the safer seat requirements (paras. 4.5 to 4.7); and
- (b) additional safety measures (paras. 4.8 to 4.19).

Measures to enhance the safety of student service vehicles

4.2 NFBs and SPLBs play an important role in providing transport services for students. As at 31 December 2016, there were 5,238 student service vehicles, including 3,169 public NFBs and 103 private NFBs with student service endorsements, and 1,966 SPLBs. According to the TD, the safety records of student service vehicles have been generally satisfactory, as indicated by the low numbers of accidents and passenger casualties (see Table 9). Notwithstanding the generally satisfactory safety records of the student service vehicles, the Government considers it important to explore measures to further enhance their safety, given that the passengers are mostly young children who may not be able to take good care of themselves, particularly in emergency situations. The Road Safety and Standards Division of the TD (see Appendix A) is responsible for compiling and monitoring accident statistics, and providing support to the Road Safety Council (Note 34) in the formulation of road safety measures.

Note 34: *The Road Safety Council is a government advisory body (consisting of government officials and community members from various professions appointed by the Secretary for Transport and Housing) to coordinate road safety activities in Hong Kong.*

Table 9

**Number of traffic accidents involving injuries of students
on student service vehicles during school trips
(2012 to 2016)**

Year	Number of traffic accidents	Number of student passenger casualties (Note)
2012	38	147
2013	48	180
2014	37	176
2015	30	112
2016	33	91

Source: TD records

Note: All the affected student passengers suffered slight injuries in these accidents.

4.3 **2001-02 review.** In 2001-02, the then Transport Bureau and the TD reviewed four possible measures to enhance the safety of passengers on student service vehicles and reported the major findings to the LegCo Panel on Transport:

- (a) ***Introduction of passenger seat belts.*** The then existing seat belt legislation only required the fitting and wearing of seat belts for drivers and front seat passengers of all vehicle types, and rear seat passengers of private cars and taxis. Extension of the same requirements to student service vehicles was not recommended at that stage based on the following assessments:
 - (i) ***Safety benefits and overseas practices.*** There were on-going debates overseas on the effectiveness of seat belts on student service vehicles and the findings had been inconclusive (see Appendix C for details of arguments for and against the seat belt requirements). Compulsory fitting and wearing of seat belts on student service vehicles were not common worldwide;

- (ii) ***Impact on operation of school transport trade.*** First, there was concern that drivers or escorts had difficulties to ensure that the seat belts were properly worn throughout the journey and consequently who should be held responsible if the seat belts were not worn. Since it would not be practicable to hold kindergarten and primary school students legally responsible for not wearing seat belts, it might be necessary to impose on the escort a duty to ensure that students had the seat belts fastened. However, the school transport trade had expressed serious reservation over this proposal (see Appendix D for views of the trade on the provision of seat belts on student service vehicles). Second, under the existing legislation, 3 children aged 3 years or above but each not exceeding a height of 1.3 metre shall be counted as 2 passengers. If compulsory fitting and wearing of seat belts were to be introduced to student service vehicles, the “3 for 2” counting rule would need to be cancelled as each child had to be provided with a seat belt. Third, if compulsory fitting and wearing of seat belts were introduced, the increases in capital outlay for a new SPLB and an NFB to be equipped with two-point lap belts were estimated to be about \$30,000 and \$0.2 to \$0.3 million respectively. Given that the “3 for 2” rule would have to be cancelled and a compulsory escort service would have to be provided, it was estimated that parents/guardians had to pay an extra \$150 to \$225 per month for each child; and
 - (iii) ***Parents’/guardians’ views.*** Based on a questionnaire survey, the Government noted that a majority of the parents/guardians supported the provision of seat belts (69% to 88%) and cancellation of the “3 for 2” counting rule (54% to 63%). However, only 20% to 37% of these parents/guardians were willing to pay more than \$100 extra each month for the enhanced services;
- (b) ***Use of safer seats.*** Safer seats referred to strong and closely spaced seats, with high and energy-absorbing backs which could protect children in the event of a crash (see Photograph 4 for an example). They were adopted in the United States and Canada in preference to seat belts on school buses. It was estimated that the cost involved would range from \$5,000 to \$25,000 for SPLBs and \$15,000 to \$60,000 for school buses. In light of their perceived benefits and the relatively lower cost required, it was recommended to further explore the feasibility of this measure for future enhancement of the safety of student service vehicles;

Photograph 4

Safer seats fitted on a student service vehicle



Source: TD records

- (c) ***Compulsory escort service.*** Since February 1997, the provision of escort service had become a mandatory requirement for school buses serving kindergarten and primary school students. In considering the SPLB operators' concerns about the adverse impact on their competitiveness and survival in the business due to the probable increase in operating cost, the Government did not impose the requirement on SPLBs at that time. Based on information provided by the trade, escort service had in fact been provided on about 90% of the SPLBs carrying kindergarten students. With an average monthly salary of \$2,000 for an escort, the additional operating cost per student per month would be around \$100. For the purpose of improving the quality and safety of the service, it was recommended that compulsory escort service should be extended to SPLBs serving kindergarten and primary school students; and
- (d) ***Enhanced training and education.*** It was recommended to liaise with the trade and relevant stakeholders to strengthen driver training and education/publicity for students on safety of student service vehicles.

4.4 In April 2004, the then Environment, Transport and Works Bureau reported to the LegCo Panel on Transport the progress of enhancing education and publicity. In regard to the use of safer seats and provision of escorts, the Panel was informed of the following:

Safety measures of student service vehicles

- (a) *Use of safer seats.* These seats had been in use on student service vehicles in the United States and Canada for more than two decades. In Canada, the number of injuries sustained by school bus occupants had been reduced by about 26% since these safer seats were introduced in 1975. Both the NFB trade and the SPLB trade agreed with the need to enhance the safety of school children on student service vehicles. As regards their three major concerns, first, the proposed safer seats would not lead to any reduction in the carrying capacity of student service vehicles as the “3 for 2” counting rule would remain. Second, in line with the established practice for new safety equipment, the proposed requirements would only apply to newly registered student service vehicles. Retrofitting of the existing fleet would not be required. Third, the new requirements would incur an additional cost of about 6% to 8% of the vehicle cost, i.e. about \$11,000 to \$25,000 for SPLBs and about \$32,000 to \$70,000 for NFBs. Based on a life span of 8 years for a new SPLB and 10 years for a new NFB, the additional amount to be borne by each student would range from \$6 to \$17 per month. Based on the above consideration, it was recommended to require newly registered student service vehicles to be equipped with safer seats according to the TD’s specifications. In this connection, the additional safety requirements recommended by the TD’s consultant would be incorporated, i.e. the provision of only front-facing seats and an energy absorbing barrier for the front-row passengers (see Photograph 5 for an example); and

Photograph 5

An energy absorbing barrier fitted on a student service vehicle



Source: TD records

- (b) ***Compulsory provision of escorts.*** It was noted that some 90% of the SPLBs carrying kindergarten students and 25% of those carrying primary school students had already provided escorts voluntarily. Based on a questionnaire survey, 97% of the parents/guardians of kindergarten students and 89% of those of primary school students supported compulsory provision of escorts. Over 50% of these parents/guardians expressed willingness to pay for the service. The estimated additional operating cost arising from the proposal was about \$100 per student per month. However, the SPLB trade supported the proposed compulsory provision of escorts on SPLBs carrying kindergarten students only. Taking into consideration the trade's view, it was recommended to make provision of escorts compulsory for SPLBs that served kindergartens (see para. 1.9(d)).

Implementation of the safer seat requirements

4.5 In 2007, the Road Traffic (Construction and Maintenance of Vehicles) Regulations were amended to require student service vehicles registered on or after 1 May 2009 to be equipped with safer seats. As the safer seat requirements only apply to newly registered vehicles, the progress of fitting safer seats on existing student service vehicles depends very much on the pace of replacing the existing vehicles by new ones or retrofitting them with safer seats on a voluntary basis. Upon Audit's request, the TD provided a breakdown of 5,261 student service vehicles as at 24 July 2017 by their passenger seat types. As can be seen from Table 10, 1,879 (36%) student service vehicles were without safer seats.

Table 10**Student service vehicles by passenger seat types
(24 July 2017)**

Type of student service vehicles	Number of vehicles		
	with safer seats	without safer seats	Total
Public NFB with student service endorsement	1,899 (59 %)	1,337 (41 %)	3,236 (100 %)
Private NFB with student service endorsement	78 (72 %)	30 (28 %)	108 (100 %)
SPLB	1,405 (73 %)	512 (27 %)	1,917 (100 %)
Total	3,382 (64 %)	1,879 (36 %)	5,261 (100 %)

Source: TD records

Remarks: As NFBs may be licensed to operate one or more types of services, not all NFBs with student service endorsement provide student service in their daily operation. According to the 2014 TD survey, about 70% of public NFBs with student service endorsement were actually providing student service (see para. 1.9(c)).

4.6 To estimate the time needed to phase out the 1,879 student service vehicles without safer seats, Audit analysed their first registration dates and fuel types to see if they fell within the Government's incentive-cum-regulatory scheme (Note 35) to phase out all pre-Euro IV diesel commercial vehicles by 31 December 2019. Audit found that:

Note 35: The scheme was launched in March 2014 with a view to improving roadside air quality and better protecting public health. Under the scheme, pre-Euro IV diesel commercial vehicles would be phased out by different retirement deadlines according to their first registration dates. Pre-Euro IV diesel commercial vehicles scrapped within the period between 1 March 2014 and the specified payment application deadlines would be eligible for ex-gratia payments. The TD would stop issuing vehicle licences to the relevant diesel commercial vehicles after specified dates, unless they could comply with the emission standards applicable to them as if they were first registered on the date of the vehicle licence application.

- (a) 851 (45%) were pre-Euro IV diesel vehicles (Note 36). They would be phased out on or before 31 December 2019 under the incentive-cum-regulatory scheme or replaced by new ones which would be required to meet the stipulated emission and safer seat requirements;
- (b) 966 (51%) were diesel vehicles which fell outside the incentive-cum-regulatory scheme (Note 37). Given that NFBs normally had a life span of around 15 years (Note 38), it was estimated that most of these student service vehicles would continue to be in operation in the coming 4 to 6 years. For example, 337 (35%) of 966 such vehicles were public NFBs first registered in 2008 and it was possible that these vehicles would be in operation up to 2023; and
- (c) the remaining 62 (4%) were liquefied-petroleum-gas-fuelled SPLBs with first registration dates between November 2001 and April 2009. As the Government's incentive scheme only covered diesel commercial vehicles, these SPLBs would only be phased out or replaced on a voluntary basis by the vehicle owners. Similar to NFBs, assuming a life span of around 15 years, some of these SPLBs without safer seats were expected to be in operation in the coming years.

4.7 To sum up, it had taken some eight years after the safer seat requirements came into operation on 1 May 2009 to phase in 3,382 (64% of the total of 5,261 as at 24 July 2017) student service vehicles with safer seats. Through a normal replacement cycle, it may take up to some 6 years to phase out/replace the remaining 1,879 student service vehicles without safer seats. In Audit's view, the TD needs to explore measures to speed up the progress of phasing in student service vehicles with safer seats, such as stepping up publicity on the benefits of safer seats so that operators

Note 36: *These vehicles had first registration dates on or before: (a) 30 September 2006 (for NFBs and those SPLBs with permitted gross vehicle weight (PGVW) over 3.5 tonnes); or (b) 31 December 2006 (for those SPLBs with PGVW not over 3.5 tonnes).*

Note 37: *These vehicles had first registration dates between: (a) 1 October 2006 (for NFBs and those SPLBs with PGVW over 3.5 tonnes); or (b) 1 January 2007 (for those SPLBs with PGVW not over 3.5 tonnes) and 30 April 2009.*

Note 38: *The Government limits the service life of diesel commercial vehicles newly registered on or after 1 February 2014 to 15 years.*

would have to respond to the increasing demand for safer student service vehicles by parents or guardians.

Additional safety measures

4.8 After the implementation of safer seat requirements in 2009, some LegCo Members expressed concern on the adequacy of safety measures on student service vehicles and requested the TD to explore further means for the protection of the passengers of student service vehicles, particularly those at young ages. In July 2010, the TD commissioned a consultant to study the feasibility of installing seat belts on student service vehicles and compare the effectiveness and safety merits of seat belts with those of safer seats in the protection of students on student service vehicles. The TD's consultant concluded in its report of March 2013 that, after taking into account the safety benefits, cost estimates, technical feasibility, operational considerations, implementation issues and legislation issues, the overall performance of safer seat alone option was as good as that of safer seat with a lap-shoulder belt option. Based on the findings of the consultancy study, the TD recommended to the THB in February 2015 that there was no imminent need to pursue the mandatory installation of seat belts on student service vehicles.

4.9 Based on various overseas research findings, the TD's consultant found that safer seats were effective in providing protection to occupants on student service vehicles regardless of occupant age and size. However, the consultant also said that the benefit of safer seats could be further enhanced (see Appendix E for a summary of overseas research findings on safer seats in the consultancy study report) as follows:

- (a) safer seats provided less significant protection to passengers aged under 4.5 years or weighing under 18 kilograms (kg) compared to older children. Head size and body weight of children aged under 4.5 years were not appropriate to take full advantage of the energy-absorbing seat back in a frontal collision in cases when the child was not restrained; and
- (b) the benefit of safer seats could be further enhanced through the use of appropriate restraint systems in cases involving lateral and side-impact crashes, rollovers and ejections. In addition to safer seats, appropriate restraint systems could provide better protection to passengers aged under 4.5 years or weighing 18 kg or less.

4.10 The TD did not have statistics on student service vehicle passengers who were aged under 4.5 years or weighing under 18 kg (hereinafter referred to as younger children) for whom safer seats alone might provide less significant protection compared with older children. However, Audit noted from the TD's records that as at February 2017, 982 (50%) of 1,970 SPLBs were serving kindergarten students (Note 39). These 982 SPLBs (Note 40) were likely serving younger children for whom additional measures to enhance their safety should be considered.

Use of child restraint device

4.11 *Use of child restraint devices in private cars.* Under the Road Traffic (Safety Equipment) Regulations (Cap. 374F), a child aged less than 3 must be restrained by an approved child restraint device (CRD — see Figure 7 for two examples) when travelling in the front seat of a private car. In 2013, the THB consulted the LegCo Panel on Transport on a proposal to enhance the safety of child passenger on private cars by raising the mandatory requirement of using CRDs to cover the rear seats. The Panel was informed that a review of 17 jurisdictions revealed that all of them required the use of CRDs in both the front and rear seats of private cars. A number of Panel Members supported the Government's proposal to enhance the safety of child passengers in private cars and two of them also considered that CRD/seat belt requirements should be imposed on student service vehicles which regularly carried child passengers. At present, the TD encourages private car drivers to use appropriate CRDs for young child passengers placed in the rear seats.

Note 39: *Information on the number of NFBs serving kindergarten students was not available because unlike SPLBs which were only allowed to provide services to schools as approved by the TD on a case-by-case basis, most NFBs with student service endorsement (i.e. public NFBs) could serve different schools without the need to obtain the TD's approval.*

Note 40: *According to the Education Bureau, kindergartens provide services to children from 3 to 6 years old (i.e. the younger children are included).*

Figure 7

Two types of CRD

(a) A child safety seat



(b) A booster seat



Source: LegCo Panel on Transport paper

Remarks: According to the TD, a child safety seat is for a passenger aged 9 months to 3 years or weighing 9 to 18 kg while a booster seat is for a passenger aged 4 to 12 years or weighing 15 to 36 kg.

4.12 **Overseas practices.** Audit conducted an Internet research of the practices on improving the protection of younger children on school buses in Canada and the United States as both jurisdictions had safer seat requirements similar to those of Hong Kong. The results are as follows:

- (a) **Canada.** The transport authority in Canada had recommended that younger children be transported in an appropriate CRD while on a school bus. With effect from April 2007, it had required all newly manufactured school buses to have a minimum number of seating positions equipped with anchorages allowing a CRD to be attached although there was no legal requirement mandating the use of CRDs by younger children on school buses; and
- (b) **United States.** According to the regulations on safety features and the safe operation of vehicles used to transport children participating in Head Start and Early Head Start programmes (i.e. a government-funded service to promote school readiness for children from birth to aged 5 in low-income families of the United States), vehicles participating in the programmes should be equipped for use of CRDs. Any child weighing 50 pounds or less should be seated in a CRD appropriate to the height and weight of the

child while the vehicle was in motion although there was no legal requirement mandating the use of CRDs by younger children on all school buses.

Provision of seat belts

4.13 Under the Road Traffic (Safety Equipment) Regulations, seat belts are required for the driver's seat in NFBs and the driver's seat cum the front passenger seat in SPLBs. There are however no seat belt requirements for any other passenger seats in both NFBs with student service endorsement and SPLBs except for public NFBs providing cross-boundary international passenger service (Note 41). In response to an enquiry of a LegCo Member on the provision of seat belts in student service vehicles in 2014, the THB indicated that:

- (a) the views on the provision of seat belts in student service vehicles varied among different overseas jurisdictions;
- (b) while seat belts could protect students in accidents, they might prevent prompt egress from the vehicles as students (especially the younger ones) might not be able to unfasten their seat belts on their own;
- (c) even when seat belts were installed, it might not be possible for the bus drivers or escorts to ensure proper wearing of seat belts by students all the time;
- (d) as student service vehicles were used to carry students of different ages, ranging from kindergarten to early secondary school students, there was practical difficulty to provide one type of seat belts that could suit students of all ages and body sizes; and
- (e) the question of who should be responsible if the seat belts were not worn was yet to be resolved.

Note 41: *Since June 2002, all public NFBs providing cross-boundary international passenger service (i.e. including cross boundary school coaches) have been required to be fitted with seat belts by way of PSL conditions and passengers have been encouraged to wear the seat belts provided on their seats on a voluntary basis.*

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The above line of arguments was similar to that of the 2001-02 review (see para. 4.3(a)). According to the TD, the above views have taken into account the 2013 consultancy study report on the feasibility of installing seat belts on student service vehicles (see para. 4.8). However, Audit noted that there had been developments both locally and overseas which needed to be taken into account in considering additional measures for enhancing the safety of student service vehicles as illustrated in paragraphs 4.14 to 4.17.

4.14 ***Safety benefits of seat belts.*** According to the TD's 2013 consultancy study report (see para. 4.8), the United States National Highway Traffic Safety Administration study had shown that lap-shoulder seat belts were remarkably superior to safer seats and lap-belts in reducing the risks of severe head and neck injuries in frontal crashes. In addition, while there were no established studies quantifying the effectiveness of safer seats, lap-belts and lap-shoulder seat belts in reducing the risks of severe injury and fatality in side-impact and rollover accidents, the TD's consultant opined that passengers should be better protected by seat belts in side-impact and rollout accidents than safer seat alone, provided that seat belts were properly worn. However, as safer seats had the distinguished benefit of being passive protective devices that did not require any action by the passengers whereas the benefits of seat belts could only be realised if worn properly, the consultant considered that safer seats could not be replaced by seat belts alone. In terms of safety benefits, the TD's consultant rated safer seats with lap-shoulder seat belts as excellent while safer seats alone and safer seats with lap-belts as average.

4.15 ***Other jurisdictions' practices.*** The TD's consultant reviewed the application of safer seats and seat belts in student service vehicles of 23 jurisdictions (see Appendix F for details). The review results suggested an increasing trend in the use of seat belts (unlike the position in 2001-02 — see para. 4.3(a)(i)):

- (a) of the 23 jurisdictions reviewed, 16 (70%) had existing or planned legislation regulating the fitting and/or wearing of seat belts on student service vehicles;
- (b) of the 7 jurisdictions with safer seat requirements, 6 (86%) also introduced requirements on the fitting and/or wearing of seat belts; and

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- (c) of the 6 jurisdictions without safer seat and seat belt requirements, 2 (i.e. South Australia and Western Australia) had introduced measures to expedite the fitting of seat belts on school buses and one (i.e. Germany) did not have relevant requirements because school transport services were usually operated on regular public transport vehicles.

As regards the parties who would be held liable for any failure to wear seat belts (para. 4.13(e)), the TD's consultant found that some of the jurisdictions reviewed had addressed this issue by making reference to the age of the passengers (see Table 11).

Table 11

**Overseas practices on parties held responsible
for failure to wear seat belts in student service vehicles
(2010-11)**

Overseas Jurisdiction	Passenger Age	Party held responsible		
		Driver	Passenger	Both driver and passenger
Australia (Queensland)	Aged < 16	✓	✗	✗
	Aged ≥ 16	✗	✓	✗
France	Aged ≤ 18	✓	✗	✗
	Aged > 18	✗	✓	✗
Japan	–	✓	✗	✗
Singapore	–	✗	✗	✓
United Kingdom	Aged < 14	✓	✗	✗
	Aged ≥ 14	✗	✓	✗
United States (New Hampshire)	Aged < 18	✓	✗	✗
	Aged ≥ 18	✗	✓	✗

Source: TD records

Safety measures of student service vehicles

4.16 ***Vehicles fitted with both safer seats and seat belts.*** While there was no mandatory requirement on the use of seat belts in student service vehicles, Audit analysis of the TD's records revealed that of the 3,382 student service vehicles fitted with safer seats as at 24 July 2017 (see Table 10 in para. 4.5), 2,094 (62%) had in fact been fitted with both safer seats and seat belts (see Table 12).

Table 12

**Student service vehicles fitted with both safer seats and seat belts
and those with safer seats only
(24 July 2017)**

Type of student service vehicles	Number of vehicles		
	Fitted with safer seats only	Fitted with both safer seats and seat belts	Total
Public NFB	868 (46%)	1,031 (54%)	1,899 (100%)
Private NFB	20 (26%)	58 (74%)	78 (100%)
SPLB	400 (28%)	1,005 (72%)	1,405 (100%)
Overall	1,288 (38%)	2,094 (62%)	3,382 (100%)

Source: Audit analysis of TD records

4.17 ***Types of seat belt installed.*** Seat belts installed at the operators' discretion might not be subject to certification and approval by the TD. In a sample check of the TD's records of 30 student service vehicles fitted with both safer seats and seat belts, Audit found that all of them were equipped with lap-belts which according to the 2013 consultancy study report were inferior to lap-shoulder seat belts in reducing the risks of severe head and neck injuries in frontal crashes (see para. 4.14). In this connection, Audit noted that the transport authorities in the United States and Canada (both jurisdictions have safer seat requirements similar to those of Hong Kong) had made recommendations on the type of seat belts fitted in student service vehicles:

- (a) in November 2015, the United States National Highway Traffic Safety Administration announced that student service vehicles should have lap-shoulder seat belts and various measures would be taken to achieve this mission; and
- (b) in March 2017, the Transport Canada proposed regulations requiring that seat belts optionally installed on student service vehicles should be of the lap-shoulder type in light of the research result that lap-belts could increase the injury risk in certain collisions.

4.18 ***Unresolved issues.*** In September and October 2017, in response to Audit's enquiry, the TD said that there were a number of technical, operational, implementation and legal issues to be thoroughly considered and resolved before a decision could be taken on the types of measures to further enhance the safety of student service vehicles, including but not limited to the following:

- (a) different types of CRD would be required for different age groups of school children. Given that a student service vehicle tended to carry students of different ages during the same run and there could be more than one run per day, it might not be practicable for operators to procure and store on the vehicle adequate number of different types of CRD so as to cater for different combinations of child passengers during different runs;
- (b) CRDs on student service vehicle seats could offer protection only if they were properly installed and individually adjusted to suit each child passenger. Issues relating to the practicability of properly installing and adjusting the CRD for each student needed to be examined, including the possible adverse impact on the operation due to the extra time required;
- (c) in the event that emergency evacuation from a student service vehicle was required, each child passenger needed to be unfastened from his/her CRD. While the provision of an escort had become a mandatory requirement on student service vehicles, it would not be feasible for the escort to help unfasten seat belts in a split second, rendering prompt evacuation of young children on board difficult;
- (d) there was no practicable method for the driver or the escort of student service vehicles to ensure all passengers on board had their seat belts

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properly worn throughout the journey. It might not be justifiable to place such legal liability on them; and

- (e) the installation of CRDs would require a substantial change of existing mode of operation which could have impacts on the operating cost of, and fee payable for, student service vehicles. There was a need to fully engage various stakeholders if changes were to be introduced.

4.19 Audit understands the complexity in evaluating various possible technologies for further enhancing the safety of student service vehicles. In Audit's view, besides continuously monitoring the latest developments on the use of different technologies, the TD may consider conducting a survey of stakeholders (including the operators, schools and parents) when necessary to gauge their views, preference and willingness to pay for possible enhancement options that suit the Hong Kong's context and address operational and implementation issues that may arise.

Audit recommendations

4.20 **Audit has *recommended* that the Commissioner for Transport should:**

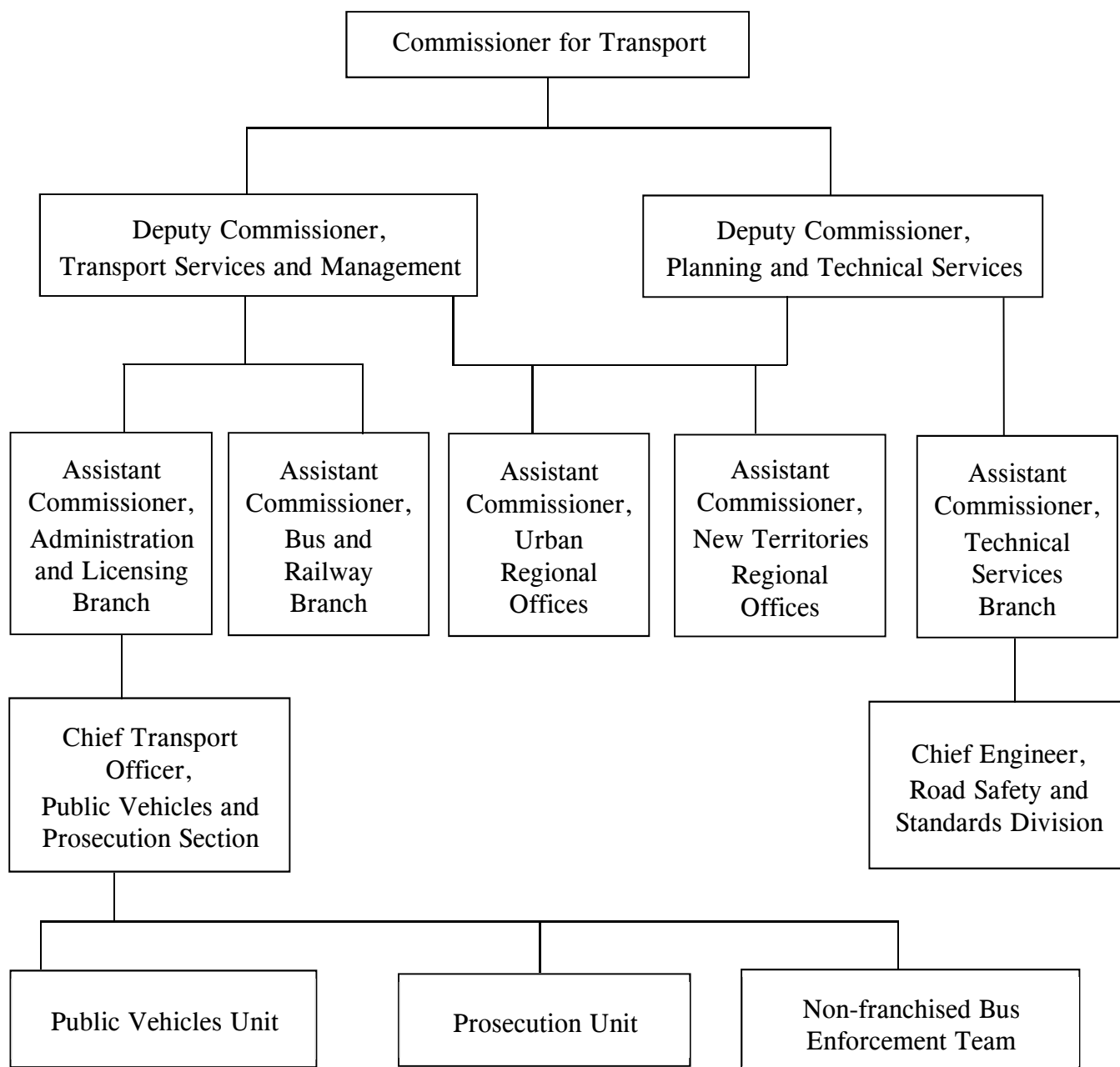
- (a) **explore measures to speed up the progress of phasing in student service vehicles with safer seats, such as stepping up publicity on the benefits of safer seats so that operators would have to respond to the increasing demand for safer student service vehicles by parents or guardians; and**
- (b) **continue to keep abreast of the latest developments in enhancing the safety of student service vehicles, and consider conducting a survey of stakeholders when necessary to gauge their views, preference and willingness to pay for possible enhancement options that suit the Hong Kong's context and address operational and implementation issues that may arise.**

Response from the Government

4.21 The Commissioner for Transport agrees with the audit recommendations. She has said that the TD will:

- (a) continue to monitor the number of student service vehicles installed with safer seats, and step up the publicity on the benefits and use of safer seats; and
- (b) continue to keep abreast of the latest developments in enhancing the safety of student service vehicles. Taking into account various factors such as the safety benefits, cost implications, implementation, operation, impact on trade and views of stakeholders, if any possible enhancement measures are to be proposed and considered suitable for Hong Kong, the TD will conduct a survey of relevant stakeholders to gauge their views, preference and willingness to pay with a view to resolving any operational and implementation issue.

**Transport Department:
Organisation chart (extract)
(30 September 2017)**



Source: TD records

Appendix B
(paras. 1.5(a) and
2.25(a) refer)

**Brief description of eight types of
public non-franchised bus services**

Type of service	Administrative code	Brief description of the service	Colour of passenger service licence certificate
Tour service	A01	A tour service is for the carriage of passengers travelling together on a journey from the places at which they are taken up to other places and back to the places at which they were taken up, such as those provided in conjunction with inbound travel service to tourists.	Red
Hotel service	A02	A hotel service is for the carriage of passengers residing at a hotel where every passenger is taken up or set down at the hotel.	Red
Student service	A03	A student service is for the carriage of students, teachers, persons in charge of the students to and from a school, university or education institution.	Red
Employees' service	A04	An employees' service is provided by an employer for the carriage to or from the place of work of passengers who are persons employed by the employer.	Red
International passenger service	A05	An international passenger service is for the carriage of passengers in either direction between any one or more of the following places, that is to say, the Hong Kong International Airport, Hung Hom Railway Station, Macau Ferry Pier or any other pier, any Hong Kong border crossing, any hotel, airline office or ferry or similar terminal.	Green

Appendix B
(Cont'd)
(paras. 1.5(a) and
2.25(a) refer)

Type of service	Administrative code	Brief description of the service	Colour of passenger service licence certificate
Residents' service	A06	A residents' service is provided by or on behalf of the management, residents or owners of any residential development for the carriage of passengers to or from the residential development.	Green
Multiple transport service	A07	A multiple transport service is for the carriage of passengers in combination with another mode of public transport service from one departure point to one destination (other than to and from a residential development) and where a combined fare is paid for the whole journey at a place other than at the boarding point of the bus or on the bus.	Green
Contract hire service	A08	A contract hire service is for catering ad-hoc demands for services that could not be met by the other seven types of services, e.g. wedding and funeral.	Red

Source: TD records

Remarks: A contract hire service is approved by the Commissioner for Transport in accordance with the RTO while the other types of services are defined in the PBSO.

**Arguments for and against seat belt requirements on
student service vehicles
(2001-02)**

The major arguments overseas in favour of and against seat belts on student service vehicles were as follows:

I. Arguments in favour of seat belts on student service vehicles:

- (a) ***Protecting children in an accident.*** Seat belts would keep children in their seats, and offer superior protection in the event of rollovers, or side impact or angle collision (in contrast to head-on or rear-impact);
- (b) ***Carryover value.*** Use of seat belts in school buses would reinforce the educational messages aimed at school-age youngsters and would have a carryover effect of seat belt usage later in their later lives; and
- (c) ***Passenger behaviour.*** Proper use of seat belts would improve student behaviour on the buses, reduce drivers' distraction, and might reduce the chances of accidents.

II. Arguments against seat belts on student service vehicles:

- (a) ***Ineffective in catastrophic accidents.*** Seat belts were of little use in the types of catastrophic accidents that caused deaths or serious injuries to passengers on-board, e.g. collisions with larger vehicles etc. Seat belts might actually prevent rapid egress from a bus in the case of a bus fire or sinking in a river, lake or other large body of water, as children might be unable to unfasten their seat belts themselves;
- (b) ***Not an effective expenditure.*** The safety record of school buses was already so good that the additional cost per bus to install lap-belts could be better spent on other safety measures;
- (c) ***No guarantee of use.*** Installing seat belts in a school bus did not mean that students would use them. In addition, it was not possible for the bus driver or escort to monitor the proper fastening and adjustment of seat belts during the whole trip. Improperly adjusted belts could prove hazardous; and
- (d) ***Seat belts cause injuries.*** Children had been injured by seat belts used as weapons by other students, and by catching their fingers in the buckles or tripping over loose belts.

Source: LegCo Panel on Transport paper

**Views of the trade on provision of seat belts
on student service vehicles
(2001-02)**

The views of the school transport trade on the provision of seat belts on student service vehicles were as follows:

- (a) the trade expressed concerns about the escorts taking up the responsibility to ensure that each and every student onboard was wearing seat belts properly during the trip. It would be very difficult to recruit escorts who were willing to take up the responsibility for the small income involved;
- (b) the risk of children using the belts as weapons to strike another student;
- (c) young children might not be able to release the buckle without assistance. In case of an emergency/accident, such as fire or submersion in water, use of seat belts could hinder evacuation even if an escort was provided;
- (d) after cancelling the “3 for 2” counting rule, the number of student service vehicles on roads would likely be increased, adding traffic on roads, in particular those in the vicinity of schools;
- (e) increase in boarding and alighting time;
- (f) some parents/guardians could not afford to use the school transport service due to the substantial increase in costs arising from cancellation of the “3 for 2” counting rule and the additional escort services. The service would ultimately serve only the relatively rich group, not the general public. This would pose hardship to the trade also;
- (g) the fact that school trips were usually fairly short and the speed of the vehicle was fairly low, rendering the use of seat belts not so useful;
- (h) insurance might not cover damages/injuries triggered by the provision/wearing of seat belts; and
- (i) more emphasis should be put on educating students to behave properly on student service vehicles during the trip.

Source: LegCo Panel on Transport paper

**Summary of overseas research findings
on safer seats in the consultancy study report of March 2013**

Factors	Findings
Merits	<ul style="list-style-type: none"> • Easy to implement compared with seat belts • Required only the modification of passenger seats and did not require any action on behalf of the student occupant
Demerits	<ul style="list-style-type: none"> • Failed to provide occupant protection in lateral and side-impacted crashes, rollovers and ejections • Failed to provide sufficient protection to occupants aged under 4.5 years or weighing under 18 kg, considering their head size and impact-energy-absorbing performance, although some marginal safety benefits to these occupants could still be achieved
Safety benefits	<ul style="list-style-type: none"> • Effective in protecting occupants in front-rear collisions or during emergency braking • In a collision, the body of the occupant moved forwards, contacting and deforming the energy-absorbing seat back in front. Therefore, the impact force was distributed across the entire upper-body area
Occupant size	<ul style="list-style-type: none"> • Head size and body weight of children aged under 4.5 years were not appropriate to take full advantage of the energy-absorbing seat back in a frontal collision in cases when the child was not restrained • In addition to compartmentalisation, appropriate restraint systems were required for occupants aged under 4.5 years or weighing 18 kg or less • Older children (aged 4.5 years or older) were well protected
Vehicle characteristics	<ul style="list-style-type: none"> • Optimum seat back height had been set out
Collision type	<ul style="list-style-type: none"> • Significant reduction in injury risk in frontal and rear-end collisions only, but not oblique and rollover collisions
Operational considerations	<ul style="list-style-type: none"> • As a passive restraint system, misuse was not really possible • No additional escort required • No adverse effects on efficiency of loading and unloading activities and emergency evacuations or adaptation of 3-for-2 seating arrangement

Source: TD records

**Other jurisdictions with safer seat
and/or seat belt requirements on student service vehicles
(2010-11)**

	Jurisdiction	Safer seats	Seat belts	
			Installation	Wearing
1.	Australia (Commonwealth)	✗	✓	✗
2.	Australia (New South Wales)	✗	✗	✓
3.	Australia (Queensland)	✓	✓ (Note 1)	✓
4.	Australia (South Australia)	✗	✗	✗
5.	Australia (Victoria)	✗	✗	✗
6.	Australia (Western Australia)	✗	✗	✗
7.	Canada	✓	✗	✗
8.	Colombia	✗	✓	✓
9.	European Union	✗	✓	✓
10.	France	✗	✓	✓
11.	Germany	✗	✗	✗
12.	Ireland	✗	✓	✓
13.	Japan	✗	✓ (Note 2)	✓
14.	Korea	✓	✓	✗
15.	Mainland China	✓	✓ (Note 3)	✗

Appendix F
(Cont'd)
(para. 4.15 refers)

	Jurisdiction	Safer seats	Seat belts	
			Installation	Wearing
16.	Singapore	✕	✓ (Note 4)	✓
17.	Sri Lanka	✕	✕	✕
18.	United Kingdom	✕	✓	✓
19.	United States (Federal)	✓	✓ (Note 5)	✕
20.	United States (New Hampshire)	✕	✓	✓
21.	United States (New Jersey)	✓	✓	✓
22.	United States (New York)	✓	✓	✕
23.	Zimbabwe	✕	✕	✕

Source: TD records

Note 1: The requirement applied to buses with 17 seats or more in extreme operation environment only.

Note 2: The requirement did not apply to kindergarten small buses.

Note 3: The requirement applied to student service vehicles serving primary school only.

Note 4: The requirement applied to small buses with seating capacity of 15 or less only.

Note 5: The requirement applied to small student service vehicles with a gross vehicle weight of 4,536 kg or less only.

Remarks: The safer seat and seat belt requirements in the 23 jurisdictions were based on the TD's consultant's research conducted between 2010 and 2011.

Acronyms and abbreviations

Audit	Audit Commission
CRD	Child restraint device
CSB	Civil Service Bureau
HKPF	Hong Kong Police Force
kg	Kilogram
LegCo	Legislative Council
NFB	Non-franchised bus
NFBET	Non-Franchised Bus Enforcement Team
PBSO	Public Bus Services Ordinance
PGVW	Permitted gross vehicle weight
PSL	Passenger Service Licence
PSLC	Passenger Service Licence Certificate
PVU	Public Vehicles Unit
ROs	Regional Offices
RTO	Road Traffic Ordinance
SPLB	School private light bus
TAC	Transport Advisory Committee
TD	Transport Department
THB	Transport and Housing Bureau

CHAPTER 5

Development Bureau Land Registry

Operation of the Land Registry

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

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OPERATION OF THE LAND REGISTRY

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OPERATION OF THE LAND REGISTRY

Executive Summary

1. The Land Registry (LR), headed by the Land Registrar, aims to provide an efficient and effective land registration system to facilitate the orderly conduct of land transactions. In addition to ensuring secure and customer friendly land registration and information services, the LR's missions also include advocating reform of Hong Kong's land registration system through introduction of title registration. The Land Registry Trading Fund (LRTF) was established under the Trading Funds Ordinance (Cap. 430) on 1 August 1993 to manage and account for the operation of the LR. The Land Registrar is the General Manager of the LRTF.

2. The LR is accountable to the Development Bureau (DEVB) and the Financial Services and the Treasury Bureau (FSTB) for its business and financial performance respectively. The DEVB provides policy steer for the LR's work and the FSTB monitors the LR's financial performance. Under the Trading Funds Ordinance, the LRTF is required to achieve a reasonable return on the fixed assets employed. During the 24-year period from 1993-94 to 2016-17, the LRTF achieved the target rates of return on Average Net Fixed Assets (ANFA) except for one year in 2015-16 (actual of 4.1 % against target of 6.9%). The Audit Commission (Audit) has recently conducted a review to examine the operation of the LR.

Provision of services

3. The LR's main services include: (a) land registration services which involve the registration of documents affecting land under the Land Registration Ordinance (Cap. 128 — the LRO) and maintaining up-to-date land registers; (b) land information services for searching land registers and supplying copies of registered documents and related records; and (c) owners' corporation services which involve registration of owners' corporations and maintenance of a register of owners' corporations under the Building Management Ordinance (Cap. 344) (paras. 1.3 and 2.2).

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4. ***Need to update target completion date for tidying up exercise of land registers.*** The LR maintains over 3 million land registers involving registered particulars (accumulated since 1844) of about 23.7 million land documents. Between 1986 and 1997, a computerisation exercise had been conducted to convert the manual land registers to computerised records (which were later converted to records in the Integrated Registration Information System (IRIS) launched in February 2005). According to the LR, in the IRIS: (a) certain information was not shown in some land registers due to reasons including information that might not have been recorded on the manual land registers or not input into the computerised land registers during the computerisation exercise; and (b) some computerised land registers (before implementing the IRIS) contained partial address in the “address” field, with the remaining part of the address in the “property remarks” field, as the length of the “address” field was limited. Since June 2007, the LR has been conducting a tidying up exercise for filling up the related information. However, according to the LR, there might be a slippage in completing the exercise which was originally targeted for completion by the end of 2018 (paras. 2.4 to 2.8).

5. ***Need to enhance accuracy of information in land registers.*** According to the LR, typographical errors or discrepancies in the entries in the land registers (collectively referred to as “errors” by the LR) are identified from time to time through its quality control check and daily operation, and external parties’ amendment requests. From 2012-13 to 2016-17, the total number of errors (classified into conversion, registration and memorial errors) corrected in the land registers each year ranged from 5,737 to 7,564. There is a need for the LR to keep under review the errors corrected in the land registers and, where warranted, perform more detailed analysis (e.g. seriousness and possible causes) of the corrected errors for monitoring and taking measures to enhance the accuracy of the land registers (paras. 2.9 to 2.12 and 2.14).

6. ***Need to keep under review performance of New Territories Search Offices (NTSOs).*** The LR has three NTSOs in Tsuen Wan, Tai Po and Yuen Long providing counter search and copying, and owners’ corporation services. Audit noted that, during 2012-13 to 2016-17, the three NTSOs: (a) had incurred operating losses ranging from \$0.9 million to \$2 million each year; and (b) had low patronage. For each of the five years, the daily average number of visitors requesting search and copying services at two NTSOs was below 55 and owners’ corporation services at each NTSO was not more than 5 (paras. 2.27 and 2.28).

Implementation of land title registration system

7. At present, Hong Kong operates a deeds registration system for recording land and property transactions under the LRO. The system only confers priority on registered deeds and serves as an index of registered instruments to the public. It provides no proof that the person registered as the owner has good title to the property and gives no guarantee to title. In order to establish title to property, it is necessary for the purchaser's solicitors in every case to check the historical title documents relating to all the transactions affecting the property that extend to not less than 15 years before entering into a new transaction of that property. Since the late nineteenth century, many common law jurisdictions have implemented a land title registration system (LTRS), which provides conclusive evidence of title to property (paras. 1.14 and 1.15).

8. In July 2004, the Land Titles Ordinance (Cap. 585 — the LTO) was enacted. The LTO aims to provide for a new LTRS that registers the titles to and the interests in land, with a view to providing greater certainty to property titles and simplifying conveyancing. However, up to September 2017, the LTO had not yet come into force and the LTRS had not been implemented. Over the years, the implementation of the LTRS involved various complex issues. In general, there were considerable deliberations and divergent views among various stakeholders on three main issues, namely conversion mechanism, rectification arrangements and indemnity arrangements. The LR had made various proposals to address the issues. Up to September 2017, it was still working towards forging a consensus with the stakeholders on the way forward in implementing the LTRS (paras. 1.16, 3.5 to 3.7 and 3.22).

9. *Under-estimation of complexity of the issues and the work involved in implementing LTO and LTRS.* In December 2002, the Government introduced a Land Titles Bill into the Legislative Council (LegCo). During the scrutiny of the Bill by the Bills Committee, the Government proposed to commence the LTO two years after its enactment, and undertook to conduct a review of the LTO during the two-year period between its enactment and commencement (post-enactment review) and to take follow-up actions on various issues raised during the scrutiny of the Bill. In the event, the LTO was enacted in July 2004. However, up to September 2017, 13 years after its enactment, the LTO had not yet been implemented. The LR's post-enactment review found that substantial amendments to the LTO were required. Apparently, the

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LR had under-estimated the complexity of the issues and the work involved in implementing the LTO and the LTRS (paras. 3.9, 3.10 and 3.23).

10. *Need to set a target LTRS implementation date and devise an action plan.* During 2004-05 to 2009-10, the LR had set target time and devised action plans for implementing the LTRS, and submitted them to the LTO Steering Committee (established by the LR in November 2004 to steer the review of the LTO) for information. However, since then, the LR had not set a target LTRS implementation date and devised an action plan with implementation timetable for steering and coordinating the various work for implementing the LTRS (paras. 3.12 and 3.26).

11. *Need to make additional efforts to implement the LTRS.* In February 2009, a Joint Subcommittee on Amendments to Land Titles Ordinance was established under the LegCo Panel on Development and the LegCo Panel on Administration of Justice and Legal Services to monitor the preparation of amendments to the LTO in a more focused manner and provide input in the bill drafting process. At the meetings of the LegCo Joint Subcommittee held in December 2010 and June 2011, LegCo Members had expressed: (a) disappointment with the poor progress of the Government's work in bringing the new LTRS into operation; (b) concerns that the Government had yet to come to any policy decision after gathering views and concerns from major stakeholders; and (c) regret with the Government's unsatisfactory progress since 2004 in taking forward the LTO amendment exercise. Up to September 2017, the LTO had not yet come into force and the LTRS had not been implemented. To reap the benefits of implementing the LTRS, there is a need for the DEVB and the LR to make additional efforts to implement the LTRS as early as possible, taking into account LegCo Members' concerns (paras. 3.16, 3.29 and 3.30).

Financial issues and performance reporting

12. *Need to conduct regular fee reviews of all fee items.* The LR charges customers statutory fees (specified in the Land Registration Fees Regulations (Cap. 128B)) and non-statutory fees (i.e. those fees not specified in the Regulations) for its services. Since its establishment in 1993, the LR conducted five fee reviews of all fee items at a time interval of 3 to 7 years between each review (i.e. in 1998, 2005, 2008, 2011 and 2016). Audit noted that the fee review in 2016 found that the overall cost recovery rate of non-statutory fees was only 67%. In the event, the LR revised the non-statutory fees in April 2017. The overall fee increase was 75%, with

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certain fee items increased significantly by 100% to 200%. There is scope for the LR to review fees more regularly so that the percentage of fee increase would be more moderate (paras. 4.2, 4.4, 4.7 and 4.8).

13. ***Need to keep under review the business operation and cost recovery of services.*** Registration of document is the LR's main services, which accounted for a high portion of the LR's turnover (ranging from 36% to 56% from 2010-11 to 2016-17). In recent years, the business volume of the services had dropped significantly. The number of land documents delivered for registration had dropped significantly by 45% and the related revenue dropped by 47% from 2010-11 to 2016-17. Audit noted that, for the registration of document services, there was a drastic change from over-recovery of costs of \$93 million in 2010-11 to under-recovery of costs of \$80 million in 2015-16. The significant under-recovery of costs might be one of the factors for the non-achievement of the target rate of return on ANFA in 2015-16 (actual of 4.1% against target of 6.9%). As the LR's business operation is dependent on the property market conditions, there is a need for the LR to keep under review its business operation and the cost recovery of its services, particularly the registration of document services (paras. 4.9 to 4.11).

14. ***Lack of differential pricing for different means of providing a service.*** The LR provides search and copying services by different means of delivery (e.g. counter service and online service). Although the cost for providing a service varied significantly with the means of delivery, the LR charged the same service fee. For example, in 2015-16, the LR charged \$15 for a service fee item while the cost of providing the service through counter was \$105 and online was \$11 (para. 4.12).

15. ***Need to review the compilation of actual performance information.*** Audit examination of the LR's compilation of actual performance information against the 30 performance targets for 2016-17 revealed that, for 24 performance targets, the LR compiled the actual performance information manually on a sample basis. In view of the limited sample size (e.g. 12 working days a year) in the compilation of actual performance information, Audit is concerned whether the compiled results could fairly reflect the LR's actual performance. Audit also noted that the LR relied on a manual system for compiling the actual performance information. There is merit for the LR to consider using more technology in compiling its actual performance information as far as practicable (paras. 4.17, 4.18 and 4.20).

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Audit recommendations

16. Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Land Registrar should:

Provision of services

- (a) update the LR's target completion date for the tidying up exercise of the land registers and endeavour to meet the target date (para. 2.22(a));
- (b) keep under review the errors corrected in the land registers and, where warranted, perform more detailed analysis of the corrected errors for monitoring and taking measures to enhance the accuracy of the land registers (para. 2.22(b));
- (c) keep under review and take measures to further improve the performance of NTSOs, taking into account the cost-effectiveness of operating these offices and the need for their services (para. 2.38(a));

Financial issues and performance reporting

- (d) conduct regular fee reviews of all fee items and revise the fees where necessary (para. 4.14(a));
- (e) keep under review the LR's business operation and the cost recovery of the LR's services, particularly the registration of document services, with a view to taking measures as far as possible to address the impact of the property market conditions on the services (para. 4.14(b));
- (f) consider adopting differential pricing for different means of providing a service (para. 4.14(c));
- (g) critically review the compilation of actual performance information for the 24 performance targets to ensure that the actual performance information is fairly presented (para. 4.26(a)); and

Executive Summary

- (h) consider using more technology in compiling the LR's actual performance information as far as practicable (para. 4.26(c)).

17. Audit has also *recommended* that the Secretary for Development and the Land Registrar should:

Implementation of land title registration system

- (a) fully assess the complexity of the issues and the work involved in taking forward the implementation of the LTRS (para. 3.31(a));
- (b) set a target LTRS implementation date and devise an action plan with timetable for implementing the LTRS as soon as practicable, having regard to the assessment of the complexity of the issues and the work involved, views of stakeholders and the experience gained in the past years (para. 3.31(b));
- (c) report the target LTRS implementation date and submit the action plan to the LTO Steering Committee for consideration (para. 3.31(c)); and
- (d) make additional efforts to implement the LTRS as early as possible, taking into account LegCo Members' concerns and the audit findings on the implementation of the LTRS (para. 3.31(d)).

Response from the Government

18. The Secretary for Development and the Land Registrar generally agree with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

Missions and functions of Land Registry

1.2 The Land Registry (LR), headed by the Land Registrar, aims to provide an efficient and effective land registration system to facilitate the orderly conduct of land transactions. Its missions are to:

- (a) ensure secure and customer friendly land registration and information services;
- (b) develop the LR's human resources, information technology and service environment so as to ensure improvement in service quality and value to its customers; and
- (c) advocate reform of Hong Kong's land registration system through introduction of title registration.

1.3 The LR performs the following main functions:

- (a) registration of documents affecting land (Note 1) under the Land Registration Ordinance (Cap. 128 — the LRO (Note 2)) and maintaining up-to-date land registers (Note 3);

Note 1: *In general, a document affects land if it calls for or prevents a change of land title or itself creates an interest in land.*

Note 2: *The LRO provides for the registration of deeds, conveyances, judgments and other instruments affecting real or immovable property, the keeping of LR records, and other matters relating to land registration.*

Note 3: *A land register records the owner particulars and incumbrances registered against each property.*

Introduction

- (b) provision of facilities for search of the land registers and supply of copies of registered documents and related records;
- (c) provision of property information to government departments and agencies; and
- (d) registration of owners' corporations and maintaining a register of owners' corporations under the Building Management Ordinance (Cap. 344 — the BMO).

Land Registry Trading Fund

1.4 On 1 August 1993, the Land Registry Trading Fund (LRTF) was established under the Trading Funds Ordinance (Cap. 430 — the TFO) to manage and account for the operation of the LR. The LRTF was financed by an initial capital injection of \$118.3 million and a loan of \$236.6 million from the Capital Investment Fund (Note 4). The loan was fully repaid in August 2003.

1.5 The Land Registrar is the General Manager of the LRTF. According to the TFO, the general manager of a trading fund is required to manage the trading fund with the objectives of:

- (a) providing an efficient and effective operation that meets an appropriate standard of service;
- (b) within a reasonable time, meeting expenses incurred in the provision of the government service and financing liabilities of the trading fund out of the income of the trading fund, taking one year with another; and

Note 4: *On 1 April 1990, the Legislative Council established the Capital Investment Fund by Resolution for the purpose of financing investments in the Mass Transit Railway Corporation (which became the MTR Corporation Limited on 30 June 2000), the Kowloon-Canton Railway Corporation, the Hong Kong Housing Authority, the New Hong Kong Tunnel Company Limited and such other bodies as the Finance Committee of the Legislative Council may specify.*

- (c) achieving a reasonable return, as determined by the Financial Secretary, on the fixed assets employed.

As a trading fund, the LR can retain the revenue generated from its business to cover the cost of service provision on a self-financing basis.

Governance framework

1.6 The LR is accountable to the Development Bureau (DEVB — Note 5) and the Financial Services and the Treasury Bureau (FSTB) for its business and financial performance respectively. The DEVB provides policy steer for the LR's work and the FSTB monitors the LR's financial performance.

1.7 A Framework Agreement, which governs the relationship between the Secretary for Development and the Land Registrar (as the head of the LR and the General Manager of the LRTF), came into effect on 1 August 1993. The Framework Agreement sets out the responsibilities of the Secretary and the Land Registrar, and the functions and objectives, services and organisation, financial planning and control, and pay and personnel of the LRTF.

1.8 According to the Framework Agreement:

- (a) the Secretary for Development is responsible for, inter alia:
 - (i) formulating and reviewing the Government's policies and aims with respect to the registration of land;

Note 5: *In July 2007, the DEVB was formed to take up, inter alia, the policy matters on the LR. Before July 2007, the policy responsibilities had been taken up by the then Housing, Planning and Lands Bureau (July 2002 to June 2007), the then Planning and Lands Bureau (January 2000 to June 2002), the then Planning, Environment and Lands Bureau (July 1997 to December 1999), and the then Planning, Environment and Lands Branch (before July 1997). For simplicity, all previous policy bureaux and branch responsible for the policy matters on the LR are referred to as the DEVB in this Audit Report.*

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- (ii) setting the policy objectives of the LRTF; and
 - (iii) setting performance targets for the LRTF in consultation with the Land Registrar; and
- (b) the Land Registrar is responsible to the Secretary for Development for, inter alia:
 - (i) managing and operating the business of the LRTF and achieving the performance targets of the LRTF; and
 - (ii) advising on policy and legislative issues concerning land registration and the registration of title to land.

1.9 Under the Framework Agreement, the LRTF is required to submit annually a medium-range corporate and business plan to the Secretary for Financial Services and the Treasury for approval of the financial aspects of the plan and to the Secretary for Development for the overall approval of the plan. The plan sets out the LR's development for the coming five years and serves as the basis on which the LR's performance is evaluated.

1.10 Under the TFO, the LRTF's annual report, together with the audited financial statements, is required to be tabled in the Legislative Council (LegCo) each year.

Staff strength

1.11 The LR is organised into three functional branches and a number of supporting divisions. An extract of the LR's organisation chart is at Appendix A. As of June 2017, the LR had 583 staff, comprising 484 (83%) civil servants and 99 (17%) contract staff.

Financial performance of LRTF

1.12 Under the TFO, the LRTF is required to achieve a reasonable return on the fixed assets employed (see para. 1.5(c)). According to the FSTB, the rate of return is calculated as the LRTF's total comprehensive income (excluding interest income and interest expenses) divided by its Average Net Fixed Assets (ANFA — Note 6). The target rates of return on ANFA of the LRTF as determined by the Financial Secretary from 1993-94 to 2021-22 were as follows:

Period	Target rate of return on ANFA
1993-94 to 2005-06	10.0%
2006-07 to 2011-12	8.3%
2012-13 to 2016-17	6.9%
2017-18 to 2021-22	5.9%

During the 24-year period from 1993-94 to 2016-17, the LRTF achieved the target rates of return on ANFA except for one year in 2015-16 (see Appendix B).

1.13 Table 1 shows the financial performance of the LRTF from 2012-13 to 2016-17. Breakdowns of the turnover and operating costs of the LRTF for 2016-17 are shown in Figures 1 and 2 respectively.

Note 6: *ANFA is the average of the opening and closing balances of fixed assets in a financial year. Fixed assets for this purpose include property (e.g. land and buildings), plant and equipment, and intangible assets (e.g. computer software licences).*

Table 1

**Financial performance of LRTF
(2012-13 to 2016-17)**

Particulars	2012-13 (\$ million)	2013-14 (\$ million)	2014-15 (\$ million)	2015-16 (\$ million)	2016-17 (\$ million)
Turnover (a)	502	431	412	387	409
Operating costs (b)	362	370	384	373	382
Profit from operations (c) = (a) – (b)	140	61	28	14	27
Other income (Note 1) (d)	30	28	26	32	23
Profit before notional profits tax (e) = (c) + (d)	170	89	54	46	50
Notional profits tax (Note 2) (f)	27	14	8	7	8
Profit for the year (Note 3) (g) = (e) – (f)	143	75	46	39	42
Rate of return on ANFA	34.0%	15.8%	7.8%	4.1%	8.1%
Target rate of return on ANFA	6.9%				

Source: LRTF records

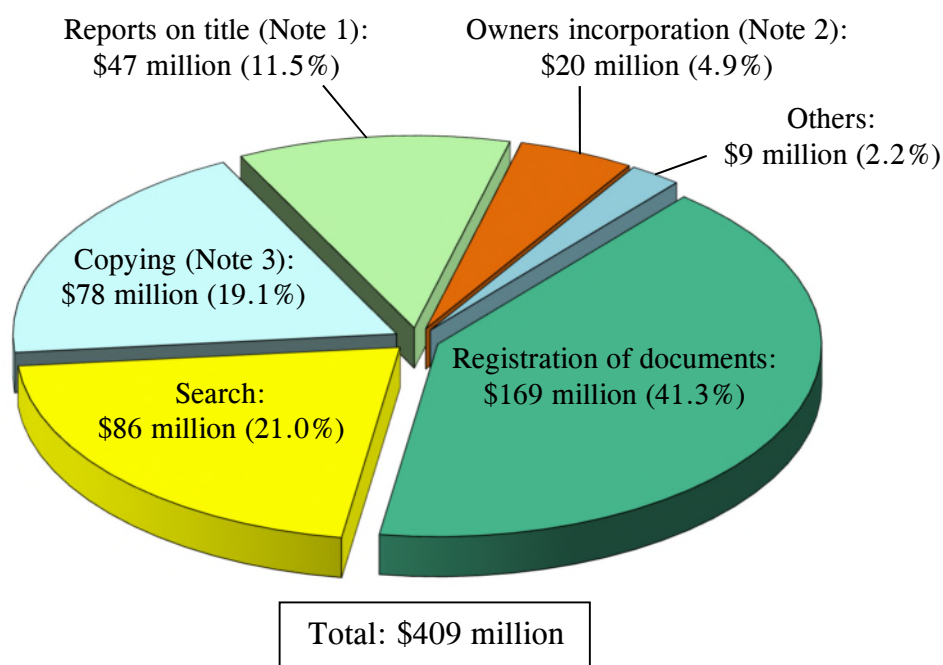
Note 1: Other income mainly included interest income.

Note 2: The LRTF does not need to pay profits tax under the Inland Revenue Ordinance (Cap. 112). However, for trading-fund purposes, it is required to pay the Government an amount equivalent to profits tax payable calculated on the basis of the provisions of the Inland Revenue Ordinance.

Note 3: Profit for the year was the same as total comprehensive income for the year (see para. 1.12) as there was no other comprehensive income.

Figure 1

**Turnover of LRTF
(2016-17)**



Source: LRTF records

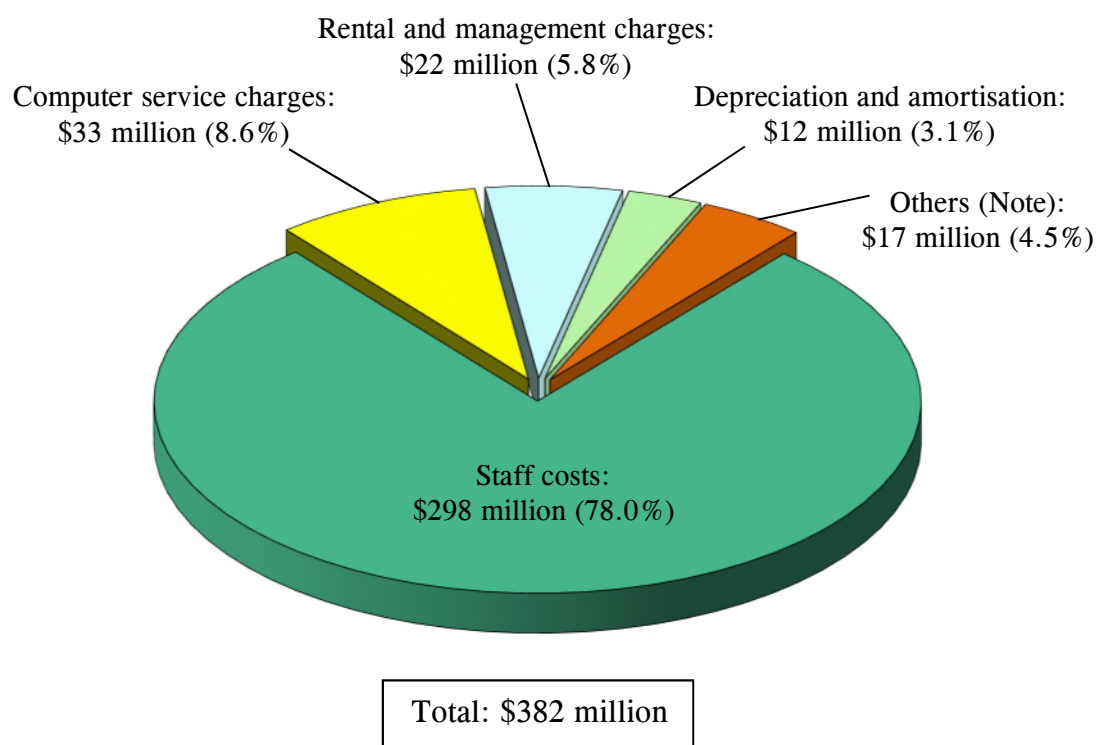
Note 1: “Reports on title” refers to services provided to government bureaux and departments such as conducting searches of the LR records, compiling reports of such searches, and preparing and verifying memorials to accompany documents for registration at the LR.

Note 2: “Owners incorporation” refers to income from services in administering the BMO. According to Financial Circular No. 3/2013 “Charging Arrangements for Trading Funds”, the LRTF collects on the Government’s behalf and pays into the general revenue such fees received from services provided under the BMO. The LRTF charges the Government for the full cost for providing the services under the BMO.

Note 3: “Copying” refers to services for supply of copies of registered documents and related records.

Figure 2

**Operating costs of LRTF
(2016-17)**



Source: LRTF records

Note: Others mainly included general operating expenses and central administrative overheads.

Land registration system in Hong Kong

1.14 At present, Hong Kong operates a deeds registration system (DRS) for recording land and property transactions under the LRO which was enacted in 1844 and is one of the oldest pieces of Hong Kong legislation still in use. The DRS only confers priority on registered deeds and serves as an index of registered instruments to the public. It provides no proof that the person registered as the owner has good title to the property and gives no guarantee to title. In order to establish title to property, it is necessary for the purchaser's solicitors in every case to check the historical title documents relating to all the transactions affecting the property that extend to not less than 15 years (as production of these documents is required under the Conveyancing and Property Ordinance (Cap. 219)) before entering into a new transaction of that property. According to the LR, the advantage of the DRS is its simplicity. The complexities of advice on title are left to the legal profession.

1.15 Since the late nineteenth century, many common law jurisdictions have implemented a land title registration system (LTRS). The LTRS provides conclusive evidence of title to property. It has proved to be an effective system for ensuring security and ease in dealing with property rights in jurisdictions with a high volume of property transactions.

1.16 In July 2004, the Land Titles Ordinance (Cap. 585 — the LTO) was enacted. The LTO aims to provide for a new LTRS that registers the titles to and the interests in land, with a view to providing greater certainty to property titles and simplifying conveyancing. In enacting the LTO, the Government undertook at the request of LegCo to carry out a comprehensive review before bringing the LTO into effect. Up to September 2017, the LTO had not yet been implemented.

Audit review

1.17 In April 2017, the Audit Commission (Audit) commenced a review to examine the operation of the LR. The review focuses on the following areas:

- (a) provision of services (PART 2);
- (b) implementation of LTRS (PART 3); and
- (c) financial issues and performance reporting (PART 4).

Audit has found room for improvement in the above areas, and has made a number of recommendations to address the issues.

Acknowledgement

1.18 Audit would like to acknowledge with gratitude the full cooperation of the staff of the DEVB and the LR during the course of the audit review.

PART 2: PROVISION OF SERVICES

2.1 This PART examines the services provided by the LR, focusing on:

- (a) land registration services (see paras. 2.2 to 2.23); and
- (b) land information and owners' corporation services (see paras. 2.24 to 2.40).

Land registration services

2.2 Land registration services involve the registration of documents affecting land and maintaining up-to-date land registers. The deeds lodgement service is provided at the LR's Customer Centre in the Queensway Government Offices (QGO). According to the LR, there are currently over 3 million land registers (involving a total of about 23.7 million land documents). The number of land documents delivered for registration from 2012-13 to 2016-17 ranged from about 420,000 to 600,000 each year (see Table 2).

Table 2

**Number of land documents delivered for registration
(2012-13 to 2016-17)**

Year	Number of land documents
2012-13	598,843
2013-14	424,634
2014-15	505,894
2015-16	445,889
2016-17	468,630

Source: LR records

Land registration procedures

2.3 The LR's land registration procedures are as follows:

- (a) **Inputting.** Upon receipt of a deed or other document and the accompanying memorial (Note 7) lodged for registration, a Clerical Assistant will input the particulars in the memorial as required under Regulation 10 of the Land Registration Regulations (Cap. 128A) into the Integrated Registration Information System (IRIS — Note 8). The memorial entry will appear in the relevant land register under the “Deeds Pending Registration” section on the following day;
- (b) **Checking.** An Assistant Clerical Officer will scrutinise the document (i.e. first tier checking) to determine whether it is registrable under the LRO and its subsidiary legislation and whether the particulars required by Regulation 6 of the Land Registration Regulations are accurately contained in the memorial. The officer will also check if there are any data input errors and make necessary amendments;
- (c) **Counter checking.** A Clerical Officer will counter check the registration (i.e. second tier checking — Note 9) to ensure that the document is registrable. If the counter checking results are in order, the officer will endorse the registration of the document. The corresponding memorial entry will be moved from the “Deeds Pending Registration” section to the “Owner Particulars” section or “Incumbrances” section (as appropriate) of the relevant land register on the following day; and

Note 7: *A memorial in a form specified under the LRO is required to accompany each document lodged for registration. It contains the particulars of the document (e.g. date and nature of the document, address of the premises affected and name of the parties involved) as required under Regulation 6 of the Land Registration Regulations.*

Note 8: *In February 2005, the LR launched the IRIS to replace the old computer systems which were fully launched in 1997. The IRIS supports more efficient working procedures within the LR, provides Internet based services to customers and can be developed over time to meet new services and changing workload or organisational requirements.*

Note 9: *According to the LR, under the existing registration guidelines, the officer should counter check the registration of certain types of documents including Court Orders, Undertaking, Deed of Grant, Deed of Licence, and Deed of Confirmation.*

- (d) **Imaging.** The registered document will be scanned into the IRIS before it is returned to the lodging party. The imaged document is then made available for public search.

***Need to update target completion date for
tidying up exercise of land registers***

2.4 According to the LR:

- (a) it maintains over 3 million land registers involving registered particulars of about 23.7 million land documents. The particulars entered into the land registers have been accumulated since 1844; and
- (b) throughout the years, land records were kept in different modes which had gone through various changes at different departments responsible for deeds registration, as follows:
 - (i) before 1949, registration of instruments affecting properties in Hong Kong Island and Kowloon was performed by the then Land Office (established in 1844 under the LRO) administered by different departments. In 1949, the Land Office merged with other functions (e.g. the Companies Registry and the then Office of the Official Receiver in Bankruptcy) to form the then Registrar General's Department;
 - (ii) before 1982, registration of instruments affecting properties in the New Territories was performed by the District Land Offices administered by the District Officers or District Land Officers. In 1982, the Registrar General's Department started a phased programme to take over all District Land Offices' land registration functions. Such programme was completed in 1990; and
 - (iii) in May 1993, upon the disestablishment of the Registrar General's Department, the LR was formed to take up the land registration functions of the Department.

Provision of services

2.5 Before 1986, the land registers were kept manually. In 1986, a conversion exercise was commenced to convert the land registers from manual to computerised records (hereinafter referred to as the computerisation exercise). In 1997, the LR completed the computerisation exercise. The computerised records in the old computer systems were then converted to records in the IRIS which was launched in February 2005 (see Note 8 to para. 2.3(a)).

2.6 According to the LR, in the IRIS:

- (a) certain information (e.g. names of owners or nature of registered documents of historical transactions) was not shown in some land registers due to reasons including information that might not have been recorded on the manual land registers before the computerisation exercise or not input into the computerised land registers during the computerisation exercise in view of cost-effectiveness; and
- (b) some computerised land registers contained partial address in the “address” field, with the remaining part of the address in the “property remarks” field, as the length of the “address” field in computerised land registers was limited (before the implementation of the IRIS in 2005).

2.7 To address the information issue of the land registers as mentioned in paragraph 2.6, the LR conducted screening of all its land registers. Since June 2007, the LR has been conducting a tidying up exercise for filling up the related information to meet customers’ expectation of complete land registers and strengthen the reliability of the land records. As of April 2017:

- (a) of the 3.25 million memorial entries (Note 10) with possible particulars found not shown, some 2.5 million (77%) had been checked and updated as needed;
- (b) all of the 120,000 registers with possible partial address had been checked and updated as needed; and

Note 10: *A memorial entry contains major particulars disclosed in a memorial entered into the computerised land register.*

- (c) of the 110,000 registers with possible nature of documents found not shown, some 14,000 (13 %) had been checked and updated as needed. The LR was exploring an approach to update the remaining registers using its information system.

2.8 According to the LR:

- (a) the tidying up exercise was originally targeted for completion by the end of 2018; and
- (b) due to high staff turnover and some vacant contract staff posts not filled, there might be a slippage in completing the exercise.

In Audit's view, in order to strengthen the completeness and reliability of land registers, the LR needs to update its target completion date for the tidying up exercise and endeavour to meet the target date.

Need to enhance accuracy of information in land registers

2.9 According to the LR, typographical errors or discrepancies in the entries in the land registers (collectively referred to as "errors" by the LR) regarding the 23.7 million land documents (see para. 2.4(a)) are identified from time to time by the following means:

- (a) ***Quality control check of LR.*** Apart from the two-tier checking mechanism (see para. 2.3(b) and (c)), LR officers randomly select 50 documents each day from those registered on the same day for checking by repeating the registration procedures for the documents selected. Any discrepancies identified will be investigated and rectified;
- (b) ***Daily operation of LR.*** From time to time, LR officers may spot errors in the land registers when carrying out daily operation (e.g. when processing the registration of documents for a particular property); and

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- (c) ***External parties' amendment requests.*** External parties may request amendment of registered data on the land registers.

The identified errors will be corrected after checking and approval by officers of higher rank (Land Registration Officers).

2.10 The LR classifies the identified errors into the following three types:

- (a) ***Conversion errors.*** They include errors made long time ago when converting the land registers from manual to computerised records in the computerisation exercise completed in 1997 and errors occurred in the manual land registers historically before computerisation which were inherited by the LR from its predecessors (see para. 2.4(b));
- (b) ***Registration errors.*** They are errors made during the course of registration of documents since the commencement of the LRO in 1844; and
- (c) ***Memorial errors.*** They are errors made primarily by the lodging solicitors when completing the memorial for lodging a document for registration (Note 11).

2.11 From 2012-13 to 2016-17, the total number of errors corrected in the land registers each year ranged from 5,737 to 7,564 (see Table 3). The number of conversion errors corrected fluctuated during the years ranging from 2,926 to 5,722. The number of registration and memorial errors in general declined from 2,820 to 1,162 and 728 to 436 respectively in the past five years.

Note 11: *Under Regulation 7 of the Land Registration Regulations, every memorial shall be verified by the lodging party that the memorial contains a just and true account of the several particulars therein set forth as required by the Regulations. According to the LR's registration procedures, its officers are required to check whether the particulars required by Regulation 6 of the Regulations are accurately contained in the memorial (see para. 2.3(b)).*

Table 3

**Number of errors corrected in land registers
(2012-13 to 2016-17)**

Year	Number of errors corrected			
	Conversion errors	Registration errors	Memorial errors	Total
2012-13	3,103 (47 %)	2,820 (42 %)	728 (11 %)	6,651 (100 %)
2013-14	4,309 (57 %)	2,394 (32 %)	861 (11 %)	7,564 (100 %)
2014-15	2,926 (51 %)	2,061 (36 %)	750 (13 %)	5,737 (100 %)
2015-16	3,947 (65 %)	1,520 (25 %)	562 (10 %)	6,029 (100 %)
2016-17	5,722 (78 %)	1,162 (16 %)	436 (6 %)	7,320 (100 %)

Source: Audit analysis of LR records

2.12 To facilitate the conduct of land and property transactions, it is imperative that the land registers contain accurate registered information. While the LR's analysis of the corrected errors by the three types generally gives information of their nature, Audit considers that, to provide better management information for monitoring the accuracy of the land registers, there is merit to perform more detailed analysis of the errors identified. For example, regarding registration errors, it may be beneficial to perform analysis of:

- (a) ***Seriousness of the errors.*** The registration errors may, for example, involve typographical errors of name of property owners and addresses. While the information in the land registers is not conclusive evidence of title to property, errors in the information in the land registers may cause confusion and inconvenience to users of the information; and
- (b) ***Possible causes of the errors.*** Such analysis may also cover how the errors were made and whether any LR officer had persistently made errors for monitoring and taking follow-up actions (e.g. strengthening training for the officers concerned).

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2.13 According to the LR:

- (a) the majority of the errors were identified by LR officers during the quality control check and daily operation (see para. 2.9(a) and (b)), and the rest by external parties;
- (b) the errors were mainly minor in nature, such as typographical errors (e.g. “Agreement for Sale and Purchase” mistyped as “Agreement for Sale and Purchaser”, “XX Bank, Limited” mistyped as “XX Bank Limited” and “Ltd.” mistyped as “Ltd”);
- (c) it had implemented various measures over the years to enhance the accuracy in data input and registration which had attributed to the decline in the number of registration and memorial errors. These measures included the implementation of the e-Memorial Form (see para. 2.15), double data entry of the “consideration” and “premises affected” fields, mandatory second tier checking for certain types of instruments, separating the data input function from the registration function, provision of a comprehensive set of registration guidelines for staff’s compliance and the implementation of a Knowledge Management System for staff’s easy reference;
- (d) conversion errors included errors made long time ago (see para. 2.10(a)). As these errors were historical, it was not possible to ascertain from the manual land registers who made the errors;
- (e) regarding the errors made when converting the land registers from manual to computerised records in the computerisation exercise completed in 1997, the old land registration computer system had already been replaced by the IRIS in 2005 (see Note 8 to para. 2.3(a)). Therefore, performing analysis of these errors was impossible; and
- (f) regarding registration and memorial errors, manual checking of the errors will involve a lot of resources and is not practicable.

2.14 Audit considers that the LR needs to keep under review the errors corrected in the land registers and, where warranted, perform more detailed analysis of the corrected errors for monitoring and taking measures to enhance the accuracy of the land registers.

Need to improve usage of e-Memorial Form

2.15 A lodging party is required to submit a memorial together with the document lodged for registration at the LR (see para. 2.3(a)). In November 2007, to facilitate the lodging party in preparing the memorial, the LR launched an e-Memorial Form as an alternative to the conventional pre-printed form being provided at a cost (\$15 for each book of 100 forms). The e-Memorial Form is an electronic template of the memorial available on the LR's website for free downloading. The e-Memorial Form was enhanced in July 2009 and January 2012 (Note 12).

2.16 Table 4 shows the usage rate of the e-Memorial Form from 2012-13 to 2016-17. While its usage rate had generally increased over the years, the conventional pre-printed forms still accounted for about one-third of the total number of forms received. As the use of e-Memorial Form would improve the efficiency and accuracy of updating the land registers, Audit considers that the LR needs to take measures to further promote the use of e-Memorial Form.

Note 12: *In July 2009, the LR enhanced the e-Memorial Form by adopting the two-dimensional barcode technology so that key particulars filled up in the form were converted into a two-dimensional barcode to be printed on the form. By scanning the barcode, the data therein would be read into the IRIS. In January 2012, two versions of the e-Memorial Form were introduced, namely a basic version with an auto-fill function and another one with data import function.*

Table 4

Usage rates of e-Memorial Forms
(2012-13 to 2016-17)

Year	Total number of pre-printed forms and e-Memorial Forms received (a)	Number of e-Memorial Forms received (b)	Usage rate of e-Memorial Forms $(c) = \frac{(b)}{(a)} \times 100\%$
2012-13	598,843	323,048	54%
2013-14	424,634	238,875	56%
2014-15	505,894	301,986	60%
2015-16	445,889	284,848	64%
2016-17	468,630	318,957	68%

Source: Audit analysis of LR records

*Need to explore the way forward for
the one-stop stamp duty collection and deed registration service*

2.17 A document to be registered at the LR, if chargeable with stamp duty under the Stamp Duty Ordinance (Cap. 117), is required to be duly stamped at the Stamp Office of the Inland Revenue Department (IRD) before it is delivered to the LR for registration. In February 2003, with a view to providing better services to the public, the IRD proposed that the LR could collect stamp duty on behalf of the IRD and provide a one-stop stamp duty collection and deed registration service (hereinafter referred to as the one-stop service). In response, in March 2003, the LR agreed in principle to provide the one-stop service. In December 2005, the LR informed the IRD that amendments to the TFO were required to enable the LR to provide agency services to government departments.

2.18 The one-stop service was originally planned to be launched in August 2006. In June 2006, it was considered that administrative means be explored for implementing the one-stop service as the legislative amendment exercise might not be initiated until after the LTO work (see PART 3) had proceeded first. In September 2006, the LR informed the IRD that the proposed amendments to the TFO would only be taken forward after passing the amendment bill for the LTO. In December 2010, the LR invited the IRD to consider empowering the LR to collect stamp duty on the IRD's behalf through incidental amendments to the Stamp Duty Ordinance.

2.19 In September and October 2017, the IRD informed Audit that:

- (a) the Stamp Duty Ordinance did not prevent arrangements where an entity collected stamp duty on behalf of the IRD. At present, the Hongkong Post, being a trading fund, and some designated convenience stores collect stamp duty on behalf of the IRD without the need of making amendments to the Stamp Duty Ordinance;
- (b) the duty payers could also pay stamp duty via electronic means (e.g. credit card);
- (c) in 2006, the IRD considered that the one-stop service might be able to boost the take-up rate of the e-Stamping service (launched in August 2004 with the take-up rate of around 40% at that time) and would save time for stamping and registration; and
- (d) in 2016-17, the e-Stamping service take-up rate increased to 75%, which indicated that the e-Stamping service had been well received by the public. Thus, the IRD considered that there was no urgent need to implement the one-stop service.

2.20 In September and October 2017, the LR informed Audit that:

- (a) although the convenience that the one-stop service could bring to customers might not be as great as initially envisaged with the introduction of online payment of stamp duty by the IRD, the LR was still exploring the option as proposed by the IRD; and

- (b) the Hongkong Post was empowered under the subsidiary legislation of the TFO for the Post Office Trading Fund (Cap. 430E) to provide agency services for government departments, public bodies and public utilities. Under this provision, the Hongkong Post could collect stamp duty on the IRD's behalf without any corresponding amendments to the Stamp Duty Ordinance. As there was no similar provision under the subsidiary legislation of the TFO for the LRTF (Cap. 430A) empowering the LR to provide agency services for government departments, and the services to be provided by the LRTF as specified under the subsidiary legislation included "any service that the Land Registrar may be authorised to provide under or by virtue of any Ordinance", amendments to either the subsidiary legislation or the Stamp Duty Ordinance would be required to enable the LR to collect stamp duty on behalf of the IRD.

2.21 In Audit's view, to provide better services to the public, the LR needs to, in collaboration with the IRD, explore the way forward for the one-stop service.

Audit recommendations

2.22 **Audit has *recommended* that the Land Registrar should:**

- (a) **update the LR's target completion date for the tidying up exercise of the land registers and endeavour to meet the target date;**
- (b) **keep under review the errors corrected in the land registers and, where warranted, perform more detailed analysis of the corrected errors (e.g. seriousness and possible causes of the errors) for monitoring and taking measures to enhance the accuracy of the land registers;**
- (c) **take measures to further promote the use of e-Memorial Form; and**
- (d) **in collaboration with the Commissioner of Inland Revenue, explore the way forward for the one-stop stamp duty collection and deed registration service.**

Response from the Government

2.23 The Land Registrar generally agrees with the audit recommendations. She has said that the LR will explore using the IRIS for tracking and monitoring the errors that were made after the implementation of the IRIS in 2005.

Land information and owners' corporation services

Search and copying services

2.24 The LR provides services for searching land registers and supplying copies of registered documents and related records. Search and copying services are provided over the Internet via the IRIS and search counters at the Customer Centre in the QGO and three New Territories Search Offices (NTSOs) in Tsuen Wan, Tai Po and Yuen Long. During 2012-13 to 2016-17, about 90% of searches had been conducted online and the remaining 10% over the counter (see Table 5).

Provision of services

Table 5

**Search and copying services
(2012-13 to 2016-17)**

Service	2012-13 (No.)	2013-14 (No.)	2014-15 (No.)	2015-16 (No.)	2016-17 (No.)
<i>Search services</i>					
Online search	5,011,354 (91 %)	4,260,234 (91 %)	4,738,037 (92 %)	4,647,371 (92 %)	4,893,606 (92 %)
Counter search	474,907 (9 %)	410,299 (9 %)	434,553 (8 %)	399,435 (8 %)	426,355 (8 %)
Total	5,486,261 (100 %)	4,670,533 (100 %)	5,172,590 (100 %)	5,046,806 (100 %)	5,319,961 (100 %)
<i>Copying services</i>					
Imaged copies and photocopies of land records supplied	795,329	829,181	778,354	797,303	747,969

Source: Audit analysis of LR records

Owners' corporation services

2.25 The LR is responsible under the BMO and the TFO for carrying out owners' corporation services, including:

- (a) processing and approval of applications for owners' corporation registration;
- (b) issuing certificates of registration;
- (c) maintenance of a register of corporations;

- (d) filing of the prescribed documents under the BMO in individual corporation files; and
- (e) provision of search services of the register of corporations and the corporation files (hereinafter referred to as the owners' corporation records) to the public.

2.26 The owners' corporation records are kept manually in the LR offices in the QGO and the three NTSOs based on the districts where the owners' corporations are situated (Note 13). These offices provide owners' corporation services on a district basis. As of June 2017, there were 10,550 owners' corporations, of which 8,780 (83%) were served by the QGO office and 1,770 (17%) by the three NTSOs.

Need to keep under review performance of NTSOs

2.27 ***Financial performance.*** The three NTSOs in Tsuen Wan, Tai Po and Yuen Long (each manned by four to five staff and located at government buildings with net floor area of 80 square metres to 146 square metres) provide counter search and copying, and owners' corporation services. Audit noted that all the three NTSOs had incurred operating losses ranging from \$0.9 million to \$2 million each year during 2012-13 to 2016-17 (see Table 6). The operating losses for the NTSOs in Tsuen Wan, Tai Po and Yuen Long had, in general, been increasing during the first four years and decreased in 2016-17. Their respective operating losses in 2016-17 were \$1.3 million, \$1.1 million and \$1.6 million.

Note 13: *The owners' corporation records are kept in the relevant LR offices as follows:*

<i>LR office</i>	<i>Districts where the owners' corporations are situated</i>
<i>QGO office</i>	<i>Hong Kong Island, Kowloon and Islands</i>
<i>Tsuen Wan Search Office</i>	<i>Tsuen Wan and Tuen Mun</i>
<i>Tai Po Search Office</i>	<i>North, Sai Kung, Sha Tin and Tai Po</i>
<i>Yuen Long Search Office</i>	<i>Yuen Long</i>

Table 6

Operating losses of three NTSOs
(2012-13 to 2016-17)

NTSO	Operating loss (\$'000) (Note 1)				
	2012-13	2013-14	2014-15	2015-16	2016-17 (Note 2)
Tsuen Wan	1,412	1,776	1,977	2,031	1,328
Tai Po	1,214	1,178	1,642	1,861	1,077
Yuen Long	887	1,513	1,603	1,666	1,570

Source: LR records

Note 1: According to the LR: (a) the income of the NTSOs in Tsuen Wan, Tai Po and Yuen Long could normally cover their direct operating costs; (b) their income was not able to cover their direct operating costs only occasionally; and (c) during 2012-13 to 2016-17, the NTSO in Tsuen Wan was not able to cover its direct operating costs from 2013-14 to 2015-16 while the NTSOs in Tai Po and Yuen Long were not able to cover their direct operating costs only in 2015-16.

Note 2: According to the LR, the decrease in operating loss for each of the three NTSOs in 2016-17 was mainly due to the increase in business volume in general and the increase in reimbursement from the Home Affairs Department for administering the BMO mainly arising from the rectification of charging basis (i.e. including accommodation costs for the area of public search and storage space of owners' corporation records in the calculation) in order to recover full costs incurred in providing the required services under the BMO with effect from 2015-16 (resulting in an increase in 2016-17 reimbursement and the recovery of 2015-16 under-provision in 2016-17).

Remarks: The revenue of NTSOs included fees received from search and copying services, and reimbursement from the Home Affairs Department for administering the BMO while the expenditure included staff costs, rental and management charges, other operating expenses and allocated costs from the LR Headquarters.

2.28 ***Operational performance.*** The operational performance of each of the three NTSOs for the five-year period from 2012-13 to 2016-17 is shown at Appendix C. Audit noted that:

- (a) for each of the five years, the daily average number of visitors requesting search and copying services was below 55 for the NTSOs in Tsuen Wan and Tai Po, and below 100 for the NTSO in Yuen Long. The daily average number of visitors were 35, 40 and 76 for the respective NTSOs in 2016-17;
- (b) for each of the five years, the daily average number of visitors requesting owners' corporation services at each NTSO was not more than 5. The daily average number of visitors had been dropping from 5 to 3 for the NTSO in Tai Po. The NTSO in Yuen Long had the lowest daily average number of visitors of 2 to 3 for each of these years;
- (c) the demand for search and copying services at each NTSO had fluctuated during the five-year period. In 2016-17, each NTSO processed around 51,000 to 64,000 search requests and around 4,000 to 9,000 copying requests; and
- (d) the demand for owners' corporation services had fluctuated during the five-year period. Each NTSO processed not more than 15 registration applications during each of the five years and handled not more than 47 inspections in 2016-17.

2.29 ***Proposal to close the three NTSOs shelved.*** Before May 2009, the LR had four other NTSOs located in the North District, Sai Kung (both offices closed in April 2007), Tuen Mun (closed in May 2008) and Sha Tin (closed in May 2009). In view of the decreasing demand for counter services and cost-effectiveness in maintaining these offices, after consulting the Home Affairs Department (HAD — Note 14) and the related District Councils, the LR closed these offices. In June 2009, the LR further consulted the HAD on its proposal to close the remaining three NTSOs and centralise their services at the Customer Centre in the QGO in view of the low

Note 14: *The Secretary for Home Affairs, who is the authority of the BMO, is responsible for administering the legislation and providing the resources for the owners' corporation services. The HAD is the executive department regarding owners' corporation matters.*

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demand for their services and their continued operating losses. In July 2009, the HAD stated that it did not support the proposal because:

- (a) the LR's proposal acted against the Government's policy objective of promoting effective building management and maintenance; and
- (b) owners' corporation services should be easily accessible and the LR's proposal would cause great inconvenience and difficulty to residents in the New Territories. The HAD envisaged that there would be considerable objection and concerns from the public and LegCo.

The LR's proposal has since then been shelved.

2.30 In view of their continued operating losses and low patronage (see paras. 2.27 and 2.28), Audit considers that the LR needs to keep under review and take measures to further improve the performance of NTSOs, taking into account the cost-effectiveness of operating these offices and the need for their services.

Need to explore the feasibility of computerising owners' corporation records

2.31 At present, the LR keeps owners' corporation records manually at the offices concerned (see para. 2.26). It considers that computerisation of the records would bring about benefits (e.g. preserving records in a more secure way, enabling the provision of cross-district search services, and enhancing operational efficiency and cost-effectiveness in the maintenance, access and backup of related records).

2.32 In October 2011, the LR proposed to the HAD to computerise owners' corporation records, including the keeping, maintaining and searching of the records. In response, in April 2012, the HAD said that the proposed computerisation project was supported having regard to the growing trend towards e-services provided by the Government. In June 2012, the LR informed the HAD of the estimated cost of the feasibility study and the need for legislative amendments to the BMO to support computerisation of owners' corporation records without parallel running of the manual operations. Pending the availability of funding for the feasibility study, in July 2013, the LR further proposed to the HAD to proceed direct to system analysis and design stage of the proposal in order to save cost and time. The proposal was later shelved

because of the need to sort out the appropriate funding arrangement for the proposal. In March and May 2017, having regard to the trend towards e-services provided by the Government, the LR revisited the computerisation proposal with the HAD. In June 2017, the HAD agreed to consider incorporating suitable express enabling provisions in the BMO to pave the way for operating the electronic mode of owners' corporation services, whilst the appropriate funding arrangement should be explored in parallel. In Audit's views, the LR needs to, in collaboration with the HAD, explore the feasibility of computerising the owners' corporation records.

Low subscription of e-Alert service for property owners

2.33 In July 2015, the LR launched an e-Alert service for subscription by property owners to improve customer service. Under the service, when a document is lodged for registration against a relevant property, an e-mail notification will be sent to the owner.

2.34 According to the LR:

- (a) the majority of the start-up costs for developing the e-Alert service for property owners had been absorbed by the LR's existing resources. The costs of hiring contract staff to assist in the development of the service amounted to about \$0.95 million;
- (b) recurrent costs in providing the service had been absorbed by the LR's existing resources; and
- (c) it had carried out a number of promotional activities for the service, including issuing press release, posting related message on its website, issuing letters to owners' corporations and displaying posters and/or distributing leaflets at its offices, public libraries and community halls.

2.35 Audit noted that for the e-Alert service for property owners, in the fee proposal submitted to the FSTB for approval in February 2015, the LR estimated that the number of subscription orders would reach about 41,000 per year. However, during the two-year period from July 2015 (launch of the e-Alert service) to June 2017, the LR had only received 263 subscription orders (with revenue of some

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\$38,000) for the service, falling far short of the LR's estimate of 41,000 orders per year.

2.36 In September 2017, in response to Audit's enquiry, the LR said that:

- (a) the LR had conducted customer service survey, online survey and face-to-face interview at its customer counter to assess the potential demand for the e-Alert service for property owners. In light of the very favourable responses collected from the survey/interview, in the fee proposal first submitted to the FSTB for approval in December 2012, the LR estimated that the number of subscription orders would reach about 41,000 per year; and
- (b) since the e-Alert service for property owners was a new service and there was no previous business volume for reference, the 41,000 subscription orders per year was only a guestimate that could be made by the LR.

2.37 In view of the low subscription of the e-Alert service for property owners, Audit considers that the LR needs to ascertain the reasons for the low subscription and make continued efforts to improve and promote the service.

Audit recommendations

2.38 **Audit has *recommended* that the Land Registrar should:**

- (a) **keep under review and take measures to further improve the performance of NTSOs, taking into account the cost-effectiveness of operating these offices and the need for their services;**
- (b) **in collaboration with the Director of Home Affairs, explore the feasibility of computerising the owners' corporation records; and**
- (c) **ascertain the reasons for the low subscription of the e-Alert service for property owners and make continued efforts to improve and promote the service.**

Response from the Government

2.39 The Land Registrar generally agrees with the audit recommendations. She has said that:

- (a) the LR will continue with efforts to improve the performance of the NTSOs. Possible measures will be explored to improve the performance of the NTSOs;
- (b) the HAD did not support the proposal to close the three NTSOs (see para. 2.29); and
- (c) maintenance of the three NTSOs for the operation and delivery of services requires a minimum number of staff. On-going performance monitoring is in place to optimise manpower utilisation in the NTSOs. For example, staff of the NTSOs have been assigned additional tasks of preparing reports on owners' corporation records for "reports on title" requested by government departments and agencies, and compiling returns to the HAD on registration of owners' corporations and filing of documents.

2.40 The Director of Home Affairs agrees with the audit recommendation in paragraph 2.38(b).

PART 3: IMPLEMENTATION OF LAND TITLE REGISTRATION SYSTEM

3.1 This PART examines the work of the DEVB and the LR in implementing the LTRS.

Background

Limitations of DRS

3.2 At present, the LR operates the DRS for recording interests in land and property in Hong Kong through a system of registering deeds. The DRS only confers priority on registered deeds and gives no guarantee to title (see para. 1.14). In order to establish title, every time there is a transaction of a property, the title documents have to be checked again.

3.3 According to the LR, although the DRS in Hong Kong has been modernised through computerisation, the DRS has inherent limitations, including the following:

- (a) over time, uncertainties can arise as to the interpretation of the various documents, which can give rise to the delays, costs of litigation and difficulty in dealing with particular properties;
- (b) there are rights over property (called unregistered interests) that are allowed by the common law even though they have not been registered. The fact that unregistered interests may exist gives rise to uncertainties, costs and complications in conveyancing; and
- (c) safekeeping of the huge volumes of historical documents on each property is a burden for banks and individual owners. There is risk of damage, loss or theft.

Converting to LTRS desirable

3.4 Many common law jurisdictions have implemented the LTRS since the late nineteenth century. Under the LTRS, the title to land and property is registered. The title register provides conclusive evidence of title to property and it is no longer necessary to review the historical title documents to prove title. The Government started to review the desirability of converting the DRS to the LTRS in May 1988 and concluded it desirable to do so in December 1988 (Note 15).

LTO not implemented long time after its enactment

3.5 The Government introduced a Land Titles Bill in 1994 and a revised one in 2002 into LegCo (see paras. 3.8 and 3.9). In July 2004, the LTO was enacted. The LTO aims to provide for the LTRS which will bring about benefits of providing greater certainty to property titles and simplifying the procedures of checking title documents upon conveyancing (see Appendix D for the main features of the two systems). However, up to September 2017, the LTO had not yet come into force and the LTRS had not been implemented.

3.6 Over the years, the implementation of the LTRS involved various complex issues. In general, there were considerable deliberations and divergent views among various stakeholders on the following three main issues:

- (a) conversion mechanism:
 - (i) the conversion mechanism is the means to bring existing land and properties to which the LRO currently applies over to the titles registered under the LTRS, and governs how the unregistered interests that may exist under the common law are to be handled during the conversion; and

Note 15: *In May 1988, a Working Party on Title Registration, chaired by the then Registrar General (head of the then Registrar General's Department — see para. 2.4(b)) with members comprising practising solicitors and academia, was set up to consider the desirability of converting the DRS to the LTRS. In December 1988, the Working Party, after considering the major types of registration systems operating in other jurisdictions, concluded that conversion to the LTRS was desirable.*

Implementation of land title registration system

- (ii) during the deliberations, there existed divergent views on the conversion mechanism among stakeholders. Some stakeholders preferred a compulsory and automatic conversion arrangement (i.e. all land registers would be converted to the LTRS immediately on the commencement day of the LTO or automatically by the end of an interim period), while other stakeholders preferred to convert the existing land registers gradually;
- (b) rectification arrangements:
 - (i) where the title register becomes inaccurate due to fraud, a void or voidable instrument, mistake or omission, it may be rectified. Rectification refers to the procedures to allow for correcting errors in the title register, including dealing with whether to restore an innocent former owner's title to a property if he has lost it as a result of fraud; and
 - (ii) during the deliberations, some stakeholders objected to the mandatory rectification rule (the MR rule — see para. 3.11(b)) as it might undermine public confidence in the title register as conclusive evidence of titles, while others considered it necessary to retain the rule so that the defrauded former owners could recover their properties; and
- (c) indemnity arrangements:
 - (i) a person who has relied on the title register and suffered loss due to its inaccuracy (as a result of fraud by any person resulting in loss of ownership, or loss due to any mistake or omission of LR officers) may claim indemnity. Indemnity is the compensation that will be paid to an innocent person if he suffers loss due to such inaccuracy in the title register; and
 - (ii) during the deliberations, the Government considered that a cap should be set on the indemnity for each case of loss of title due to fraud, while some stakeholders expressed concerns on setting a cap and the level of the cap if one had to be set.

According to the LR, the three main issues are highly complex and closely interrelated, such that proposals to address one issue would have implications on the other two issues. The LR also considers that, in addition to these three main issues, the implementation of the LTRS involves complicated legal concepts and technical issues, which require detailed consideration (e.g. treatment of existing rights under the common law and unregistered interest created prior to the implementation of the LTRS, and interface with other legislation (see para. 3.14(c)(i)).

3.7 The work of the DEVB and the LR in the implementation of the LTRS is shown in paragraphs 3.8 to 3.22 and a summary of the LR's proposals to address the three main issues is at Appendix E. Audit has found room for improvement in their work (see paras. 3.23 to 3.31).

Government's efforts in implementation of land title registration system

3.8 ***Land Titles Bill introduced in 1994.*** In November 1994, the Government introduced a Land Titles Bill into LegCo with a view to converting the DRS to the LTRS. The Bills Committee had concerns on certain provisions in the Bill (mainly related to the automatic conversion mechanism, known as midnight conversion — Note 16). Since the issues could not be resolved before the end of the legislative session in July 1995, the Bill lapsed.

3.9 ***Revised Land Titles Bill introduced in 2002.*** After the lapse of the Bill in 1995, the Government maintained dialogue with various stakeholders and a number of amendments were subsequently made to the original Bill. After consulting the then LegCo Panel on Planning, Lands and Works (in January and November 1999 and July 2002) and further consulting concerned parties, in December 2002, the Government introduced a revised Land Titles Bill into LegCo (2002 Bill). The 2002 Bill proposed to convert the land registers under the DRS to the LTRS gradually with conversion to take place upon the first transfer of the property supported by a solicitor's certificate of good title (known as gradual conversion). A Bills Committee was formed to scrutinise the 2002 Bill during March 2003 to June 2004.

Note 16: *Under the proposed midnight conversion mechanism, land registers under the DRS would be deemed to be title registers under the LTRS automatically on the day when the new system came into operation.*

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3.10 ***Enactment of LTO in 2004.*** During the scrutiny of the 2002 Bill by the Bills Committee, due to reservation about the requirement for a solicitor's certificate of good title, the conversion mechanism was revised to allow for automatic conversion of existing land registers. The Government proposed to commence the LTO two years after its enactment so as to allow sufficient time for putting in place the relevant regulations and finalising the guidance notes for legal practitioners and members of the public. The Government also undertook to conduct a review of the LTO during the two-year period between its enactment and commencement (post-enactment review) and to take follow-up actions on various issues (Note 17) raised during the scrutiny of the Bill by the Bills Committee. In the event, the 2002 Bill (as amended by all the amendments moved by the Government during the scrutiny by the Bills Committee) was passed by LegCo and the LTO was enacted in July 2004.

3.11 Under the enacted LTO, the three main issues are, in general, addressed as follows:

- (a) ***Conversion mechanism.*** Due to reservations about the requirement for a solicitor's certificate of good title under the gradual conversion mechanism (see para. 3.9), an automatic conversion mechanism known as daylight conversion is introduced, as follows:
 - (i) from the commencement day of the LTO, new land will be registered under the LTRS;

Note 17: *These issues mainly involved follow-up actions on four areas, namely: (1) making of rules and regulations; (2) preparation of guidelines and guidance notes; (3) consideration of further consequential amendments arising from the Bill; and (4) review of various clauses of the Bill after its enactment.*

- (ii) upon the expiry of a 12-year period (from the commencement day), all existing land registered under the LRO will be brought automatically to the LTRS except where either a caution against conversion (Note 18) stands or where matters lodged for registration under the LRO have not yet completed registration; and
 - (iii) during the 12-year period, all unregistered interests could be protected by registration of a notice of a claim known as caveat under the LRO;
- (b) ***Rectification arrangements.*** The court shall order the rectification of the title register in favour of an innocent former owner who lost his title as a result of fraud and a void instrument (referred to as the MR rule) and the innocent purchaser will be protected by a capped indemnity (see (c) below). The LR may rectify any error or omission on the LR's volition if the rectification will not materially affect the owner's interest. For other cases on application, the court may order rectification if it is satisfied that the entry was obtained or omitted as a result of mistake, omission, or a void or voidable instrument; and
- (c) ***Indemnity arrangements.*** There will be an indemnity scheme for an innocent person who suffered loss due to an inaccuracy in the title register. For the loss due to an entry in or omitted from the register as a result of mistake or omission of LR officers, full compensation will be provided. For the loss due to fraud which resulted in the loss of ownership of a property, the indemnity payable would be capped at the lesser of the value of interest in land or an amount determined by the Financial Secretary by notice published in the Gazette. The proposed cap is \$30 million for each case.

Note 18: *Cautions against conversion to the title register can be registered under the LRO within the 12-year period. Such cautions may be registered only in respect of any claim of title to the land or beneficial interest in the land, and will lapse after 12 months unless the cautioner has commenced court proceedings to establish his claim. Cautioners are required to take prompt action to bring a conclusion to the dispute on title or interest.*

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3.12 *Post-enactment review.* In November 2004, the LR established a Land Titles Ordinance Steering Committee (the LTO Steering Committee — Note 19) to steer the review of the LTO (see Appendix F for its terms of reference).

3.13 In May 2007, the Government informed the then LegCo Panel on Planning, Lands and Works that:

- (a) the estimated time of taking at least two years to carry out the post-enactment review and preparatory work was made on the assumption that the main outstanding work was in relation to the subsidiary legislation, not the principal ordinance;
- (b) the Government had either resolved or identified solutions for most of the issues (see Note 17 to para. 3.10) raised during the scrutiny of the 2002 Bill by the Bills Committee;
- (c) however, during the post-enactment review of the LTO, further issues (Note 20) were identified. These involved significant matters where amendments to the LTO were essential before the legislation could be brought into operation; and
- (d) substantial amendments to the LTO were required to ensure the efficient operation of the new system. A Land Titles (Amendment) Bill (LT(A)B)

Note 19: *The LTO Steering Committee is chaired by the Land Registrar, and comprises 6 official members (including representatives from the DEVB, the LR, the Lands Department and the Department of Justice) and 7 non-official members (i.e. representatives from The Law Society of Hong Kong, The Real Estate Developers Association of Hong Kong, the Hong Kong Association of Banks, The Hong Kong Mortgage Corporation Limited, the Estate Agents Authority, the Consumer Council and the Heung Yee Kuk).*

Note 20: *There were a total of 18 issues which included: (1) concept of registration of instruments; (2) instruments not effectual until registered; (3) date of registration; (4) overriding interests; (5) severance of joint tenancy; (6) consequential amendments in other legislation; (7) court orders; (8) transmission; (9) cautions; (10) caveats; (11) definitions in the LTO; (12) liability of government; (13) filing of standard terms documents; (14) restriction order; (15) rectification by the Land Registrar; (16) indemnity provisions; (17) exclusion; and (18) practical implications.*

would be prepared and submitted to LegCo before commencement of the new system.

3.14 In December 2008, the Government informed the LegCo Panel on Development that, in addition to the ongoing effort to deal with matters reported in May 2007, there remained several substantial matters arising from the post-enactment review awaiting finalisation before the LT(A)B could be brought to LegCo for consideration, as follows:

- (a) ***Modifications to conversion mechanism.*** The LR found that:
 - (i) there were cases where ownership of property could not be determined from the land register known as indeterminate ownership registers (e.g. multiple registers of same lot number or single register that appears to contain more than one chain of title to the same property). Under the enacted LTO, there was no mechanism for the Government to withhold these cases from conversion or to deal with the consequences if they were converted automatically; and
 - (ii) there was a risk that, upon conversion, the title register might be inaccurate and the Government might be liable for any loss caused to parties due to inaccuracy in the title register. The Government might be exposed to unknown liabilities from the conversion day unless pre-conversion screenings of each individual land register were conducted;
- (b) ***Rectification and indemnity arrangements.*** The LR found that:
 - (i) the MR rule (see para. 3.11(b)) might have the unintended effect of reducing confidence in the title register and reducing the effectiveness of the LTRS in improving the efficiency with which conveyancing could be conducted; and
 - (ii) various provisions in the enacted LTO needed to be clarified and some new provisions needed to be added to remove ambiguities and reduce the risk of disputes that might slow down the resolution of claims for indemnity and add to costs; and

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- (c) ***Other matters.*** The LR found that:
- (i) ***Relationship between the LTO and other legislation.*** Under the enacted LTO, other legislation was allowed to prevail over the LTO. However, during the post-enactment review, the LR noted that there should be clarity as to how the provisions of the LTO would operate in relation to provisions in other legislation. For example, where another legislation could not stand together or run in parallel with the LTO, a decision should be made on which one should prevail; and
 - (ii) ***Arrangements for updating land boundaries.*** Under the DRS, land boundaries are not guaranteed. The enacted LTO provided an avenue for land owners to apply to the Director of Lands for determination of boundaries regarding their lots (brought under the LTO) and registration of the resultant plans in the LR (Note 21).

The Government also informed the Panel that a three-month public consultation would be launched to solicit public views and submitted the consultation papers to the Panel in December 2008.

3.15 ***Public consultation in 2009.*** From January to March 2009, a three-month public consultation was conducted to gauge views from the public and stakeholders regarding a modified conversion mechanism, and proposed modifications to the rectification and indemnity arrangements to address the issues mentioned in paragraph 3.14(a) and (b). Under the consultation papers, a gradual upgrading conversion approach was proposed, and exceptions to the MR rule were introduced to confine its scope of application. The consultation revealed that the public in general supported retaining the automatic conversion mechanism under the enacted LTO and preserving the MR rule (see para. 3.11(a) and (b)).

Note 21: *The Government subsequently considered it more appropriate to examine the issues of land boundaries as a separate exercise from the amendment of the LTO in view of the complexity of the issues.*

3.16 ***Set up of a Joint Subcommittee in 2009.*** In February 2009, in view that the preparation of amendments to the LTO involved important and complicated issues, a Joint Subcommittee on Amendments to Land Titles Ordinance (the LegCo Joint Subcommittee) was established under the LegCo Panel on Development and the LegCo Panel on Administration of Justice and Legal Services to monitor the work in a more focused manner and provide input in the bill drafting process.

3.17 ***Two-stage conversion mechanism.*** Subsequent to the public consultation conducted in 2009, there were divergent views from stakeholders as to the application of the MR rule (see para. 3.11(b)). A key stakeholder expressed that the MR rule would undermine the certainty of title and conclusiveness of the title register, and work against the objective of simplifying conveyancing procedures. This was because a purchaser might be encouraged to go behind the title register to investigate previous transactions in order to obtain greater assurance that his title would not be at risk. The stakeholder advocated the adoption of immediate indefeasibility of titles (Note 22) to ensure title certainty for current owners. However, the idea was opposed by another key stakeholder who strongly favoured the retention of the MR rule under the enacted LTO to protect the interests of innocent former owners. In May 2011, the Government proposed a two-stage conversion mechanism (see Appendix G for details) and modifications to the rectification and indemnity arrangements to address the conflicting views and balance the concerns of various stakeholders.

3.18 ***Dissolution of LegCo Joint Subcommittee.*** At the meeting of the LegCo Joint Subcommittee in June 2011:

- (a) the Government reported the latest positions of the follow-up actions taken on issues identified by the Bills Committee (see Note 17 to para. 3.10) and further issues identified during the post-enactment review (see Note 20 to para. 3.13(c));
- (b) the Government informed the LegCo Joint Subcommittee that:

Note 22: *Under the principle of “immediate indefeasibility”, a bona fide purchaser for value who relies on the title register in dealing with the registered owner, registers a transfer and takes possession of the property obtains an indefeasible title, even though the transfer instrument to the owner with whom he has dealt with is void for fraud or forged.*

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- (i) the stakeholders indicated that they would examine the proposed two-stage conversion mechanism and revert with their comments. The Government aimed to come up with a consolidated proposal that was acceptable to the stakeholders by the end of 2011, and thereafter consulted the public on the proposal for amending the LTO during the first and second quarters of 2012; and
- (ii) while the Government would simultaneously continue with the preparation of the necessary amendments to the LTO, the Government would only be able to come up with a full package of the necessary amendments after consideration of the views received from the public;
- (c) the LegCo Joint Subcommittee agreed that there should be no need to continue its work in the 2011-12 legislative session as the Government would mainly engage the stakeholders represented in the LTO Steering Committee and thereafter the public in the coming year with a view to arriving at a general consensus on the way forward for the implementation of the LTO; and
- (d) the Chairman of the LegCo Joint Subcommittee considered that it would be appropriate for the Government to report the work progress with relevant proposals to the Panel on Development and the Panel on Administration of Justice and Legal Services after formulating a full package of the necessary amendments to the LTO.

In the event, in October 2011, the LegCo Joint Subcommittee was dissolved after submitting a report to the LegCo Panel on Development and the LegCo Panel on Administration of Justice and Legal Services.

3.19 ***Revised two-stage conversion mechanism.*** In June 2013, taking into account comments received from members of the LTO Steering Committee on the proposed two-stage conversion mechanism (see para. 3.17), the LR further revised the conversion proposal for members' comments (Note 23).

3.20 ***Four conversion options for existing land.*** In developing the revised two-stage conversion mechanism proposal in 2013, the LR considered that basic screening (Note 24) of land registers to identify cases with broken or multiple title chains was necessary as it would help reduce the LR's indemnity risks in view of the unlimited liability for the indemnity payment due to mistake or omission of LR officers (see para. 3.11(c)). The LR thus explored further options for conversion of existing land registered under the LRO with basic screening incorporated. In June 2014, the LR put up four conversion options (see Appendix H for details) for comments by the members of the LTO Steering Committee. During June 2014 to November 2016, the LR had conducted various discussions and exchanged views with individual members of the LTO Steering Committee on the four conversion options.

3.21 In December 2016, the LTO Steering Committee held a meeting to discuss the four conversion options and consolidate stakeholders' views in taking forward the LTO review exercise. At the meeting, the majority of members indicated support for implementation of the LTRS on new land only at this stage (i.e. "new land first" proposal under Option D — Appendix H) as this option would secure an early implementation of the LTRS in Hong Kong and would enable early enjoyment of

Note 23: *For example, the LR proposed to amend the opt-out caution mechanism for preserving the MR rule (see item (c) in Appendix G) as follows:*

- (a) only owner of existing land registered under the LRO who is the registered owner on the date of primary conversion may register an opt-out caution once during the 12 years from primary conversion;*
- (b) once registered, the opt-out caution has to be withdrawn before subsequent transfer or transmission of the land can be accepted for registration; and*
- (c) there will not be automatic full conversion until the registration of a withdrawal of the opt-out caution.*

Note 24: *Basic screening is a simple and cursory check of the entries shown on the land registers and the memorials of the registered instruments affecting ownership of the property for identifying any apparent broken or multiple chains of title. Registered instruments would not be checked unless necessary.*

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benefits by the public. One key stakeholder expressed disagreement with the need to do any screening of the land registers and insisted that the idea of mass conversion of all titles at one time as provided in the LTO should be maintained. The Land Registrar said that:

- (a) provided that members considered Option D as a possible way forward, the LR would look into it further;
- (b) the LR was open to all conversion options but it hoped that consensus could be reached among members to screen out the less favourable options so that efforts could be focused on more probable ones;
- (c) the LR would continue to have dialogue with the key stakeholder who had concerns on the need/effectiveness of basic screening (see Note 24 to para. 3.20);
- (d) the LR was working to conduct a study on the latest developments on title registration legislation and good practices being adopted in some overseas common law jurisdictions (Note 25);
- (e) members would be updated in due course on the study findings and any refined proposals taking into account their views; and
- (f) as it would take some time to conduct the study and refine the proposals in the light of members' views and findings of the study, there was no particular implementation timetable for the LTRS at this stage.

3.22 According to the LR, up to September 2017, it was still working towards forging a consensus with the stakeholders on the way forward in implementing the LTRS.

Note 25: *Taking into account the suggestions from members of the LTO Steering Committee, the LR selected six common law jurisdictions, namely England and Wales (United Kingdom), Scotland (United Kingdom), New Zealand, New South Wales (Australia), Singapore and Penang (Malaysia) for the study.*

Under-estimation of complexity of the issues and the work involved in implementing LTO and LTRS

3.23 The Government proposed to the Bills Committee that the LTO would commence two years after its enactment in July 2004. However, up to September 2017, 13 years after its enactment, the LTO had not yet been implemented. The LR's post-enactment review found that substantial amendments to the LTO were required. Apparently, the LR had under-estimated the complexity of the issues and the work involved in implementing the LTO and the LTRS in view of the following:

- (a) in December 2006, the LR informed the DEVB that the LR:
 - (i) had made too optimistic assessment of the time needed to deal with the outstanding issues raised in 2004;
 - (ii) had not appreciated the impact of the changes of the LTO in 2004 on other legislation (see para. 3.14(c)(i)); and
 - (iii) considered introducing the LT(A)B in the 2006-07 legislative session not achievable in practice;
- (b) in May 2007, the Government informed the then LegCo Panel on Planning, Lands and Works that, as further issues were identified during the post-enactment review of the LTO, substantial amendments to the LTO were required, and the LR would prepare and submit an amendment bill to LegCo (see para. 3.13(c) and (d));
- (c) in December 2008, the Government informed the LegCo Panel on Development that there remained several substantial matters awaiting finalisation before the amendment bill could be brought to LegCo for consideration (see para. 3.14); and
- (d) in June 2011, the Government informed the LegCo Joint Subcommittee that it aimed to come up with a consolidated proposal that was acceptable to the stakeholders by the end of 2011, and thereafter consulted the public on the proposal for amending the LTO during the first and second quarters of 2012 (see para. 3.18(b)(i)). However, none of these have materialised.

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3.24 In September and October 2017, the DEVB and the LR informed Audit that:

- (a) the Government had committed to conducting a post-enactment review when the LTO was enacted in 2004. In view of the divergent views from various stakeholders and the complexity of the LTO (see paras. 3.6 to 3.22), the review was ongoing in spite of various proposals (see Appendix E) formulated by the Government to address these complicated issues;
- (b) the two-stage conversion mechanism proposed in 2011 and developed since then in consultation with stakeholders (see paras. 3.19 to 3.22) had addressed the main conflicting views of the stakeholders regarding the MR rule (see para. 3.17). However, stakeholders still had comments on certain aspects of the mechanism; and
- (c) in view of the stakeholders' inclination, the LR was exploring the "new land first" proposal (see para. 3.21) and was seeking the stakeholders' views.

3.25 In Audit's view, the DEVB and the LR need to fully assess the complexity of the issues and the work involved in taking forward the implementation of the LTRS.

Need to set a target LTRS implementation date and devise an action plan

3.26 Audit noted that in earlier years (during 2004-05 to 2009-10), the LR had set target time and devised action plans for implementing the LTRS, and submitted them to the LTO Steering Committee for information. However, since then, the LR had not set a target LTRS implementation date and devised an action plan with implementation timetable for steering and coordinating the various work for implementing the LTRS (e.g. the preparation of the LT(A)B, drafting of subsidiary legislation, preparation of rules and guidelines for staff and practitioners, and development of title registration information system).

3.27 In September 2017, the LR informed Audit that:

- (a) despite enormous and continuous efforts made by the LR over the years, a general consensus among stakeholders on the main issues, particularly the conversion mechanism, had not been reached. As such, it was not practical to prepare a realistic implementation timetable for the LTRS at this stage; and
- (b) once a general consensus among stakeholders on the main issues had been reached, the LR would prepare an implementation timetable for the LTRS and provide it to the LTO Steering Committee for consideration.

3.28 In Audit's view, the DEVB and the LR need to set a target LTRS implementation date and devise an action plan with timetable for implementing the LTRS as soon as practicable, having regard to the assessment of the complexity of the issues and the work involved (see paras. 3.23 to 3.25), views of stakeholders and the experience gained in the past years. The DEVB and the LR also need to report the target LTRS implementation date and submit the action plan to the LTO Steering Committee for consideration.

Need to make additional efforts to implement the LTRS

3.29 Audit noted that the LegCo Joint Subcommittee had expressed concerns over the poor/unsatisfactory progress of the Government's work in implementing the LTRS. At its last two meetings held in December 2010 and June 2011, LegCo Members had expressed:

- (a) disappointment with the poor progress of the Government's work in bringing the new LTRS into operation;
- (b) concerns that the Government had yet to come to any policy decision after gathering views and concerns from major stakeholders, and that it was not possible to come up with a timetable for the LT(A)B; and

Implementation of land title registration system

- (c) regret with the Government's unsatisfactory progress since 2004 in taking forward the LTO amendment exercise despite a substantial commitment of time and public resources over the years, and considered that this was attributed to the Government's swaying policy stance on certain core issues over the years.

3.30 Up to September 2017, the LTO had not yet come into force and the LTRS had not been implemented. According to the LR, since the enactment of the LTO in July 2004, it had incurred about \$24 million per year on average in staff costs on matters concerning the review of the LTO, preparation of the LT(A)B, engagement of stakeholders on the proposed legislative amendments (including the 2009 consultation exercise — see para. 3.15) and implementation of the LTRS. To reap the benefits of implementing the LTRS, Audit considers that the DEVB and the LR need to make additional efforts to implement the LTRS as early as possible, taking into account LegCo Members' concerns and the audit findings on the implementation of the LTRS.

Audit recommendations

3.31 **Audit has *recommended* that the Secretary for Development and the Land Registrar should:**

- (a) **fully assess the complexity of the issues and the work involved in taking forward the implementation of the LTRS;**
- (b) **set a target LTRS implementation date and devise an action plan with timetable for implementing the LTRS as soon as practicable, having regard to the assessment of the complexity of the issues and the work involved, views of stakeholders and the experience gained in the past years;**
- (c) **report the target LTRS implementation date and submit the action plan to the LTO Steering Committee for consideration; and**
- (d) **make additional efforts to implement the LTRS as early as possible, taking into account LegCo Members' concerns and the audit findings on the implementation of the LTRS.**

Response from the Government

3.32 The Secretary for Development and the Land Registrar generally agree with the audit recommendations. They have said that:

- (a) the LTRS is inherently complicated involving complex legal issues and carries significant implications. Throughout the years, regarding the main issues of conversion mechanism, rectification and indemnity arrangements which are closely interrelated, different proposals have been made to address and balance the conflicting views of the stakeholders, whose stances have evolved;
- (b) conversion of land and property (involving over 3 million land registers) under the DRS dating back to over a hundred years to the LTRS is a very challenging task;
- (c) stakeholders have a strong preference for automatic conversion mechanism for Hong Kong, which is not the approach generally adopted in other common law jurisdictions. Many of these jurisdictions have converted to title registration gradually involving parallel running of title registration and their original systems over a considerable period of time;
- (d) for rectification and indemnity arrangements, there are divergent views of stakeholders regarding protection of the rights of former land/property owners versus the rights of current land/property owners; and
- (e) hence, despite enormous and continuous efforts made over the years, a general consensus among the major stakeholders over the main issues has yet to be reached.

PART 4: FINANCIAL ISSUES AND PERFORMANCE REPORTING

4.1 This PART examines the financial issues and performance reporting of the LR, focusing on:

- (a) fees and charges (see paras. 4.2 to 4.15); and
- (b) performance reporting (see paras. 4.16 to 4.28).

Fees and charges

4.2 The LR charges customers the following two types of fees for its services:

- (a) **Statutory fees.** These fees are registration, search and copying fees specified in the Land Registration Fees Regulations (Cap. 128B). As of June 2017, there were a total of 25 fee items specified in the Regulations. Their fee revisions have to be made through amending the Regulations; and
- (b) **Non-statutory fees.** These fees refer to those not specified in the Land Registration Fees Regulations in (a) above. As of June 2017, there were a total of 44 fee items for services provided to the public or exclusively to government bureaux and departments (B/Ds). These services mainly include reports on title services (exclusively available to B/Ds), supply of computerised memorial day book (Note 26) and monthly memorial information on mortgage transactions (Note 27), and e-Alert services. Fee revisions for these services have to be supported by the DEVB and approved by the FSTB.

Note 26: *Memorial day book refers to a record of essential particulars (such as memorial number, nature and date of the document, address of the premises affected and consideration) of all the memorials of the relating documents lodged for registration each day.*

Note 27: *Monthly memorial information on mortgage transactions refers to a record of essential memorial information (such as nature and date of the document, address of the premises affected and consideration) extracted from documents related to mortgage transactions and lodged for registration within a month.*

4.3 According to Financial Circular No. 6/2016 “Fees and Charges”:

- (a) for trading fund fees, the general principle is that fees should normally be set to recover full cost (including the cost of capital, which is measured on the basis of ANFA) on an overall basis;
- (b) fees should generally be reviewed and, where necessary, revised on an annual basis;
- (c) in preparing their fee proposals, Directors of Bureaux and Controlling Officers (also applicable to trading funds’ General Managers) should ensure that the fee structure and levels are conducive to achieving the target (such as full-cost recovery), and take into account fairness and user-friendliness; and
- (d) revision of trading fund fees will be considered in the context of approving the financial aspects of their Business and Corporate Plans.

Need to conduct regular fee reviews of all fee items

4.4 Under the TFO, the LRTF is required to achieve a reasonable return on the fixed assets employed (see para. 1.5(c)). To meet this financial objective, the LR should in general set its fees at levels adequate to recover the full cost of providing the services (see para. 4.3(a)) and to attain the target rate of return on ANFA (see para. 1.12) on an overall basis. In this regard, the LR conducts a fee review on an overall basis annually in the context of formulating its Corporate-cum-Annual Business Plan. Since its establishment in 1993, the LR conducted five fee reviews of all fee items supported by costing statements (hereinafter referred to as the fee review of all fee items) at a time interval of 3 to 7 years between each review (i.e. in 1998, 2005, 2008, 2011 and 2016).

4.5 After noting that the financial projections in the LR’s Corporate-cum-Annual Business Plan for 2016-17 forecasted operating loss positions in the coming years, in April 2016, the FSTB requested the LR to conduct a fee review and submit a fee proposal by December 2016. The LR then conducted a fee review of all fee items based on 2015-16 financial results and found that:

Financial issues and performance reporting

- (a) services charged with statutory fees achieved an overall cost recovery rate of 105%; and
- (b) services charged with non-statutory fees achieved an overall cost recovery rate of 67%.

4.6 The LR considered that there was no need to revise the statutory fees. After obtaining the policy support of the DEVB and the approval of the FSTB, in April 2017, the LR revised its non-statutory fees (involving 37 fee items — Note 28). The LR estimated that, after the fee revision, the overall cost recovery rate for services charged with non-statutory fees would be 102% in 2017-18.

4.7 Audit noted that the LR reviewed the overall cost recovery rates of statutory and non-statutory fees in 2011 based on 2010-11 financial results and found that the rates were 146% and 134% respectively. Hence, no fee revision was made. The review conducted five years later in 2016 found that the overall cost recovery rate of non-statutory fees was only 67% and revision of fees was made in April 2017. The overall fee increase was 75%. There was a significant fee increase for certain items, for example, the increase for 16 of the 37 fee items reached 100% to 200% (Note 29).

4.8 In this connection, Audit noted that, in providing policy support for the LR's fee revision proposal for non-statutory fees in December 2016, the DEVB invited the LR to consider reviewing fees at regular intervals so that the percentage of fee increase would be more moderate in every fee review exercise. Audit considers that the LR needs to conduct regular fee reviews of all fee items and revise the fees where necessary.

Note 28: *In the fee revision proposal for non-statutory fees completed in December 2016, the LR reviewed 43 fee items, proposed to delete 4 fee items and maintain the fee levels of 2 fee items. Therefore, in April 2017, the LR revised 37 (43 – 4 – 2) fee items. After the launch of the e-Alert service for authorised institutions (involving 5 fee items) in February 2017, there were a total of 44 (37 + 2 + 5) non-statutory fee items as of June 2017 (see para. 4.2(b)).*

Note 29: *According to the LR, to avoid a drastic fee increase in April 2017, the fee increase for services exclusively available to B/Ds was restricted to not more than 200%, while that for services available to both B/Ds and the public restricted to not more than 50% in general.*

Need to keep under review the business operation and cost recovery of services

4.9 Registration of document is the LR's main services. The revenue from the services accounted for a high portion of its turnover (see Table 7). In recent years, the business volume of the services had dropped significantly. The number of land documents delivered for registration had dropped significantly by 45 % from 859,840 in 2010-11 to 468,630 in 2016-17 and the related revenue had also dropped significantly by 47 % (from \$319 million to \$169 million).

Table 7

**Revenue from and business volume of registration of document services
(2010-11 to 2016-17)**

Year	Turnover (\$ million)	Revenue from registration of document services (\$ million)	Land documents delivered for registration (Number)
2010-11	573	319 (56%)	859,840
2011-12	427	212 (50%)	573,104
2012-13	502	214 (43%)	598,843
2013-14	431	157 (36%)	424,634
2014-15	412	183 (44%)	505,894
2015-16	387	166 (43%)	445,889
2016-17	409	169 (41%)	468,630

Source: Audit analysis of LR records

Financial issues and performance reporting

4.10 The LR conducted two fee reviews of all fee items in 2011 and 2016 (see para. 4.4). According to the results of the fee reviews, for registration of document services, there was a drastic change from over-recovery of costs of \$93 million in 2010-11 to under-recovery of costs of \$80 million in 2015-16 (see Table 8).

Table 8

**Cost recovery of registration of document services
(2010-11 and 2015-16)**

Year	Revenue (a) (\$ million)	Cost (b) (\$ million)	Over / (under) recovery of costs (c) = (a) – (b) (\$ million)	Rate of recovery (d) = $\frac{(a)}{(b)} \times 100\%$
2010-11	319	226	93	141 %
2015-16	166	246	(80)	67 %

Source: Audit analysis of LR records

4.11 According to the LR, the revenue from registration of document services is very much susceptible to the volatility of the property market conditions. Audit noted that the revenue and business volume of these main services of the LR had dropped significantly over the years and the services had a significant under-recovery of costs of \$80 million in 2015-16 (see paras. 4.9 and 4.10). This might be one of the factors for the non-achievement of the target rate of return on ANFA in 2015-16 (actual of 4.1% against target of 6.9%). While the target rate of return on ANFA was achieved in 2016-17 (actual of 8.1% against target of 6.9%), in view of the fact that the LR's business operation is dependent on the property market conditions, Audit considers that the LR needs to keep under review its business operation and the cost recovery of its services, particularly the registration of document services, with a view to taking measures as far as possible to address the impact of the property market conditions on the services.

Lack of differential pricing for different means of providing a service

4.12 The LR provides search and copying services by different means of delivery, including counter service and online service. Audit noted that although the cost for providing a service varied significantly with the means of delivery, the LR charged the same service fee. For example, in 2015-16, the LR charged:

- (a) \$10 for a service fee item while the cost of providing the service through counter was \$30 and online was \$5; and
- (b) \$15 for another service fee item while the cost of providing the service through counter was \$105 and online was \$11.

4.13 In this connection, Audit notes that the Companies Registry charges different fees for online and onsite image record search. For example, for image record search of a set of financial statements, the Companies Registry charges \$21 for a downloaded copy requested by a registered online user, and \$35 for a hard copy requested by an onsite user. The LR needs to consider adopting differential pricing for different means of providing a service.

Audit recommendations

4.14 **Audit has recommended that the Land Registrar should:**

- (a) **conduct regular fee reviews of all fee items and revise the fees where necessary;**
- (b) **keep under review the LR's business operation and the cost recovery of the LR's services, particularly the registration of document services, with a view to taking measures as far as possible to address the impact of the property market conditions on the services; and**
- (c) **consider adopting differential pricing for different means of providing a service.**

Response from the Government

4.15 The Land Registrar generally agrees with the audit recommendations.

Performance reporting

4.16 The LR's performance measures include:

- (a) **Performance targets.** The LR sets performance targets (a total of 30 targets for 2016-17) under 9 service types (Note 30). These targets are expressed as a compliance rate (i.e. the percentage of providing a service within a specified service standard). The LR publishes the performance targets and results in its annual reports (available on its website) and Corporate-cum-Annual Business Plans; and
- (b) **Productivity targets.** The LR sets 3 productivity targets for its registration, search and copying services. These targets are expressed as an average output per man-day and are not published.

Need to review the compilation of actual performance information

4.17 Audit examination of the LR's compilation of actual performance information against the 30 performance targets for 2016-17 revealed that:

- (a) for 6 performance targets (Note 31) involving low volume of transactions, the LR compiled the actual performance information manually based on all transactions taken place; and

Note 30: *The 9 service types are: (1) registration of land documents; (2) registration of withheld instruments redelivered for registration; (3) amendment of registered data; (4) counter search of land registers; (5) supply of imaged copies of land records; (6) supply of certified copies of land records; (7) sale of memorial day book; (8) sale of monthly memorial information on mortgage transactions; and (9) telephone enquiry services.*

Note 31: *The 6 performance targets are under 3 service types, namely (1) amendment of registered data; (2) sale of memorial day book; and (3) sale of monthly memorial information on mortgage transactions.*

- (b) for the remaining 24 performance targets (Note 32), the LR compiled the actual performance information manually on a sample basis. The samples were selected based on a pre-scheduled time (see examples in Table 9).

Table 9

**Examples of sample basis for
compilation of actual performance information**

Service	Service standard	Sample basis
Registration of land documents	15 working days	Registered documents returned to the lodging party on the last working day of each month (i.e. 12 working days a year)
Registration of withheld instruments redelivered for registration	16 working days	Instruments redelivered for registration on the third working day of each month (i.e. 12 working days a year)
Counter search of land registers	15 minutes	Customers arrived at the counter during 11:00 am to 11:30 am on Friday of each week (i.e. 52 samples a year, with each sample covered transactions taken place during a 30-minute duration)

Source: Audit analysis of LR records

Note 32: *The 24 performance targets are under 6 service types, namely (1) registration of land documents; (2) registration of withheld instruments redelivered for registration; (3) counter search of land registers; (4) supply of imaged copies of land records; (5) supply of certified copies of land records; and (6) telephone enquiry services.*

4.18 In view of the limited sample size in the compilation of actual performance information for the 24 performance targets (see para. 4.17(b)), Audit is concerned whether the compiled results could fairly reflect the LR's actual performance. In Audit's view, the LR needs to critically review the compilation of actual performance information for the 24 performance targets to ensure that the actual performance information is fairly presented.

4.19 Audit also noted that, in compiling the actual performance information for the target on registration of land documents for 2016-17, 20,563 documents should have been selected based on the LR's sample basis. However, 1,961 complicated cases (10% of the total 20,563 cases) were excluded from the compilation of actual performance. According to the LR, the complicated cases included, for example, cases requiring the advice of the LR's Legal Services Division which needed detailed consideration of the legal issues or cases pending clarifications by the lodging parties which were beyond the control of the LR. Audit considers that the LR needs to disclose the basis for compiling the actual performance information for the target.

4.20 Audit also noted that the LR relied on a manual system for compiling the actual performance information. In Audit's view, there is merit for the LR to consider using more technology (e.g. IRIS — see Note 8 to para. 2.3(a)) in compiling its actual performance information as far as practicable.

Performance targets and productivity targets

4.21 ***Need to set more challenging performance targets.*** The LR reviews its performance pledges and targets annually. During 2012-13 to 2016-17, the LR had raised some of its targets in 2012-13, 2013-14 and 2016-17. Audit noted that the LR had achieved all performance targets during 2012-13 to 2016-17. In particular, Audit noted that 6 performance targets (Note 33) had consistently been over-achieved. Examples are shown in Table 10.

Note 33: *The 6 performance targets which had consistently been over-achieved included 1 target for registration of land documents, 1 target for registration of withheld instruments redelivered for registration, 2 targets for amendment of registered data, and 2 targets for telephone enquiry services.*

Table 10

**Examples of performance targets with persistent over-achievement
(2012-13 to 2016-17)**

Service	Service standard	Target performance (% meeting service standard)	Actual performance (% meeting service standard)				
			2012-13	2013-14	2014-15	2015-16	2016-17
(a) Registration of land documents	15 working days	92	99.1	99.4	99.6	99.4	99.7
(b) Amendment of registered data for:							
(i) simple cases	3 working days	93 (92 for 2012-13)	99.2	99.0	99.7	99.6	100.0
(ii) complicated cases	10 working days	92	98.8	99.0	99.4	99.8	99.6

Source: LR records

4.22 According to the good practices promulgated in Civil Service Bureau (CSB) Circular No. 7/2009 “Performance Pledges in the Civil Service” issued in September 2009, performance targets should be challenging enough to drive continuous improvement while being realistic and achievable, and persistent over-achievements may provide a basis for B/Ds to review the pledges and raise standards. As 6 of the 30 performance targets have been consistently over-achieved during 2012-13 to 2016-17, the LR needs to consider setting more challenging performance targets.

Financial issues and performance reporting

4.23 *Need to set more challenging productivity targets.* The LR has three productivity targets and reviews them annually. Audit noted that the LR had achieved all productivity targets during 2012-13 to 2016-17. While the LR raised two productivity targets (i.e. items (b)(i) and (b)(ii) in Table 11) in 2012-13, Audit noted that the LR had still consistently over-achieved the two targets during 2012-13 to 2016-17. Audit considers that the LR needs to consider setting more challenging productivity targets.

Table 11

**Productivity targets
(2012-13 to 2016-17)**

Particulars	Average output per man-day (Number)									
	2012-13		2013-14		2014-15		2015-16		2016-17	
	Target	Actual	Target	Actual	Target	Actual	Target	Actual	Target	Actual
(a) Registration of deeds	37	45	37	39	37	42	37	39	37	38
(b) Provision of counter / self-service search services on:										
(i) land registers (including certified copies)	85 (Note)	96	85	93	85	91	85	93	85	94
(ii) imaged copies (including certified copies)	76 (Note)	84	76	96	76	80	76	89	76	80

Source: LR records

Note: The target average output per man-day for items (b)(i) and (b)(ii) were 82 and 74 respectively in 2011-12.

4.24 Audit noted that, prior to 2014, the LR had included the productivity targets and actual performance in its Corporate-cum-Annual Business Plans. However, no such information had been included since 2014. Audit considers that, to enhance accountability, the LR needs to consider including the productivity targets and actual performance in its Corporate-cum-Annual Business Plans.

4.25 *No performance target set for owners' corporation services.* According to the good practices promulgated in CSB Circular No. 7/2009, performance pledges should cover all departmental services that have a public interface. While the LR publishes on its website the time required for processing and approving an application for registration of owners' corporation (ranging from one to three months) for general information, it has not set performance targets for the owners' corporation services (e.g. time for registration of owners' corporation and searching of owners' corporation records). In Audit's view, the LR needs to, in consultation with the HAD, consider setting and publishing performance targets for the owners' corporation services.

Audit recommendations

4.26 **Audit has recommended that the Land Registrar should:**

- (a) **critically review the compilation of actual performance information for the 24 performance targets to ensure that the actual performance information is fairly presented;**
- (b) **for registration of land documents, disclose the basis for compiling the actual performance information for the performance target;**
- (c) **consider using more technology in compiling the LR's actual performance information as far as practicable;**
- (d) **consider setting more challenging performance targets and productivity targets;**

Financial issues and performance reporting

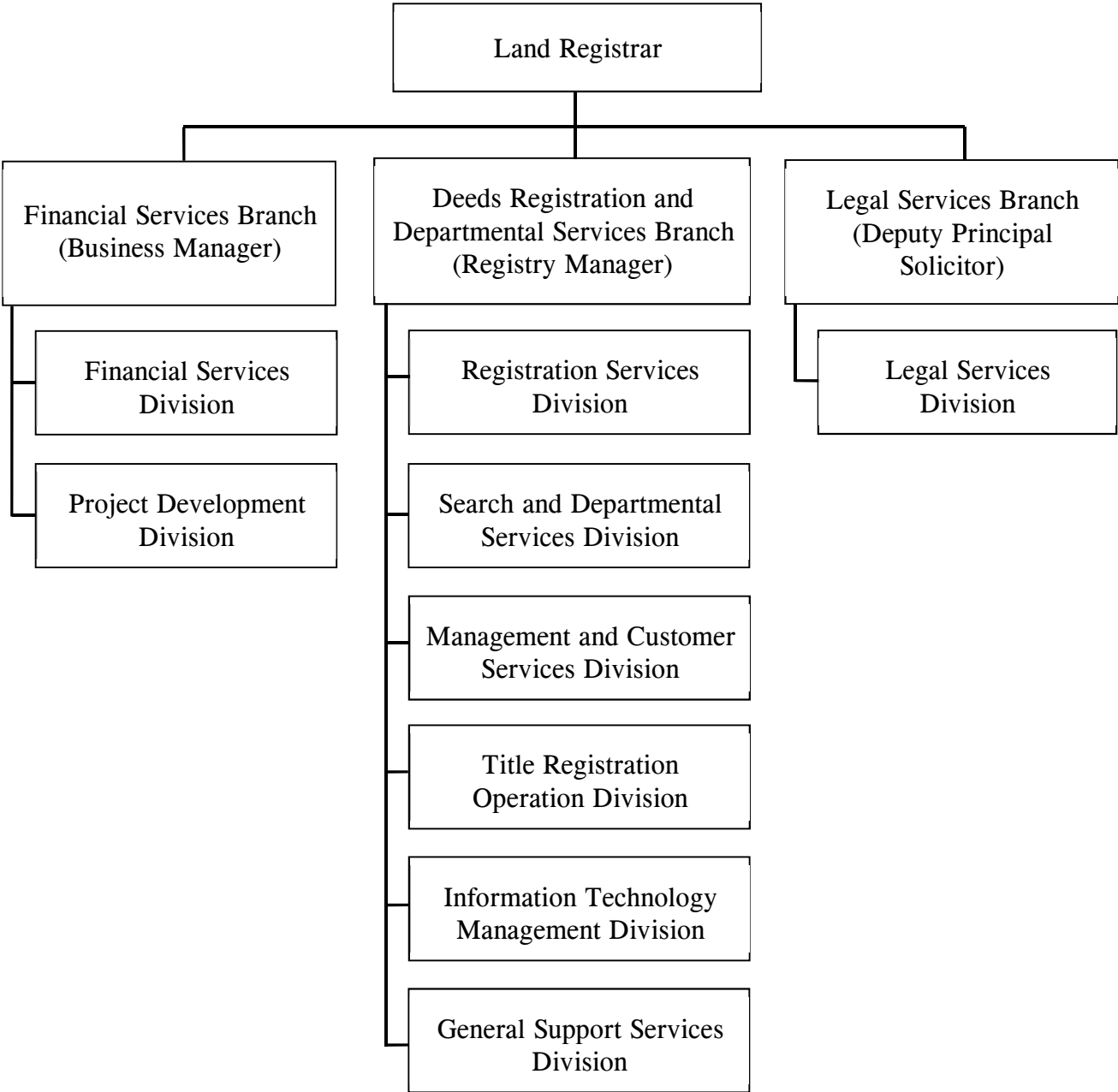
- (e) **to enhance accountability, consider including the productivity targets and actual performance in the LR's Corporate-cum-Annual Business Plans; and**
- (f) **in consultation with the Director of Home Affairs, consider setting and publishing performance targets for the owners' corporation services.**

Response from the Government

4.27 The Land Registrar generally agrees with the audit recommendations.

4.28 The Director of Home Affairs agrees with the audit recommendation in paragraph 4.26(f).

**Land Registry:
Organisation chart (extract)
(30 June 2017)**



Source: LR records

**Rates of return on ANFA of the LRTF
(1993-94 to 2016-17)**

Year	Rate of return on ANFA (Note 1)	
	Target	Actual
1993-94	10.0%	9.0% (Note 2)
1994-95		10.3%
1995-96		14.7%
1996-97		29.1%
1997-98		37.3%
1998-99		14.8%
1999-00		23.6%
2000-01		25.7%
2001-02		26.4%
2002-03		20.6%
2003-04		22.0%
2004-05		32.0%
2005-06		31.5%
2006-07	8.3%	20.9%
2007-08		36.0%
2008-09		18.8%
2009-10		38.5%
2010-11		52.6%
2011-12		19.7%
2012-13	6.9%	34.0%
2013-14		15.8%
2014-15		7.8%
2015-16		4.1%
2016-17		8.1%

Source: LRTF records

Note 1: Since 2006-07, the rate of return on ANFA is calculated as the LRTF's total comprehensive income (excluding interest income and interest expenses) divided by its ANFA. Before 2006-07, the LRTF had included interest income in the calculation of the rate of return on ANFA.

Note 2: For 1993-94, the actual rate of return on ANFA of 9% was calculated based on financial results for eight months from establishment of the LRTF in August 1993 to March 1994. According to the LRTF, the annualised actual rate of return on ANFA was 13.5%, exceeding the target return of 10%.

**Operational performance of the three NTSOs
(2012-13 to 2016-17)**

NTSO	2012-13 (No.)	2013-14 (No.)	2014-15 (No.)	2015-16 (No.)	2016-17 (No.)
Tsuen Wan					
<i>Search and copying services</i>					
Search	61,092	61,476	49,643	48,304	64,070
Copying	4,448	3,652	3,621	3,011	3,920
<i>Owners' corporation services</i>					
Registration application processed	12	12	8	15	10
Document filed	2,502	2,519	2,573	2,473	2,426
Inspection handled	53	35	28	37	47
<i>Daily average visitor</i>					
Search and copying services	32	30	33	33	35
Owners' corporation services	5	4	5	5	5
Total	37	34	38	38	40
Tai Po					
<i>Search and copying services</i>					
Search	62,928	47,719	60,447	49,932	62,778
Copying	9,669	8,002	7,645	8,040	7,497
<i>Owners' corporation services</i>					
Registration application processed	9	8	8	11	12
Document filed	2,243	2,147	2,006	2,124	2,345
Inspection handled	863	320	46	20	28
<i>Daily average visitor</i>					
Search and copying services	53	49	49	43	40
Owners' corporation services	5	4	4	3	3
Total	58	53	53	46	43
Yuen Long					
<i>Search and copying services</i>					
Search	50,049	46,540	52,577	38,108	51,202
Copying	13,149	9,948	10,005	9,302	8,581
<i>Owners' corporation services</i>					
Registration application processed	6	4	11	5	10
Document filed	1,101	1,006	1,309	1,095	1,392
Inspection handled	-	1	-	37	35
<i>Daily average visitor</i>					
Search and copying services	96	92	89	82	76
Owners' corporation services	3	2	3	2	3
Total	99	94	92	84	79

Source: Audit analysis of LR records

Main features of DRS and LTRS

Main feature	DRS	LTRS
(a) Certainty of title	<ul style="list-style-type: none"> No certainty of title Registration in the land register (being an index of registered instruments) does not confer title Deeds are the evidence of title 	<ul style="list-style-type: none"> Certainty of title Registration in the title register will confer title Title register will be the conclusive evidence of title
(b) Title checking in conveyancing	<ul style="list-style-type: none"> Checking of historical deeds for not less than 15 years to establish title to property is necessary 	<ul style="list-style-type: none"> Checking of historical deeds to establish title to property will no longer be necessary
(c) Indemnity	<ul style="list-style-type: none"> No compensation is payable by the Government in fraud cases The Government is liable for losses due to negligence of LR officers in failing to register any instrument delivered for registration that complies with the registration requirements 	<ul style="list-style-type: none"> An indemnity will be payable to compensate an innocent person who suffers loss (by reason of an entry in/omitted from the title register) as a result of fraud resulting in loss of ownership, or loss due to mistake or omission of LR officers
(d) Completeness of registers	<ul style="list-style-type: none"> Unwritten land interest is not registrable (Note) An owner registered on the land register may be subject to unwritten interests 	<ul style="list-style-type: none"> Unwritten land interest will be registrable (Note) The title register will be more complete and accurate. In general, purchasers acquiring properties with value and registered in the title register will not be affected by unregistered interests

Source: LR records

Note: Unregistered land interest refers to any unwritten interest (e.g. an interest by a spouse who has contributed to mortgage payments) or interest under unregistered instruments. Under the existing DRS and the LRO, unwritten land interest is not registrable and needs not be registered in order to carry legal effect, and unregistered instruments shall, as against any subsequent bona fide purchaser or mortgagee for valuable consideration of the same land, be absolutely null and void. Under the LTRS, unregistered interest is unenforceable against subsequent purchasers who obtained the property for value and registered as owner.

Appendix E
(paras. 3.7 and
3.24(a) refer)

**Summary of the LR's proposals to address the three main issues
(September 2017)**

Year	Conversion mechanism	Rectification arrangement	Indemnity arrangement
1994 (see para. 3.8)	Midnight conversion	No mandatory rectification	For the loss of title due to fraud, compensation with a cap will be provided for the person suffered
2002 (see para. 3.9)	Gradual conversion		
2004 (see paras. 3.10 and 3.11)	Daylight conversion	Mandatory rectification	For the loss due to mistake or omission of LR officers, compensation for actual loss will be provided for the person suffered
2009 (see para. 3.15)	Modified conversion mechanism (with gradual upgrading of titles)	Mandatory rectification with proposed exceptions to confine its scope of application	
2011 (see para. 3.17 and Appendix G)	Two-stage conversion	Mandatory rectification will apply during primary conversion period. Mandatory rectification will not apply after full conversion to the LTRS. During primary conversion period, property owners who wish to preserve mandatory rectification may opt out from full conversion by registering an opt-out caution	
2013 (see para. 3.19)	Revised two-stage conversion	Mandatory rectification will apply during primary conversion period. Mandatory rectification will not apply after full conversion to the LTRS. Mandatory rectification is only available to owners who have acquired title prior to primary conversion. Such owners who wish to preserve mandatory rectification may opt out from full conversion by registering an opt-out caution. Such owners can only opt out once during the primary conversion period. The opt-out caution has to be withdrawn before subsequent transfer of the property	
2014 (see para. 3.20 and Appendix H)	Four conversion options		

Source: Audit analysis of LR records

Terms of reference of LTO Steering Committee

- (a) To consider, review and monitor progress concerning matters arising from the LTO including, but not limited to, the following:
 - (i) recommendations by the LTO Review Committee (Note 1) on amendments to the LTO, arising from or as a consequence of the review of the LTO;
 - (ii) the rules, regulations, forms, guidelines and explanatory notes for the LTO recommended by the LTO Review Committee;
 - (iii) the development of IT in support of the LTO;
 - (iv) recommendations by the LTO Education Committee (Note 2) on public education and training in preparation for the implementation of the LTO; and
 - (v) recommendations by the LTO Implementation Committee (Note 3) on the various aspects relating to implementation of the LTO.
- (b) To consider and make recommendation to the Secretary for Development on the commencement date of the LTO.
- (c) To liaise with such interested bodies as may be necessary to carry into full effect the functions and purposes of the Committee.
- (d) Such other matters as may arise from time to time concerning the LTO and its implementation as the Committee deems necessary or appropriate.

Source: LR records

Note 1: The LTO Review Committee reviews the LTO and makes recommendations to the LTO Steering Committee on the amendments to the LTO arising from or as a consequence of the review.

Note 2: The LTO Education Committee plans for and implements publicity and public education programmes for the LTRS, both locally and overseas.

Note 3: The LTO Implementation Committee is responsible for all matters necessary to prepare for implementation of the LTO, including reviewing the existing administrative and operational systems, recommending changes and preparing staff and customers for the change.

**Main features of two-stage conversion mechanism
(May 2011)**

- (a) Upon the commencement of the LTO, immediate indefeasibility (see Note 22 to para. 3.17) would forthwith apply to new land. For existing land registered under the LRO, the conversion process would involve two stages of automatic conversion, as follows:
 - (i) after a preparation period from the date of commencement of the LTO, all such land except those subject to deeds pending registration would undergo the first stage of conversion (primary conversion) and would be automatically brought under the LTO on a designated date; and
 - (ii) after 12 years from the primary conversion, the land which had undergone the first stage of conversion would undergo the final stage of conversion (full conversion) and automatically be fully converted to registered land under the LTRS, except where the land was subject to, for example, an opt-out caution (see item (c) below) and a Land Registrar's Caution against Conversion (LRCAC — Note). Upon full conversion, immediate indefeasibility would apply.
- (b) During the 12 years from the primary conversion, a person having an unregistered interest in a property might give a notice of his claim by registering a warning notice.
- (c) During the 12 years from the primary conversion, a registered owner who wished to preserve the MR rule might choose to register an opt-out caution against his own property. The effect of registering an opt-out caution was to prevent the property from automatic full conversion of title, so that the MR rule would continue to apply.

Source: LR records

Note: Under the LRCAC mechanism, the Land Registrar will be empowered to exclude cases for which ownership of property could not be determined from the land register from automatic full conversion to the LTRS. The land against which an LRCAC is registered will remain under primary conversion until the LRCAC is removed.

Four conversion options for existing land registered under the LRO (June 2014)

Upon the commencement of the LTO, the LTRS will be implemented on new land immediately. The arrangements for existing land registered under the LRO under each conversion option are as follows:

- (a) **Option A.** All existing land registered under the LRO (except those subject to stopped deeds) will undergo primary conversion. Basic screening will then be performed on a gradual basis and cases for which ownership of property could not be determined from the land registers identified during the 12-year period from the primary conversion will be withheld from full conversion through the LRCAC mechanism (see Note in Appendix G);
- (b) **Option B.** Basic screening will be performed on land registers of existing land registered under the LRO before the designated date of primary conversion and identified cases where ownership of property could not be determined from the land registers will be withheld from primary conversion through the LRCAC mechanism. All cases identified would remain governed by the LRO;
- (c) **Option C.** There will be gradual primary conversion of existing land registered under the LRO as and when basic screening have been completed on individual land registers concerned for identifying cases where ownership of property could not be determined from the land registers upon applications for registration of assignments have been received. Individual land registers would have their own dates for primary conversion and full conversion; and
- (d) **Option D.** The LTRS will be implemented on new land only at the initial stage, while conversion of existing land registered under the LRO will be pursued at a later stage when possible solutions have been worked out and actual experience with the operation of the LTRS has been gained.

Source: LR records

Acronyms and abbreviations

ANFA	Average Net Fixed Assets
Audit	Audit Commission
BMO	Building Management Ordinance
B/Ds	Government bureaux and departments
CSB	Civil Service Bureau
DEVB	Development Bureau
DRS	Deeds registration system
FSTB	Financial Services and the Treasury Bureau
HAD	Home Affairs Department
IRD	Inland Revenue Department
IRIS	Integrated Registration Information System
LegCo	Legislative Council
LR	Land Registry
LRCAC	Land Registrar's Caution against Conversion
LRO	Land Registration Ordinance
LRTF	Land Registry Trading Fund
LT(A)B	Land Titles (Amendment) Bill
LTO	Land Titles Ordinance
LTRS	Land title registration system
MR	Mandatory rectification
NTSO	New Territories Search Office
QGO	Queensway Government Offices
TFO	Trading Funds Ordinance

CHAPTER 6

**Home Affairs Bureau
Home Affairs Department**

Regulation of hotels and guesthouses

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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REGULATION OF HOTELS AND GUESTHOUSES

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REGULATION OF HOTELS AND GUESTHOUSES

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1. The Hotel and Guesthouse Accommodation Ordinance (HAGAO — Cap. 349) provides a licensing regime to regulate premises that provide hotel and guesthouse accommodation at a fee. Licensed premises shall meet the building structure and fire safety standards specified in the Buildings Ordinance (Cap. 123) and the Fire Services Ordinance (Cap. 95). The main purpose is to safeguard lodgers and the public (e.g. residents of nearby premises) against risks of building safety and fire safety. The Secretary for Home Affairs is the Hotel and Guesthouse Accommodation Authority under the HAGAO. The Office of the Licensing Authority (OLA) under the Home Affairs Department (HAD) is delegated by the Authority to administer the HAGAO (e.g. issuing licences and performing relevant enforcement duties), which accounts for a significant proportion of the workload of the OLA. As at 30 June 2017, there were 2,024 establishments licensed under the HAGAO, comprising 286 licensed hotels (providing 77,724 rooms) and 1,738 licensed guesthouses (providing 14,029 rooms). The OLA had an establishment of 130 full-time posts and 58 part-time posts. For 2017-18, the estimated staff cost of the OLA is \$66.3 million. The Audit Commission (Audit) has recently conducted a review on the regulation of hotels and guesthouses.

Regulating licensed establishments

2. *Processing applications for new and renewal licences.* Licence applications usually go through a number of stages, such as “initial inspection” (the OLA inspects the premises concerned and specifies the required improvement works), “improvement works” (applicants carry out the required improvement works), and “follow-up inspection” (the OLA ascertains the completion of the required improvement works). The lead time for granting a licence comprises the times spent on individual stages of a licence application. Audit noted that:

- (a) *Need to monitor lead time.* For new licence applications, the average lead time was long (e.g. 469 calendar days in 2017);

Executive Summary

- (b) ***Need to enhance performance management practices.*** Of the nine “target times” which the OLA set for different stages of applications, two were published performance pledges and the remaining seven were internal targets only. The internal targets had generally not been attained. Furthermore, the seven internal targets had not been published for improving transparency and accountability, and management information for monitoring attainment had not been generated for them; and
 - (c) ***Long processing time due to many rounds of submission.*** During the stages of “improvement works” and “follow-up inspection”, applicants’ submission of full information to the OLA on the completion of improvement works could be a long process which would lengthen the lead time for granting licences (paras. 2.2 to 2.6, 2.8 and 2.10).
3. ***Renewing licences for unprotected cases.*** Under section 9(1) of the HAGAO, a renewal licence application may be submitted not less than three months before the expiration date of the existing licence (referred to as a “protected case”). According to section 9(5) of the HAGAO, for a protected case, the existing licence will remain in effect until the application is determined (e.g. approved or rejected) by the OLA, regardless of the expiration date of the existing licence. On the other hand, a renewal licence application submitted within three months before the expiration date of the existing licence is not protected by section 9(5) (referred to as an “unprotected case”). Audit noted that:
- (a) ***Disparities in lead times for renewing licences.*** Due to the OLA’s established practice to accord priority to processing unprotected cases, the average lead time for granting renewal licences for unprotected cases was notably shorter than that for protected cases (e.g. 90 calendar days for unprotected cases in 2017, versus the 134 calendar days for protected cases); and
 - (b) ***Need to better promote timely submission of applications.*** A considerable proportion (e.g. 61% in the first six months of 2017) of unprotected cases were still approved after the expiration of existing licences. It had been the OLA’s practice to remind licensees to submit applications for renewal licences in a timely manner under section 9(1). However, there were still many unprotected cases (e.g. 209 cases in 2016) in which the operator might fall into the state of operating without a valid licence (paras. 2.17 to 2.20, 2.22 and 2.24).

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4. *Need to ensure compliance with licence requirements.* In 2016, the OLA's Building Safety Unit (BSU) conducted annual inspections on 76 establishments which had a 2-year or 3-year licence for monitoring compliance with building safety requirements. The OLA's Fire Safety Team (FST), which conducted annual inspections on all establishments with a 2-year or 3-year licence, also separately inspected these 76 establishments for monitoring compliance with fire safety requirements. The BSU and the FST found that a total of 12 (16%) establishments had areas of non-compliance. Audit noted that: (a) in other inspections conducted by the OLA, the percentage of establishments having areas of non-compliance was higher (e.g. in approving renewal licence applications in 2016, 25% of the 533 establishments with a 2-year or 3-year licence were found to have areas of non-compliance); and (b) there were areas for improvement relating to annual inspections, namely, the selection of establishments for the BSU's annual inspections was not risk-based, annual inspections were not conducted on a surprise basis, and information on the progress and results of annual inspections was not compiled for management consideration (paras. 2.30 to 2.32).

Combating unlicensed establishments

5. *Need to monitor the increasing number of unresolved suspected cases.* The OLA's Enforcement Team identifies suspected unlicensed establishments from various sources (e.g. complaints from the public). The Team takes follow-up actions on suspected cases, such as inspecting the premises concerned, and instigating prosecutions where there is sufficient evidence of operation of unlicensed establishments. Despite the efforts in completing follow-up actions, the number of suspected cases in progress (i.e. outstanding cases) had doubled from 644 as at 1 January 2012 to 1,322 as at 30 June 2017. Of the 1,322 outstanding cases, many (270 cases or 20%) had been outstanding for more than three years. Audit noted that it was not the OLA's practice to compile and report information on the number of outstanding suspected cases and their outstanding durations for consideration by the HAD management (paras. 3.3 to 3.6).

6. *Investigating suspected unlicensed establishments.* Audit noted the following issues:

- (a) *Difficulties in collecting evidence for prosecution.* Of the 270 suspected cases which had been outstanding for over three years as at 30 June 2017, prosecutions had been instigated for 90 (33%) cases.

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However, for the remaining 180 (67%) cases, evidence for prosecution had been difficult to collect;

- (b) *Need for effective measures in conducting investigations.* Some unlicensed establishments were being advertised and booked on websites. Audit noted cases where unlicensed establishments operating on such websites did not show the full address and did not serve walk-in lodgers. Although this mode of operation would require additional measures (e.g. conduct of decoy operations) to supplement the OLA's investigations, they had not always been taken; and
- (c) *Need to make reference to overseas experiences.* As the HAGAO was currently under review, a number of overseas cities had already enacted legislation to combat illegal provision of sleeping accommodation through the Internet (paras. 3.10, 3.11, 3.14 and 3.16).

7. *Need for enhanced measures for prosecuting unlicensed establishments.* Under the HAGAO, a person who operates an unlicensed establishment is liable on conviction to a fine of \$200,000 and imprisonment for 2 years, and a fine of \$20,000 for each day the offence continues. Audit noted that some operators of unlicensed establishments were recalcitrant regardless of repeated prosecutions. For imprisonment cases, the person caught red-handed and prosecuted was usually a keeper rather than the business owner behind. There is a need to give a clear message to the community that operating unlicensed establishments is a criminal offence, which may risk the life and property of lodgers and the public. Audit noted that the continuous offence provision under the existing HAGAO (i.e. imposing a fine of \$20,000 for each day the offence continues) had so far not been invoked (paras. 3.19, 3.20, 3.22 and 3.24).

Other administrative and licensing issues

8. *Need to step up efforts in recovering costs.* The Hotel and Guesthouse Accommodation (Fees) Regulations (Cap. 349B) have prescribed the fees for issuing new licences and renewal licences. It is the Government's policy that fees charged by the Government should in general be set at levels adequate to recover the full cost of providing the goods or services. Audit noted that, in 2016-17, full cost recovery was still not achieved for the licensing of hotels and guesthouses. The cost recovery rates ranged from 32% to 75% for new licences, and from 40% to 72% for renewal

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licences. Since the last revision in November 2007, the HAD had made five attempts to revise the licence fees but all the fee proposals had not been taken forward (paras. 4.2, 4.3 and 4.6 to 4.8).

9. *Need to closely monitor caseloads of Licensing Inspectors.* Cases of suspected unlicensed establishments are each assigned to a responsible officer (case officer). Case officers need to follow up their cases and conduct inspections on the premises concerned. The OLA's Licensing Inspectors were all designated as case officers and new cases are assigned to them in sequence. According to the OLA, this allocation mechanism is in line with the principle and spirit of corruption prevention by limiting individual officers' control on the allocation of cases. As at 30 June 2017, the 24 Licensing Inspectors had in total a caseload of 1,322 outstanding cases. Audit noted that the caseloads of individual Licensing Inspectors were quite uneven, ranged from 32 cases (i.e. 58% of the average caseload of 55 cases) to 75 cases (i.e. 136% of the average caseload). Licensing Inspectors with heavier caseloads generally tended to have more long outstanding cases. There was a risk that Licensing Inspectors with heavy caseloads could not deal with their cases expeditiously and effectively. Audit also noted that it was not the practice of the OLA to compile statistics of caseloads for management information, or for discussion in regular management meetings (paras. 4.12 to 4.17).

10. *Need to conduct comprehensive review of issues relating to home-stay lodging.* There have been calls to develop home-stay lodging in Hong Kong. In July 2017, when reporting to the Legislative Council Panel on Home Affairs the progress in the review of the HAGAO, the HAD expressed that the development of home-stay lodging involved land use, planning, tourism, environmental and transport issues, which were under the purview of different bureaux and departments. The HAD was exploring with relevant bureaux and departments the idea of drawing up a set of guidelines to cater for licence applications for home-stay lodging, with a view to simplifying the licence requirements without compromising building safety and fire safety. In Audit's view, in drawing up the proposed guidelines for home-stay lodging, the HAD needs to address a number of issues, including the possible need to differentiate home-stay lodging from other types of guesthouses, consult relevant stakeholders, and consider whether overseas examples on the regulation of home-stay lodging may be applicable to Hong Kong (paras. 4.21 to 4.23).

Executive Summary

Audit recommendations

11. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Director of Home Affairs should:**

- (a) **keep the lead time for granting licences under closer monitoring, with a view to taking timely action to improve the lead time where necessary (para. 2.15(a));**
- (b) **expedite action to enhance the HAD's practices in managing performance on internal targets, taking into account factors such as the need for setting and publishing appropriate target times (para. 2.15(b));**
- (c) **step up efforts to facilitate applicants' submission of the required information on the completion of improvement works (para. 2.15(d));**
- (d) **look into the considerable and persistent disparities in lead times between protected cases and unprotected cases, and take necessary action to rectify the situation (para. 2.26(a));**
- (e) **step up the OLA's efforts in promoting timely submission of applications under section 9(1) of the HAGAO (para. 2.26(b));**
- (f) **monitor the effectiveness of annual inspections in identifying non-compliance with licence requirements (para. 2.34(a));**
- (g) **take necessary measures to enhance the conduct of annual inspections, having regard to the need for taking a risk-based approach, incorporating surprise elements into inspections, and compiling adequate management information (para. 2.34(b));**
- (h) **ensure that adequate management information for monitoring outstanding suspected cases is compiled (para. 3.7(a));**
- (i) **explore further measures to facilitate the investigations of suspected unlicensed establishments (para. 3.17(a));**

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- (j) **keep in view, for warranted cases, the possible invoking of the continuous offence provision under the existing HAGAO (para. 3.26);**
- (k) **take measures to ensure that a work plan for revising the licence fees of hotels and guesthouses is formulated in a timely manner, and monitor the implementation of the work plan (para. 4.10(a) and (c));**
- (l) **more closely monitor the caseloads of Licensing Inspectors (para. 4.19(a)); and**
- (m) **in drawing up the proposed guidelines for home-stay lodging, in collaboration with the relevant bureaux and departments, conduct a comprehensive review of issues relevant to home-stay lodging (para. 4.24).**

Response from the Government

12. The Director of Home Affairs agrees with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 The Hotel and Guesthouse Accommodation Ordinance (HAGAO — Cap. 349) provides a licensing regime to regulate premises that provide hotel and guesthouse accommodation at a fee. Licensed premises shall meet the building structure and fire safety standards specified in the Buildings Ordinance (Cap. 123) and the Fire Services Ordinance (Cap. 95). The main purpose of the licensing regime is to safeguard lodgers and the public (e.g. residents of nearby premises) against risks of building safety and fire safety.

1.3 Under the HAGAO, hotels and guesthouses are premises that provide short-term sleeping accommodation for any person who pays for the services and facilities (Note 1). Pursuant to the Hotel and Guesthouse Accommodation (Exclusion) Order (Cap. 349C), the HAGAO does not apply to certain premises which comprise:

- (a) premises providing accommodation with a tenancy period of 28 consecutive days or more for each letting; and

Note 1: *According to the HAGAO, hotels and guesthouses mean any premises whose occupier, proprietor or tenant holds out that, to the extent of his available accommodation, he will provide sleeping accommodation for any person presenting himself who appears able and willing to pay a reasonable sum for the services and facilities provided and is in a fit state to be received.*

Introduction

- (b) bedspace apartments, child care centres, clubs, elderly homes and homes for the disabled. These premises are under the regulation of other ordinances (Note 2).

Licensing hotels and guesthouses

1.4 The Secretary for Home Affairs is the Hotel and Guesthouse Accommodation Authority (the Authority) under the HAGAO. The Office of the Licensing Authority (OLA) under the Home Affairs Department (HAD) is delegated by the Authority to administer the HAGAO, including issuing licences (see paras. 1.5 to 1.8) and performing relevant enforcement duties (see paras. 1.9 to 1.12).

1.5 To apply for a licence, the applicants' premises to be used as hotels or guesthouses must be approved for domestic or hotel/guesthouse use by the Building Authority of the Buildings Ordinance. The premises must also be in compliance with the requirements relating to building structure, fire safety and sanitary conditions as specified in the Buildings Ordinance and the Fire Services Ordinance. The OLA will conduct inspections on the premises concerned to ensure compliance. The OLA may issue to the applicants a letter of requirements specifying the required upgrading works. The OLA will also conduct further inspections to ascertain the completion of the required upgrading works. A licence is granted only if all the licence requirements are met.

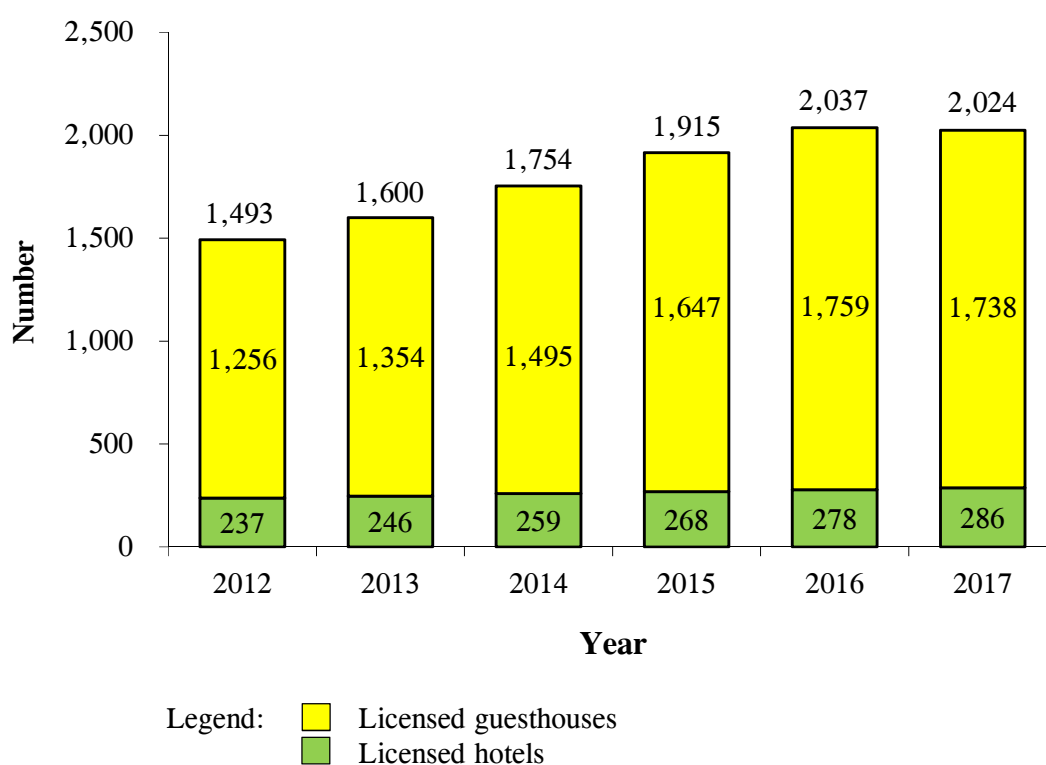
1.6 A licence is only valid for a period of time. The OLA has set criteria for different licence periods which vary from one to seven years (e.g. a period of one to three years for non-purpose-built premises, while purpose-built premises may have a period of four to seven years). To enable the continuous operation of the licensed premises without interruption, the licensee may apply for renewal of the licence not less than three months prior to its expiration. The HAGAO provides that for such an application, the licence will remain in effect until the application is determined (e.g. approved or rejected) by the OLA (see para. 2.17).

Note 2: *The ordinances relevant to these premises comprise Bedspace Apartments Ordinance (Cap. 447), Child Care Services Ordinance (Cap. 243), Clubs (Safety of Premises) Ordinance (Cap. 376), Residential Care Homes (Elderly Persons) Ordinance (Cap. 459), and Residential Care Homes (Persons with Disabilities) Ordinance (Cap. 613).*

1.7 As at 30 June 2017, there were 2,024 establishments operating on premises licensed under the HAGAO. Different types of licences had been issued for these establishments according to the type of accommodation provided, which comprised “hotel” licences (286 establishments), “guesthouse (general)” licences (1,552 establishments), “guesthouse (holiday flat)” licences (140 establishments) and “guesthouse (holiday camp)” licences (46 establishments). For simplicity, establishments with “hotel” licences are hereinafter referred to as licensed hotels. Establishments with other types of licences are hereinafter referred to as licensed guesthouses. Figure 1 shows the number of licensed hotels and licensed guesthouses in 2012 to 2017.

Figure 1

**Licensed hotels and guesthouses
(2012 to 2017)**



Source: HAD records

Remarks: Figures for 2012 to 2016 show the position as at 31 December of the year. Figures for 2017 show the position as at 30 June of the year.

Introduction

1.8 As at 30 June 2017, of the 2,024 establishments, there were 286 licensed hotels (providing 77,724 rooms) and 1,738 licensed guesthouses (providing 14,029 rooms).

Combating unlicensed establishments

1.9 Provision of sleeping accommodation on unlicensed premises may risk the life and property of lodgers and the public. Operation of unlicensed establishments is also a criminal offence, which is liable on conviction to a fine of \$200,000 and imprisonment for two years. The OLA has adopted a multi-pronged approach to combating unlicensed establishments, including strengthening law enforcement action, enhancing deterrent effect and stepping up publicity (see paras. 1.10 to 1.12).

1.10 For suspected unlicensed establishments (e.g. identified through public complaints), the OLA conducts inspections to follow up the cases. It will instigate prosecutions if there is sufficient evidence. In recent years, to strengthen its efforts in combating unlicensed guesthouses, the OLA has increased its staff resources for enforcement work and recruited frontline staff with law enforcement experience.

1.11 To achieve a greater deterrent effect, if a licensee is convicted of an offence involving operation of an unlicensed establishment, the OLA may cancel or refuse to renew licences held by the licensee concerned. The OLA can also pass information on convicted cases to relevant parties (e.g. the Inland Revenue Department, the Rating and Valuation Department, mortgage banks, property owners, owners' corporations and management offices of the buildings concerned) for taking necessary follow-up actions under their purview (e.g. prosecution against tax evasion).

1.12 As regards publicity, the OLA takes measures to remind lodgers (e.g. tourists to Hong Kong) to patronise licensed hotels and guesthouses. Such measures include making announcements in public interest on radio, television and the Internet, displaying posters and banners, distributing publicity leaflets, and disseminating messages on the Government's official websites. The OLA has also uploaded a full list of licensed establishments onto its website for easy reference by lodgers and the general public. It has also launched a mobile application for searching licensed establishments.

Organisational structure and key activities of OLA

1.13 The OLA comprises three units, namely, the Building Safety Unit (BSU), the Fire Safety, Enforcement and Prosecution Unit, and the Entertainment Licensing and Administration Unit. The three units are overseen by a Chief Officer (a Chief Building Surveyor). Appendix A shows an organisation chart of the OLA as at 30 June 2017. Table 1 summarises the key activities of the OLA in administering the HAGAO in the period from 2012 to 2017 (up to 30 June 2017).

Table 1

**Key activities of OLA in administering HAGAO
(2012 to June 2017)**

	2012	2013	2014	2015	2016	2017 (up to June)
	(Number)					
<i>Licensing hotels and guesthouses</i>						
New licence applications received	394	391	340	302	144	86
Applications processed	227	269	314	411	312	133
Applications in progress at year end	325	447	473	364	196	149
Renewal licence applications received (Note)	555	553	762	715	1,236	939
Applications processed	574	533	687	772	883	620
Applications in progress at year end	178	198	273	216	569	888
<i>Combating unlicensed establishments</i>						
Complaints and referrals received	1,824	1,744	2,070	1,713	1,843	1,122
Inspections conducted	6,791	9,889	13,153	13,188	13,574	7,237
Prosecutions instigated	131	170	147	149	158	77

Source: HAD records

Note: The HAD had restricted the licence period for guesthouse (general) licences and guesthouse (holiday flat) licences to a period of: (i) not more than 24 months for licences issued during 1 September 2014 to 27 December 2015; and (ii) not more than 12 months for licences issued thereafter. According to the HAD, the restrictions were intended to prepare the trade for the future licensing regime (see para. 1.15) and to facilitate the trade complying with the three new administrative enhancement measures introduced on 28 December 2015 (viz. requiring licensees to procure third party risks insurance, to provide a 24-hour manned counter, and to indicate clearly the type of licence issued (see para. 1.7) in promotional materials/advertisements). The restrictions were subsequently removed on 1 March 2017, in view of the trade's general compliance with the administrative enhancement measures. Most licences falling under categories (i) and (ii) expired starting from September 2016 and December 2016 respectively. Hence, there was an upsurge in the number of renewal licence applications in 2016 and 2017.

1.14 The administration of the HAGAO accounts for a significant proportion of the OLA's workload. Apart from the HAGAO, the OLA also administers six other ordinances (Note 3). As at 30 June 2017, the OLA had an establishment of 130 full-time posts and 58 part-time posts. Personnel of the OLA included professional and technical staff seconded from the Buildings Department, and disciplined service staff seconded from the Fire Services Department, as well as non-civil service contract staff (e.g. Licensing Inspectors). For 2017-18, the estimated staff cost of the OLA is \$66.3 million.

Proposed modifications to licensing regime

1.15 The HAGAO was enacted in 1991. To enhance the licensing regime, the Government conducted a public consultation in July and August 2014 to gauge public views on the matter. Issues addressed included:

- (a) operation of guesthouses might cause nuisance and annoyance to residents living in the same building. However, the HAGAO does not specify the consideration of the Deed of Mutual Covenant of the building concerned (e.g. whether commercial activities are allowed) or local residents' views in processing applications for licences. Legislative amendments would be needed to provide express provisions to enable the OLA to take into account the Deed of Mutual Covenant and local residents' views; and
- (b) legislative amendments would be needed to facilitate the OLA to collect evidence to prosecute unlicensed guesthouses, and to enhance the deterrent effect of penalties.

1.16 In March 2015, the Government informed the Panel on Home Affairs of the Legislative Council (LegCo) of the outcome of the public consultation and the legislative proposals. In July 2017, the Government informed the Panel of the

Note 3: *The six other ordinances administered by the OLA are the Amusement Game Centres Ordinance (Cap. 435), Bedspace Apartments Ordinance (Cap. 447), Clubs (Safety of Premises) Ordinance (Cap. 376), Gambling Ordinance (Cap. 148), Karaoke Establishments Ordinance (Cap. 573), and Miscellaneous Licences Ordinance (Cap. 114).*

Introduction

progress on the legislative proposals. The Government intended to introduce the amendment bill into LegCo in 2018.

Audit review

1.17 In 2006, the Audit Commission (Audit) completed a review entitled “Licensing of hotels and guesthouses”. The results were reported in Chapter 8 of the Director of Audit’s Report No. 47 of October 2006. In April 2017, Audit commenced a review on the regulation of hotels and guesthouses. The review focused on the following areas:

- (a) regulating licensed establishments (PART 2);
- (b) combating unlicensed establishments (PART 3); and
- (c) other administrative and licensing issues (PART 4).

1.18 Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

Acknowledgement

1.19 Audit would like to acknowledge with gratitude the assistance and full cooperation of the staff of the HAD during the course of the audit review.

PART 2: REGULATING LICENSED ESTABLISHMENTS

2.1 This PART examines the OLA’s work in regulating licensed hotels and guesthouses, focusing on the following issues:

- (a) processing applications for new and renewal licences (paras. 2.2 to 2.16);
- (b) renewing licences for unprotected cases (paras. 2.17 to 2.27); and
- (c) ensuring compliance with licence requirements (paras. 2.28 to 2.35).

Processing applications for new and renewal licences

2.2 The OLA issues licences for hotels and guesthouses under the HAGAO. Licence applicants comprise prospective operators who apply for new licences, and existing operators (i.e. existing licensees) who apply for renewal licences. Applications usually go through six stages:

- (a) ***Acknowledgement of applications.*** The OLA conducts initial vetting on the applications received (e.g. checking that all required documents are received) and issues to the applicants an “acknowledgement”;
- (b) ***Initial inspection.*** The OLA inspects the premises concerned and prepares inspection reports. The OLA may issue to the applicants a letter specifying the required improvement works (i.e. “letter of requirements” specifying the upgrading works for new licence applications and “letter for rectification” specifying the rectification works for renewal licence applications). Appendix B shows the general licence requirements under the HAGAO;
- (c) ***Improvement works.*** The applicants carry out the required improvement works and submit a “completion report” together with other relevant information (e.g. photographs showing completed works, and manufacturers’ test reports and certificates of materials used) for the OLA’s checking;

Regulating licensed establishments

- (d) ***Follow-up inspection.*** The OLA checks the completion reports and information submitted and inspects the premises concerned to ascertain the completion of the required improvement works. The OLA compiles a “compliance report” to support the approval for applications;
- (e) ***Approval of applications.*** The OLA approves the applications which meet the licence requirements, prepares the licences and issues to the applicants a “collection letter” for collecting the licences. Applications not meeting the requirements are refused; and
- (f) ***Collection of licences.*** Upon payment of licence fees, applicants collect the licences from the OLA.

The OLA has been using a computer system named Application Tracking Facility System to keep track of the processing time and progress of individual applications at various stages.

2.3 Of the six stages, the OLA has set target processing times (i.e. target times) for the four stages for which the OLA is primarily responsible (i.e. “acknowledgement of applications”, “initial inspection”, “follow-up inspection” and “approval of applications”). For the other two stages for which applicants are primarily responsible (i.e. “improvement works” and “collection of licences”), no target times have been set. Table 2 shows the OLA’s nine target times set for the four stages. Of the nine target times, two are published performance pledges (i.e. “acknowledgement of applications” and “initial inspection” for new licence applications) and the remaining seven are internal targets only.

Table 2

Stages of licence applications and target times

Stage	Target time in working days		
	New licence applications	Renewal licence applications involving rectification works	Renewal licence applications not involving rectification works
Acknowledgement of applications	4* (100 %)	5 (100 %)	
Initial inspection	22* (100 %)	49 (94 %)	39 (67 %)
Improvement works (Note 1)	N.A.		
Follow-up inspection	20 (78 %)	30 (96 %)	N.A.
Approval of applications	8 (38 %)	14 (38 %)	
Collection of licences (Note 2)	N.A.		

Source: HAD records

Note 1: The OLA has not set target times for “improvement works”. According to the OLA, it is applicants’ responsibility to carry out such works within the time limit allowed. Normally, the OLA allows 6 months (for guesthouses) or 12 months (for hotels) for applicants to complete upgrading works for new licence applications. Extensions of time to complete upgrading works may be granted by the OLA.

Note 2: The OLA has not set target times for “collection of licences”. Normally, the OLA advises applicants to pay licence fees and collect licences within 14 days from the date of the collection letter.

Remarks: 1. The two target times with an asterisk are the OLA’s performance pledges. The seven target times without an asterisk are the OLA’s internal targets.

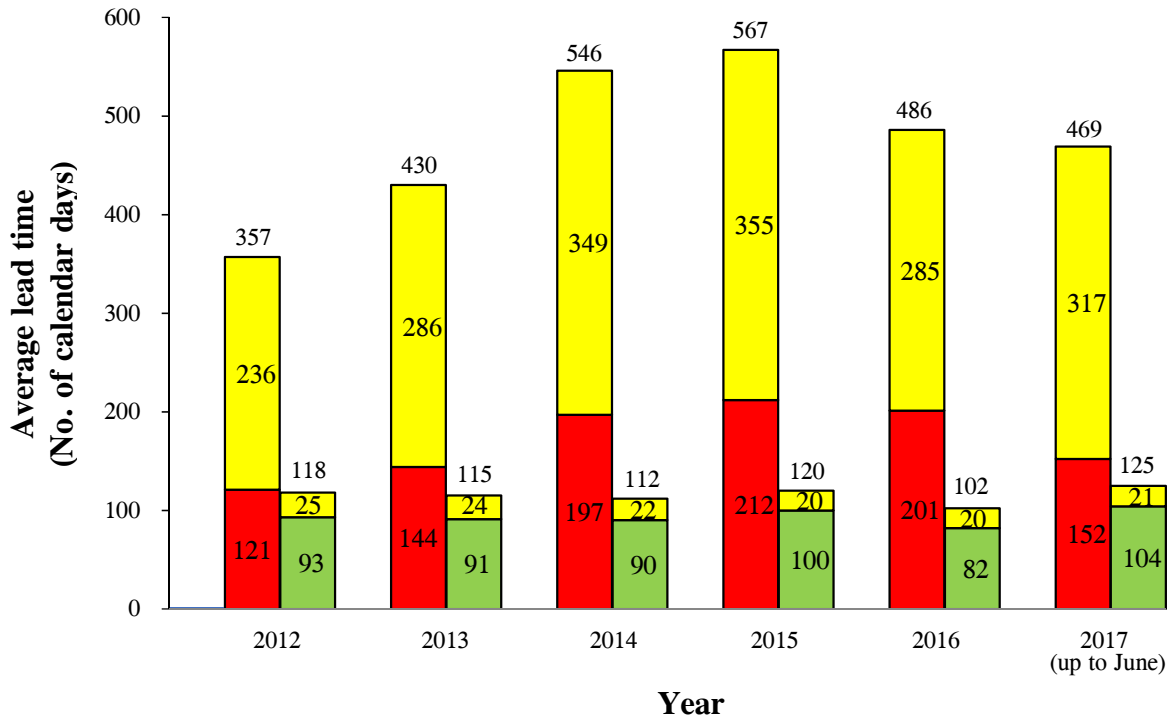
2. Percentages of cases attaining target times in 2017 (up to 30 June 2017) are shown in brackets.

Need to monitor lead time

2.4 The lead time for granting a licence refers to the time (in calendar days) which has elapsed since the OLA received the application. The lead time comprises the times spent on individual stages of a licence application. Figure 2 shows that during the period from 2012 to 2017 (up to 30 June 2017), for new licence applications, the average lead time had increased by 59% from 357 days in 2012 to 567 days in 2015 and had then decreased by 17% to 469 days in 2017. For renewal licence applications, the average lead time had increased slightly by 6% from 118 days in 2012 to 125 days in 2017.

Figure 2

Average lead time for granting licences
(2012 to June 2017)



Legend:

- Applicants' average action time (for "improvement works" and "collection of licences") for new licence applications or renewal licence applications
- OLA's average processing time for new licence applications
- OLA's average processing time for renewal licence applications

Source: Audit analysis of HAD records

Remarks: The majority of renewal licence applications were received more than three months before the licence expiration date. According to the HAD, for efficient use of resources, the OLA processed these applications after they had been received some time when the licence expiration date drew near. For these renewal licence applications, in calculating the OLA's average processing time, they were taken as if they had been received three months before the licence expiration date.

Regulating licensed establishments

2.5 For new licence applications, the long average lead time of over a year (e.g. 469 days in 2017) is not entirely satisfactory. Any increasing trend of the average lead time (e.g. during the period from 2012 to 2015) is also a cause for concern. According to the OLA, it has kept the lead time for new licence applications under close watch through a number of measures, namely, monitoring the progress in processing completion reports on a weekly basis, and holding meetings within the OLA and monthly meetings with the HAD management to monitor the lead time. Nevertheless, Audit noted that the OLA's internal targets were generally not attained (see paras. 2.6 to 2.7) and there was room for improving the HAD's practices in managing performance on internal targets and the lead time (see paras. 2.8 to 2.14).

Internal targets not attained

2.6 According to the HAD, the two performance pledges (see Table 2 in para. 2.3) are the OLA's promulgated commitments of performance to the public. The OLA spares more efforts and resources to meet these two performance pledges as far as possible. Whereas the seven internal targets (see Table 2 in para. 2.3) are the OLA's internal reference for guiding its work priority. Audit noted that in 2017 (up to 30 June 2017), while the two performance pledges (i.e. the pledges on "acknowledgement of applications" and "initial inspection" for new licence applications) were attained, the seven internal targets were generally not attained, as follows:

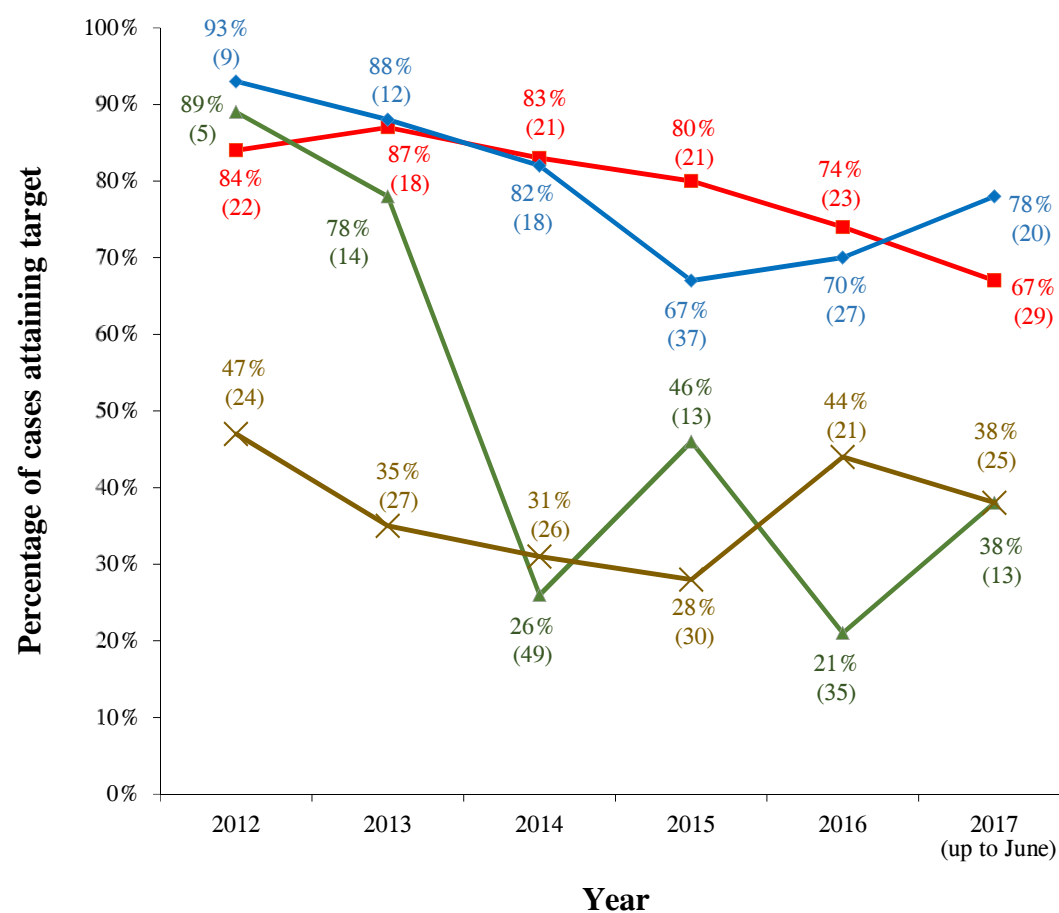
- (a) one internal target, i.e. the target on "acknowledgement of applications" for renewal licence applications, was 100% attained;
- (b) two internal targets, i.e. the targets on "initial inspection" and "follow-up inspection" for renewal licence applications involving rectification works, were 94% and 96% respectively attained (slightly short of 100%); and
- (c) for the remaining four internal targets, the percentages of cases attaining the targets ranged from 38% to 78%.

2.7 For the four internal targets mentioned in paragraph 2.6(c), Figure 3 further shows that, during the period from 2012 to 2017 (up to 30 June 2017), the percentages of cases attaining the targets had generally decreased, as follows:

- (a) *Initial inspection for renewal licence applications not involving rectification works.* The percentage had decreased from 84% in 2012 to 67% in 2017;
- (b) *Follow-up inspection for new licence applications.* The percentage had decreased from 93% in 2012 to 78% in 2017;
- (c) *Approval of applications for new licences.* The percentage had decreased from 89% in 2012 to 38% in 2017; and
- (d) *Approval of applications for renewal licences.* The percentage had decreased from 47% in 2012 to 38% in 2017.

Figure 3

Attainment of four internal targets (2012 to June 2017)



- Legend:
- Initial inspection for renewal licence applications not involving rectification works (with a target time of 39 working days)
 - ◆ Follow-up inspection for new licence applications (with a target time of 20 working days)
 - ▲ Approval of applications for new licences (with a target time of 8 working days)
 - ✕ Approval of applications for renewal licences (with a target time of 14 working days)

Source: Audit analysis of HAD records

Remarks: Figures in brackets show the average processing times in working days.

Need to enhance performance management practices

2.8 The HAD's practices in managing performance on internal targets were not entirely satisfactory. Audit noted that:

- (a) ***Some internal targets not met.*** For some internal targets, there were significant disparities between the target time and the processing time attained. For example, in 2017 (up to June 2017):
 - (i) the average processing time for the approval of applications for new licences was 13 working days, which was 63 % longer than the target of 8 working days (see Figure 3 in para. 2.7); and
 - (ii) the average processing time for the approval of applications for renewal licences was 25 working days, which was 79 % longer than the target of 14 working days (see Figure 3 in para. 2.7).

The HAD needs to ascertain the reasons for the disparities and take improvement measures;

- (b) ***Internal targets not published.*** While the two performance pledges (see para. 2.3) had been published in the public domain (e.g. on the OLA website), the seven internal targets had not been published. There was room for improving transparency and accountability by publishing more targets;
- (c) ***Management information not generated.*** For the two published performance pledges, management information was generated monthly from the Application Tracking Facility System (see para. 2.2) for monitoring by the HAD. However, no similar management information on attainment was generated for the seven internal targets for regular monitoring by the HAD; and
- (d) ***Data in computer system not updated promptly.*** According to its laid-down procedures, within four days after completing an action in processing licence applications, the OLA needs to update the data stored in the Application Tracking Facility System. However, this requirement had not always been followed (e.g. in 2016, only 88 % of the updates were performed within four days).

Regulating licensed establishments

In September 2017, the HAD informed Audit that it started in July 2017 a review on the appropriateness of the internal targets, with a view to publishing more target times.

2.9 Audit considers that the HAD needs to expedite action to enhance its practices in managing performance on internal targets, taking into account Audit's findings as shown in paragraph 2.8 which include the need for setting appropriate target times and publishing them for the purpose of enhancing transparency and public accountability. The HAD also needs to take measures to ensure that the target times set are satisfactorily attained.

Long processing time due to many rounds of submission

2.10 Audit noted that during the stages of “improvement works” and “follow-up inspection” (see para. 2.2(c) and (d)), applicants had not always submitted full information on the completion of improvement works (i.e. completion reports and supporting documents) in a timely manner. Furthermore, the submission of full information could sometimes be a long process which would lengthen the lead time for granting licences. Case 1 shows an example.

Case 1**Submission of information on improvement works
(June 2015 to March 2017)**

1. In June 2015, the OLA received a new licence application for a 6-room guesthouse. After completing initial inspections in July 2015, the OLA issued in August 2015 to the applicant a letter of requirements on the upgrading works required to be completed within six months (i.e. by February 2016).

2. In February 2016, the applicant submitted a completion report, which was missing some documents (e.g. copies of reports/documents submitted to the Buildings Department under the Minor Works Control System — see para. 2.13) and was not accepted by the OLA. Some of the missing documents were subsequently submitted in April 2016.

3. In May 2016, the applicant submitted another completion report, which was again missing some documents (see para. 2 above) and was not accepted by the OLA. Some of the missing documents were subsequently submitted in June and July 2016. The OLA then conducted the follow-up inspection and found that the upgrading works were not satisfactorily completed.

4. After the aforementioned 5 submissions of reports/documents, during the period from July 2016 to February 2017, the applicant made another 11 submissions of reports/documents. Finally, in February 2017, the OLA concluded that the upgrading works were satisfactorily completed. In March 2017, the licence was approved.

5. In the 13-month period from the submission of the first completion report in February 2016 to the satisfactory completion of the upgrading works in February 2017, the applicant made 16 submissions of reports/documents. In the submissions, very often, documents (e.g. copies of reports/documents submitted to the Buildings Department under the Minor Works Control System) were missing, incomplete, inconsistent or not acceptable.

Audit comments

6. The many rounds of submission of reports/documents, due to incomplete information submitted by the applicant, hindered the progress of approving and granting the licence by the OLA.

Source: Audit analysis of HAD records

Regulating licensed establishments

2.11 Audit noted that, for new licence applications, the average number of rounds of submission was 2.2, 2.1, 2.3, 2.7, 2.8 and 3.2 respectively for each year during 2012 to 2017 (up to 30 June 2017). The average number of submissions was increasing. For renewal licence applications, the average number of rounds of submission was either 1 or 1.1 during the same period.

2.12 The OLA has implemented a number of measures to facilitate applicants carrying out improvement works and submitting information on the completion of such works. For example:

- (a) since 2011, “A Layman’s Guide to Licence Applications under the HAGAO”, setting out the general requirements and procedures of applying for licences, has been uploaded onto the OLA’s website;
- (b) since September 2013, the OLA has held meetings with applicants and their agents (e.g. consultants and contractors) to go through the letter of requirements or any list of outstanding requirements;
- (c) since July 2015, for information of applicants, e-mail addresses of responsible officers have been uploaded onto the Application Tracking Facility System (to which applicants have access); and
- (d) since August 2017 (during the course of this audit review), all licence conditions and requirements have been uploaded onto the OLA’s website.

2.13 The OLA has also published on its website a set of questions and answers on common mistakes of licence applicants in carrying out improvement works and in submitting information on the completion of improvement works. However, Audit noted that the questions and answers have not been updated since they were first published in June 2009. For example, with the introduction of the Minor Works Control System (Note 4) under the Buildings Ordinance in December 2010, licence applicants are required to submit to the OLA copies of reports/documents prepared under the system. As the OLA has not updated the set of questions and answers with

Note 4: *The Minor Works Control System aims to facilitate building owners and occupants carrying out small-scale building works safely and lawfully through simplified requirements.*

this requirement, applicants may miss submitting these reports/documents to the OLA.

2.14 Audit considers that the HAD needs to step up its efforts to facilitate applicants' submission of the required information on the completion of improvement works.

Audit recommendations

2.15 Audit has *recommended* that the Director of Home Affairs should:

- (a) **keep the lead time for granting licences under closer monitoring, with a view to taking timely action to improve the lead time where necessary;**
- (b) **expedite action to enhance the HAD's practices in managing performance on internal targets, taking into account factors such as the need for setting and publishing appropriate target times (see para. 2.8);**
- (c) **take measures to ensure that the internal target times set are satisfactorily attained; and**
- (d) **step up efforts to facilitate applicants' submission of the required information on the completion of improvement works.**

Response from the Government

2.16 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD will:

- (a) monitor the lead time for granting licences more closely, with a view to taking timely action for improvement;
- (b) enhance the practices in managing performance on internal targets, and suitably review the appropriateness of such targets, with a view to publishing appropriate target times; and

Regulating licensed establishments

- (c) step up efforts to further facilitate applicants' submission of the required information as promulgated in the relevant guidelines uploaded onto the OLA's website.

Renewing licences for unprotected cases

2.17 Under section 9(1) of the HAGAO, a licensee may submit a renewal licence application not less than three months before the expiration date of the existing licence (hereinafter referred to as a “protected case”). According to section 9(5) of the HAGAO, for a protected case, the existing licence will remain in effect until the application is determined (e.g. approved or rejected) by the OLA, regardless of the expiration date of the existing licence. This protects the applicant from any inconvenience caused by the lead time, namely, the risk of possible disruption of hotel/guesthouse operation if the renewal licence application cannot be approved in time. When the application is approved, the licence is deemed to be renewed on the day immediately after the expiration date.

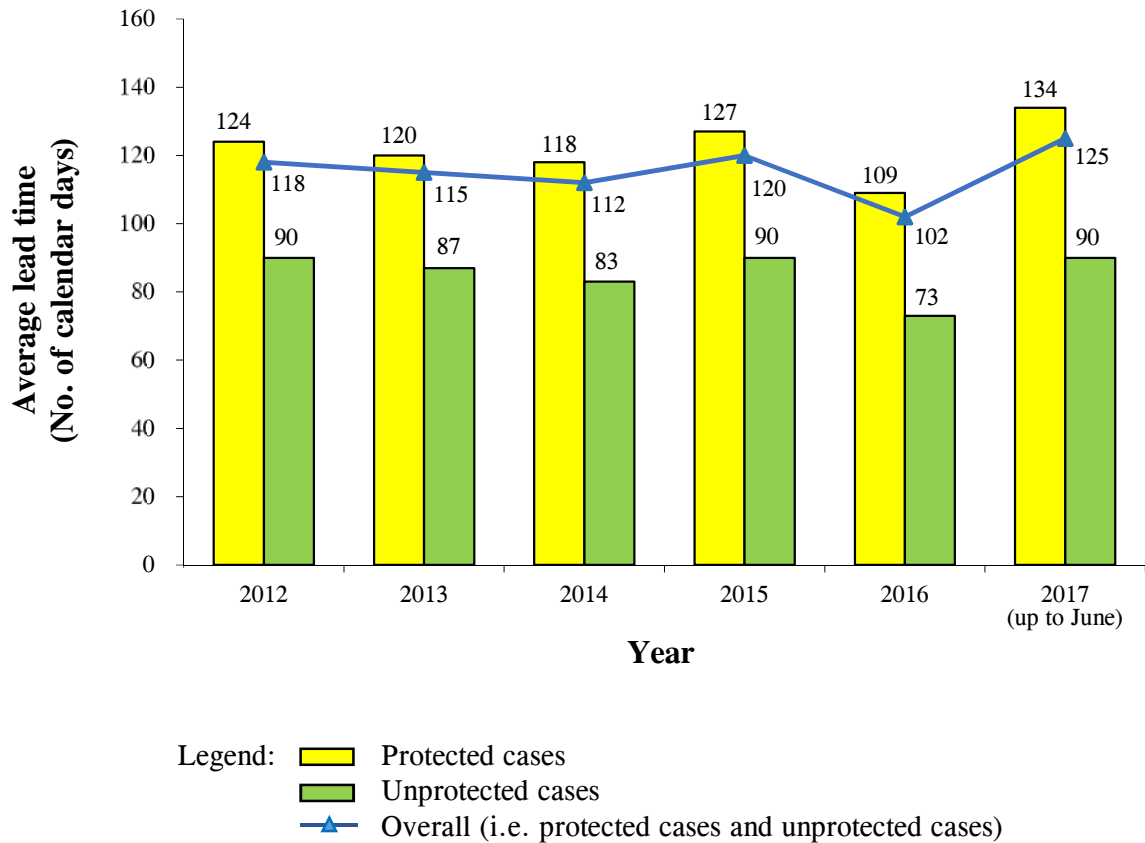
2.18 A renewal licence application submitted within three months before the expiration date of the existing licence (hereinafter referred to as an “unprotected case” — i.e. not submitted under section 9(1)) is not protected by section 9(5). Accordingly, the existing licence will lapse on the expiration date if the application cannot be approved in time. During the period from 2012 to 2017 (up to June 2017), the proportions of unprotected cases received ranged from 14% (79 cases in 2013) to 20% (110 cases in 2012).

Disparities in lead times for renewing licences

2.19 Figure 4 shows that, during the period from 2012 to 2017 (up to 30 June 2017), the average lead time for granting renewal licences for unprotected cases was notably shorter than that for protected cases. In 2017, the average lead time was 90 calendar days for unprotected cases, which was 33% less than the 134 calendar days for protected cases.

Figure 4

**Average lead time for granting renewal licences
(2012 to June 2017)**



Source: Audit analysis of HAD records

2.20 Audit noted that, for both unprotected cases and protected cases, applications were required to go through the same stages of processing (see para. 2.2). The much shorter lead time for unprotected cases over the years was mainly due to the OLA's established practice to accord priority to these cases and expedite action in processing them. According to the OLA, this practice had taken into account the consequence to the licensees concerned if the applications were not approved before the licence expiration date (see para. 2.23).

2.21 While noting the OLA's rationale for its practice (see para. 2.20), Audit considers that the HAD needs to look into the considerable and persistent disparities in lead times between protected cases and unprotected cases (see Figure 4 in para. 2.19), and take necessary action to rectify the situation.

Need to better promote timely submission of applications

2.22 Audit noted that despite that the OLA accorded priority to processing unprotected cases, a considerable proportion of such cases were still approved after the expiration of existing licences. Table 3 shows that, during the period from 2012 to 2017 (up to 30 June 2017), the proportions ranged from 11% in 2016 to 61% in 2017.

Table 3

**Approval of applications for renewal licences in unprotected cases
(2012 to June 2017)**

Approval	No. of unprotected cases with applications approved					
	2012	2013	2014	2015	2016	2017 (up to June)
Before licence expiration date	58 (53%)	52 (69%)	77 (70%)	98 (70%)	159 (89%)	52 (39%)
After licence expiration date	52 (47%)	23 (31%)	33 (30%)	43 (30%)	19 (11%)	81 (61%)
Total	110 (100%)	75 (100%)	110 (100%)	141 (100%)	178 (100%)	133 (100%)

Source: Audit analysis of HAD records

2.23 For both hotel/guesthouse operators and the OLA in unprotected cases, approval of applications after the expiration of existing licences carries undesirable consequences. Firstly, applications are not protected by section 9(5) of the HAGAO (see para. 2.18). The existing licences will lapse upon expiration, rendering the hotels and guesthouses concerned no longer licensed establishments. These hotels and guesthouses need to stop operation until the applications are approved. Secondly, according to the OLA's practices, all unprotected cases with applications not yet approved upon the expiration of existing licences are referred internally to its Enforcement Team for combating any operation of unlicensed establishments (see para. 3.3). The follow-up of many such cases will create extra workload of the OLA.

2.24 To remind licensees to submit applications for renewal licences under section 9(1) of the HAGAO, it has been the OLA's practice to issue reminders (including follow-up reminders) and make telephone calls to licensees during the last four months before the expiration of licences. The OLA has also alerted the trade of the risk of disruption of operation associated with late submission of applications. However, as reflected by the many unprotected cases in which applications had not been submitted in a timely manner under section 9(1) (ranging from 79 cases in 2013 to 209 cases in 2016, during the period from 2012 to 2016), the OLA's practice was not entirely effective. In these cases, the operator might fall into the state of operating without valid licence. There were, in particular, cases where licensees repeatedly failed to submit timely applications under section 9(1). Audit noted that in one extreme case, a licensee persistently failed to submit timely applications in 8 out of 9 instances during 2008 to 2017.

2.25 Audit considers that the HAD needs to step up the OLA's efforts in promoting timely submission of applications under section 9(1) of the HAGAO.

Audit recommendations

2.26 **Audit has *recommended* that the Director of Home Affairs should:**

- (a) **look into the considerable and persistent disparities in lead times between protected cases and unprotected cases, and take necessary action to rectify the situation; and**
- (b) **step up the OLA's efforts in promoting timely submission of applications under section 9(1) of the HAGAO.**

Response from the Government

2.27 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD will suitably review the existing measures to promote timely submission of applications under section 9(1) of the HAGAO.

Ensuring compliance with licence requirements

2.28 Under the HAGAO, licences can be issued for a period up to 84 months (7 years). For licensees with good records in complying with licence requirements, it is the practice of the OLA to issue to them licences for periods of 2 or 3 years, and for periods of 4 to 7 years if the establishment concerned is a purpose-built hotel/guesthouse.

2.29 Of the licences issued for the 2,024 establishments as at 30 June 2017, 1,269 (63%) were 1-year licences, 696 (34%) were 2-year or 3-year licences, and 59 (3%) were licences with periods ranging from 4 to 7 years (Note 5). The OLA has established mechanisms to monitor licensees' compliance with licence requirements for the different types of licences:

- (a) **1-year licences.** For establishments with 1-year licences, the OLA fully checks compliance with licence requirements when processing renewal licence applications;
- (b) **2-year or 3-year licences.** For establishments with these licences, the OLA's BSU and Fire Safety Team (FST) conduct annual inspections during the licence period:
 - (i) **BSU.** 20% of the establishments are selected annually on a random basis and inspected for compliance with building safety requirements; and
 - (ii) **FST.** All the establishments are inspected annually for compliance with fire safety requirements; and
- (c) **Licences with periods ranging from 4 to 7 years.** The BSU does not conduct annual inspections for establishments with these licences, while the FST does. In parallel with the FST's annual inspections of all these establishments, the OLA requires all these licensees to submit annually an

Note 5: *The 2,024 licensed establishments included 286 hotels. Of them, 25 hotels held 1-year licences, 202 hotels held 2-year licences or 3-year licences, and 59 hotels held licences with licence periods ranging from 4 to 7 years.*

authorised person's certificate to certify compliance with licence requirements (Note 6).

Need to ensure compliance with licence requirements

2.30 In 2016, the BSU conducted annual inspections on 76 establishments which had a 2-year or 3-year licence (see para. 2.29(b)(i)). The FST, which conducted annual inspections on all such establishments (see para. 2.29(b)(ii)), also separately inspected these 76 establishments. The BSU and the FST found that a total of 12 (16%) establishments had areas of non-compliance (Note 7).

2.31 Audit noted that in other inspections conducted by the OLA, the percentage of establishments found to have areas of non-compliance was higher. For example:

- (a) in 2013, subsequent to a fire at a commercial-cum-residential building, the OLA conducted inspections on the 5 licensed guesthouses which were located in the same building but did not have fires. In 3 (60%) of the 5 guesthouses, irregularities (such as addition of beds, addition of storage cabinets in corridors, and blocking of smoke detectors) were found; and
- (b) in 2016, the OLA approved renewal licence applications of 876 establishments, which included 533 establishments with a 2-year or 3-year licence. Of the 533 establishments, 133 (25%) establishments were found to have areas of non-compliance with building safety or fire safety requirements. The 25% was higher than the 16% of establishments revealed through annual inspections of the BSU and the FST (see para. 2.30).

Note 6: *An authorised person refers to an architect, engineer or surveyor whose name is on the authorised persons' register kept under the Buildings Ordinance. The authorised person's certificate needs to certify that the establishment concerned has not undergone any substantial alteration, has been operated according to licence requirements, and has been properly maintained regarding building safety and fire safety.*

Note 7: *Follow-up actions were subsequently taken by the licensees to rectify the areas of non-compliance.*

Regulating licensed establishments

2.32 In this connection, Audit noted areas for improvement in relation to the conduct of annual inspections, as follows:

- (a) ***Not risk-based.*** The 20% of establishments for the BSU's annual inspections were selected on a random basis. Adopting a risk-based approach in selecting establishments would improve the effectiveness of annual inspections in detecting non-compliance (e.g. taking into account establishments' track records in complying with requirements);
- (b) ***No surprise elements.*** Arrangements were made with the establishments concerned prior to the conduct of annual inspections. However, the ad hoc inspections in 2013 (see para. 2.31(a)), which revealed that a significant percentage of establishments had areas of non-compliance, were conducted on a surprise basis; and
- (c) ***Inadequate management information.*** It was not the OLA's practice to compile management information on annual inspections for consideration by the head of the OLA or by the HAD management. Regular information (e.g. on the progress and results of annual inspections) would facilitate the management making informed decisions on enhancing the conduct of inspections.

2.33 Audit considers that the HAD needs to monitor the effectiveness of annual inspections in identifying non-compliance with licence requirements, and take necessary measures to enhance the conduct of annual inspections.

Audit recommendations

2.34 **Audit has *recommended* that the Director of Home Affairs should:**

- (a) **monitor the effectiveness of annual inspections in identifying non-compliance with licence requirements; and**
- (b) **take necessary measures to enhance the conduct of annual inspections, having regard to the need for taking a risk-based approach, incorporating surprise elements into inspections, and compiling adequate management information.**

Response from the Government

2.35 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD will:

- (a) enhance the Application Tracking Facility System to better monitor the inspections; and
- (b) review the method of selecting licensed premises for annual inspections for enhancement with a view to incorporating a risk-based approach and surprise elements, as appropriate.

PART 3: COMBATING UNLICENSED ESTABLISHMENTS

3.1 This PART examines the OLA's work in combating unlicensed establishments, focusing on the following issues:

- (a) keeping watch on suspected unlicensed establishments (paras. 3.2 to 3.8);
- (b) investigating suspected unlicensed establishments (paras. 3.9 to 3.18); and
- (c) prosecuting unlicensed establishments (paras. 3.19 to 3.27).

Keeping watch on suspected unlicensed establishments

3.2 Operation of unlicensed establishments is a criminal offence (see para. 1.9). Within the OLA, the Enforcement Team (see Appendix A) is responsible for combating unlicensed establishments (Note 8).

3.3 To identify suspected unlicensed establishments, the Enforcement Team collects information from various sources. Examples are complaints from the public, referrals from other departments (e.g. the Buildings Department, the Fire Services Department, the Hong Kong Police Force, and the Immigration Department), internal referrals (e.g. unprotected cases referred from the BSU — see para. 2.23), and information collected by the Enforcement Team itself (e.g. through conducting surveillance operations at selected buildings and browsing websites). Taking into account the information collected, cases will be opened or updated:

Note 8: *As at 30 June 2017, the Enforcement Team had a manpower of 75 staff, including 8 disciplined service staff, 32 non-civil service staff (e.g. Senior Licensing Inspectors and Licensing Inspectors) and 35 part-time staff (i.e. Licensing Assistants).*

- (a) for premises which have not been investigated before, the Enforcement Team will open new cases of suspected unlicensed establishments (hereinafter referred to as “suspected cases”); and
- (b) for premises which were previously or are currently under investigation, the Enforcement Team will reactivate the previous “suspected cases”, update the reactivated “suspected cases” or the “suspected cases” currently under investigation, and follow up the updated “suspected cases”.

The Enforcement Team takes a series of follow-up actions on suspected cases, such as inspecting the premises concerned, collecting evidence of operation of unlicensed establishments, and instigating prosecutions where there is sufficient evidence.

3.4 The Enforcement Team will close a suspected case when follow-up actions are completed, namely, when no unlicensed establishment is discovered, or when the unlicensed establishment discovered is no longer operating (e.g. after the case has been prosecuted). Suspected cases with follow-up actions in progress are referred to as “outstanding” cases (including cases for which prosecutions are in-progress). During the period from January 2012 to June 2017, the number of outstanding suspected cases had doubled from 644 as at 1 January 2012 to 1,322 as at 30 June 2017 (see Table 4).

Combating unlicensed establishments

Table 4

**Number of suspected cases
(2012 to June 2017)**

	2012	2013	2014	2015	2016	2017 (up to June)
Outstanding cases as at 1 January (a)	644	1,163	1,086	1,223	1,170	1,249
Cases opened or reactivated (b)	1,008	958	1,166	891	1,135 (Note)	751 (Note)
Cases closed (c)	489	1,035	1,029	944	1,056	678
Outstanding cases as at 31 December (d)=(a)+(b)-(c)	1,163	1,086	1,223	1,170	1,249	1,322 (as at 30 June)

Source: Audit analysis of HAD records

Note: The increased number of cases was partly due to a bulk complaint on hundreds of suspected unlicensed guesthouses, made in July 2016 by an association of licensed guesthouses. Taking into account the information provided in the bulk complaint, 176 and 144 suspected cases were opened or reactivated in 2016 and 2017 respectively.

Remarks: For some cases, full addresses of the suspected unlicensed establishments were not known (e.g. not provided by complainants). These cases included complaints lodged against certain buildings, certain floors of certain buildings or certain websites (see Case 3 of para. 3.11). As at 30 June 2017, of the 1,322 outstanding cases, there were 111 such cases.

Need to monitor the increasing number of unresolved suspected cases

3.5 Despite the Enforcement Team's efforts in completing follow-up actions on suspected cases (e.g. 1,056 cases closed in 2016 — see Table 4 in para. 3.4), as at 30 June 2017, there were still 1,322 outstanding cases. Of these outstanding cases, many (270 cases or 20%) had been outstanding for more than three years (see Table 5). There was a risk that some unlicensed establishments related to these outstanding cases had been in operation for a long time.

Table 5

**Age analysis of outstanding suspected cases
(30 June 2017)**

Time elapsed since case opened/reactivated	No. of cases	Percentage
≤ 1 year	662	50 %
> 1 year and ≤ 2 years	231	18 %
> 2 years and ≤ 3 years	159	12 %
> 3 years and ≤ 4 years	109	8 %
> 4 years and ≤ 5 years	73	5 %
> 5 years	88 (Note 1)	7 %
Total	1,322	100 %

Source: Audit analysis of HAD records

Note 1: One extreme case had been outstanding for 15 years since June 2002.

Note 2: The 270 cases included 90 (33%) cases for which prosecutions had been instigated.

3.6 On a regular basis, the OLA reported to the HAD management on its activities in combating unlicensed establishments. The information reported included statistics on prosecutions and convictions under the HAGAO. However, it was not the OLA's practice to compile and report information on the number of outstanding suspected cases (see Table 4 in para. 3.4) and their outstanding durations (see Table 5 in para. 3.5) for consideration by the HAD management. Such management information would facilitate monitoring long outstanding suspected cases, as well as making informed decisions to enhance follow-up actions on suspected cases where necessary.

Audit recommendations

- 3.7 **Audit has *recommended* that the Director of Home Affairs should:**
- (a) **ensure that adequate management information for monitoring outstanding suspected cases is compiled; and**
 - (b) **keep the number of outstanding suspected cases, particularly those long outstanding cases, under close watch, with a view to taking timely measures for enhancing follow-up actions on suspected cases.**

Response from the Government

3.8 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD has been monitoring outstanding cases with the aid of the Enforcement Management Information System, and will enhance efforts on this front.

Investigating suspected unlicensed establishments

- 3.9 To investigate suspected cases, the Enforcement Team conducts inspections and collects evidence of operation of unlicensed establishments, as follows:
- (a) initial inspections are conducted to collect circumstantial evidence of operation of unlicensed establishments, such as the presence of guesthouse signboards, advertising posters, keepers for the establishments, and lodgers at the establishments; and
 - (b) where circumstantial evidence indicates that unlicensed establishments are operating, further inspections are conducted to collect evidence for instigating prosecutions. The inspections usually include decoy operations (i.e. Enforcement Team staff pretending to be lodgers to patronise the unlicensed establishments).

Difficulties in collecting evidence for prosecution

3.10 As shown in Table 5 of paragraph 3.5, as at 30 June 2017, 270 suspected cases had been outstanding for a long period of time (more than three years). Among these 270 long outstanding suspected cases, prosecutions had been instigated for 90 (33%) cases. For the remaining 180 (67%) cases, evidence for prosecution had been difficult to collect. Case 2 shows an example.

Case 2

Difficulties in collecting evidence for prosecuting a long outstanding suspected case (January 2012 to June 2017)

1. In January 2012, a member of the public lodged with the HAD a complaint on the illegal operation of an unlicensed establishment. The establishment in question was located in a flat within a multi-storey building. The Enforcement Team accordingly opened a suspected case.

2. Up to 30 June 2017, in more than five years, the Enforcement Team received nine more complaints on the illegal operation at the establishment, and paid 66 visits to the establishment for conducting inspections and decoy operations. Of the 66 visits:

- (a) in 58 visits, inspecting staff could not enter the establishment. The door was not answered; and
- (b) in 8 visits, inspecting staff successfully entered the establishment. The staff found that:
 - (i) the establishment had three rooms, with lodgers from, for example, the Mainland, Taiwan, Malaysia and Singapore; and
 - (ii) in one instance in January 2017, the lodgers admitted that they rented the place for several days through Website A (see para. 3.11).

3. The establishment did not serve walk-in lodgers nor did it have a keeper. It also did not display any signboards nor advertising posters. As at 30 June 2017, some five years had elapsed since the case was opened, sufficient evidence had not been collected for prosecution.

Audit comments

4. The OLA was unable to collect sufficient evidence of operation of the unlicensed establishment for prosecution. Further measures are required to facilitate the investigations of suspected unlicensed establishments not serving walk-in lodgers.

Source: Audit analysis of HAD records

Need for effective measures in conducting investigations

3.11 Website A (see Case 2 in para. 3.10), and other similar websites, are commonly referred to as online marketplaces. They provide platforms for various types of temporary accommodation, including hotels and guesthouses, and home-stay lodging (Note 9). Through such websites, operators (including homeowners) can offer sleeping accommodation and interact with lodgers to conclude a renting. This mode of operation would require additional measures (e.g. conduct of decoy operations) to supplement the OLA's investigations. However, decoy operations had not always been conducted (see Case 3 for an example).

Note 9: *Home-stay lodging refers to the staying of lodgers in the homes of local people.*

Case 3

Decoy operations not conducted (January to June 2017)

1. In January 2017, the Enforcement Team opened a suspected case upon receiving a complaint on an unlicensed establishment operating through Website A. The complaint provided the establishment's webpage on Website A but not its full address.

2. Since then until 30 June 2017, for five times, the Enforcement Team staff visited the establishment's webpage on Website A. The establishment's full address was not found. In three times, the Enforcement Team staff sent messages (through Website A) to the establishment's operator enquiring about the establishment (e.g. its availability), but the operator did not respond.

3. Due to operational considerations, the Enforcement Team did not arrange its staff to conduct decoy operations through Website A (i.e. pretending to be lodgers to patronise the establishment). As at 30 June 2017, five months had elapsed since the case was opened, there had been no progress in the investigation.

Audit comments

4. In browsing Website A, Audit noted that the establishment's operator also provided 40 rental units other than the one in question. The OLA did not have effective measures for investigating suspected unlicensed establishments which operated through Website A.

Source: HAD records and information on the Internet

3.12 About Website A, Audit further noted that:

- (a) the number of public complaints on unlicensed establishments operating through Website A (e.g. Case 3 in para. 3.11) had increased from 11 in 2015 to 35 in 2016, and further to 65 in 2017 (up to 30 June 2017); and

- (b) according to the OLA, up to 30 June 2017, among the unlicensed establishments which had been prosecuted, 6 of them had been found operating through Website A. The 9 prosecutions of the 6 unlicensed establishments accounted for 1% of the 832 prosecutions since 2012.

Based on Audit's browsing of Website A, a total of 8,000 rental units in Hong Kong were posted on the Website in July 2017. Upon enquiry, the HAD informed Audit in September 2017 that the OLA had since July 2012 continuously made appeals to online platforms, namely, requesting them to post only licensed establishments on their websites and to help publicise the licence requirements under the HAGAO.

3.13 The use of online platforms is becoming more common these days. There is a risk that more unlicensed establishments would be operating through these platforms. Audit considers that the HAD needs to explore further measures to facilitate the investigations of suspected unlicensed establishments operating through online platforms. The HAD also needs to enhance its efforts in appealing to online platform operators to post only licensed establishments on their websites.

Need to make reference to overseas experiences

3.14 The HAGAO is currently under review (see para. 1.15). The proposed legislative amendments intended to enable the OLA to take stronger enforcement actions are as follows:

- (a) if there is sufficient evidence, circumstantial or otherwise, showing that any premises are used as an unlicensed establishment, the owner, tenant or occupier (not including a lodger) of the premises are liable to prosecution. Under the present legislation, only the persons who operate, keep, manage or control the establishment are liable; and
- (b) the OLA can apply to the Court for a search warrant to allow enforcement officers to enter into, or break in when necessary, a suspected unlicensed establishment.

3.15 The above amendments, however, may not be entirely relevant to help overcome certain difficulties in investigations. For example, for unlicensed establishments operating through online platforms:

Combating unlicensed establishments

- (a) while circumstantial evidence may provide the basis for instigating prosecutions against owners, tenants or occupiers (see para. 3.14(a)), such evidence (e.g. the presence of signboards, advertising posters, and keepers) may not be available (see Case 2 of para. 3.10); and
- (b) for many suspected unlicensed cases, full addresses of the establishments concerned are difficult to ascertain (see Case 3 of para. 3.11). It may not be feasible for the OLA to apply for a search warrant (see para. 3.14(b)) to collect evidence for these cases.

3.16 In this connection, Audit noted that a number of overseas cities had enacted legislation to combat illegal provision of sleeping accommodation through the Internet. Audit considers that in exploring further measures to combat unlicensed establishments, the HAD may make reference to overseas experiences.

Audit recommendations

3.17 **Audit has *recommended* that the Director of Home Affairs should:**

- (a) **explore further measures to facilitate the investigations of suspected unlicensed establishments;**
- (b) **step up efforts in appealing to online platform operators to post only licensed hotels and guesthouses on their websites; and**
- (c) **in exploring further measures to combat unlicensed establishments, consider making reference to overseas experiences as appropriate.**

Response from the Government

3.18 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD will:

- (a) explore the feasibility of further measures to facilitate investigation and combating of suspected unlicensed establishments, making reference to overseas experience as appropriate; and

- (b) step up publicity measures, including appeals to online platform operators to post only licensed hotels and guesthouses on their websites.

Prosecuting unlicensed establishments

3.19 Under the HAGAO, a person who operates an unlicensed establishment is liable on conviction to a fine of \$200,000 and imprisonment for 2 years, and a fine of \$20,000 for each day the offence continues.

Recalcitrant operators

3.20 In the period from 2012 to 2017 (up to 30 June 2017), 832 prosecutions were instigated by the OLA on 467 unlicensed establishments, resulting in 779 convictions. Table 6 shows the distribution of the 832 prosecutions among the 467 unlicensed establishments.

Combating unlicensed establishments

Table 6

**Number of prosecutions instigated on unlicensed establishments
(2012 to June 2017)**

No. of prosecutions per establishment (a)	No. of establishments (b)	Total no. of prosecutions (c) = (a) × (b)
1	295	295
2	90	180
3	36	108
4	14	56
5	17	85
6	4	24
7	7	49
8	2	16
9	1	9
10	1	10
Total	467	832

Source: Audit analysis of HAD records

3.21 Audit analysed the penalties imposed on the 779 convictions (see para. 3.20) resulted from the 832 prosecutions and noted that:

- (a) for 727 convictions, fines had been imposed, the amounts of which ranged from \$100 to \$60,000. The most common amount was \$8,000 (231 times); and
- (b) for 79 convictions, imprisonment had been imposed, the durations of which ranged from 1 day to 4 months. The most common duration was 2 months (23 times).

3.22 Audit noted that, for fined cases, an unscrupulous operator might treat penalties as part of operating costs regardless of repeated prosecutions. For imprisonment cases, the person caught red-handed and prosecuted was usually a

keeper rather than the operator behind (i.e. the business owner). Case 4 shows an example.

Case 4

An unlicensed establishment repeatedly prosecuted (May 2006 to June 2017)

1. In May 2006, the OLA received a complaint on an unlicensed establishment which was a guesthouse. The OLA carried out usual enforcement actions (e.g. inspections and decoy operations). Up to 30 June 2017, in more than 10 years, the OLA instigated 14 prosecutions on the unlicensed guesthouse. Details of the prosecutions and penalties imposed were as follows:

- (a) a total of 7 offenders were prosecuted and convicted, each was convicted from one to six times;
- (b) fines were imposed on 13 convictions. The amounts of fines ranged from \$2,000 to \$20,000 (imposed on the third conviction of an offender who was convicted three times); and
- (c) imprisonment was imposed on 4 convictions, namely, the third to sixth convictions of an offender. The durations of imprisonment were respectively one month (suspended), three months (suspended), two weeks, and two months (plus three months of suspended imprisonment then activated).

2. In February 2017, the case was closed since the unlicensed guesthouse was under renovation and ceased to operate.

Audit comments

3. The operator of the unlicensed guesthouse was recalcitrant. There is a need for enhanced measures (see paras. 3.23 to 3.25) to give a clear message to the community that operating unlicensed establishments is a criminal offence, which may risk the life and property of lodgers and the public.

Source: Audit analysis of HAD records

Need for enhanced measures for prosecuting unlicensed establishments

3.23 The HAGAO is currently under review (see para. 1.15). The proposed legislative amendments intended to enhance the deterrent effect on operating unlicensed establishments are as follows:

- (a) to increase the maximum fine from \$200,000 to \$500,000, and the maximum imprisonment from 2 years to 3 years; and
- (b) to enable the OLA to apply to the Court, upon the second conviction of an unlicensed establishment, to issue a closure order against the premises concerned for 6 months.

3.24 It is pertinent to note that under section 5 of the existing HAGAO, a person who operates an unlicensed establishment is liable on conviction to a fine of \$20,000 for each day the offence continues (see para. 3.19). However, this continuous offence provision has so far not been invoked.

3.25 Audit considers that the HAD needs to keep in view, for warranted cases, the possible invoking of the continuous offence provision under the existing HAGAO, as well as the possible invoking of other relevant offence provisions (e.g. issuing closure orders — see para. 3.23(b)) in the future.

Audit recommendation

3.26 **Audit has *recommended* that the Director of Home Affairs should keep in view, for warranted cases, the possible invoking of the continuous offence provision under the existing HAGAO, as well as the possible invoking of other relevant offence provisions (e.g. issuing closure orders) in the future.**

Response from the Government

3.27 The Director of Home Affairs agrees with the audit recommendation.

PART 4: OTHER ADMINISTRATIVE AND LICENSING ISSUES

4.1 This PART examines other administrative and licensing issues relating to the regulation of licensed hotels and guesthouses, focusing on the following issues:

- (a) cost recovery (paras. 4.2 to 4.11);
- (b) caseloads of Licensing Inspectors (paras. 4.12 to 4.20); and
- (c) home-stay lodging (paras. 4.21 to 4.25).

Cost recovery

4.2 According to Financial Circular No. 6/2016 entitled “Fees and Charges”, it is the Government’s policy that fees charged by the Government should in general be set at levels adequate to recover the full cost of providing the goods or services. Government fees should generally be reviewed and, where necessary, revised on an annual basis.

4.3 The Hotel and Guesthouse Accommodation (Fees) Regulations (Cap. 349B) have prescribed the fees for issuing new licences and renewal licences. According to the Regulations, the fees payable are based on the licence period and the number of rooms of the licensed establishment. Currently, the fees for new licences range from \$4,570 (for a 1-year licence of an establishment with one to three rooms) to \$107,100 (for a 7-year licence of an establishment with more than 500 rooms). The fees for renewal licences range from \$2,650 to \$63,150 respectively. The amounts of fees collected in 2016-17 totalled \$3.9 million.

Audit review in 2006

4.4 In 2006, Audit carried out a review of the licensing of hotels and guesthouses. The review indicated that:

Other administrative and licensing issues

- (a) up to June 2006, the objective of full cost recovery had not yet been achieved for the issuing of licences;
- (b) substantial work was carried out in processing licence applications which were subsequently rejected/withdrawn. However, the cost of such work had been excluded from the OLA's costing exercises; and
- (c) a licensee might apply to transfer his licence to another person. A fee of \$140 was collected by the OLA for the transfer in accordance with the Schedule of the Fees for Official Signatures and Miscellaneous Services Notice (Cap. 2M) (Note 10). The fee of \$140 might not have recovered the full cost (Note 11).

4.5 In response to the above observations, the Director of Home Affairs informed Audit in September 2006 that:

- (a) the licence fees under the Hotel and Guesthouse Accommodation (Fees) Regulations were being reviewed, and the fee proposals were being prepared in accordance with the Financial Services and the Treasury Bureau (FSTB) guidelines to achieve full cost recovery (Note 12); and
- (b) the OLA would review whether the cost in processing rejected/withdrawn applications should be recovered. The OLA would also consider the feasibility of revising the fee to be charged for transfer of licences. The implementation of both recommendations would require legislative

Note 10: *The Hotel and Guesthouse Accommodation (Fees) Regulations have not prescribed any fee for transfer of licences. According to the Public Finance Ordinance (Cap. 2), where any Ordinance requires or authorises any transfer of any document by a public officer, such fee shall be payable therefor as may be prescribed by law. If no fee is prescribed, the fee stated in the Schedule of the Fees for Official Signatures and Miscellaneous Services Notice is to be adopted.*

Note 11: *In processing an application for transferring a licence, the OLA would carry out additional work such as vetting the application for any irregularities, and ascertaining whether the transferee had maintained good records if the licence concerned was a multi-year licence.*

Note 12: *The fee proposals had been finalised. After completing the necessary procedures, a new set of fees took effect on 1 November 2007.*

amendments to the Hotel and Guesthouse Accommodation (Fees) Regulations of the HAGAO.

The audit observations and the Director of Home Affairs' response were included in Chapter 8 of the Director of Audit's Report No. 47 of October 2006.

Need to step up efforts in recovering costs

4.6 Audit noted that, in 2016-17, full cost recovery was still not achieved for the licensing of hotels and guesthouses. Based on the HAD's costing review conducted at the 2016-17 price level, the cost recovery rates of the current licence fees (see para. 4.3) ranged from 32% to 75% for new licences, and from 40% to 72% for renewal licences.

4.7 A chronology of the HAD's attempts to revise the licence fees of hotels and guesthouses is at Appendix C. The chronology shows little progress in revising the licence fees over the years since the last revision in November 2007. It is worth noting that:

- (a) ***New licences and renewal licences.*** The current licence fees took effect about 10 years ago in November 2007 (see Item 1 in Appendix C). Since November 2007, the HAD had made five attempts involving five fee proposals (see Items 2, 4, 6, 8 and 11 in Appendix C) to revise the licence fees. However, none of the proposals had been implemented;
- (b) ***Rejected/withdrawn applications.*** For unsuccessful applications, no licences would be issued and hence no licence fees would be collected (see para. 4.4(b)). To help recover the cost in processing rejected/withdrawn applications, the HAD intended to split the fees of new licences into application fees and licence fees (see Item 2 in Appendix C). According to the HAD, the new fee structure would involve more complicated legislative process; and
- (c) ***Transfer of licences.*** The Hotel and Guesthouse Accommodation (Fees) Regulations did not prescribe any fee for transfer of licences (see Note 10 to para. 4.4(c)). The HAD intended to introduce a new fee for such transfer (see Item 2 in Appendix C). According to the HAD, the

Other administrative and licensing issues

new fee would involve more complicated legislative process. Meanwhile, the OLA adopted a fee of \$155 for transfer of licences, which was the fee stated in the Schedule of the Fees for Official Signatures and Miscellaneous Services Notice (see Note 10 to para. 4.4(c)).

4.8 In the aforementioned five attempts, shortage of time (see Items 7, 10, 13 and 16 of Appendix C) was the major reason for not taking forward the fee proposals. In Audit's view, good planning is essential for the timely revision of licence fees. Furthermore, it is not satisfactory that under-recovery of cost has persisted for more than a decade.

4.9 In this connection, Audit noted that the HAD had informed the FSTB in November 2016, March 2017 and June 2017 that:

- (a) it was more appropriate to revise the licence fees after completing the amendment of the HAGAO; and
- (b) subject to the progress in amending the HAGAO, a work plan for revising the licence fees would be formulated in due course.

Audit considers that the HAD needs to, taking into account the need for recovering the various costs (i.e. in issuing and transferring licences, and in processing rejected/withdrawn licence applications), instigate measures to ensure that the work plan for revising the licence fees is formulated in a timely manner. The HAD also needs to monitor the implementation of the work plan to ensure that the objective of cost recovery is achieved.

Audit recommendations

4.10 **Audit has *recommended* that the Director of Home Affairs should:**

- (a) **take measures to ensure that a work plan for revising the licence fees of hotels and guesthouses is formulated in a timely manner;**

- (b) **in formulating the work plan, take into account the need for recovering the costs in issuing and transferring licences, as well as the costs in processing rejected/withdrawn licence applications; and**
- (c) **monitor the implementation of the work plan to ensure that the objective of cost recovery is achieved.**

Response from the Government

4.11 The Director of Home Affairs agrees with the audit recommendations. She has said that the HAD will take into account the progress of amending the HAGAO and formulate a work plan for revising the licence fees in due course.

Caseloads of Licensing Inspectors

4.12 The OLA's Enforcement Team is responsible for investigating unlicensed establishments. Cases of suspected unlicensed establishments (e.g. identified through public complaints) are each assigned to a responsible officer (case officer). Case officers need to follow up their cases and conduct inspections on the premises concerned.

4.13 As at 30 June 2017, the OLA had 24 Licensing Inspectors (non-civil service contract staff) who were all designated as case officers. They were overseen by the supervisory staff (Note 13) of the Enforcement Team. Working under the Licensing Inspectors were 35 Licensing Assistants (part-time staff) who assisted in duties such as conducting inspections.

4.14 When a suspected unlicensed establishment is first identified, the Enforcement Team will open a new file for the case. Licensing Inspectors take turns

Note 13: *As at 30 June 2017, the supervisory staff comprised 2 Assistant Divisional Officers, 6 Senior Station Officers and 6 Senior Licensing Inspectors.*

Other administrative and licensing issues

on a cycle basis to take up new files (Note 14). According to the OLA, this allocation mechanism:

- (a) aims to ensure fairness in work allocation and encourage Licensing Inspectors to take responsibility to complete their allocated cases efficiently; and
- (b) is in line with the principle and spirit of corruption prevention by limiting individual officers' control on the allocation of cases.

Need to closely monitor caseloads

4.15 As at 30 June 2017, the 24 Licensing Inspectors had in total a caseload of 1,322 outstanding cases (Note 15). On average, each Licensing Inspector had a caseload of 55 outstanding cases. Table 7 shows that the caseloads of individual Licensing Inspectors were quite uneven, ranged from 32 cases (i.e. 58% of the average caseload of 55 cases) to 75 cases (i.e. 136% of the average caseload of 55 cases).

Note 14: *According to the HAD, in circumstances where different locations (e.g. different units in a building) are suspected to be involved in an unlicensed establishment's operation, a series of files will be opened. Each file in the series corresponds to a suspected location. New files are allocated one by one to Licensing Inspectors. For files in a series, the entire series is allocated in one lot, as if the entire series is a single file. Licensing Inspectors take turns on a cycle basis to take up new files/new series of files.*

Note 15: *Outstanding cases were cases for which follow-up actions, e.g. investigation and prosecution actions, were in progress. Licensing Inspectors were also responsible for following up outstanding cases under other ordinances (see Note 3 to para. 1.14). Caseloads under the HAGAO accounted for the majority (about 90%) of Licensing Inspectors' caseloads.*

Table 7

**Caseloads of Licensing Inspectors
(30 June 2017)**

Caseload (No. of outstanding cases)	No. of Licensing Inspectors with the caseload	Average no. of outstanding cases per Licensing Inspector	Average no. of long outstanding cases per Licensing Inspector (Note)
32 to 40	6	36	6
41 to 50	3	48	10
51 to 60	6	55	9
61 to 70	5	67	13
71 to 75	4	73	22
Overall	24	55	11

Source: Audit analysis of HAD records

Note: Long outstanding cases referred to those cases which remained outstanding for more than three years.

4.16 The large variations in caseloads among the 24 Licensing Inspectors was not satisfactory. For Licensing Inspectors with heavy caseloads, there was a risk that cases of suspected unlicensed establishments could not be dealt with expeditiously and effectively. In fact, as can be seen from Table 7, Licensing Inspectors with heavier caseloads generally tended to have more long outstanding cases.

4.17 Audit noted that it was not the practice of the OLA to compile statistics of caseloads for management information, or for discussion in regular management meetings. Upon enquiry, the HAD informed Audit in September 2017 that if the caseload of an Licensing Inspector was getting unmanageable, the supervisor (i.e. the Senior Licensing Inspector) would review the situation and assign other Licensing Inspectors to assist as appropriate. The Senior Licensing Inspector would also conduct inspections personally if the situation warranted.

Other administrative and licensing issues

4.18 Audit considers that the HAD needs to monitor the caseloads of Licensing Inspectors more closely and take early measures to rectify any unsatisfactory caseload situation where necessary (e.g. promptly reallocating cases where caseloads are excessively high or low, and enhancing the efficiency of individual Licensing Inspectors).

Audit recommendations

4.19 Audit has *recommended* that the Director of Home Affairs should:

- (a) more closely monitor the caseloads of Licensing Inspectors; and
- (b) take early measures to rectify any unsatisfactory caseload situation where necessary.

Response from the Government

4.20 The Director of Home Affairs agrees with the audit recommendations.

Home-stay lodging

4.21 There have been calls to develop home-stay lodging in Hong Kong. From the tourism perspective, developing more diversified tourist accommodation can help attract a wider range of tourists to Hong Kong.

Need to conduct comprehensive review of issues relating to home-stay lodging

4.22 In July 2017, when reporting to the LegCo Panel on Home Affairs the progress in the review of the HAGAO, the HAD provided in the meeting paper the following information about home-stay lodging:

- (a) the development of home-stay lodging involved land use, planning, tourism, environmental and transport issues, which were under the purview of different bureaux and departments;

- (b) there was both demand for and supply of home-stay lodging in Hong Kong as with other places. Some tourists looked for this unique type of accommodation experience, while some residential flat owners looked for letting their flats as short-term accommodation to tourists;
- (c) if home-stay lodging involved the provision of short-term sleeping accommodation at a fee, a licence under the HAGAO was required. It was pertinent to note that the OLA issued guesthouse (holiday flat) licences to holiday flats which were a type of guesthouses operating on New Territories exempted houses (Note 16). The building safety and fire safety requirements applicable to holiday flats were generally more relaxed as compared to those applicable to general guesthouses; and
- (d) the HAD was exploring with relevant bureaux and departments the idea of drawing up a set of guidelines to cater for licence applications for home-stay lodging, with a view to simplifying the licence requirements without compromising building safety and fire safety.

4.23 In Audit's view, in drawing up the proposed guidelines for home-stay lodging, the HAD needs to address the following issues:

- (a) the need to differentiate home-stay lodging from other types of guesthouses. The OLA also needs to delineate clearly the circumstances in which a home-stay lodging licence, a guesthouse (general) licence or a guesthouse (holiday flat) licence is applicable. This is particularly important because the licence requirements for home-stay lodging are intended to be simpler and less stringent (see para. 4.22(d));
- (b) the need to conform with the proposed legislative amendments when enacted, namely, the legislative amendments that the OLA will take into account the Deed of Mutual Covenant of the building concerned

Note 16: *New Territories exempted houses generally refer to those village houses situated in the New Territories which by virtue of the Buildings Ordinance (Application to the New Territories) Ordinance (Cap. 121) are exempted from certain provisions of the Buildings Ordinance and its subsidiary regulations, including the need for obtaining prior approval and consent to the commencement of works from the Buildings Department.*

Other administrative and licensing issues

(e.g. whether commercial activities are allowed) and local residents' views in processing a licence application; and

- (c) the need to consult relevant stakeholders and to consider whether overseas examples on the regulation of home-stay lodging may be applicable to Hong Kong.

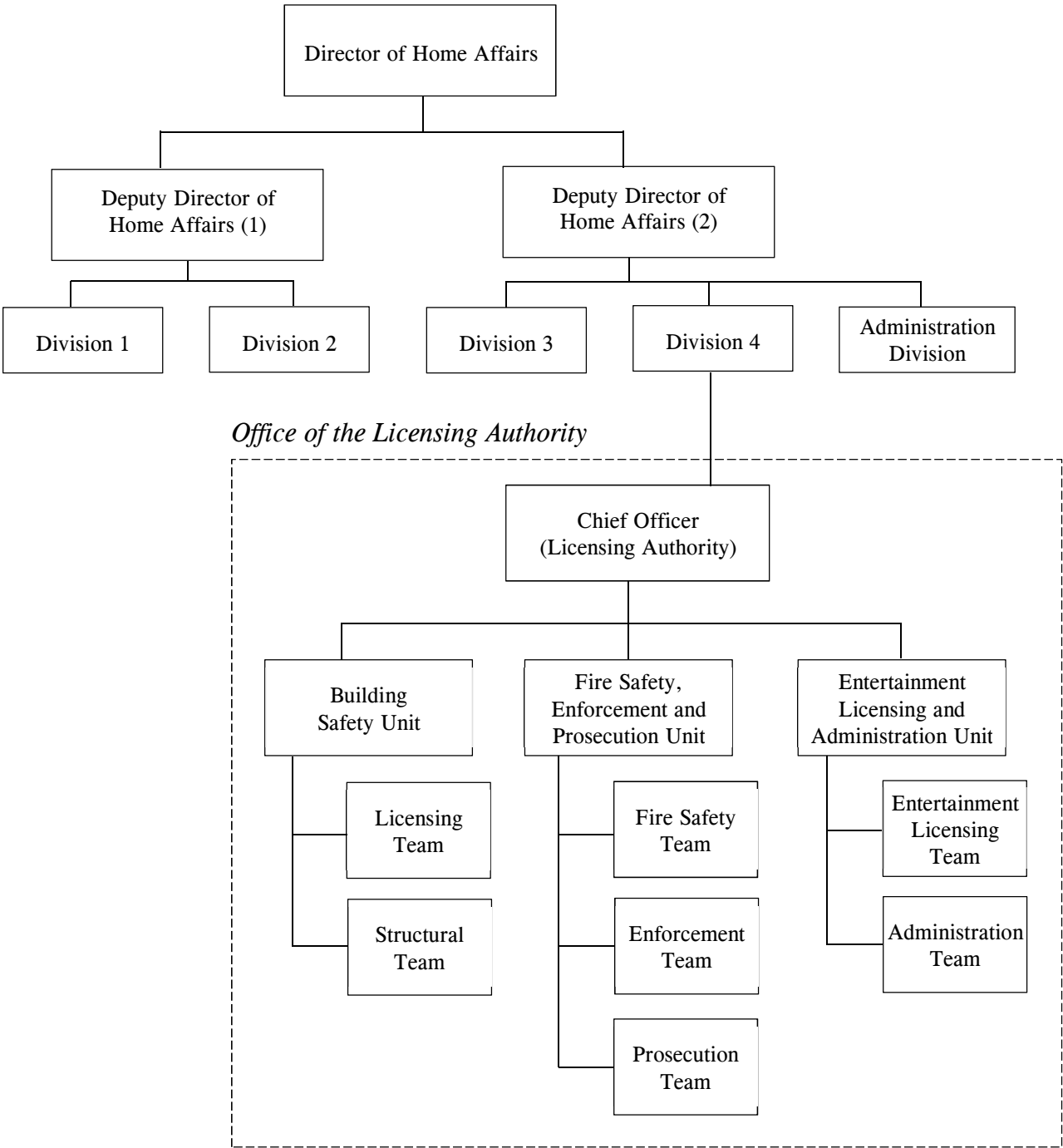
Audit recommendation

4.24 **Audit has *recommended* that the Director of Home Affairs should, in drawing up the proposed guidelines for home-stay lodging, in collaboration with the relevant bureaux and departments, conduct a comprehensive review of issues relevant to home-stay lodging, including those issues raised by Audit in paragraph 4.23.**

Response from the Government

4.25 The Director of Home Affairs agrees with the audit recommendation. She has said that the HAD will explore the feasibility to take forward this audit recommendation.

Office of the Licensing Authority
Organisation chart
(30 June 2017)



Source: HAD records

General licence requirements under Hotel and Guesthouse Accommodation Ordinance

1. Building safety, health and sanitation requirements

The premises should:

- (a) satisfy the following Codes of Practice issued by the Buildings Department:
 - (i) provision of means of escape in case of fire;
 - (ii) fire resisting construction; and
 - (iii) means of access for firefighting and rescue;
- (b) comply with statutory requirements of the Minor Works Control System;
- (c) be free of unauthorised building works; and
- (d) have:
 - (i) adequate lighting and ventilation; and
 - (ii) sufficient sanitary fitments, i.e. waterclosets, wash hand basins, baths and/or showers, together with proper water supply and drainage systems.

2. Fire safety requirements

The premises should satisfy the requirements under:

- (a) the Fire Services Department's Codes of Practice for minimum fire service installations and equipment and inspection, testing and maintenance of installations and equipment;
- (b) the Building (Ventilating Systems) Regulations (Cap. 123J) for ventilation systems;
- (c) the Electricity (Wiring) Regulations (Cap. 406E) and the relevant codes of practice with regard to all fixed electrical installation works; and
- (d) the Gas Safety Ordinance (Cap. 51) with regard to the use, installation and set up of all gas works.

Source: HAD records

Chronology of attempts to revise licence fees for hotels and guesthouses (November 2007 to June 2017)

Item	Date	Key event
1	1.11.2007	A new set of licence fees took effect.
<i>First attempt</i>		
2	10.9.2008	The HAD submitted to the Home Affairs Bureau (HAB) fee proposals (at the 2008-09 price level) for revising the licence fees. The proposals included the introduction of a new fee structure (i.e. splitting fees of new licences into application fees and licence fees — see para. 4.7(b)) and the licence transfer fee (see para. 4.7(c)).
3	16.4.2009	The HAD dropped the fee proposals, as the Government extended the freeze on fees affecting the public's livelihood (introduced in July 2008) to March 2010.
<i>Second attempt</i>		
4	9.7.2010	The HAD submitted to the HAB fee proposals (at the 2010-11 price level) for revising the licence fees.
5	7.10.2010	The HAB gave policy support for the fee proposals of July 2010. However, the HAD did not take forward the proposals, as it planned to revise the licence fees of hotels and guesthouses as well as clubs and bedspace apartments in one go.
<i>Third attempt</i>		
6	12.5.2011	The HAD submitted to the HAB fee proposals (at the 2011-12 price level) for revising the licence fees of hotels and guesthouses, as well as fee proposals for clubs and bedspace apartments.
7	4.5.2012	The HAB's policy support for the fee proposals of May 2011 was still outstanding. The HAD proposed to the HAB (which subsequently gave support) to drop the fee proposals due to the following reasons: (a) the financial year 2011-12 had elapsed; and (b) a restructuring of the OLA was underway, which would affect licence processing procedures and processing costs.

Appendix C
(Cont'd)
(paras. 4.7 and 4.8 refer)

Item	Date	Key event
<i>Fourth attempt</i>		
8	23.4.2013	The HAD submitted to the HAB fee proposals (at the 2013-14 price level) for revising the licence fees.
9	2.10.2013	The HAB gave policy support for the fee proposals of April 2013.
10	25.10.2013	<p>The HAD informed the FSTB and the HAB that, since the HAB's policy support was only obtained in October 2013:</p> <p>(a) introduction of the new fee structure and the licence transfer fee, which would require more complicated legislative amendments, would be deferred and incorporated into the review of the HAGAO (see para. 1.15); and</p> <p>(b) legislative amendments for revising the existing fees would be postponed from March 2014 to July 2014, which was still within the 2013-14 legislative year.</p>
<i>Fifth attempt</i>		
11	6.11.2013	<p>The HAD submitted to the HAB and the FSTB fee proposals (at the 2014-15 price level, but without the new fee structure and the licence transfer fee) for revising the licence fees.</p> <p>The HAB's policy support and the FSTB's endorsement were sought simultaneously.</p>
12	12.12.2013	The HAB gave policy support for the fee proposals of November 2013.
13	20.12.2013	The HAD proposed to the HAB and the FSTB that, to allow more time for consulting the trade, the legislative amendments for revising the existing fees would be postponed from the 2013-14 to the 2014-15 legislative year.
14	4.2014 to 11.2014	The FSTB made enquiries about the fee proposals of November 2013.
15	17.11.2014	The FSTB gave endorsement for the fee proposals of November 2013.

Appendix C
(Cont'd)
(paras. 4.7 and 4.8 refer)

Item	Date	Key event
16	16.12.2014	<p>The HAD informed the FSTB and the HAB that it would drop the fee proposals due to the following reasons:</p> <p>(a) the schedule to go through the necessary legislative process would be extremely tight; and</p> <p>(b) the review of the HAGAO (see para. 1.15) was underway, which would affect licence processing procedures and processing costs.</p>
<i>Recent developments</i>		
17	15.7.2015	Upon the HAB's enquiry, the HAD deliberated that, having regard to the reaction from the trade to the proposed amendments to the HAGAO, the new fee structure and the new licence fees would not be incorporated into the review of the HAGAO (see item 10), but would be postponed to after the review.
18	up to 30.6.2017	Although the HAD had performed reviews of the licence fees (at the 2016-17 and 2017-18 price levels), it had not submitted fee proposals to the HAB.

Source: HAD records

Acronyms and abbreviations

Audit	Audit Commission
BSU	Building Safety Unit
FST	Fire Safety Team
FSTB	Financial Services and the Treasury Bureau
HAB	Home Affairs Bureau
HAD	Home Affairs Department
HAGAO	Hotel and Guesthouse Accommodation Ordinance
LegCo	Legislative Council
OLA	Office of the Licensing Authority

CHAPTER 7

**Education Bureau
Vocational Training Council**

Hong Kong Design Institute

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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HONG KONG DESIGN INSTITUTE

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HONG KONG DESIGN INSTITUTE

Executive Summary

1. The Vocational Training Council (VTC) is a statutory body established in 1982 to provide vocational and professional education and training in Hong Kong. The VTC's training courses leading to formal qualifications are funded by the Education Bureau (EDB). The Hong Kong Design Institute (HKDI) is one of the 13 member institutions of the VTC. Prior to the establishment of the HKDI, the VTC's design-related Higher Diploma (HD) programmes were offered by the Hong Kong Institute of Vocational Education (IVE) at different campuses. In February 2006, the VTC proposed to bring together its three design-related departments of the IVE in five IVE campuses by accommodating them in the dedicated HKDI on a single, purpose-built campus. The proposal also included the reprovisioning of the ageing infrastructure of IVE (Lee Wai Lee) (IVE(LWL)) on a site adjacent to the HKDI. In June 2007, the Finance Committee (FC) of the Legislative Council (LegCo) approved funding of \$992.8 million in September 2006 prices, which was equivalent to \$1,006.3 million in money-of-the-day prices, for the construction of a new VTC campus in Tiu Keng Leng (hereinafter referred to as the Tiu Keng Leng Campus (TKL Campus)) accommodating the HKDI and IVE(LWL). The actual construction cost incurred for the TKL Campus was \$1,287.3 million. The new campus was put into use in 2010/11 (unless stated otherwise, all years mentioned hereinafter refer to academic years). In 2016/17, the four academic departments of the HKDI had 185 teaching staff and offered 21 full-time two-year HD programmes (comprising 19 subvented and 2 self-financed programmes) to secondary school leavers. The total number of students enrolled was 5,476. The Audit Commission (Audit) has recently conducted a review of the HKDI.

Management of programmes

2. *Over-enrolment of new students and high percentage of short contract staff.* There was over-enrolment of Year 1 new students in many programmes in the past years. In 2013, a Programme Board of the HKDI expressed concern on the situation of student over-enrolment of its programmes and suggested that over-enrolment should be avoided in order to ensure the teaching quality and to prevent oversupply of graduates in the market and in the industry. In 2016/17, 13 of the 21 programmes were over-enrolled. Teaching staff establishment is revised based

Executive Summary

on actual enrolment. The total teaching staff establishment of the HKDI increased by 23, 20 and 16 in 2014/15, 2015/16 and 2016/17 respectively due to over-enrolment. Of the 59 additional teaching staff posts, 55 were filled by staff with a contract duration of one year or less (hereinafter referred to as short contract staff). It was stipulated in the instruction issued by the VTC Headquarters that the posts of short contract staff should not exceed 15% of the total number of teaching posts in accordance with the approved programme plan. Due to over-enrolment of students, the overall percentages of short contract staff were 25%, 26% and 25% for 2014/15, 2015/16 and 2016/17 respectively. In 2016/17, for three academic departments, the percentages were 41%, 30% and 17% respectively (paras. 2.3, 2.4, 2.9 and 2.10).

3. ***Need to provide more analysis in programme proposals and conduct manpower survey on design industry.*** In the period 2012/13 to 2016/17, there were 14 new programmes. Before a new programme is introduced, a programme proposal will be prepared outlining the details of the programme. The proposal will be submitted to the VTC Design Discipline Academic Committee for endorsement and to the VTC Vocational Education and Training Academic Board for approval. Audit reviewed the programme proposals for five new programmes and found that some planning information should be added, for example: (a) no information was included in the programme proposals on how the planned numbers of student enrolment were derived; and (b) no details were included in the proposals on the impact on teaching staff resources. Moreover, Training Boards of the VTC conduct regular manpower surveys and publish manpower reports for various industries. However, manpower needs of some programmes offered by the HKDI are not covered by the manpower surveys of the Training Boards. In the Design Discipline Advisory Board meeting held in November 2011, members considered that a formal manpower survey on design industry would provide better understanding on the manpower requirement in design sector and the findings would be useful to the development of HKDI's programmes. Up to July 2017, no manpower survey on the design industry had been conducted (paras. 2.13 to 2.15 and 2.17 to 2.19).

4. ***Evaluation of programme performance.*** The performance of the HKDI's programmes is measured against seven indicators, viz. enrolment rate, retention rate, pass rate, employment rate, further study rate, student satisfaction and employer satisfaction (para. 2.22). Audit noted that:

Executive Summary

- (a) ***Need to monitor completion rates of programmes.*** The VTC reported the retention rates of modules of its HD programmes (i.e. the weighted average of the retention rates of the individual modules of the programme) but not the completion rate of its HD programmes (i.e. the graduation rate of a cohort of students for the two-year HD programmes). The module retention rates were considerably higher than the programme completion rates because some students might have completed the modules they had started but not completed all the required modules for the programme (paras. 2.22 to 2.24);
 - (b) ***Low completion rates.*** The completion rates of some programmes were low (para. 2.26);
 - (c) ***Target employment rate not met.*** The overall employment rate for graduates of the HKDI's HD programmes was 86.4% in 2016 and had been lower than the target employment rate of 90% set by the VTC since 2012. In particular, the employment rates for graduates of four programmes had not achieved the 90% target in every year of 2014 to 2016 (paras. 2.28 and 2.29); and
 - (d) ***Room for improvement in conducting employer satisfaction surveys.*** The employer satisfaction surveys conducted for graduates of 2014 and 2015 only covered a small number of employers of HKDI graduates. Some programmes were not covered in the surveys. For those programmes covered in the surveys, only a small number of employers were surveyed for each programme, ranging from 1 to 6 (para. 2.38).
5. ***Need to improve the extent of performance reporting.*** The VTC discloses on its website various information/statistics (e.g. number of enrolment, number of graduates and employment rate) of the HKDI together with some other member institutions as a whole. Moreover, the VTC discloses on its website the employment rate of HD programme graduates and the number of HD programmes graduates successfully articulated to full-time degree programmes. However, there was no information on the number of graduates who were employed and those who were seeking employment, and the percentage of graduates who successfully articulated to full-time degree programmes (paras. 2.42 and 2.43).

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6. *Need to arrange more relevant industrial attachment.* Industrial attachment (IA) has been included as a mandatory graduation requirement of all HD programmes starting from the 2012/13 intake. There are four categories of IA. Audit noted that: (a) Category A, i.e. attachment in field or industry relevant to the programme of study, is the most preferred category of IA. In the period 2012/13 to 2015/16, while the number of Category A of IA for the HKDI students increased from 710 to 1,282, the proportion of this Category decreased from 70% (i.e. 710 out of 1,015) to 52% (i.e. 1,282 out of 2,477), compared to the corresponding figures for the average of all VTC HD programmes ranging from 82% to 86% in the same period; and (b) the minimum duration of IA for some HD programmes in design discipline offered by two other tertiary institutions were much longer than that by the HKDI (paras. 2.46, 2.47 and 2.50).

Campus development and management

7. *Different views on project cost of winning design of HKDI.* In April 2006, the VTC organised a design competition for the HKDI. Contestants were required to keep their project costs strictly within the budget of \$378 million. However, the cost estimate of the winning design was \$470.4 million. The design included a number of cost saving options which, according to the contestant, could reduce the cost estimate by \$93 million to \$377.4 million. On 10 November 2006, the Jury Panel made its final adjudication and recommended the winning design. On 13 November 2006, the VTC Council Secretariat sought the endorsement of the VTC Estates Committee and approval of the VTC Standing Committee on the recommendation of the Jury Panel. The Committees were informed that, taking into account the cost saving options and the views of the Technical Committee for the competition, the revised cost estimate was \$405 million, which exceeded the construction budget for the design competition of \$378 million. On 20 November 2006, the Standing Committee and the Estates Committee held a joint meeting to ratify the Jury Panel's recommendation. However, there was no documentary evidence showing that the Jury Panel was informed of the assessment made by the Technical Committee on the cost saving options included in the winning design on 10 November 2006 when the Panel made its final adjudication (paras. 3.4 to 3.6, 3.8 and 3.9).

8. *Project development of HKDI.* In the project development stage of the HKDI, various structural schemes, i.e. steel primarily (Steel Scheme), reinforced concrete primarily (RC Scheme), and a mix of steel and reinforced concrete (modified Hybrid Scheme), were considered by the VTC. No documentary evidence was available to show that the schemes had been thoroughly discussed and that the

Executive Summary

modified Hybrid Scheme had been well justified (paras. 3.13, 3.15 and 3.25). Audit observed that:

- (a) ***Application for funding from FC not based on modified Hybrid Scheme which was adopted for construction.*** According to the VTC's guidelines, before funding application can be submitted to LegCo, the VTC needs to submit architectural design and costing to the Architectural Services Department (ArchSD) for approval. In the preparation of the funding application to the FC, the VTC submitted the project cost estimate of \$992.8 million based on the RC Scheme to the ArchSD for vetting in March and April 2007. However, on 30 April 2007, the VTC adopted the modified Hybrid Scheme. No documentary evidence was available showing that the VTC had submitted any revised cost estimate to the ArchSD to take into account the fact that the modified Hybrid Scheme was adopted. On 15 June 2007, the project consultant revised the project estimate from \$992.8 million to \$1,064.1 million based on the modified Hybrid Scheme. There was no documentary evidence showing that the VTC had submitted the revised project estimate of \$1,064.1 million to the ArchSD. In the event, the project cost estimate quoted in the funding application paper submitted to the FC on 22 June 2007 was \$992.8 million indicating the adoption of the RC Scheme (paras. 3.16 and 3.17);
- (b) ***RC Scheme not followed.*** In November 2006, when the VTC Standing Committee and the VTC Estates Committee ratified the recommendation of the Jury Panel, the winning design was based on the RC Scheme. Moreover, the project cost estimate submitted by the VTC for vetting by the ArchSD in March 2007 and the project estimate approved by the FC in June 2007 was based on the RC Scheme. Notwithstanding this, the HKDI was eventually built using the modified Hybrid Scheme (para. 3.22);
- (c) ***More accurate information should have been provided to the VTC Council and the committees.*** At a joint meeting of the Standing Committee, Estates Committee and Steering Committee of the VTC held in February 2008, it was reported that the drawings of the RC Scheme had not yet been cleared by the Buildings Department. Audit noted that the three Committees were not informed that the project team had not submitted the drawings of the superstructure based on the RC Scheme to the Buildings Department for clearance (para. 3.24); and

Executive Summary

- (d) ***Project progress reports not submitted to EDB.*** After approval of FC funding, the EDB had not required the VTC to submit progress reports together with updated budget forecasts and outturn income and expenditure statements at quarterly intervals for the TKL Campus development project according to Financial Circular No. 9/2004 (paras. 3.28 and 3.29).

9. ***Management of campus.*** Audit noted the following issues:

- (a) ***Tennis court not open to the public.*** In June 2007, when seeking funding from the FC of LegCo for the construction of the new TKL Campus, the EDB informed the FC that student sports and amenity facilities (i.e. swimming pool, basketball courts, tennis court and gymnasium) at the new campus would be open to the public during non-school hours. However, the tennis court had not been open to the public (paras. 3.35 and 3.36);
- (b) ***Incorrect utilisation rates.*** The HKDI periodically calculated the utilisation rates of teaching venues for management information. For some of the teaching venues, the utilisation rates reported were overstated (para. 3.38);
- (c) ***Room for increasing the use of the Auditorium for event rental.*** For the period from 2013/14 to 2016/17, Audit noted that, for 81 to 129 days a year, the Auditorium was closed for maintenance, and usage of the Auditorium by external parties was on the low side, ranging from 2 to 10 days a year (para. 3.39); and
- (d) ***Malfunction of lifts and escalators.*** There are 13 lifts and 4 escalators (2 long ones and 2 short ones) at the TKL Campus. The number of breakdown cases of lifts and escalators had increased by 174% from 53 cases in 2014 to 145 cases in 2016. All three routine maintenance and service contracts of the lifts and escalators stipulate that the monthly system service availability shall be maintained at at least 99%. The service availability records were not available and the HKDI had not monitored the system service availability. Audit analysis of the log books revealed that the monthly system service availability of 4 escalators had decreased from 99.7% in January 2015 to 71.0% in June 2017. In the absence of suitable roof and enclosure, the services of the two short escalators needed to be suspended during rainy days or adverse weather conditions. Audit examined the service records for the period from 1 January 2017 to

Executive Summary

30 June 2017 and noted that the 2 short escalators were suspended from operation in 21.2% of the available operating time because of adverse weather. One long escalator had been suspended from operation since 31 March 2017 due to a contractual dispute with the contractor (paras. 3.44 to 3.47, 3.49 and 3.50).

Administrative issues

10. ***Inadequacies in inventory management.*** According to the VTC's requirements, annual stocktaking should be conducted in each financial year. In the 7-year period 2010-11 to 2016-17, stocktaking had not been conducted for three financial years 2010-11, 2012-13 and 2014-15. Stocktaking exercise for financial year 2016-17 was pending as at September 2017. Moreover, a long time had been taken to complete the three stocktaking exercises for 2011-12, 2013-14 and 2015-16. A total of 810 inventory items of original cost of \$2.7 million were found missing in the three annual stocktaking exercises for 2011-12, 2013-14 and 2015-16 (paras. 4.3 to 4.6).

11. ***Campus environmental targets not met.*** Using the 2013/14 as the reference year, the Corporate Environmental Office of the VTC Headquarters set the following campus environmental targets for a two-year review period from 2014/15 to 2015/16: (a) 5% reduction on water consumption; (b) 5% reduction on electricity consumption; and (c) 5% reduction on quantity of paper ordered. Audit noted that the last two of the three environmental targets were not achieved. In April 2016, in order to review energy consumption and improve energy efficiency, the VTC engaged a consultant to conduct an energy audit. In November 2016, the consultant identified several energy saving opportunities to enhance the energy performance. Up to September 2017, the recommendations of the consultancy report were still being followed up by the Safety, Health and Environment Task Force and Central Committee on Safety, Health and Environment (paras. 4.19, 4.20, 4.22, 4.23 and 4.25).

Audit recommendations

12. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in the Executive Summary. Audit has recommended that the Executive Director, VTC should:**

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Management of programmes

- (a) ensure as far as possible that the number of students enrolled should not exceed the plan by a significant margin and any significant deviation from the plan should be fully justified (para. 2.11(a));
- (b) take measures to plan the teaching staff requirement more accurately and to address the high percentage of short contract staff (para. 2.11(d));
- (c) include in the programme proposals more details on the planned number of student intake and impact on teaching staff (para. 2.20(a));
- (d) consider conducting a manpower survey on the design industry periodically and take into account the results of the survey in its programme planning and review (para. 2.20(b));
- (e) consider monitoring the programme completion rates in addition to the module retention rates (para. 2.40(a));
- (f) ascertain the reasons for lower completion rates of some programmes and identify areas for improvement (para. 2.40(b));
- (g) take measures to improve the employment rate of HKDI graduates with a view to meeting the target employment rate of 90% (para. 2.40(c));
- (h) review the criteria for selecting employers for the employer satisfaction survey and take measures to encourage graduates to give consent for the VTC to contact their employers (para. 2.40(e));
- (i) disclose the key performance information and statistics of the HKDI and the other member institutions separately, such as the enrolment

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rate, completion rate, employment rate and employers' satisfaction on its graduates (para. 2.44(a));

- (j) disclose on its website information on the number and the percentage of HKDI graduates who successfully obtained employment and those who successfully articulated to full-time degree programmes (para. 2.44(b));
- (k) take measures to increase the proportion of Category A of IA for the HKDI's HD programmes (para. 2.51(a));
- (l) conduct a review on the minimum duration of IA for the HKDI's HD programmes and consider if there is merit in extending the minimum duration (para. 2.51(c));

Campus development and management

- (m) for future design competitions, if the competition requires the entry designs to fulfil the mandatory budget requirements, thoroughly assess the cost estimates submitted by the contestants before the Jury Panel made its final decision on the result of the competition (para. 3.10);
- (n) for future capital projects:
 - (i) provide up-to-date cost estimate to the ArchSD for comments in seeking funding from the FC of LegCo (para. 3.31(a));
 - (ii) enhance project information provided to the Council and the relevant committees to facilitate them to make informed decisions (para. 3.31(c)); and
 - (iii) take measures to ensure that before adopting a development scheme, the various schemes should be thoroughly discussed and the decision to adopt a particular scheme should be well justified and approved (para. 3.31(d));
- (o) further explore the feasibility of opening the tennis court to the public during non-school hours (para. 3.53(a));

Executive Summary

- (p) take measures to ensure the correctness of the utilisation rates of teaching venues (para. 3.53(b));
- (q) monitor the problem of repeated breakdown cases of the lifts and escalators and, if necessary, take action to address the problem (para. 3.53(f));
- (r) ensure that the contractor attain the performance target on maintenance services under the maintenance and service contract of escalators (para. 3.53(g));
- (s) explore whether any measures can be taken to increase the operating time of the two short escalators and endeavour to resume as soon as possible the service of the long escalator which had been suspended (para. 3.53(h) and (i));

Administrative issues

- (t) conduct annual stocktaking in a timely manner in each financial year according to the inventory guidelines (para. 4.10(a));
- (u) strengthen its inventory control to minimise loss of inventories (para. 4.10(b)); and
- (v) endeavour to achieve the campus environmental targets (para. 4.26(a)).

13. Audit has also *recommended* that the Secretary for Education should, for future government subvented projects, in accordance with Financial Circular No. 9/2004, take measures to ensure that the VTC submits to the EDB project progress reports together with updated budget forecasts and outturn income and expenditure statements upon approval of capital subventions and thereafter at quarterly intervals (para. 3.32).

Response from the VTC and the Government

Executive Summary

14. The Executive Director, VTC and the Secretary for Education agree with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 The Vocational Training Council (VTC) is a statutory body established in 1982 to provide vocational and professional education and training in Hong Kong. The VTC is funded by government subvention under two bureaux, namely the Education Bureau (EDB) and the Labour and Welfare Bureau. Training courses leading to formal qualifications are funded by the EDB and industry-specific and subject-specific training courses of short duration and programmes which do not lead to formal qualifications are funded by the Labour and Welfare Bureau. In 2016-17, the subventions from the EDB and the Labour and Welfare Bureau were \$2,767 million and \$307 million respectively. The Hong Kong Design Institute (HKDI) is one of the 13 member institutions of the VTC (see Appendix A).

1.3 Prior to the establishment of the HKDI, the VTC's design-related Higher Diploma (HD) programmes were offered by the Hong Kong Institute of Vocational Education (IVE) at different campuses. The VTC considered such arrangement not conducive to students' learning and development. In February 2006, the VTC proposed to bring together its three design-related departments (i.e. (a) Design; (b) Fashion and Textiles; and (c) Printing and Digital Media) of the IVE in five IVE campuses by accommodating them in the dedicated HKDI on a single, purpose-built campus. It considered that the integration would pool resources and foster synergy among the design-related departments, and enhance the teaching and learning environment for the delivery of quality design education in Hong Kong. The proposal also included a plan to re-provision the ageing infrastructure of IVE (Lee Wai Lee) (IVE(LWL)) on a site adjacent to the HKDI.

1.4 In June 2007, the Finance Committee (FC) of the Legislative Council (LegCo) approved funding for the construction of a new VTC campus in Tiu Keng Leng (hereinafter referred to as the Tiu Keng Leng Campus (TKL Campus)) accommodating the HKDI and IVE(LWL). The HKDI was put into use in academic

Introduction

year 2010/11 (unless stated otherwise, all years mentioned hereinafter refer to academic years).

Academic programmes offered by the HKDI

1.5 The HKDI has four academic departments. The four departments are:

- (a) ***Department of Design Foundation Studies (DFS)***. The Department of DFS provides broad-based foundation studies for students to develop their interests, preferences and strengths, providing a solid foundation for progression to their study pathways;
- (b) ***Department of Communication Design and Digital Media (CDM)***. The Department of CDM provides programmes in the areas including Creative Media, Visual Communications, Transmedia and Advertising Design;
- (c) ***Department of Fashion and Image Design (FID)***. The Department of FID provides programmes in the areas including Fashion Design, Fashion Image Design and Fashion Business; and
- (d) ***Department of Product and Interior Design (PID)***. The Department of PID (Note 1) provides programmes in the areas including Product, Interior and Exhibition Design and Architectural Design.

1.6 In 2016/17, the four academic departments of the HKDI offered 21 full-time two-year HD programmes (comprising 19 subvented and 2 self-financed programmes) to secondary school leavers (see Appendix B). The total number of students enrolled was 5,476. The tuition fee for subvented programmes and self-financed programmes were \$31,570 and \$53,400 per student per year respectively. Table 1 shows the number of programmes offered and number of students enrolled by the four departments.

Note 1: *The Department of PID was renamed the Department of Architecture, Interior and Product Design with effect from 2017/18.*

Table 1
Number of programmes offered and students enrolled
(2016/17)

	Academic department				Total
	DFS	CDM	FID	PID	
(a) Subvented programme					
No. of programmes	1	6	5	7 (Note)	19
No. of planned enrolment	118	1,781	870	1,393	4,162
No. of student enrolled	152	2,202	919	1,651	4,924
(b) Self-financed programme					
No. of programmes	-	1	1	-	2
No. of planned enrolment	-	287	338	-	625
No. of student enrolled	-	250	302	-	552
(c) Total (a) + (b)					
No. of programmes	1	7	6	7	21
No. of planned enrolment	118	2,068	1,208	1,393	4,787
No. of student enrolled	152	2,452	1,221	1,651	5,476

Source: Audit analysis of HKDI records

Note: Students enrolled in HD in Product, Interior and Exhibition Design (Subject Group) in the first semester will progress to three programmes in the second semester, subject to their choice, academic performance and availability of places. Therefore the number of programmes in the second semester will be 9.

Remarks: Number of enrolment in this table refers to the total number of new enrolment of Year 1 and progressing enrolment of Year 2.

1.7 There are two buildings located in the TKL Campus, namely the HKDI and IVE(LWL). The HKDI and IVE(LWL) share some facilities, for example, the Learning Resource Centre, the Language Centre, the Student Development Office and the sports facilities including the swimming pool and the fitness centre. The VTC monitors the income and expenditure of the TKL Campus as a single accounting unit. Income received and expenditure incurred by the TKL Campus are not allocated to

Introduction

the HKDI and IVE(LWL) separately. For the financial year 2016-17, the TKL Campus received income of \$257 million from programme fees, hire of accommodation and other sundry fees. The expenditure incurred was \$456 million, comprising staff expenditure of \$389 million and operating expenditure of \$67 million (Note 2).

Professional Education and Engagement Centre

1.8 Apart from offering full-time design-related HD programmes to secondary school leavers, the HKDI also offers part-time training programmes through its Professional Education and Engagement Centre on a self-financed basis (see Appendix C). The programmes offered by the Centre include professional diploma/certificate courses and non-award-bearing seminars and workshops. In 2016/17, the Centre offered 24 professional diploma/certificate courses, 3 seminars and 12 workshops. The total number of students enrolled were 1,348. For the financial year 2016-17, the total income received by the Centre amounted to \$5.4 million, whilst total expenditure incurred was about \$4 million, comprising staff expenditure of \$1.7 million and operating expenditure of \$2.3 million.

Organisation of HKDI

1.9 As at 30 June 2017, the HKDI had an establishment of 560 staff, comprising a Principal (Note 3), two Vice Principals (Note 4), 256 teaching staff (Note 5),

Note 2: *The operating expenditure of \$67 million did not include costs of the VTC's central administration and support services (for example, human resources and information technology services and major repairs and maintenance services).*

Note 3: *The Principal of the HKDI also serves as the Principal of IVE(LWL).*

Note 4: *The two Vice Principals are Vice Principal (Academic) and Vice Principal (Administration). They also oversee the operation of IVE(LWL).*

Note 5: *The total number of teaching staff was 256, comprising 185 staff of the four academic departments (DFS, CDM, FID and PID — see para. 1.5), 2 for providing services to students with special education needs, 52 of the Language Centre and 17 of the Student Development Office. The 69 teaching staff of the Language Centre and the Student Development Office deliver modules on language and whole person development to students of both the HKDI and IVE(LWL).*

144 academic supporting staff and 157 administrative staff (Note 6). An organisation chart of the HKDI as at 30 June 2017 is shown at Appendix C.

1.10 As the HKDI is one of the 13 member institutions of the VTC (see para. 1.2), the VTC Headquarters is responsible for some management functions of the HKDI, such as:

- (a) hiring of staff with contract duration of more than one year and staff with open-ended contract;
- (b) processing procurement in excess of \$50,000; and
- (c) major repairs and maintenance.

1.11 Various boards and committees are established under the governance structure of the VTC. The following boards/committees are pertinent to the operation of the HKDI (see Appendix D):

- (a) ***Vocational Education and Training Academic Board (VETAB)***. The VETAB is the academic governing body of the VTC. It sets the overall VTC academic policies, and oversees and approves all aspects of the VTC's academic activities. It also approves the annual programme plan which provides the number of planned enrolment for new intake and progressing intake of each programme;
- (b) ***Design Discipline Academic Committee (DEAC)***. The DEAC reports to the VETAB. It is responsible for the strategic development and academic management of the programmes with advice from the Design Institute Advisory Board (DIAB) and the Design Discipline Advisory Board (DEDAB) (see (e) and (f) below);
- (c) ***Design Discipline Quality Assurance Committee (DEQAC)***. The DEQAC oversees the implementation of the Quality Assurance System and makes recommendations to DEAC and appropriate boards and committees;

Note 6: *The total number of administrative staff was 157, of whom 152 staff provide services to both the HKDI and IVE(LWL) and 5 staff provide services to the Professional Education and Engagement Centre of the HKDI.*

Introduction

- (d) **Programme Boards.** There are four Programme Boards which are responsible for formulating procedures for the design, delivery and development of the HKDI programme curricula, setting academic standards, maintaining academic quality, and reviewing and evaluating the programmes regularly to ensure continuous improvement. The four Programme Boards are CDM Programme Board, FID Programme Board, PID Programme Board (Note 7) and Visual Arts Programme Board;
- (e) **DIAB.** The DIAB gives advice and steering to the HKDI in providing design education, which include:
 - (i) advising on the manpower requirements of the design industry;
 - (ii) advising on and making recommendations to the DEAC on review of the developments of the HKDI; and
 - (iii) receiving a report annually from the DEDAB (see (f) below) on the programme planning and curriculum development; and
- (f) **DEDAB.** The DEDAB recommends to the VETAB on the academic management, which includes:
 - (i) strategic development for the programmes and services offered;
 - (ii) course planning, curriculum development and quality assurance of the programmes offered;
 - (iii) new programmes in emerging areas; and
 - (iv) articulation pathways for further studies and lifelong learning for HKDI graduates.

Note 7: *The PID Programme Board was renamed the Architecture, Interior and Product Design Programme Board with effect from 2017/18.*

TKL Campus

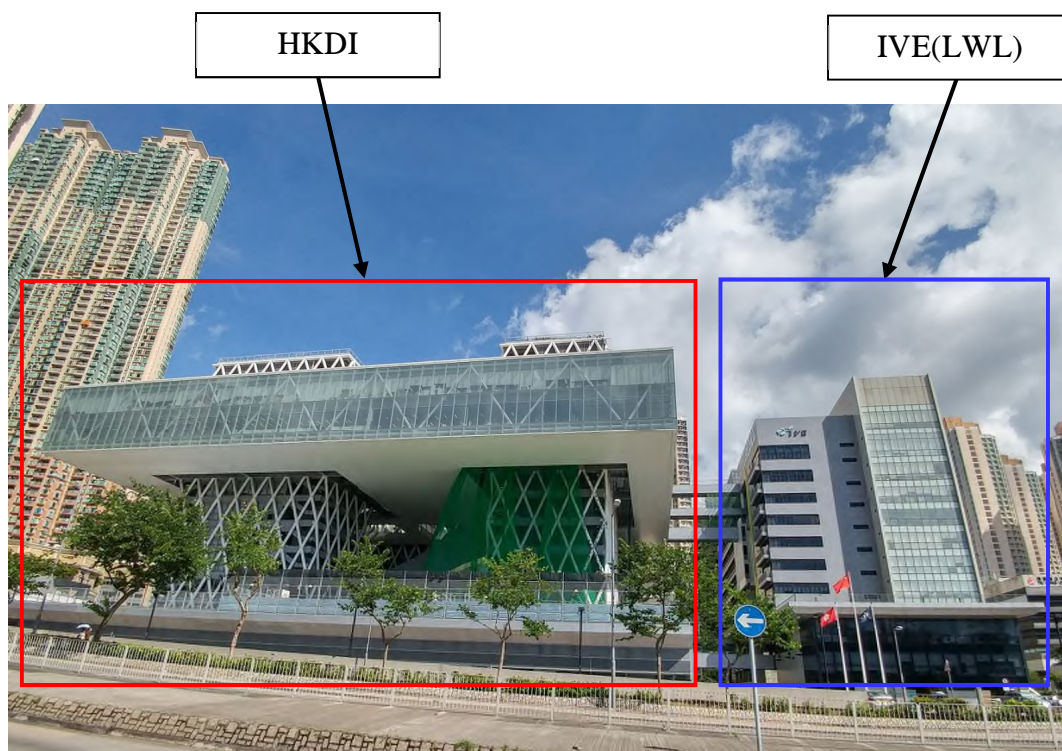
1.12 In June 2007, the FC approved funding of \$1,006.3 million for the proposed TKL Campus. In the paper seeking the FC's approval, the then Education and Manpower Bureau (Note 8) informed the FC that there was a need for the construction of the new campus (see Photograph 1) at Tiu Keng Leng to accommodate the new HKDI campus (see para. 1.3) and to reprovision IVE(LWL). The FC was informed that:

- (a) the new HKDI campus would provide facilities including design studios, television, film and audio studios, drawing rooms, workshops, and language and computer laboratories. The facilities would provide the necessary infrastructure to help the HKDI fulfil its mission to become a leading international provider of foundation studies and lifelong learning in design;
- (b) the ageing infrastructure of IVE(LWL) campus located in Kowloon Tong required upgrading in order to support a modernised provision of vocational education and training;
- (c) IVE(LWL) offered courses in relation to jewellery, watches and clocks, and optics industries, which required design and technology to drive their growth and development. Putting the HKDI and IVE(LWL) campuses on adjacent sites would help achieve better synergy among the various academic disciplines and departments of the IVE; and
- (d) the HKDI, together with the related IVE(LWL) academic departments (i.e. Business Administration, Computing and Information Management, and Engineering Management and Technology Departments) to be accommodated at the new campus, would provide “one-stop” training services for design-related industries ranging from product design, technology, manufacturing, sales and marketing to after-sales services. This would strengthen the capacity of the industries concerned and enhance the content and value of their products and services.

Note 8: *In January 2003, the then Education Department was merged with the then Education and Manpower Bureau. In July 2007, the Bureau was renamed the EDB upon the reorganisation of the Government Secretariat.*

Photograph 1

HKDI and IVE(LWL) at TKL Campus



Source: Photograph taken by Audit Commission on 15 August 2017

1.13 The new campus was put into use in 2010/11. The actual construction cost incurred for the TKL Campus was \$1,287.3 million (Note 9). The TKL Campus has a total net operating floor area of about 43,000 square metres (m²). According to the FC paper of June 2007, the TKL Campus was designed as an open campus. Landscaped areas on the podium would be accessible to the general public. The student sports and amenity facilities (i.e. swimming pool, basketball courts, tennis court and gymnasium) at the new campus would also be open to the public during non-school hours.

Note 9: *The difference of \$281 million between the actual construction cost of \$1,287.3 million and the amount of \$1,006.3 million approved by the FC was funded by the surpluses from the VTC's self-financing activities, the VTC's Council Reserve, Government annual block grant and capital subventions for minor works, and donations (see para. 3.3).*

Audit review

1.14 In March 2017, the Audit Commission (Audit) commenced a review of the HKDI (Note 10). The audit has focused on the following areas:

- (a) management of programmes (PART 2);
- (b) campus development and management (PART 3); and
- (c) administrative issues (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

General response from the VTC

1.15 The Executive Director, VTC agrees with all the audit recommendations. She has said that continuous improvement is always the goal of the VTC in enhancing its performance.

Acknowledgement

1.16 Audit would like to acknowledge with gratitude the full cooperation of the staff of the EDB and the HKDI during the course of the audit review.

Note 10: *While IVE(LWL) is also accommodated in the TKL Campus, the audit review focused on the HKDI and did not cover the operations of IVE(LWL), which is one of the nine IVE campuses.*

PART 2: MANAGEMENT OF PROGRAMMES

2.1 This PART examines the management of programmes, focusing on the following areas:

- (a) enrolment of new students (paras. 2.2 to 2.12);
- (b) programme planning (paras. 2.13 to 2.21);
- (c) evaluation of programme performance (paras. 2.22 to 2.41);
- (d) performance reporting (paras. 2.42 to 2.45); and
- (e) industrial attachment (paras. 2.46 to 2.52).

Enrolment of new students

2.2 In September each year, the HKDI reviews its programme plan and determines the number of planned Year 1 new student enrolment for each programme to be offered in the next academic year. The revised programme plan is submitted to the VETAB (see para. 1.11(a)) for approval in December each year. In 2016/17, the HKDI had a total student enrolment of 5,476, including Year 1 new students of 2,729.

Many programmes were over-enrolled

2.3 Audit noted that there had been over-enrolment of Year 1 new students in many programmes in the past years. In 2013, the CDM Programme Board (see para. 1.11(d)) of the HKDI expressed concern on the situation of student over-enrolment of its programmes and suggested that over-enrolment should be avoided in order to ensure the teaching quality and to prevent oversupply of graduates in the market and in the industry. At various meetings of the Board held in 2016, the possible impact of over-enrolment of students was discussed. The Board members pointed out that:

- (a) equipment would be insufficient for the over-enrolment;
- (b) some external examiners (Note 11) had reflected that they had difficulty in handling the student assessments with large number of students; and
- (c) over-enrolment situation would affect the resources and manpower.

2.4 Table 2 shows the over-enrolment of Year 1 new students for the period 2014/15 to 2016/17. In 2016/17, 13 of the 21 programmes were over-enrolled.

Table 2
Over-enrolment of Year 1 new students
(2014/15 to 2016/17)

Year	No. of programmes offered	No. of programmes with over-enrolment	All programmes			Over-enrolled programmes		
			Planned enrolment	Actual enrolment	Over-enrolment	Planned enrolment	Actual enrolment	Over-enrolment
2014/15	13	12	2,190	2,795	605 (27.6%)	2,040	2,648	608 (29.8%)
2015/16	17	13	2,220	2,804	584 (26.3%)	1,710	2,382	672 (39.3%)
2016/17	21	13	2,265	2,729	464 (20.5%)	1,530	2,143	613 (40.1%)

Source: Audit analysis of HKDI records

Remarks: Number of actual enrolment in this table was the enrolment figure as at 15 October of the year.

Note 11: *An external examiner is appointed for each programme to oversee the overall academic standards/performance of learners in the programme. The duties of an external examiner include vetting the examination papers and marking schemes, and checking the marking of a representative sample of examination scripts, student projects and other assessment works.*

Management of programmes

2.5 Audit noted that for some programmes, the over-enrolment situation had persisted for many years. For instance, for 9 of the 12 over-enrolled programmes in 2014/15, the over-enrolment situation remained in 2015/16 and 2016/17. An analysis of the number of planned enrolment and actual enrolment of these 9 programmes is shown in Table 3.

Table 3

**Nine programmes which had been over-enrolled for three years
(2014/15 to 2016/17)**

Academic department	No. of programmes	2014/15		2015/16		2016/17	
		Planned enrolment	Actual enrolment	Planned enrolment	Actual enrolment	Planned enrolment	Actual enrolment
CDM	4	660	1,014 (154 %)	570	976 (171 %)	570	911 (160 %)
PID	3	600	719 (120 %)	450	629 (140 %)	420	604 (144 %)
FID	1	300	360 (120 %)	300	309 (103 %)	240	262 (109 %)
DFS	1	60	69 (115 %)	60	64 (107 %)	60	84 (140 %)
Overall	9	1,620	2,162 (133 %)	1,380	1,978 (143 %)	1,290	1,861 (144 %)

Source: Audit analysis of HKDI records

2.6 Despite the over-enrolment situation, in 2015/16, the HKDI reduced the number of planned new student intake for 3 of the 9 over-enrolled programmes and in 2016/17, for 2 of the 9 programmes. Audit examination of these programmes revealed that there is no documentary evidence showing:

- (a) the action taken by the HKDI to mitigate the possible adverse impact on the teaching quality of the programmes; and
- (b) the justifications for reducing the number of planned Year 1 student enrolment.

2.7 In December 2016, the CDM Programme Board reported to the DEQAC that:

- (a) the over-enrolment created keen competition and stresses in the learning environment;
- (b) the students had expressed that there were inadequate printers in Learning Resources Centre; and
- (c) a review on planned intake should be conducted for 2017/18. In planning the number of student admission, the resource requirements in manpower and facilities had to be taken into account.

2.8 Audit considers that the HKDI needs to ensure that the number of students enrolled should not exceed the plan by a significant margin. Significant deviation from the plan should be fully justified and managed to mitigate the possible adverse impact on the quality of the programmes.

High percentage of staff with short-term contracts

2.9 Every year in April, the HKDI plans the teaching staff establishment for the next academic year based on planned enrolment. Teaching staff establishment is then revised based on actual enrolment in October. If there is over-enrolment, the HKDI will seek the additional teaching staff posts from the Headquarter's Human Resources Division (HRD). The total teaching staff establishment of the HKDI increased by 23, 20 and 16 (see Table 4) to 177, 186 and 185 in 2014/15, 2015/16 and 2016/17 respectively due to over-enrolment. Of the 59 additional teaching staff posts, 55 were filled by staff with a contract duration of one year or less (hereinafter referred to as short contract staff).

Table 4
Number of additional teaching staff posts
(2014/15 to 2016/17)

	Academic department				Total
	DFS	CDM	FID	PID	
2014/15					
Additional teaching staff posts	3	14	3	3	23
Posts filled by:					
(a) Short contract staff	3	12	3	2	20
(b) Staff with contract duration of more than one year or with open-ended contract	—	2	—	1	3
2015/16					
Additional teaching staff posts	3	12	—	5	20
Posts filled by:					
(a) Short contract staff	3	12	—	5	20
(b) Staff with contract duration of more than one year or with open-ended contract	—	—	—	—	—
2016/17					
Additional teaching staff posts	3	7	2	4	16
Posts filled by:					
(a) Short contract staff	3	6	2	4	15
(b) Staff with contract duration of more than one year or with open-ended contract	—	1	—	—	1

Source: Audit analysis of HKDI records

2.10 It was stipulated in the instruction issued by the Headquarter's HRD that the posts of short contract staff should not exceed 15% of the total number of teaching posts in accordance with the programme plan approved by the VETAB in December every year. Audit analysed the percentage of these short contract staff to the total number of teaching staff and found that due to over-enrolment of students, the overall percentages were 25%, 26% and 25% for 2014/15, 2015/16 and 2016/17 respectively (see Table 5). In 2016/17, for three academic departments (i.e. DFS, CDM and PID), the percentages of short contract staff were 41%, 30% and 17% respectively. Employing too many short contract staff might affect staff stability and morale, and thereby the teaching quality. The HKDI needs to take measures to plan the teaching staff requirement more accurately and to address the high percentage of short contract staff.

Table 5

**Percentages of short contract staff to total number of teaching staff
(2014/15 to 2016/17)**

	Academic department				Overall
	DFS	CDM	FID	PID	
2014/15					
Number of teaching staff (a)	27	70	40	40	177
Number of short contract staff (b)	11	21	7	6	45
Percentage of short contract staff (c) = (b) ÷ (a) × 100 %	41 %	30 %	18 %	15 %	25 %
2015/16					
Number of teaching staff (a)	35	74	36	41	186
Number of short contract staff (b)	15	23	3	7	48
Percentage of short contract staff (c) = (b) ÷ (a) × 100 %	43 %	31 %	8 %	17 %	26 %
2016/17					
Number of teaching staff (a)	34	74	35	42	185
Number of short contract staff (b)	14	22	3	7	46
Percentage of short contract staff (c) = (b) ÷ (a) × 100 %	41 %	30 %	9 %	17 %	25 %

Source: Audit analysis of HKDI records

Audit recommendations

2.11 Audit has *recommended* that the Executive Director, VTC should:

- (a) ensure as far as possible that the number of students enrolled should not exceed the plan by a significant margin and any significant deviation from the plan should be fully justified;
- (b) take measures to mitigate the possible adverse impact of over-enrolment on the programmes;

Management of programmes

- (c) **take into account the actual number of enrolment in previous years in planning the number of students to be enrolled; and**
- (d) **take measures to plan the teaching staff requirement more accurately and to address the high percentage of short contract staff.**

Response from the VTC

2.12 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) the VTC has always been taking measures to meet planned places though the intake is subject to many external factors such as the admission results of the Joint University Programmes Admission System and other incentive schemes offered;
- (b) additional teaching and supporting staff, equipment and facilities, and other necessary resources have been provided to cater for the additional places; and
- (c) ratio of short contract staff will be closely monitored.

Programme planning

2.13 In the period 2012/13 to 2016/17, there were 14 new programmes. Before a new programme is introduced, the pertinent Programme Board conducts a feasibility study and prepares a feasibility study report. The feasibility study report is then submitted to the DEDAB and DEAC for comments and endorsement. After endorsement by the DEDAB and DEAC, a programme proposal will be prepared outlining the details of the programme, including its structure, contents, number of student intake, and staff resources planning. The proposal will be submitted to the DEAC for endorsement and to the VETAB for approval. The procedures for development of a new programme are shown at Appendix E. Audit reviewed the

programme proposals for five new programmes (Note 12) and found that some planning information should be added.

Need to provide more analysis in programme proposals

2.14 ***Planned numbers of student enrolment.*** Audit noted that the programme proposals had stated the needs for the proposed new programmes and the planned enrolment of student intakes for the proposed programmes. However, no information was included in the proposals on how the planned numbers were derived. It would be helpful for reviewers of the proposals to have on the programme proposals the rationale behind the planned numbers, for instance, whether they were derived from the estimated demand and/or the capacity of the HKDI.

2.15 ***Impact on teaching staff resources.*** In all the five programme proposals reviewed by Audit, it was stated that the departments concerned were experienced in the area and that there was no strong impact on staffing for offering the new programmes. However, no further details were included in the programme proposals on the impact on teaching staff resources. For instance, it was not stated in the proposals how the additional staff hours for the new programme were to be met.

2.16 Audit considers that in proposing a new programme, it is important that more analysis on the planned number of student intake and impact on staffing are given.

Note 12: *Of the five new programmes examined by Audit, two programmes were over-enrolled for the period 2013/14 to 2016/17 (the percentage of over-enrolment ranged from 2% to 137%, averaging 30%). Additional short contract staff were employed for the two over-enrolled programmes. One programme was under-enrolled for 2015/16 and 2016/17 (the percentage of under-enrolment was 14% and 31% for the two years respectively) and two programmes were under-enrolled in 2016/17 (the percentage of under-enrolment was 5% and 30% for the two programmes).*

Need to conduct manpower survey on design industry

2.17 Training Boards of the VTC conduct regular manpower surveys and publish manpower reports for various industries. Manpower surveys conducted by four Training Boards are relevant to the HKDI. They are Fashion and Textile Training Board, Jewellery, Watch and Clock Training Board, Media and Communications Training Board, and Print Media and Publishing Training Board. However, manpower needs of some programmes offered by the HKDI are not covered by the manpower surveys of the Training Boards, such as:

- (a) HD in Architectural Design;
- (b) HD in Landscape Architecture;
- (c) HD in Product, Interior and Exhibition Design;
- (d) HD in Furniture and Lifestyle Product Design; and
- (e) HD in Stage and Set Design.

For these programmes, the Programme Boards have to obtain information on the industry manpower demand from a number of channels, including the manpower surveys conducted by the external trade or design bodies, the government statistics and the advisory boards such as the DEDAB and the DIAB served by industry members. For instance, the annual statistics (such as the number of establishments, persons engaged and vacancies analysed by industry sub-class) from the Census and Statistics Department provide the basic information on manpower demand related to various design programmes.

2.18 In the DEDAB meeting held in November 2011, members discussed whether there was any survey on the manpower demand and supply of the design industry. They considered that a formal manpower survey on design industry would:

- (a) provide better understanding on the manpower requirement in design sector and the findings would be useful to the development of HKDI's programmes; and
- (b) be useful to both education and industry sectors.

2.19 Up to July 2017, no manpower survey on the design industry had been conducted. The HKDI needs to consider conducting a manpower survey on the design industry periodically and take into account the results of the survey in its programme planning and review.

Audit recommendations

2.20 Audit has *recommended* that the Executive Director, VTC should:

- (a) include in the programme proposals more details on the planned number of student intake and impact on teaching staff, for instance, how the number of student intake is derived and how the additional teaching staff resources are to be met; and
- (b) consider conducting a manpower survey on the design industry periodically and take into account the results of the survey in its programme planning and review.

Response from the VTC

2.21 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) the HKDI will work with the VTC's Quality Assurance and Accreditation Office in reviewing the programme proposals; and
- (b) the VTC will consider the need for conducting the manpower survey recommended.

Evaluation of programme performance

2.22 There is a Quality Assurance System to monitor the quality of the programmes of the HKDI. Under the system, the HKDI submits Programme Quality Analysis Report annually to the Headquarters. The performance of the HKDI's programmes is measured against seven indicators:

Management of programmes

- (a) **Enrolment rate.** This is the actual number of students enrolled as at 15 October expressed as a percentage of planned places;
- (b) **Retention rate.** This is the weighted average of the retention rates of the individual modules of the programme. The retention rate of a module is calculated by dividing the number of students assessed at the end of module by the number of students enrolled at the start of module;
- (c) **Pass rate.** This is the weighted average of the pass rates of the individual modules of the programme. The pass rate of a module is calculated by dividing the number of students obtaining a pass in the module by the number of students assessed at the end of the module;
- (d) **Employment rate.** This is calculated by dividing the number of graduates who are employed by the sum of the number of graduates who are employed and the number of graduates who are seeking employment;
- (e) **Further study rate.** This is calculated by dividing the number of graduates in full-time study by the total number of graduates;
- (f) **Student satisfaction.** This is an assessment of the students' satisfaction with the programme they study. The score for student satisfaction is obtained from analysing the results of student feedback survey; and
- (g) **Employer satisfaction.** This is an assessment of the employers' satisfaction with the graduates' performance. The score for employer satisfaction is obtained from analysing the results of employer satisfaction survey.

Need to improve monitoring of completion rate of programmes

2.23 Under the Memorandum of Administrative Arrangement (MAA) signed between the VTC and the EDB, the VTC is required to set performance indicators and targets. One of the indicators specified in the MAA is “target completion rate of its trainees”. It was stipulated in the MAA that the targets and actual results of completion rates should be reported to the EDB annually. Audit examination of the annual submissions made by the VTC to the EDB revealed that the VTC reported the retention rates of modules of its HD programmes (see para. 2.22(b)) but not the completion rate of its HD programmes.

2.24 Audit noted that from 2012/13 to 2014/15, the module retention rates were considerably higher than the programme completion rates. A programme completion rate measures the graduation rate of a cohort of students for the two-year HD programmes. A programme consists of many modules. A student completes a programme after he had completed all the required modules. Some students may have completed all the modules they had started but not completed the required modules for the programme. Therefore, the module retention rate is higher than the programme completion rate. Table 6 shows the module retention rates and programme completion rates for the period 2012/13 to 2014/15.

Table 6

**Module retention rate and programme completion rate
(2012/13 to 2014/15)**

Year	Module retention rate (Note 1) (a)	Programme completion rate (Note 2) (b)	Difference (c) = (a) – (b)
2012/13	98%	86%	12%
2013/14	98%	84%	14%
2014/15	97%	80%	17%

Source: Audit analysis of HKDI records

Note 1: The module retention rate is the weighted average of the retention rates of all individual modules offered in the academic year.

Note 2: The programme completion rate is the percentage of students of a particular intake year who have fulfilled all the graduation requirements of a programme.

Remarks: The programme completion rates of 2013/14 and 2014/15 were not the final figures as students were allowed to complete the programme within the maximum period of five academic years. Therefore, the completion rates for 2013/14 and 2014/15 may increase in the next few years.

2.25 To measure the programme performance, the HKDI needs to consider monitoring the completion rates of programmes (i.e. percentage of students who complete the programmes) in addition to the module retention rates.

Programmes with low completion rates

2.26 The overall programme completion rates for 2012/13, 2013/14 and 2014/15 were 86%, 84% and 80% respectively (see Table 6 and Appendix F). Audit analysis of the programme completion rates for the 2012/13 to 2014/15 intakes revealed that:

- (a) the programme completion rates of the HD in Architecture Design were particularly low. For each of the three years of 2012/13 to 2014/15, its completion rate was significantly lower than the overall rate. The differences were 15%, 26% and 29% respectively. They had dropped significantly from 71% of the students enrolled for 2012/13 to 51% of the students enrolled for 2014/15 (see Table 7); and
- (b) the completion rate for the HD in Landscape Architecture dropped significantly from 88% of the students enrolled for 2012/13 to 68% of the students enrolled for 2014/15 (see Table 7). The completion rates of the students enrolled for 2012/13 and 2013/14 were higher than the overall completion rate, but of the students enrolled for 2014/15, the rate was lower than the overall rate by 12%.

Table 7

**Two programmes with low completion rate
(2012/13 to 2014/15 intake)**

HD programme	2012/13	2013/14	2014/15
Architecture Design			
– Students enrolled (a)	48	66	77
– Students awarded with HD (b)	34	38	39
– Completion rate (c) = (b) ÷ (a) × 100 %	71 %	58 %	51 %
Landscape Architecture			
– Student enrolled (a)	26	71	62
– Students awarded with HD (b)	23	64	42
– Completion rate (c) = (b) ÷ (a) × 100 %	88 %	90 %	68 %
All programmes	86 %	84 %	80 %

Source: Audit analysis of HKDI records

2.27 Audit considers that the HKDI needs to ascertain the reasons for lower completion rate of some programmes (see para. 2.26(a) and (b)) and identify areas for improvement.

Target employment rate not met

2.28 The VTC sets a target employment rate (see para. 2.22(d)) of 90% for its HD programmes. Audit noted that the overall employment rate of the HKDI's HD programmes had been lower than the target rate of 90% since 2012 (see Table 8).

Table 8**Employment rate of graduates
(2011 to 2016)**

Year of graduation	Employment rate
2011	90.8%
2012	87.7%
2013	87.8%
2014	84.1%
2015	83.9%
2016	86.4%

Source: HKDI records

2.29 The overall employment rates of HD programme graduates for 2014, 2015 and 2016 were 84%, 84% and 86% respectively (see Appendix G). Audit analysed the employment rate of individual programmes for graduates of 2014 to 2016 and noted that:

- (a) for graduates of 2014, 9 (60%) of the 15 programmes had employment rate below target, ranging from 61% to 84%. For graduates of 2015, 12 (80%) of the 15 programmes had employment rate below target, ranging from 67% to 89%. For graduates of 2016, 8 (53%) of 15 programmes had employment rate below target, ranging from 75% to 88% (see Table 9); and

Table 9

**Analysis of employment rate for graduates of HD programmes
(2014 to 2016)**

	2014 Graduates	2015 Graduates	2016 Graduates
Number of programmes with employment rate below the target rate of 90 % (a)	9	12	8
Number of programmes offered (b)	15	15	15
Percentage of programmes with employment rate below the target rate of 90 % (c) = (a) ÷ (b) × 100 %	60 %	80 %	53 %
Employment rate of programmes below the target rate of 90 %	61 % to 84 %	67 % to 89 %	75 % to 88 %

Source: Audit analysis of HKDI records

- (b) in particular, the employment rates of four programmes had not achieved the 90% target in every year of 2014 to 2016.

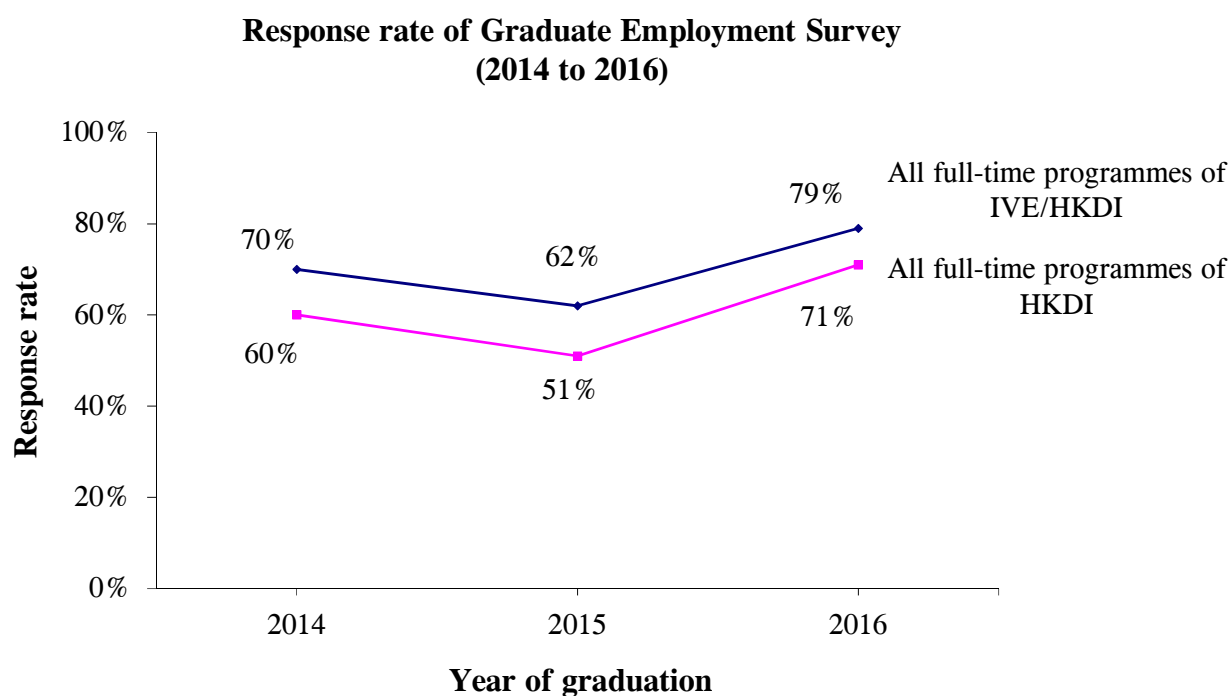
2.30 Audit considers that the HKDI needs to step up efforts to improve the employment rate of HKDI graduates for the programmes with lower employment rates.

Need to improve the response rate of Graduate Employment Survey

2.31 The Headquarter's Statistics Section conducts Graduate Employment Survey of full-time programmes offered by the IVE and the HKDI in January each year (i.e. 6 months after graduation) by sending questionnaires to the graduates to study their employment situation. The survey results provide information on the employment rate of graduates, which is one of the performance indicators under the Quality Assurance System (see para. 2.22(d)).

2.32 The IVE and the HKDI are the two member institutions of the VTC that offer the great majority of HD programmes and thus the VTC often analyses statistics relating to the IVE and the HKDI together. Audit analysed the response rate of Graduate Employment Survey for full-time graduates of the HKDI of the years 2014 to 2016 and noted that the rate was lower than the overall response rate for graduates of all full-time programmes of the IVE/HKDI (see Figure 1).

Figure 1



Source: Audit analysis of HKDI records

2.33 Figure 1 indicates that there was an overall increase in response rate for graduates of 2016 as a result of:

- (a) allowing graduates to complete and submit questionnaires on-line through the VTC's webpage; and
- (b) providing incentive by offering a coffee e-coupon for the first 500 graduates who completed the survey.

2.34 Despite the increase in response rate of employment survey on graduates of 2016, the response rate for graduates of HKDI programmes (i.e. 71%) was still on the low side as compared with the graduates of sub-degree programmes of other higher education institutions (see Table 10).

Table 10

**Response rate of employment survey on graduates of
sub-degree programmes of higher education institutions
(2016)**

Institution	Response rate
A	98%
B	97%
C	93%
D	93%
E	88%
F	85%
G	84%
H	84%
IVE/HKDI	79%
HKDI	71%

Source: Information Portal for Accredited Post-secondary Programmes website and Audit analysis of HKDI records

2.35 Audit considers that the HKDI needs to take measures to improve the response rate of Graduate Employment Survey of HKDI graduates to enhance the usefulness and representativeness of the information collected from the survey.

Need to cover more graduated students' employers in employer satisfaction surveys

2.36 The VTC engaged a consultant to conduct employer satisfaction survey in August every year (i.e. one year after graduation) by sending questionnaires to graduated students' employers to collect information on the employers' satisfaction with the training programmes of graduates and the graduates they employed. For those graduates who fulfil the following criteria, their employers will be invited to participate in the survey:

- (a) graduates who engage in full-time job relevant to their study;
- (b) graduates who are employed by the same company for at least six months prior to the survey period; and
- (c) graduates who give consent for the VTC to contact their employers for the survey.

2.37 The results of the employer satisfaction survey provide an assessment on the level of employers' satisfaction (which is rated on a scale of 1 (very poor) to 10 (excellent)) on the students they employed. According to the results of the survey on the 2014 and 2015 graduates, the overall satisfaction level of employers of HKDI graduates on a scale of 1 to 10 was 7.7 and 7.3 respectively.

2.38 Audit noted from the surveys conducted for graduates of 2014 and 2015 that:

- (a) the surveys only covered a small number of employers of HKDI graduates:
 - (i) the number of questionnaires sent out was 46 and 45 for employed graduates of 2014 and 2015 respectively, representing 7% of 668 employed graduates of 2014 and 8% of 544 employed graduates of 2015 (Note 13); and

Note 13: *The number of employed graduates refers to those who replied that they were in full-time employment in the Graduate Employment Survey. The actual number of employed graduates might be larger.*

- (ii) 43 and 35 questionnaires were returned for the survey conducted for graduates of 2014 and 2015 respectively;
- (b) some programmes were not covered in the surveys. No questionnaires had been sent to the employers of 78 employed graduates of 2014 of five programmes and of 17 employed graduates of 2015 of three programmes. As a result, the employers' views on graduates of these programmes could not be ascertained; and
- (c) for those programmes covered in the surveys, only a small number of employers were surveyed for each programme, ranging from 1 to 6.

2.39 As employers' satisfaction is one of the performance indicators in the Quality Assessment System (see para. 2.22(g)), the representativeness of the data collected from the survey is important. Audit considers that the HKDI needs to review the criteria for selecting employers for the employer satisfaction survey and take measures to encourage graduates to give consent for the VTC to contact their employers, with a view to covering more graduates' employers in the survey.

Audit recommendations

2.40 **Audit has *recommended* that the Executive Director, VTC should:**

- (a) **consider monitoring the programme completion rates in addition to the module retention rates;**
- (b) **ascertain the reasons for lower completion rates of some programmes and identify areas for improvement;**
- (c) **take measures to improve the employment rate of HKDI graduates with a view to meeting the target employment rate of 90%;**
- (d) **take measures to improve the response rate of Graduate Employment Survey of HKDI graduates to enhance the usefulness and representativeness of the information collected from the survey; and**

- (e) review the criteria for selecting employers for the employer satisfaction survey and take measures to encourage graduates to give consent for the VTC to contact their employers, with a view to covering more graduates' employers in the survey.

Response from the VTC

2.41 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) the VTC will consider monitoring the programme completion rate;
- (b) the VTC will ascertain the reasons for low completion rates of some programmes, and identify areas for improvement;
- (c) the VTC will take measures to improve the employment rate of HKDI graduates; and
- (d) the VTC's Statistics Section has explored approaches to:
 - (i) improve the response rate of the Graduate Employment Survey;
 - (ii) review the criteria for selecting employers for the employer satisfaction survey; and
 - (iii) encourage graduates to give consent for the VTC to contact their employers.

Performance reporting

Need to improve the extent of performance reporting

2.42 *Need to consider disclosing separately performance information of HKDI.*

The VTC discloses on its website various information/statistics (e.g. number of enrolment, number of graduates and employment rate) for the IVE, HKDI, School of Business and Information Systems, and Youth College as a whole. The related information of the HKDI was not reported separately. To measure and report the HKDI's performance, and its progress in achieving its mission, the VTC needs to consider disclosing separately the HKDI's key performance information and statistics, such as the:

- (a) enrolment rate;
- (b) completion rate;
- (c) employment rate; and
- (d) employers' satisfaction on its graduates.

2.43 *Need to enhance information on employability and articulation.* The VTC discloses on its website the employment rate of HD programme graduates and the number of HD programmes graduates successfully articulated to full-time degree programmes. For instance, for the 2016 graduates, it was disclosed on the website that the employment rate was 90% and more than 3,000 graduates successfully articulated to full-time degree programmes (see Table 11). However, there was no information on the number of graduates who were employed and those who were seeking employment, and the number of graduates out of whom 3,000 articulated successfully to full-time degree programmes. It would be much more useful to the users of the website if the information about graduates who successfully obtained employment and graduates who successfully articulated to full-time degree programmes is given in terms of both:

- (a) the number of graduates; and
- (b) the percentage of graduates.

Table 11

**Information on employment and articulation of graduates of
HD programmes disclosed on VTC website
(2016)**

	Successfully secured employment	Successfully secured articulation
Percentage of graduates	“IVE/HKDI HD graduates enjoy 90% employment rate” (Note)	Not disclosed
Number of graduates	Not disclosed	“Over 3,000 HD graduates were successfully admitted to full-time degree programmes”

Source: VTC records

Note: The VTC calculated the employment rate by dividing the number of graduates who were employed by the sum of the number of graduates who were employed and the number of graduates who were seeking employment.

Remarks: The VTC did not disclose graduate information of the HKDI and other member institutions separately.

Audit recommendations

2.44 **Audit has recommended that the Executive Director, VTC should consider:**

- (a) disclosing separately the key performance information and statistics of the HKDI and those of other member institutions, such as the enrolment rate, completion rate, employment rate and employers' satisfaction on its graduates; and
- (b) disclosing on its website information on HKDI graduates who successfully obtained employment and those who successfully articulated to full-time degree programmes in terms of:
 - (i) the number of graduates; and
 - (ii) the percentage of graduates.

Response from the VTC

2.45 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) when considering possibility of separate disclosure of the information, the VTC has to pay regard to the consistency in handling information packaging and messaging in respect of all HD programmes, given that both the HKDI and the IVEs are offering the same programme type; and
- (b) the VTC will consider disclosing on its website the information on the number and the percentage of graduates.

Industrial attachment

2.46 To strengthen students' readiness for the workplace and to facilitate a smooth transition from study to work, industrial attachment (IA) has been included as a mandatory graduation requirement of all HD programmes starting from 2012/13 intake. There are four categories of IA:

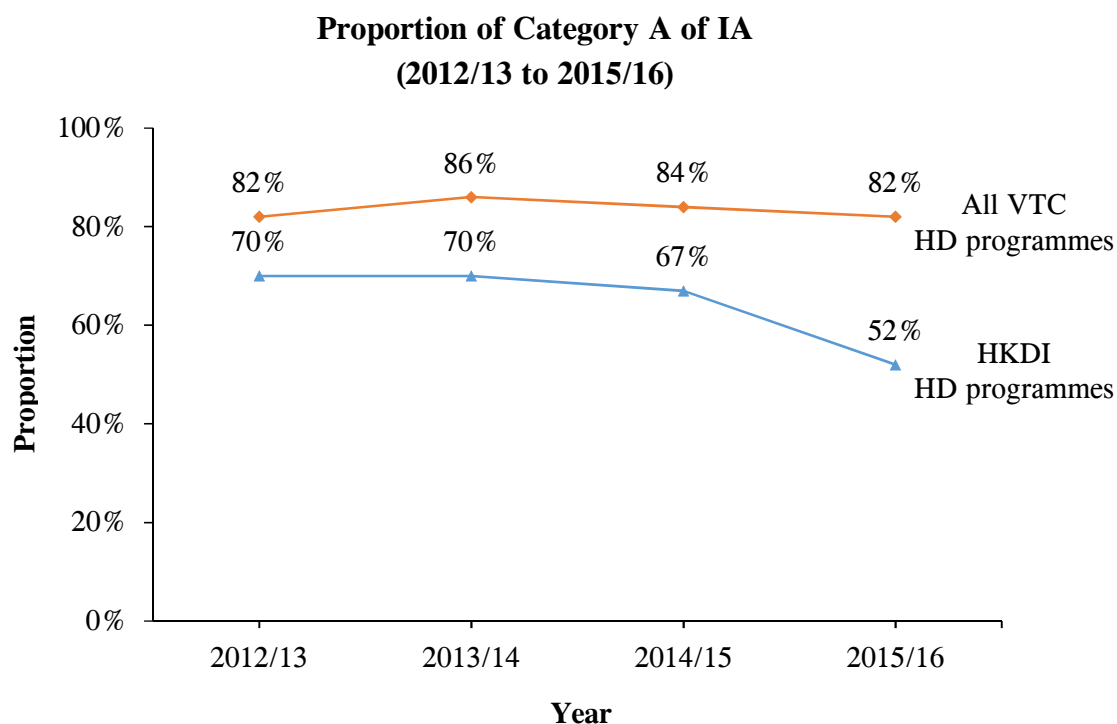
- (a) **Category A.** This refers to attachment in field or industry relevant to the programme of study;
- (b) **Category B.** This refers to workplace experience through industry-based projects conducted at home, on campus or other operating units of the VTC;
- (c) **Category C.** This refers to other structured experiential learning experience (e.g. attachment in a field or industry not directly related to the programme of study); and
- (d) **Category D.** This refers to general workplace experience.

Category A is the most preferred category of IA while Category D is the least preferred category of IA. An IA module consists of a minimum of 90 hours of industrial placements or industry-based projects sponsored/initiated by industry partners.

Need to increase the proportion of Category A of IA

2.47 Category A is the most preferred category of IA (see para. 2.46). Statistics of IA arrangements in the period 2012/13 to 2015/16 revealed that while the number of Category A of IA for the HKDI students increased from 710 to 1,282, the proportion of this Category decreased from 70% (i.e. 710 out of 1,015) to 52% (i.e. 1,282 out of 2,477), compared to the corresponding figures for the average of all VTC HD programmes ranging from 82% to 86% in the same period (see Figure 2).

Figure 2



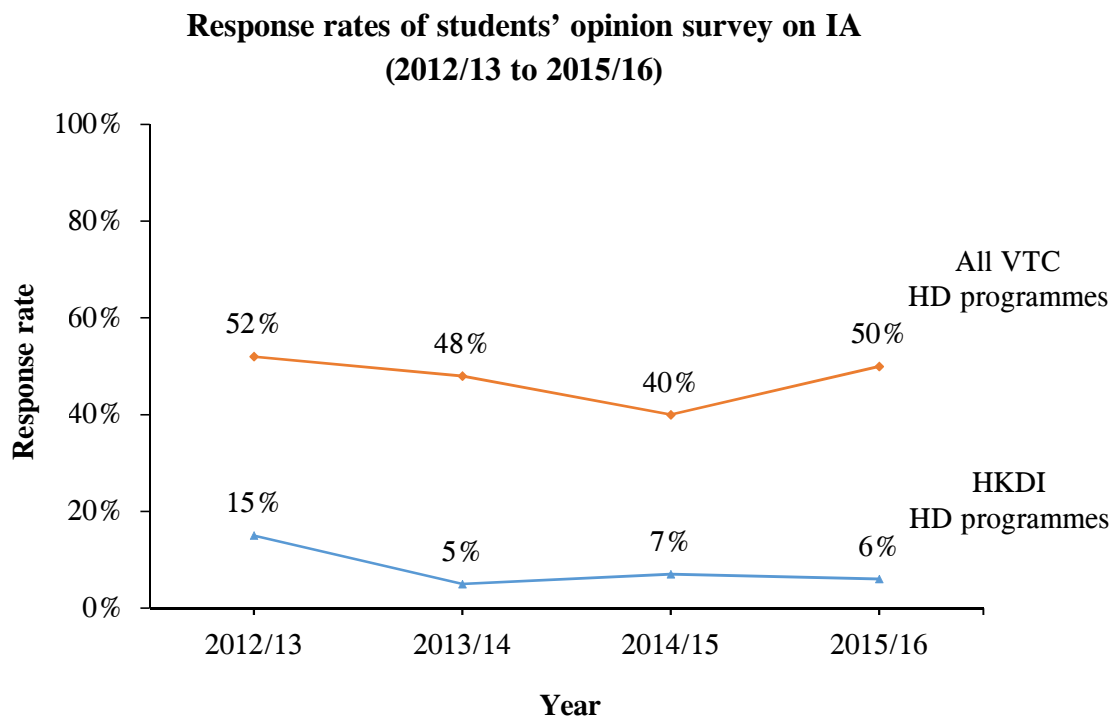
Source: Audit analysis of HKDI records

Need to improve the response rates of students' opinion survey on IA

2.48 The VTC conducts students' opinion surveys to evaluate the effectiveness of the IA programme. Findings and recommendations are provided to the academic disciplines to enhance implementation of the IA programme. Audit noted that the response rates of the students' opinion survey on IA for the HKDI HD programmes were on the low side and decreased from 15% (i.e. 154 responded out of 1,015) in 2012/13 to 6% (i.e. 151 responded out of 2,477) in 2015/16. The HKDI response

rates were much lower than the overall rates of all the VTC HD programmes (ranged from 40% to 52%) in the same period (see Figure 3). Audit considers that the low response rates of the students' opinion survey may render the survey results less representative. The HKDI needs to ascertain the reasons for the low response rates and take improvement measures.

Figure 3



Source: Audit analysis of HKDI records

Need to review minimum duration of IA

2.49 According to a DEDAB paper issued in June 2014, some industry partners commented that:

- (a) short IA durations were ineffective for student learning and even disruptive for the organisations providing IA; and
- (b) longer attachment duration (two months or more) would be needed for an IA arrangement to achieve mutual benefits for both students and employers.

Management of programmes

2.50 Audit noted that the minimum duration of IA for some HD programmes in design discipline offered by two other tertiary institutions were 120 hours and 1 month respectively, much longer than the minimum of 90 hours for the HKDI's programmes. Furthermore, the minimum duration of IA for the HKDI had not been reviewed since 2012/13. Audit considers that the HKDI needs to conduct a review on the minimum duration of IA and consider if there is merit in extending the minimum duration.

Audit recommendations

2.51 Audit has *recommended* that the Executive Director, VTC should:

- (a) take measures to increase the proportion of Category A of IA for the HKDI's HD programmes;
- (b) ascertain the reasons for the low response rates of the students' opinion survey on IA for the HKDI and take improvement measures; and
- (c) conduct a review on the minimum duration of IA for the HKDI's HD programmes and consider if there is merit in extending the minimum duration.

Response from the VTC

2.52 The Executive Director, VTC agrees with the audit recommendations. She has said that the VTC will consider the recommendations and review the prevailing policy and practice for improvement where appropriate.

PART 3: CAMPUS DEVELOPMENT AND MANAGEMENT

3.1 This PART examines the campus development and management, focusing on the following areas:

- (a) design competition of HKDI (paras. 3.4 to 3.11);
- (b) project development of HKDI (paras. 3.12 to 3.34); and
- (c) management of campus (paras. 3.35 to 3.54).

Background

3.2 After discussions between the VTC and the EDB, it was decided in February 2006 to develop the HKDI and IVE(LWL) together at the TKL Campus to achieve synergy (see paras. 1.3 and 1.12). In June 2007, the FC approved the funding for the project with a project estimate of \$992.8 million in September 2006 prices, which was equivalent to \$1,006.3 million in money-of-the-day prices (Note 14). The development of the TKL Campus was completed in April 2010 and put into use in 2010/11.

3.3 The actual construction cost of the TKL Campus was \$1,287.3 million. The difference of \$281 million between the actual construction cost of \$1,287.3 million and the amount of \$1,006.3 million approved by the FC was funded by the surpluses from the VTC's self-financing activities (\$170.8 million), the VTC's Council Reserve (\$76 million), Government annual block grant and capital subventions for minor works (\$33.7 million) and donations (\$0.5 million) (see Table 12).

Note 14: *Money-of-the-day prices show the estimated cost of a project after allowing for forecasted inflationary increases in construction prices during the period of construction.*

Table 12

Actual construction cost and funding source of TKL Campus

	Amount (\$ million)
Actual construction cost	
Superstructure works (including building services)	1,171.9
Foundation works	46.4
Architectural consultancy	43.9
Information technology infrastructure and surveillance camera system	10.6
Quantity surveying consultancy	3.3
Others (e.g. signage, loose furniture and equipment)	11.2
Total	1,287.3
Funding source	
Funding approved by FC	1,006.3
Surpluses from VTC's self-financing activities	170.8
VTC's Council Reserve	76.0
Government annual block grant and capital subventions for minor works	33.7
Donations	0.5
Total	1,287.3

Source: VTC records

Design competition of HKDI

3.4 In April 2006, the VTC organised a design competition for the HKDI. A Jury Panel, which was assisted by a Technical Committee, was appointed by the VTC to assess the competition entries (Note 15). A Competition Document stipulated the rules, requirements and conditions of the competition. It was stated in the Competition Document that:

- (a) contestants were required to keep the project cost strictly within the budget of \$378 million;
- (b) any contestant who did not abide by the rules, requirements or conditions as set out in the Competition Document might result in disqualification from the competition;
- (c) the decisions of the Jury Panel should be final and could not be appealed against; and
- (d) the VTC's decision regarding all aspects of the competition was final and binding on all contestants.

Table 13 shows the relationship between the construction budget of \$378 million for the competition and the cost estimate of \$1,006.3 million approved by the FC in June 2007.

Note 15: *The Jury Panel had seven jurors, comprising a member of the DIAB, a member of the VTC Council, a member of the VTC Estates Committee, two international renowned architects and two academics.*

Table 13

**Relationship between the construction budget for the design competition
and the cost estimate approved by the FC in June 2007**

	Amount (\$ million)
(a) 2005 Government Capital Works Resource Allocation Exercise for construction of new HKDI campus – construction budget for design competition: \$378 million – other costs of the project: \$107.4 million	485.4
(b) 2006 Government Capital Works Resource Allocation Exercise for reprovisioning of IVE(LWL)	388.2
(c) Adjustments (including cost of additional piling works, upgrade to University Grants Committee institution buildings standards, etc.)	119.2
(d) Cost estimate approved by the FC in September 2006 prices (a) + (b) + (c)	992.8
(e) Provision for price adjustment	13.5
(f) Cost estimate approved by the FC in money-of-the-day prices (d) + (e)	1,006.3 (Note)

Source: Audit analysis of VTC records

Note: The difference between the actual construction cost of \$1,287.3 million and the amount of \$1,006.3 million approved by the FC was mainly attributable to: (a) higher awarded tender prices of the superstructure contract and the building services contract than the corresponding cost estimates; and (b) variation orders on the works contracts. A reason for the higher awarded tender prices was that the modified Hybrid Scheme was adopted (see paras. 3.21(c), 3.21(f) and 3.22(f)) instead of the Reinforced Concrete Scheme, based on which the construction cost was calculated for the application for FC funding.

3.5 The cost estimate of the winning design submitted on 27 October 2006, in which the campus consisted of a podium with four towers supporting a sky platform, was \$470.4 million. The design included a number of cost saving options which, according to the contestant, could reduce the cost estimate by \$93 million to \$377.4 million (i.e. \$0.6 million lower than the cost ceiling of \$378 million).

Different views on project cost of winning design

3.6 On 10 November 2006, the Jury Panel made its final adjudication and recommended the winning design. On 13 November 2006, the VTC Council Secretariat sought the endorsement of the VTC Estates Committee and approval of the VTC Standing Committee on the recommendation of the Jury Panel. The terms of references of the VTC Standing Committee and the VTC Estates Committee were at Appendix H and Appendix I respectively. The Committees were informed that, taking into account the cost saving options and the views of the Technical Committee for the competition (Note 16), the estimated construction cost of the design could be reduced by \$65.4 million (see Table 14). The Committees were also informed that the revised cost estimate was \$405 million, which exceeded the allowed construction budget for the design competition of \$378 million specified by the VTC by \$27 million (7%).

Note 16: *The main role of the Technical Committee was to pre-examine the entry designs according to the Competition Document and assess whether the entry designs fulfilled the mandatory requirements of the competition and local regulations were met.*

Table 14

Comparison of cost saving options proposed in the winning design
and the assessment made by the Technical Committee

Possible cost saving options	Amount of savings		
	Estimated in the submission of the winning design (\$ million) (a)	Estimated by the Technical Committee (\$ million) (b)	Difference (\$ million) (c) = (b) – (a)
Use reinforced concrete truss instead of steel truss in platform and towers (i.e. using reinforced concrete structure instead of steel structure)	50	30	(20)
Separate funding for noise abatement measures	22	–	(22)
Relocate basement car parking to ground floor	15	15	–
Separate funding for swimming pool	5.3	5.3	–
Separate funding for basketball court	0.7	0.7	–
Close up part of the void at platform and realign the four towers	–	5	5
Extra low voltage installation funded under furniture and equipment budget	–	9.4	9.4
Total	93	65.4	(27.6)

Source: Audit analysis of VTC records

3.7 The differences between the estimated cost savings submitted by the winning design and those assessed by the Technical Committee were:

- (a) different views on the cost saving option of using reinforced concrete (RC) structure instead of steel structure;
- (b) the cost saving option for noise abatement measures for \$22 million was not accepted by the Technical Committee; and
- (c) the Technical Committee recommended two additional cost saving options (i.e. \$14.4 million in total).

3.8 On 20 November 2006, the Standing Committee and the Estates Committee held a joint meeting to ratify the Jury Panel's recommendation. Although the overall cost estimate after cost saving options as assessed by the Technical Committee had exceeded the original budget ceiling by \$27 million (see para. 3.6), the Committees ratified the Jury Panel's recommendation. Members agreed that the possible shortfall be earmarked from the VTC's earnings from its self-financing programmes. The result of the competition was announced on 28 November 2006.

3.9 Audit considers that the cost saving options submitted by the contestant should have been thoroughly assessed by the Technical Committee before the Jury Panel made its final decision on the result of the competition. There was no documentary evidence showing that the Jury Panel was informed of the assessment made by the Technical Committee on the cost saving options included in the winning design on 10 November 2006, when the Panel made its final decision on the result of the competition.

Audit recommendation

3.10 Audit has *recommended* that the Executive Director, VTC should, for future design competitions, if the competition requires the entry designs to fulfil the mandatory budget requirements, thoroughly assess the cost estimates submitted by the contestants before the Jury Panel made its final decision on the result of the competition.

Response from the VTC

3.11 The Executive Director, VTC agrees with the audit recommendation. She has said that cost estimates and mandatory budget requirements would be thoroughly assessed in future design competitions.

Project development of HKDI

3.12 In November 2006, according to the conditions of the competition, the VTC awarded the architectural consultancy for the construction of the HKDI to the design architect of the winning design and its local collaborating consultant. In the same month, the architectural consultancy for the re-provisioning of IVE(LWL) was awarded through the standard two-envelope technical and fee tender system. The same local consultant was awarded the tender in the tender exercise. In December 2006, the VTC convened a Client Consultants Group (CCG) to take forward the project based on the winning design. The CCG consisted of:

- (a) members from the VTC including a Deputy Executive Director; and
- (b) project consultants.

3.13 At the CCG meeting held in February 2007, three structural schemes of the HKDI, which featured a sky platform and four towers, were discussed, namely:

- (a) ***RC Scheme.*** Under this scheme, RC would be used for floor framing, trusses and lattice;
- (b) ***Steel Scheme.*** Under this scheme, steel would be used for floor framing, trusses and lattice; and
- (c) ***Hybrid Scheme.*** Under this scheme, RC would be used for floor framing and lattice of the tower structure, and steel for floor framing and trusses of the platform.

3.14 The pros and cons analysis of the three structural designs was discussed at the meeting held on 21 March 2007. Some of the pros and cons of the three designs are listed in Table 15.

Table 15

**Comparison of the structural schemes
submitted to the CCG in March 2007**

	RC Scheme	Steel Scheme	Hybrid Scheme
Pros	(a) most conventional construction method (b) easy to maintain (c) no long procurement time for RC construction	(a) maximum space efficiency (b) lowest foundation cost (c) less formwork and falsework (d) fastest construction method for the winning design	(a) lower foundation cost (b) more open feel to spaces (c) less formwork and falsework for platform construction
Cons	(a) highest foundation cost (b) unfriendly circulation due to large truss member size of platform (c) maximal loss of usable space due to member size	(a) uncertainty in construction cost due to fluctuation of steel price (b) fire and corrosion protection required for steelwork (c) long procurement time for steelwork	(a) complicated detail between RC and steel (b) long procurement time for steelwork
Estimated cost (\$ million)	1,080	1,160	1,136

Source: VTC records

Remarks: The pros and cons of the modified Hybrid Scheme (see para 3.15) were not discussed by the CCG.

CCG adopted the modified Hybrid Scheme

3.15 On 30 April 2007, the project consultant informed the CCG that the current design was based on a composite structure of RC and steel and the finalised design based on this design option would be ready shortly. The consultant explained that the design was a modified Hybrid Scheme, under which exposed vertical structural elements (i.e. lattice of towers and diagonal truss of the platform) would be steel, and all slabs, internal walls of towers and podium would be RC structures. The consultant advised the CCG that the design option was the most structural-effective option. In the Hybrid Scheme, RC was used for the construction of lattice of the tower structure, instead of steel as in the modified Hybrid Scheme. Audit noted that no documentary evidence was available showing that the pros and cons of the modified Hybrid Scheme had been discussed by the CCG. Furthermore, there was no documentary evidence showing how the modified Hybrid Scheme would affect the costs and timing of the project.

Application for funding from FC based on RC Scheme instead of modified Hybrid Scheme adopted for construction

3.16 According to the VTC's Notes for Guidance on Capital Subventions, before funding application can be submitted to LegCo, the VTC needs to submit architectural design and costing to the Architectural Services Department (ArchSD) for approval. In the preparation of the funding application to the FC, the VTC submitted the project cost estimate of \$992.8 million (see Table 13 in para. 3.4) based on the RC Scheme to the ArchSD for vetting on 8 and 14 March and 4 and 18 April 2007. In the CCG meeting on 30 April 2007, the modified Hybrid Scheme was adopted. However, no documentary evidence was available showing that the VTC had submitted any revised cost estimate to the ArchSD to take into account the fact that the modified Hybrid Scheme was adopted.

3.17 On 1 June 2007, the VTC Estates Committee was informed that "*the new campus designed by the design team is a composite reinforced concrete and steel structure*". Furthermore, on 15 June 2007, the project consultant revised the project cost estimate from \$992.8 million to \$1,064.1 million based on the modified Hybrid Scheme. The revised estimate was \$71.3 million (7%) higher than the cost estimate of \$992.8 million submitted to the ArchSD in April 2007 mainly due to the higher cost of the modified Hybrid Scheme. There was no documentary evidence showing that the VTC had submitted the revised project cost estimate of \$1,064.1 million to the ArchSD. In the event, the project cost estimate quoted in the funding application paper

(see para. 3.2) submitted to the FC on 22 June 2007 was \$992.8 million indicating the adoption of the RC Scheme.

Need to seek agreement from the ArchSD according to VTC guidelines before issuing tender

3.18 Financial Circular No. 9/2004 “Guidelines on the Management and Control of Government Funding for Subvented Organisations” states that the Controlling Officers (Note 17) should, at various stages of the subvented building projects, seek technical advice of the ArchSD on the acceptability of the projects for subvention purposes. Areas on which the ArchSD may be consulted include project feasibility, design, scope, cost and selection of consultants and contractors.

3.19 The ArchSD is required to provide technical advice to ensure that government subvented and entrusted projects conform to government requirements by:

- (a) vetting budget, design, tender documents, tender recommendations and final accounts; and
- (b) identifying non-conformities in design, standards and tendering procedures.

3.20 The VTC’s Notes for Guidance on Capital Subventions stipulate that the VTC should seek agreement from the ArchSD before issuing tenders for the projects.

3.21 Audit noted that the VTC had not sought agreement from the ArchSD according to the VTC’s Notes for Guidance on Capital Subventions before issuing tenders for the project. Audit examination of the project records revealed that:

- (a) on 15 October 2007, the VTC submitted the draft tender document for the superstructure to the ArchSD for vetting. On 17 and 23 October 2007, the ArchSD informed the VTC that “*the submission was incomplete and inadequate for tendering*”, and asked the project consultant to submit a complete design and tender document for the ArchSD’s vetting. On

Note 17: *The Permanent Secretary for Education was the Controlling Officer for this project.*

26 October 2007, the VTC submitted the project consultant's letter to the ArchSD clarifying that the tender documents had been amended in accordance with the ArchSD's comments, and the consultant opined that the issued drawing was adequate for the tender to provide a reasonable tender price;

- (b) on 30 October 2007, the ArchSD informed the VTC that *"the completion of technical vetting depends on the completeness, adequacy and quality of submission.....We are informed by your consultants verbally today that the invitation of tender will commence tomorrow irrespective of whether we have completed the vetting or not. Please be reminded that the authority to approve the commencement of the tendering process rests with the VTC, and VTC alone will be responsible for any additional expenses associated with its approval of a tender which contains incomplete and inadequate information"*;
- (c) on 30 October 2007, the VTC invited tenders for the superstructure contract for the TKL Campus based on the modified Hybrid Scheme (Tender A), with an option of using the RC Scheme (Tender B). Tenderers were invited to quote prices on both options;
- (d) on 1 November 2007, the consultants assured the VTC in the letter that *"this tender is considered suitable for tender purpose. Nevertheless, comment from the ArchSD will be duly incorporated in the tender document and our project quantity surveyor is refining the tender document for issuing tender addendum in mid November 2007"*;
- (e) on 23 November 2007, the ArchSD reiterated to the VTC that the tender drawings were inadequate and incomplete for tendering purpose. On 28 November 2007, the consultants wrote to the VTC with a copy to the ArchSD, stating that the ArchSD's comments had been incorporated in the tender addenda;
- (f) on 12 December 2007, the tender was closed. The lowest price for Tender A was \$1,155 million and the lowest price for Tender B was \$1,032 million; and
- (g) on 19 December 2007, the ArchSD informed the VTC that for Tender B, *"there are insufficient structural details provided"*.

RC Scheme not followed

3.22 At the joint meeting of the VTC Standing Committee and VTC Estates Committee held on 20 November 2006, when the Committees ratified the recommendation of the Jury Panel for the design competition, the winning design was based on the RC Scheme. The two Committees agreed and the VTC Council approved to set aside \$40 million from VTC's self-financed programmes to meet the possible shortfall in the budget based on the cost estimate of using RC Scheme. Moreover, the project cost estimate submitted by the VTC for vetting by the ArchSD in March 2007 and the project estimate of \$1,006.3 million in money-of-the-day prices approved by the FC in June 2007 was based on the RC Scheme (see para. 3.17). Notwithstanding this, the HKDI was eventually built using the modified Hybrid Scheme. Audit examined the records and noted that although the RC Scheme was considered in November 2006 and March 2007, the Scheme had not been rigorously pursued since April 2007:

Modified Hybrid Scheme taken forward

- (a) on 30 April 2007, the project consultant informed the CCG that the current design was based on the modified Hybrid Scheme. The consultant further advised that this design option was the most structural-effective option and the finalised design would be ready shortly. On 15 June 2007, the consultant issued an updated cost estimate of \$1,064.1 million based on the modified Hybrid Scheme, which was \$71.3 million (7%) higher than the cost estimate of \$992.8 million based on the RC Scheme submitted to the ArchSD on 26 April 2007;
- (b) on 30 October 2007, the VTC issued the tender for the superstructure contract based on the modified Hybrid Scheme (Tender A). An option of using the RC Scheme (Tender B) was included in the tender and tenderers were invited to quote prices on it as well. On 28 December 2007, the VTC informed the ArchSD that the VTC had commenced cost reduction exercise with the lowest tenderer of Tender A (modified Hybrid Scheme), but not Tender B (RC Scheme);

RC Scheme not submitted to Buildings Department

- (c) on 16 November 2007, the superstructure plan based on the modified Hybrid Scheme was submitted to the Buildings Department (BD). The superstructure plan based on the RC Scheme had not been submitted to the BD;
- (d) in January 2008, the Steering Committee for the TKL Campus development project (Note 18) recommended to pursue the RC Scheme together with a list of cost reduction items for the Standing Committee's and Estates Committee's approval;
- (e) on 22 February 2008, members of the Standing Committee, Estates Committee and Steering Committee of the VTC were informed at the joint meeting of these three Committees that the RC Scheme, which had not been fully developed, was not ready for adoption and hence Tender B was not a genuine tender option (Note 19) that could be considered. The VTC Council Secretariat explained to the Committees that:
 - (i) the structural engineering consultant was still advising on changes to the construction specifications for the RC Scheme, and these changes would likely result in additional costs and might not be acceptable to the designer of the campus due to impacts on his original design; and
 - (ii) the drawings of the RC Scheme had not yet been cleared by the BD, and there could be other uncertainties and possibly more variations as the option was further developed. Some of the variations identified involved substantive items which required retendering of the contract and would push back the project timeline by about six months.

The three Committees finally endorsed undertaking pre-contract variation discussions with the lowest tenderer of Tender A; and

Note 18: *The VTC set up a Steering Committee under the Estates Committee to steer, oversee and monitor the progress of the TKL Campus development project. The terms of reference of the Steering Committee was at Appendix J.*

Note 19: *In response to Audit enquiry, the VTC informed Audit in September 2017 that Tender B was not a genuine tender because the RC Scheme was a fall-back option (see para. 3.23) and no detailed design and no submission to the BD were made for Tender B.*

Modified Hybrid Scheme approved by VTC Council

- (f) at the joint meeting of the Estates and Steering Committees of the VTC on 14 April 2008, members endorsed the recommendation to accept the tender for the superstructure contract submitted by the lowest tenderer of Tender A at an estimated cost of \$1,099.3 million, after having taken into account cost reductions from the pre-contract variations. The recommendation was subsequently approved by the VTC Council on 18 April 2008.

3.23 In response to Audit enquiry, the VTC informed Audit in September 2017 that since April 2007, the modified Hybrid Scheme had been adopted and the RC Scheme had been considered only as a fall-back option. However, Audit noted that there was no documentary evidence showing that the VTC Council or the committees had ever been explicitly informed that the RC Scheme had been considered only as a fall-back option.

More accurate information should have been provided to the VTC Council and the committees

3.24 Audit examination of the meeting minutes of the VTC Council and the committees revealed that more information should have been provided to the VTC Council and the committees. Audit noted that:

- (a) the CCG had not informed the Council and the Steering Committee, Standing Committee and Estates Committee of the VTC of the change of structural design leading to an increase of the project cost estimate by \$71.3 million from \$992.8 million to \$1,064.1 million on 15 June 2007;
- (b) in June and August 2007 respectively, the Estates Committee and the Steering Committee of the VTC were informed that *“the campus designed by the design team is a composite reinforced concrete and steel structure”*. However, the VTC Council and the committees were not informed of the cost implications due to change of structural design;
- (c) in January 2008, the Steering Committee for the TKL Campus development project recommended to pursue the RC Scheme together with a list of cost reduction items for the VTC Standing Committee’s and VTC Estates

Committee's approval. However, the Steering Committee was not informed that:

- (i) the project team had only submitted the superstructure drawings for the modified Hybrid Scheme to the BD and the drawings had already been approved; and
 - (ii) the superstructure drawings for the RC Scheme were not submitted to the BD for approval; and
- (d) at the joint meeting of the Standing Committee, Estates Committee and Steering Committee of the VTC held in February 2008 (see para. 3.22(e)), it was reported that the drawings of the RC Scheme had not yet been cleared by the BD. Audit noted that the three Committees had not been informed of the reason for the drawings of the RC Scheme not having been cleared by the BD, which was attributable to the fact that the project team had not submitted the drawings of the superstructure based on the RC Scheme to the BD for clearance.

3.25 For capital projects, various development schemes may be available to take forward the project. In the case of the HKDI, available development schemes were the RC Scheme, Steel Scheme, Hybrid Scheme and modified Hybrid Scheme. No documentary evidence was available to show that the schemes had been thoroughly discussed and that the modified Hybrid Scheme had been well justified.

Foundation was built for RC Scheme

3.26 According to the pros and cons analysis of the structural schemes submitted to the CCG in March 2007 (see Table 15 in para. 3.14), the RC Scheme would incur the highest foundation cost among the three structural schemes. Audit examination of the project records revealed that the plan of foundation for the HKDI was drawn up in February 2007 based on the assumption that a full RC structural design would be adopted for the superstructure of the HKDI.

3.27 In April 2007, the project consultant informed the CCG that the current design was based on a composite structure of RC and steel (see para. 3.15). However, no record was available showing that the project team had taken action to revise the foundation plan according to the modified hybrid superstructure and to reduce the cost of the foundation. The tender exercise carried out in May 2007 for the foundation works was based on the assumption of a full RC superstructure. In response to Audit enquiry, the VTC informed Audit in September 2017 that this was to allow for the possibility of reverting to the RC Scheme, which remained as a fall-back option as Tender B, in case Tender A was not affordable. The Council approved the award of Tender A with pre-contract variations on 18 April 2008. By that time the foundation works had largely been completed as programmed to avoid delay and higher cost.

Project progress reports not submitted to EDB

3.28 According to Financial Circular No. 9/2004, a Controlling Officer shall require a subvented organisation to submit project progress reports together with updated budget forecasts and outturn income and expenditure statements upon approval of capital subventions and thereafter at quarterly intervals.

3.29 Audit noted that, after approval of FC funding, the EDB had not required the VTC to submit progress reports together with updated budget forecasts and outturn income and expenditure statements at quarterly intervals for the TKL Campus development project. In response to Audit enquiry, the EDB informed Audit in August 2017 that:

- (a) progress of capital works projects of the VTC including progress reports would be submitted to the Estates Committee of the VTC with meetings held around three to four times a year. The ArchSD is a member of the Estates Committee; and
- (b) major issues which involved a matter of principle or substantial implications would require endorsement from the VTC's Finance Committee, Standing Committee and/or the Council of the VTC before implementation. With a representative in the VTC's Finance Committee, the Standing Committee and the Council, the EDB could tender its comments or raise queries on any works project if necessary.

Campus development and management

3.30 Audit reviewed the meeting records of the Council, Standing Committee, Estates Committee and Steering Committee of the VTC in the first year after project funding had been approved by the FC, i.e. for the period from July 2007 to June 2008. Audit noted that:

- (a) no reporting of outturn income and expenditure had been made in the Council meetings or Committee meetings; and
- (b) updated project budget forecast was only reported once in a Steering Committee meeting held in October 2007, but no representatives of the EDB or the ArchSD were present in the meeting.

Audit considers that the EDB needs to take measures to ensure that the VTC submits project progress reports together with updated budget forecasts and outturn income and expenditure statements quarterly for future government subvented projects as required by the Financial Circular.

Audit recommendations

3.31 Audit has *recommended* that the Executive Director, VTC should, for future capital projects:

- (a) **provide up-to-date cost estimate to the ArchSD for comments in seeking funding from the FC of LegCo;**
- (b) **take measures to ensure that agreement from the ArchSD is sought according to the VTC's Notes for Guidance on Capital Subventions before issuing tenders for the projects;**
- (c) **enhance project information provided to the Council and the relevant committees to facilitate them to make informed decisions;**
- (d) **take measures to ensure that before adopting a development scheme, the various schemes should be thoroughly discussed and the decision to adopt a particular scheme should be well justified and approved; and**
- (e) **take measures to ensure that the foundation of the project is developed according to the design of the superstructure.**

3.32 Audit has *recommended* that the Secretary for Education should, for future government subvented projects, in accordance with Financial Circular No. 9/2004, take measures to ensure that the VTC submits to the EDB project progress reports together with updated budget forecasts and outturn income and expenditure statements upon approval of capital subventions and thereafter at quarterly intervals.

Response from the VTC and the Government

3.33 The Executive Director, VTC agrees with the audit recommendations in paragraph 3.31. She has said that:

- (a) in a paper presented in the joint meeting of the Standing Committee, Estates Committee and Steering Committee of the VTC on 18 January 2008, it was stated that *“at its meeting on 26 October 2007, the Steering Committee noted that the cost estimates could well exceed the LegCo approved budget by over \$100 million and asked that alternative scheme be explored. The Consultant Team has put forward a more economical alternative which would use reinforced concrete (RC) for the 4 towers and the sky platform, but which would be bulky in outlook”*. The paper indicated that the RC Scheme had been considered only as a fall-back option while the modified Hybrid Scheme was adopted. Because the RC Scheme was a fall-back option, only the detailed design of the adopted modified Hybrid Scheme was submitted to the BD for approval. If the RC Scheme was also submitted to the BD for approval, it would supersede the approval of the modified Hybrid Scheme;
- (b) the VTC has, since 2014, provided to the Estates Committee details of project information and up-to-date cost estimates to the ArchSD for comments in seeking funding from the FC; and
- (c) measures will be taken to ensure thorough discussion on scheme adoption for Government subvented projects.

3.34 The Secretary for Education agrees with the audit recommendation in paragraph 3.32. He has said that since March 2017, the EDB has requested the VTC to submit progress reports to the EDB on the on-going capital works projects at quarterly intervals. He has also said that the EDB will ensure that quarterly progress reports are submitted for upcoming capital works projects, and the bureau will closely

monitor the progress of the projects to ensure compliance with the relevant Financial Circular.

Management of campus

Opening up sports and amenity facilities to the public

3.35 In June 2007, when seeking funding from the FC of LegCo for the construction of the new TKL Campus, the EDB informed the FC that student sports and amenity facilities (i.e. swimming pool, basketball courts, tennis court and gymnasium (Note 20)) at the new campus would be open to the public during non-school hours as suggested by the Sai Kung District Council.

3.36 Audit noted that the swimming pool, the basketball courts and the multi-purpose hall (Note 20) have been open to the public since October 2010. However, the tennis court had not been open to the public. In response to Audit enquiry, the HKDI informed Audit in September 2017 that the tennis court was located on the ninth floor of the campus. The campus management had great concerns on the campus safety and security, and that additional resources would be incurred on the administration and security manpower for the operations during non-school hours. Audit noted that:

- (a) in the period 2010 to 2013, the HKDI planned to open the tennis court to the public. In May 2010, the HKDI informed the Sai Kung District Council that the tennis court would be open to the public. In July 2012, the Campus Executive Committee (CEC) of the TKL Campus planned that the tennis court would be open to the public in September 2012. In January 2013, the Campus Secretariat prepared costing and resource arrangement for the operation of the tennis court for public use;
- (b) there were requests from members of the Sai Kung District Council to open the tennis court to the public; and

Note 20: *The location of the planned gymnasium is used as a multi-purpose hall. The HKDI advised Audit that under the agreed arrangement with the Sai Kung District Council, the multi-purpose hall is open to the public during non-school hours for badminton as well as other indoor sports activities.*

- (c) according to the statistics of the Leisure and Cultural Services Department, for the period from 1 to 15 June 2017, the utilisation rate of the six tennis courts in Tseung Kwan O district during non-school hours (Note 21) was 88%.

The HKDI needs to further explore the feasibility of opening the tennis court to the public during non-school hours.

Utilisation of teaching venues

3.37 The HKDI uses a computerised timetabling system to manage and record the allocation of timeslots of its teaching venues (e.g. lecture theatres, classrooms and workshops) among various academic departments and operational units. Any timeslots not allocated are available for booking by staff. All booking records are also captured in the system.

3.38 ***Incorrect utilisation rates of some teaching venues.*** The HKDI periodically calculated the utilisation rates of teaching venues for management information. The intention was to exclude the utilisation after 6:30 pm on weekdays and on weekends. However, some of the teaching venues (e.g. computer laboratories and the digital visual effects studio) were also occupied after 6:30 pm on weekdays and on weekends. The utilisation rates reported were overstated because number of hours available did not include hours after 6:30 pm on weekdays and on weekends while number of hours booked included booked hours in such period. For example, for Semester 1 of 2016/17, the utilisation rates of the following teaching venues were overstated (see Table 16).

Note 21: *The utilisation rate calculated by the Leisure and Cultural Services Department for the six tennis courts in Tseung Kwan O district covered the period from 6:00 pm to 11:00 pm on weekdays, and whole day on Saturdays, Sundays and public holidays. These hours are about the same as the non-school hours of the HKDI.*

Table 16

Examples of teaching venues with utilisation rates overstated
(Semester 1 of 2016/17)

Teaching venue	Total no. of hours booked (a)	No. of hours booked after 6:30 pm on weekdays and on weekends (b)	Utilisation rate reported to management (c) $= (a) / 750 \times 100\%$ (Note) (%)	Actual utilisation rate (d) $= [(a) - (b)] / 750 \times 100\%$ (Note) (%)	Difference (e) $= (c) - (d)$ (%)
Fashion Technology Workshop	547	141.5	73 %	54 %	19 %
Digital Visual Effects Studio	721	147	96 %	77 %	19 %
Computer Game Laboratory	695.5	138	93 %	74 %	19 %
Computer Lab	571	91	76 %	64 %	12 %
Classroom	665	85	89 %	77 %	12 %

Source: Audit analysis of HKDI records

Note: Semester 1 of 2016/17 lasted for 15 weeks. Total number of hours available for booking was defined as: number of hours available for booking per weekday (10 hours from 8:30 am to 6:30 pm) \times number of weekdays per week (5 days) \times number of weeks in the semester (15 weeks). The total number of hours available for booking in the semester was: 10 hours per day \times 5 days per week \times 15 weeks = 750 hours.

Room for increasing the use of the Auditorium for event rental

3.39 When seeking funding from the FC of LegCo in June 2007 for the construction of the TKL Campus, the FC was informed that, if available, the Auditorium would be available for event rental by the public. The Auditorium is available for booking on weekdays, weekends as well as public holidays. Audit examination of the booking records of the Auditorium for the period from 2013/14 to 2016/17 revealed that there was room for increasing the use of Auditorium for event rental (see Table 17). Audit noted that:

- (a) for 81 to 129 days a year, the Auditorium was closed for maintenance; and
- (b) usage of the Auditorium by external parties was on the low side, ranging from 2 to 10 days a year.

Audit considers that the HKDI needs to review the reasons for the large number of days needed for maintenance and take measures to reduce the number of days of maintenance. It also needs to consider promoting the availability of the Auditorium for event rental.

Table 17

**Analysis of the booking of the Auditorium
(2013/14 to 2016/17)**

	No. of days			
	2013/14	2014/15	2015/16	2016/17
Not available for booking due to maintenance	81 (27%)	129 (44%)	112 (38%)	103 (35%)
Occupied by HKDI and other VTC member institutions	176 (60%)	148 (50%)	138 (47%)	178 (60%)
Occupied by external parties	10 (3%)	3 (1%)	2 (0%)	3 (1%)
Not occupied	29 (10%)	16 (5%)	44 (15%)	12 (4%)
Total (Note)	296 (100%)	296 (100%)	296 (100%)	296 (100%)

Source: Audit analysis of HKDI records

Note: According to the HKDI, total number of days available for booking should be counted with due consideration of the manpower constraint at the Auditorium. This referred to the absence of manpower to provide support service during rest days, general holidays and statutory holidays in any given year. In case an event was held on any of these non-working days and support service was required, alternative holidays would be arranged for the staff who needed to work on these non-working days.

Need to improve booking of basketball courts and multi-purpose hall by public

3.40 **Basketball courts.** There are two basketball courts in the HKDI. They are open for booking by the public at a fee of \$80 per court per hour during non-school hours. Audit examined the booking records of the basketball courts during non-school hours for the period from 2015/16 to 2016/17 and noted that the utilisation rates ranged from 5% to 19% per semester (see Table 18).

Table 18

**Utilisation rates of basketball courts during non-school hours
(2015/16 and 2016/17)**

	Utilisation rate
2015/16	
Semester 1	19%
Semester 2	14%
Semester 3	11%
2016/17	
Semester 1	13%
Semester 2	9%
Semester 3	5%

Source: Audit analysis of HKDI records

3.41 Booking of the basketball courts can only be made in person at the Campus Secretariat during office hours (i.e. from 9:00 am to 6:00 pm on weekdays and 9:00 am to 12:00 noon on Saturdays). User can only make one booking per day (an hour per court per booking), and no on-the-day booking will be accepted. The HKDI may consider relaxing its booking rules (e.g. allowing telephone reservation and accepting on-the-day booking), with a view to facilitating the booking of the basketball courts for use during non-school hours.

3.42 **Multi-purpose hall.** There are two badminton courts in the multi-purpose hall. The hall is open for use by the public for badminton and other indoor sports activities by booking at a fee (Note 22). Audit examined the booking records of the multi-purpose hall and noted that usage of the hall by external parties was on the low side, involving 2% (70 out of 3,279 hours) and 3% (99 out of 3,540 hours) of the total available hours of the hall during the semesters in 2015/16 and 2016/17 respectively.

Note 22: As at 1 September 2017, the hire charge of the multi-purpose hall was \$695 per hour.

3.43 Booking of the multi-purpose hall is governed by the VTC's hire of accommodation procedures. Applications for hiring can only be made by organisations but not by individuals. Applications are normally accepted up to four months in advance and at the latest, one month before the start date of the hiring period. Minimum hire period is two hours. The multi-purpose hall must be hired as a whole, and the badminton courts cannot be hired separately. The HKDI may consider relaxing its booking rules for the multi-purpose hall (e.g. allowing bookings by individuals and booking of only one badminton court but not the whole hall), with a view to facilitating the booking of the multi-purpose hall for use during non-school hours.

Management of lifts and escalators

3.44 There are 13 lifts and 4 escalators (2 long ones and 2 short ones) at the TKL Campus. Two lifts serve IVE(LWL) and eleven lifts and four escalators serve the HKDI. Three contractors were engaged for providing routine maintenance and services of the lifts and escalators installed (see Table 19). The maintenance and services were managed regardless of whether the lifts/escalators serve the HKDI or IVE(LWL).

Table 19

**Contractors of lifts and escalators
(1 April 2015 to 31 March 2021)**

Lift/escalator	Registered contractor	Contract period
L1 – L11	Contractor 1	1 April 2016 – 31 March 2021
L12 – L13	Contractor 2	1 April 2016 – 31 March 2021
E1 – E4	Contractor 3	1 April 2015 – 31 March 2018

Source: HKDI records

3.45 *Malfunction of lifts and escalators.* Under the Lifts and Escalators Ordinance (Cap. 618), a log book should be kept for each lift and escalator to record all major events, including lift and escalator failure. Audit examined the log books of the 13 lifts and 4 escalators at the TKL Campus for the period from 2014 to 2016 and noted that the number of breakdown cases of lifts and escalators had increased by 174% from 53 cases in 2014 to 145 cases in 2016. Audit further noted that in 2015 and 2016, 12 (i.e. 71%) of the 17 lifts and escalators had each broken down six times or more. One of them had broken down 16 times in 2015 and another had broken down 26 times in 2016 (see Table 20).

Table 20

**Analysis of breakdown cases of lifts and escalators
(2015 and 2016)**

No. of breakdown cases	No. of lifts/escalators		Total no. of breakdown cases involved
	2015	2016	
0	0	1	0
1 – 5	5	4	23
6 – 10	5	7	89
11 – 15	6	4	129
16 – 20	1	0	16
21 – 25	0	0	0
26	0	1	26
Total	17	17	283

Source: Audit analysis of HKDI records

3.46 *Need to improve monitoring of contractors' performance.* All three routine maintenance and service contracts stipulate that the monthly system service availability (Note 23) shall be maintained at at least 99%. Audit noted that the service availability records were not available and the HKDI had not monitored the system service availability.

3.47 Audit examination of the log books of the 13 lifts and 4 escalators revealed that the monthly system service availability of the 4 escalators had decreased from 99.7% in January 2015 to 71.0% in June 2017. The number of months in which the monthly system service availability was lower than 99% had increased from two in 2015 to six in 2016. In the six months from January to June 2017, the monthly system service availability was lower than 99% in four months (see Table 21).

Table 21

**Audit analysis of the monthly system service availability of the four escalators
(January 2015 to June 2017)**

Monthly system service availability	No. of months		
	2015	2016	2017 (up to June)
99% or above	10	6	2
80% – 98%	2	6	2
79% or below	0	0	2
Total	12	12	6

Source: *Audit analysis of HKDI records*

Note 23: *According to the routine maintenance and service contracts, “service availability” is defined as:*

$$1 - \frac{\text{Total downtime}}{\text{Total operating time}} \times 100\%$$

Total downtime is the total loss of operating hours of each lift due to lift failures. Downtime due to scheduled maintenance works is not included. Total operating time is the total time that the lift/escalator is expected to be operating during the period concerned.

3.48 The escalator maintenance and service contractor was required to respond to all escalator failures by having staff on site within 1 hour to attend to the situation. Table 22 below summarises the cases where the contractor had failed to comply with the one-hour response requirement during the period January 2015 to June 2017. No record was available showing that the HKDI or VTC had taken follow-up action with the contractor.

Table 22

**Audit analysis of the one-hour response requirement of the four escalators
(January 2015 to June 2017)**

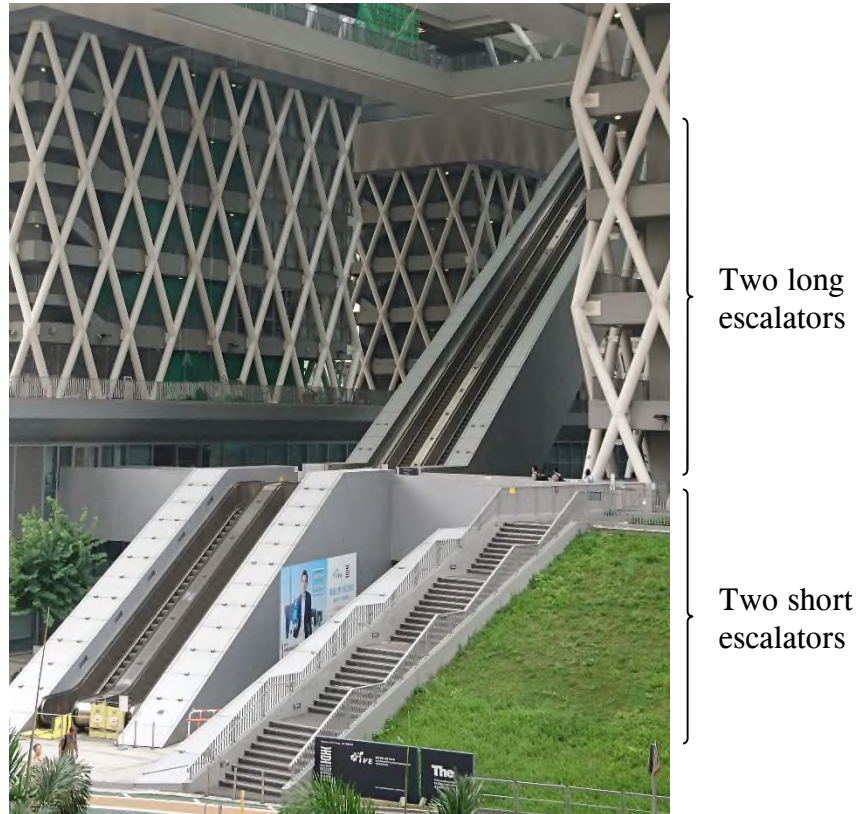
Year	No. of delayed cases	Range of delays (minutes)
2015	2	10 to 158
2016	3	5 to 145
2017 (up to June)	2	10 to 25

Source: Audit analysis of HKDI records

3.49 ***Suspension of service of two short escalators.*** There were two short escalators (i.e. E1 and E2) between the ground and first floor with vertical rise of 6.2 metres (see Photograph 2). The two short escalators are available for public use during their operation hours (i.e. 7:30 am - 7:30 pm on Mondays to Fridays and 7:30 am - 12:30 pm on Saturdays, Sundays and public holidays). Audit examined the service records for the period from 1 January 2017 to 30 June 2017 of the two escalators and noted that the two escalators were suspended from operation in 21.2% (or 744 of the total 3,504 operating hours) of the available operating time because of adverse weather (see Table 23). In response to Audit enquiry, the HKDI said that in the absence of suitable roof and enclosure, the two short escalators were exposed to weather conditions. Their services needed to be suspended during rainy days or adverse weather conditions to eliminate potential hazards.

Photograph 2

Four escalators at HKDI



Source: Photograph taken by Audit on 22 August 2017

Table 23

**Suspension of services for two short escalators
(1 January 2017 to 30 June 2017)**

Escalator	Operating time available (a) (Hour)	Suspension of services			Net operating time (e) = (a) - (b) - (c) - (d) (Hour)
		Breakdown (b) (Hour)	Maintenance (c) (Hour)	Rainfall (d) (Hour)	
E1	1,752.0	9.9	100.5	372.1	1,269.5
E2	1,752.0	19.3	100.5	372.1	1,260.1
Total	3,504.0 (100%)	29.2 (0.8%)	201.0 (5.8%)	744.2 (21.2%)	2,529.6 (72.2%)

Source: Audit analysis of HKDI records

3.50 ***Suspension of service of one long escalator.*** There were two long escalators (i.e. E3 and E4) between the first floor and seventh floor with vertical rise of 25.8 metres (Note 24) (see Photograph 2). The two long escalators are open for use of students and staff on weekdays from 7:30 am to 7:30 pm. Audit examined the service records for the period from 1 January 2017 to 30 June 2017 and noted that the two escalators had been suspended from operation a number of times. Up to 30 March 2017, the escalator E3 had been suspended for 43 hours out of 732 available operating hours due to breakdown and routine maintenance. Eighty-five steps of the escalator E3 were found damaged by the contractor on 30 March 2017. The replacement cost amounted to about \$1 million. Since then, the escalator E3 had been suspended from operation. In response to Audit enquiry, the HKDI said in August 2017 that there was a contractual dispute with the contractor regarding the

Note 24: According to the Electrical and Mechanical Services Department, long escalators generally refer to those with vertical rise of more than 15 metres.

escalator E3. Therefore, the related maintenance and service work could not be carried out and the escalator had been suspended from operation for 720 available operating hours in the period 31 March 2017 to 30 June 2017. The VTC has appointed a consultant in May 2017 to provide advice and study alternatives for the way forward. Meetings among consultant, escalator maintenance contractor and the VTC were held on 12 June 2017, 17 July 2017 and 27 July 2017. The consultant is currently preparing recommendations and a study report. In the meantime, students and teachers are using lifts or stairs to go to their classrooms and offices.

Unauthorised overnight parking

3.51 The HKDI does not allow overnight parking from 10:30 pm to 7:30 am the next day in the campus car park. Audit reviewed the records of the car park in the 5-month period from 1 January 2017 to 31 May 2017 and noted that there were 195 overnight parkings at 111 (74%) of the 151 nights in the period, involving 11 vehicles. In particular:

- (a) one vehicle parked for 97 nights (64% of 151 nights) in the period, the most among the 11 vehicles; and
- (b) one vehicle of a staff did not possess a valid parking permit issued by the HKDI.

Obstruction to emergency vehicle access (EVA)

3.52 There is an EVA provided at the TKL Campus. The purpose of the EVA is to allow safe and unobstructed access and safe operation of vehicles of the Fire Services Department. For safety reason, no parking should be allowed at places that will obstruct the EVA. During the period 19 May 2017 to 15 June 2017, Audit observed that illegal parking outside the EVA was common causing obstruction to the EVA. Sometimes, one or two private cars were parked in the public street at the entrance of the EVA. Sometimes as many as six private cars were parked there. For instance, at about noon on 14 June 2017, the EVA was obstructed by one roadside skip and six private cars (see Photograph 3).

Photograph 3

Obstruction to EVA



Source: Photograph taken by Audit on 14 June 2017 at 12:33 pm

Audit recommendations

3.53 Audit has *recommended* that the Executive Director, VTC should:

- (a) further explore the feasibility of opening the tennis court to the public during non-school hours;
- (b) take measures to ensure the correctness of the utilisation rates of teaching venues;
- (c) review the reasons for the large number of days on which the Auditorium was closed for maintenance and take measures to address the problem;
- (d) step up the promotion effort on the availability of the Auditorium for event rental;
- (e) consider taking measures to facilitate the booking of the basketball courts and the multi-purpose hall by the public;

Campus development and management

- (f) **monitor the problem of repeated breakdown cases of the lifts and escalators and, if necessary, take action to address the problem;**
- (g) **ensure that the contractor attain the performance target on maintenance services under the maintenance and service contract of escalators at TKL Campus, including the service availability and response time to breakdown;**
- (h) **explore whether any measures can be taken to increase the operating time of the two short escalators;**
- (i) **endeavour to resume as soon as possible the service of the long escalator which had been suspended;**
- (j) **take measures to prevent unauthorised overnight parking at the campus carpark; and**
- (k) **take measures to keep the EVA unobstructed at all time.**

Response from the VTC

3.54 The Executive Director, VTC agrees with the audit recommendations. She has said that the HKDI:

- (a) will explore the feasibility on the opening of tennis court to the public during non-school hours, taking due consideration of the need of student extra-curricular activities and balanced utilisation of the facilities, campus security as well as manpower and resources to provide the administrative support for the operation;
- (b) will revise the formula of the utilisation rate calculation with the enhancements in the central computerised system;
- (c) will explore the possible measures to shorten the maintenance period of the Auditorium with due consideration of the safety issues, given that the existing non-occupancy rate was 8.5% on average in the past 4 years;

- (d) will review the booking rules of the basketball courts and the multi-purpose hall, taking due consideration of manpower and resources on the administrative support for the operation, while striking the balance between the student extra-curricular activities and public needs;
- (e) has monitored control of material delivery to avoid damage of lift doors by trolleys;
- (f) has taken immediate measures to prohibit unauthorised overnight parking at the campus carpark; and
- (g) has made proactive efforts in reporting the blockage of the EVA located outside campus area to the relevant government departments for follow-up, and will put more rigorous effort to report the problem.

PART 4: ADMINISTRATIVE ISSUES

4.1 This PART examines the following administrative issues:

- (a) inventory management (paras. 4.2 to 4.11);
- (b) staff recruitment (paras. 4.12 to 4.16);
- (c) campus environmental performance (paras. 4.17 to 4.27); and
- (d) management of computer retail shop (paras. 4.28 to 4.31).

Inventory management

4.2 The VTC has issued a Stores Manual, which incorporates the stores policies, guidelines and procedures. According to the Stores Manual of the VTC, inventory stores are:

- (a) non-consumable nature and should be of a unit purchase cost exceeding \$5,000 or with expected life span over 3 years;
- (b) computer equipment including personal computer, notebook, workstation, server and specified peripherals (i.e. printer, scanner, monitor, memory card, tape backup system, writing pad and zip drive); or
- (c) custom-made software or system application.

Because many inventory items are shared between the HKDI and IVE(LWL), inventory controls (e.g. annual stocktakes) apply to TKL Campus as a whole. As at 25 May 2017, the value of the inventories at the TKL Campus amounted to about \$231 million.

Some annual stocktaking not conducted

4.3 According to the inventory guidelines of the VTC:

- (a) annual stocktaking should be conducted in each financial year; and
- (b) results of the stocktaking should be submitted to the Chief Supplies Officer of the Supplies Section before the deadlines (usually in November or December of a financial year) specified by him.

4.4 Audit found that, in the 7 financial years 2010-11 to 2016-17, stocktaking had not been conducted for three financial years namely, 2010-11, 2012-13 and 2014-15. Stocktaking exercise for financial year 2016-17 was pending as at September 2017.

Long time taken to complete stocktaking exercises

4.5 According to the inventory guidelines of the VTC, on completion of the stocktaking exercises, the inspecting officers shall submit the stocktaking report. A long time had been taken to complete the three stocktaking exercises for financial years 2011-12, 2013-14 and 2015-16. Hence, there was delay in the submission of stocktaking reports for these three stocktaking exercises to the Headquarters Supplies Section, ranging from 10.7 to 26.9 months (see Table 24).

Table 24

**Delay in completing stocktaking exercises and submitting stocktaking reports
(Financial years 2011-12 to 2015-16)**

Financial year	Deadline	Submission date	Delay (Month)
2011-12	15 December 2011	5 June 2013	17.7
2013-14	20 November 2013	17 February 2016	26.9
2015-16	18 December 2015	9 November 2016	10.7

Source: Audit analysis of HKDI records

Missing inventory items

4.6 A total of 810 inventory items of original cost of \$2.7 million were found missing in the three annual stocktaking exercises for financial years 2011-12, 2013-14 and 2015-16 (see Table 25). Amongst the 810 inventory items found missing, 623 (77%) were computer equipment; of which, 127 were desktop or notebook computers, 169 were peripherals (such as monitors, printers and scanners) and 209 were portable storage devices (i.e. external HDD drives and flash drives). According to the guidance note on data breach incident handling and notifications, the loss of staff or student personal data kept in laptop computers and USB flash drives is a data breach (Note 25), the data user shall take active remedial steps to lessen the harm or damage that may cause to the data subjects, such steps may include:

- (a) immediate gathering of essential information relating to the breach, such as what was the cause of the breach and what kind and extent of personal data were involved;
- (b) adapting appropriate measures to contain the breach, such as reporting to law enforcement agencies (e.g. the Police) and relevant regulators (e.g. the Privacy Commissioner);
- (c) assessing the risk of harm; and
- (d) giving of data breach notification to the data subjects.

However, there was no documentary evidence showing that the HKDI had taken these remedial steps to contain the harm or damage that might cause to the data subjects.

Note 25: *A data breach is generally taken to be a suspected breach of data security of sensitive or confidential data held by a data user, exposing these data to the risk of loss, unauthorised or accidental access, processing, erasure or use.*

Table 25

**Inventory items found missing during stocktaking exercises
(Financial years 2011-12 to 2015-16)**

Financial year	Total number of items checked	Number of inventory items missing	Original store value (\$)	Value at write off (\$)
2011-12	11,204	347	917,907	44,074
2013-14	12,175	262	834,725	20,360
2015-16	13,488	201	945,838	12,613
Total	36,867	810	2,698,470	77,047

Source: HKDI records

No effective actions taken to prevent recurrence of loss of inventory items

4.7 It was stipulated in the Stores Manual that for loss or deficiency where the value of stores exceeds \$50,000 and where no fraud, suspected fraud, theft or negligence is involved, the Head of Operational Unit concerned must certify that steps have been taken to prevent similar recurrence in future. In the three annual stocktaking exercises, the HKDI stated that a number of improvement measures had been taken:

- (a) departments should maintain a control list of computer equipment and accessories for internal record of inventory location;
- (b) departments should carry out surprise and full stock check and report irregularities by end of each year;
- (c) proper internal ledger/record of in/out transactions should be maintained within the departments;

Administrative issues

- (d) departments should increase the frequency of inventory inspection internally; and
- (e) the inventory users of all inventory items would be recorded clearly in the inventory list afterwards to prevent loss.

Up to September 2017, most of the improvement measures have not been implemented.

Other non-compliances with the Stores Manual

4.8 According to the Stores Manual:

- (a) internal stock verification should be conducted immediately prior to and immediately following the transfer of stores from one storage area to another; and
- (b) surprise stock and security checks should be carried out on each store unit at irregular intervals at least once every year. The officer conducting the check should record the findings in the Surprise Inspection Book.

4.9 Audit examination of the HKDI records revealed that the above inspections had not been carried out.

Audit recommendations

4.10 Audit has *recommended* that the Executive Director, VTC should ensure that the HKDI:

- (a) **conducts annual stocktaking in a timely manner in each financial year according to the inventory guidelines;**
- (b) **strengthens its inventory control to minimise loss of inventories;**

- (c) **takes the remedial measures to contain the harm or damage that might cause to the data subjects as stipulated in the guidance note on data breach incident handling and notifications;**
- (d) **effectively implements the improvement measures proposed after each stocktaking exercise and closely monitors the progress of implementation;**
- (e) **conducts internal stock verification immediately prior to and immediately following the transfer of stores from one storage area to another; and**
- (f) **conducts surprise stock and security checks on each store unit at irregular intervals at least once every year.**

Response from the VTC

4.11 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) the HKDI will review and take more rigorous effort to enhance its procedures, controls and documentation in inventory management;
- (b) the HKDI has taken immediate action to enhance staff awareness and compliance of VTC's policies on data security and protection; and
- (c) overall measures to streamline the process and enhance efficiency in inventory management are being reviewed.

Staff recruitment

4.12 Under the existing VTC practices, recruitment of staff with contract duration of more than one year and/or open-ended contract are handled by the HRD of the VTC Headquarters. The HKDI regularly conducts recruitment exercises to fill vacant posts of its short-term contract staff/part-time staff.

4.13 For a recruitment exercise, advertisements are placed in local newspapers, on the VTC website and job websites. The VTC issued a guide on recruitment and human resources matters (Human Resources Guide). According to the Human Resources Guide, applicants should be shortlisted for interview according to predetermined shortlisting criteria. A selection board should be formed to interview and select candidates for appointment. The performance of individual candidates during interviews should be recorded in a standard assessment form. A board report should be compiled to summarise the selection process and results. For recruitment of staff with contract duration of more than one year and/or open-ended contract, assessment forms and board reports should be forwarded to the Headquarters HRD for vetting.

Room for improvement in recruitment process

4.14 During the period April 2014 to March 2017, the HKDI conducted 170 recruitment exercises for short-term contract/part-time staff. Audit examined the records of 10 of the 170 recruitment exercises conducted during the period and found that there was room for improvement in the recruitment process. Details are as follows:

- (a) ***Short application period.*** According to the Human Resources Guide, the application period should normally be ten working days. Audit noted that, for four of the ten recruitment exercises, the application period was shorter than ten working days, ranging from five to nine working days; and
- (b) ***Reasons for accepting late applications not documented.*** According to the Human Resources Guide:
 - (i) late application should not be accepted, unless there is inadequate response to the recruitment exercise, and the late application has, prima facie, exceptional suitability to fill the vacant post; and
 - (ii) for any late application accepted, the justification should be recorded on file.

In the ten recruitment exercises, Audit noted that of the 197 applications accepted, 4 (2%) were late applications. These 4 late applications were submitted one to eight days after the application deadlines. There was no records available showing the reasons for accepting these late applications.

Audit recommendations

4.15 Audit has *recommended* that the Executive Director, VTC should:

- (a) ensure that the HKDI allows sufficient application period in the recruitment exercises;
- (b) ensure that late applications are not accepted unless fully justified; and
- (c) ensure that the reasons for accepting late applications are properly documented.

Response from the VTC

4.16 The Executive Director, VTC agrees with the audit recommendations. She has said that the HKDI has taken measures to ensure adherence to staff recruitment guide.

Campus environmental performance

Campus environmental targets not met

4.17 It is one of the VTC's environmental policies to reduce waste and consumption of resources, such as water, paper and electricity. The Corporate Environmental Office (CENO) of the VTC Headquarters is tasked to support environmental enhancement of the VTC and set environmental targets for compliance by various campuses.

4.18 The Safety, Health, Environmental Local Committee, comprising representatives from operational units of the campus, was set up to coordinate and implement actions as suggested by the CENO and report to the CEC on the progress of safety, health and environmental issues.

4.19 Using the 2013/14 as the reference year, the CENO set the following campus environmental targets for a two-year review period from 2014/15 to 2015/16:

- (a) 5% reduction on water consumption;
- (b) 5% reduction on electricity consumption; and
- (c) 5% reduction on quantity of paper ordered.

Interim evaluation would be conducted on an annual basis while a comprehensive review would be carried out every two years. The CENO would suggest remedial measures to address areas of non-achievement, as well as measures to meet the common environmental targets. The CENO would call returns of use of resources from local campus and compile progress reports against targets set.

4.20 For 2014/15 and 2015/16, two of the three campus environmental targets (i.e. 5% reduction on electricity consumption and 5% reduction on the quantity of paper ordered) were not achieved (see Table 26). In particular:

- (a) the electricity consumption only slightly decreased by 0.2% and 0.9% in 2014/15 and 2015/16 compared with 2013/14; and
- (b) there was an increase of 6.3% in the quantity of paper ordered in 2014/15 compared with 2013/14.

Table 26

**Achievement of campus environmental targets
(2013/14 to 2015/16)**

	2013/14	2014/15	2015/16
(a) Water consumption			
Consumption (m ³)	25,543	21,480	22,451
Consumption per student (m ³)	3.2	2.7	2.8
Increase/(Decrease) per student (%)	N/A	(15.6%)	(12.5%)
Target met	N/A	✓	✓
(b) Electricity consumption			
Consumption (kWh)	8,375,953	8,368,569	8,309,847
Consumption per student (kWh)	1,052	1,050	1,043
Increase/(Decrease) per student (%)	N/A	(0.2%)	(0.9%)
Target met	N/A	✗	✗
(c) Quantity of paper ordered			
Order of paper (reams – Note)	12,999	13,910	12,772
Order of paper per student (reams – Note)	1.6	1.7	1.6
Increase/(Decrease) per student (%)	N/A	6.3%	0%
Target met	N/A	✗	✗

Legend: ✓ – Yes
 ✗ – No
 N/A – Not applicable

Source: Audit analysis of HKDI records

Note: There are 500 sheets of paper in a ream

4.21 The progress of achievement on campus environmental targets in 2014/15 and 2015/16 was reported to the Safety, Health, Environment Local Committee, the CEC and the CENO. To address the non-achievement of environmental targets, the following remedial measures were put forward by the HKDI in both 2015 and 2016:

- (a) adopting energy saving lighting for replacement;
- (b) monitoring air-conditioning operations and shortening its operation hours;
- (c) installing timer to control lighting/air-conditioning operations; and
- (d) controlling the paper consumption and encouraging the operational units to promote e-copy.

However, there was no documentary evidence showing how these broad directions had been implemented.

Need to expedite action to take forward the consultant's recommendations

4.22 In April 2016, in order to review energy consumption and improve energy efficiency of the TKL Campus, VTC engaged a consultant to conduct an energy audit (Note 26).

4.23 In November 2016, the consultant completed the energy audit and identified several energy saving opportunities to enhance the energy performance which included:

- (a) replacing existing fluorescent lamps with Light Emitting Diode tubes (with estimated investment cost of \$1.181 million and payback period of 3.9 years);
- (b) installing energy efficient fan coil unit (with estimated investment cost of \$50,000 and payback period of 6.5 years); and

Note 26: *Energy audit is a review of how and where energy is consumed in the organisation. It helps identify energy management opportunities where savings of energy and money can be made.*

- (c) installing static pressure control for fresh air system (with estimated investment cost of \$0.5 million and payback period of 10.6 years).

4.24 The consultant recommended the VTC to:

- (a) enhance the overall energy performance in the campus;
- (b) incorporate energy metering and monitoring facilities for continuous and better monitoring of the energy consumption of the Central Building Services Installations (Note 27) in the campus; and
- (c) conduct further investigation such as feasibility study, detailed implementation plan, etc. so as to accurately evaluate the potential saving and implementation cost.

4.25 In response to Audit enquiry, the VTC informed Audit in September 2017 that the recommendations of the consultancy report were still being followed up by the Safety, Health and Environment Task Force and Central Committee on Safety, Health and Environment.

Audit recommendations

4.26 **Audit has *recommended* that the Executive Director, VTC should:**

- (a) **endeavour to achieve the campus environmental targets;**
- (b) **review the environmental measures periodically to ensure that they are effective; and**
- (c) **devise an implementation plan to take forward the consultant's recommendations so as to enhance the overall energy performance.**

Note 27: *Examples of Central Building Services Installations include Central Chiller Plant, Chilled Water Distribution System, Unitary Air Conditioning System, etc.*

Response from the VTC

4.27 The Executive Director, VTC agrees with the audit recommendations. She has said that:

- (a) the CENO will propose ways to enhance environmental awareness among staff and students in the HKDI; and
- (b) the Estates, Health and Safety Division has devised an implementation plan to enhance the overall energy performance in the campus.

Management of computer retail shop

4.28 In HKDI, there is a computer retail shop. Since June 2010, the VTC had entered into three service contracts with a computer service provider (CSP) (Note 28) (see Table 27). The CSP provides a one-stop service relating to sales of computer software and hardware at educational discount and organises training workshops at the TKL Campus for VTC students and staff. The retail store has a floor area of 31.73 m².

Note 28: *The CSP is an authorised education reseller and authorised service provider of the branded computer product company.*

Table 27

**Computer service contracts
(15 June 2010 to 14 May 2018)**

	Contract period	Monthly licence fee
1	15 June 2010 to 14 May 2013 (Note 1)	– \$14,000 (first 24 months) – \$18,000 (subsequent 12 months)
2	15 May 2013 to 14 May 2016 (Note 1)	\$40,000
3	15 May 2016 to 14 May 2018 (Note 2)	\$40,000

Source: HKDI records

Note 1: The first and second contracts were two-year fixed term contracts extendable for one year.

Note 2: The contract was a one-year fixed term contract extendable for one year.

4.29 Audit noted that the CSP did not comply with the requirements laid down in the service contracts:

- (a) ***Sales information not submitted.*** Sales information is important for setting the minimum licence fee of similar service contract in future. According to the service contracts, the CSP should provide the VTC with the information on the volume of business, including types and quantities of items sold to HKDI students and staff plus total sales in dollar value on an annual basis. The CSP did not provide such information for the first and second contracts and the HKDI did not ask the CSP to provide such information for the third contract:
 - (i) the CSP did not provide the required sales information for the first contract. In January 2013 (i.e. four months before the end of the first contract), the HKDI asked the CSP to provide the monthly sales figures since the beginning of the contract in June 2010. However, the CSP said that they were not allowed by the reseller agreement with the branded computer product company to disclose such information; and

- (ii) the HKDI asked the CSP in February 2016, three months before the end of the second contract, for sales information for the second contract. The CSP only provided the total volume of business for 2013 to 2015 without sales in dollar value and detailed breakdown by types of items to the HKDI;
- (b) ***Number of on-campus workshops fewer than required.*** According to the service contracts, the CSP should arrange for a minimum of two free on-campus workshops every six months for staff and students of the VTC. Audit noted that the CSP did not arrange sufficient number of workshops in 5 (63%) of 8 half-yearly periods from May 2013 to April 2017. Only 9 workshops had been arranged in the 8 half-yearly periods. The record on workshops arranged for the first contract was not available;
- (c) ***Annual reports not submitted.*** According to the second service contract, the CSP should provide annual reports on the programmes/workshops/seminars/events/activities organised within 3 months after the completion of services of each year. Audit noted that the CSP did not submit the three annual reports required for the second contract; and
- (d) ***Insurance not taken out as required.*** According to the service contracts, the CSP should effect and maintain at all times comprehensive insurance at its own expense in relation to claims against the VTC and the CSP arising as a result of the CSP's negligence. Audit noted that:
 - (i) except for the periods 24 April 2014 to 23 April 2016 and 24 April 2017 to 23 April 2018, comprehensive insurance was not taken out as required to provide the necessary insurance coverage; and
 - (ii) the insurance policy for periods 24 April 2014 to 23 April 2016 and 24 April 2017 to 23 April 2018 only covered claims against the CSP instead of the VTC and the CSP.

Audit recommendation

4.30 Audit has *recommended* that the Executive Director, VTC should ensure that the CSP complies with all the requirements laid down in the service contracts.

Response from the VTC

4.31 The Executive Director, VTC agrees with the audit recommendations. She has said that the HKDI will take measures to ensure that the CSP complies with all requirements laid down in the service contract.

**Member institutions of the VTC
(2017)**

1. Technological and Higher Education Institute of Hong Kong
2. Institute of Professional Education and Knowledge
3. School for Higher and Professional Education
4. Hong Kong Institute of Vocational Education
5. HKDI
6. Hotel and Tourism Institute
7. Chinese Culinary Institute
8. International Culinary Institute
9. Maritime Services Training Institute
10. Youth College
11. Pro-Act by VTC
12. Integrated Vocational Development Centre
13. Shine Skills Centre

Source: VTC records

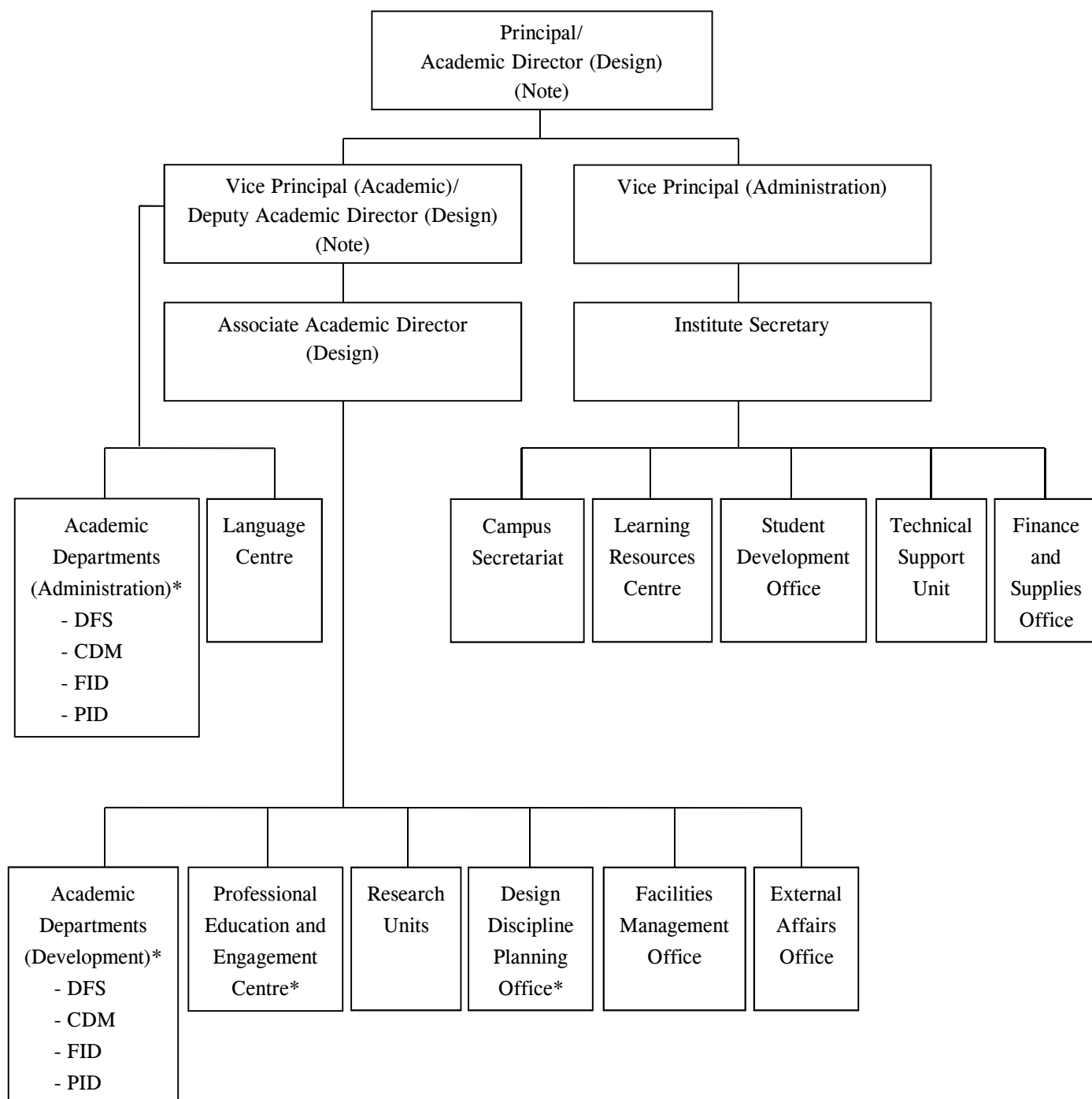
Appendix B
(para. 1.6 refers)

**HD programmes offered by HKDI
(2016/17)**

Programme		Subvented / Self-financed
Department of DFS		
1	Visual Arts and Culture	Subvented
Department of CDM		
2	Creative Media	Subvented
3	Film and Television	Subvented
4	Digital Music and Media	Subvented
5	Visual Communication	Subvented
6	Publication Design and Print Media	Subvented
7	Transmedia	Subvented
8	Advertising Design	Self-financed
Department of FID		
9	Fashion Image Design	Subvented
10	Fashion Branding and Buying	Subvented
11	Fashion Media Design	Subvented
12	Costume Design for Performance	Subvented
13	Fashion Design Menswear	Subvented
14	Fashion Design	Self-financed
Department of PID		
15	Product, Interior and Exhibition Design (Subject Group)	Subvented
16	Architectural Design	Subvented
17	Landscape Architecture	Subvented
18	Jewellery and Image Product Design	Subvented
19	Furniture and Lifestyle Product Design	Subvented
20	Stage and Set Design	Subvented
21	Jewellery Design and Technology	Subvented

Source: HKDI records

**HKDI: Organisation chart
(30 June 2017)**

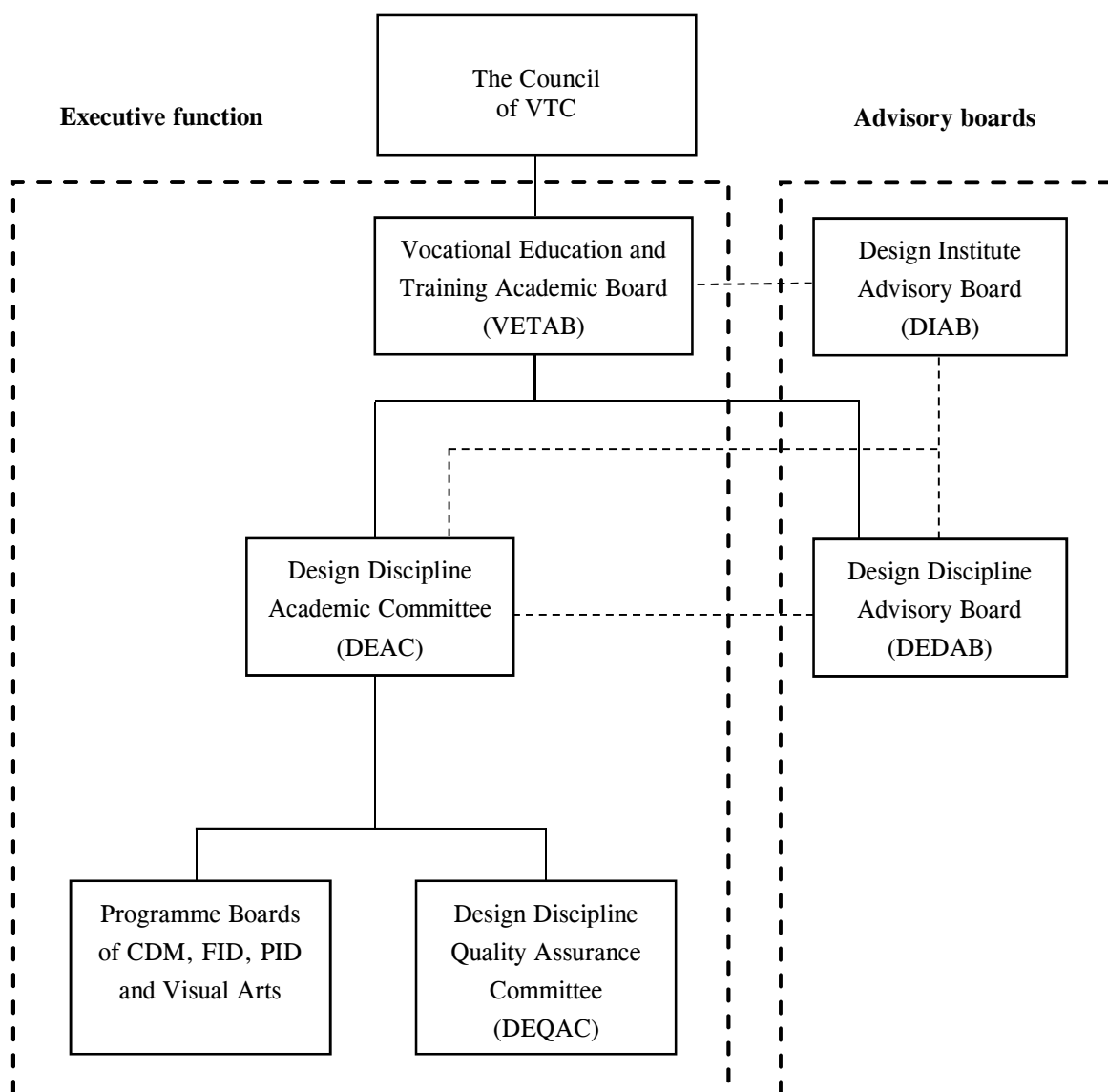


Legend: * Except for the four Academic Departments (DFS, CDM, FID and PID), the Design Discipline Planning Office and the Professional Education and Engagement Centre, all other staff and operating units provide administrative and supporting services to both the HKDI and IVE(LWL).

Source: *HKDI records*

Note: *The Principal and Vice Principal also serve as the Academic Director and Deputy Academic Director of the Design Discipline respectively.*

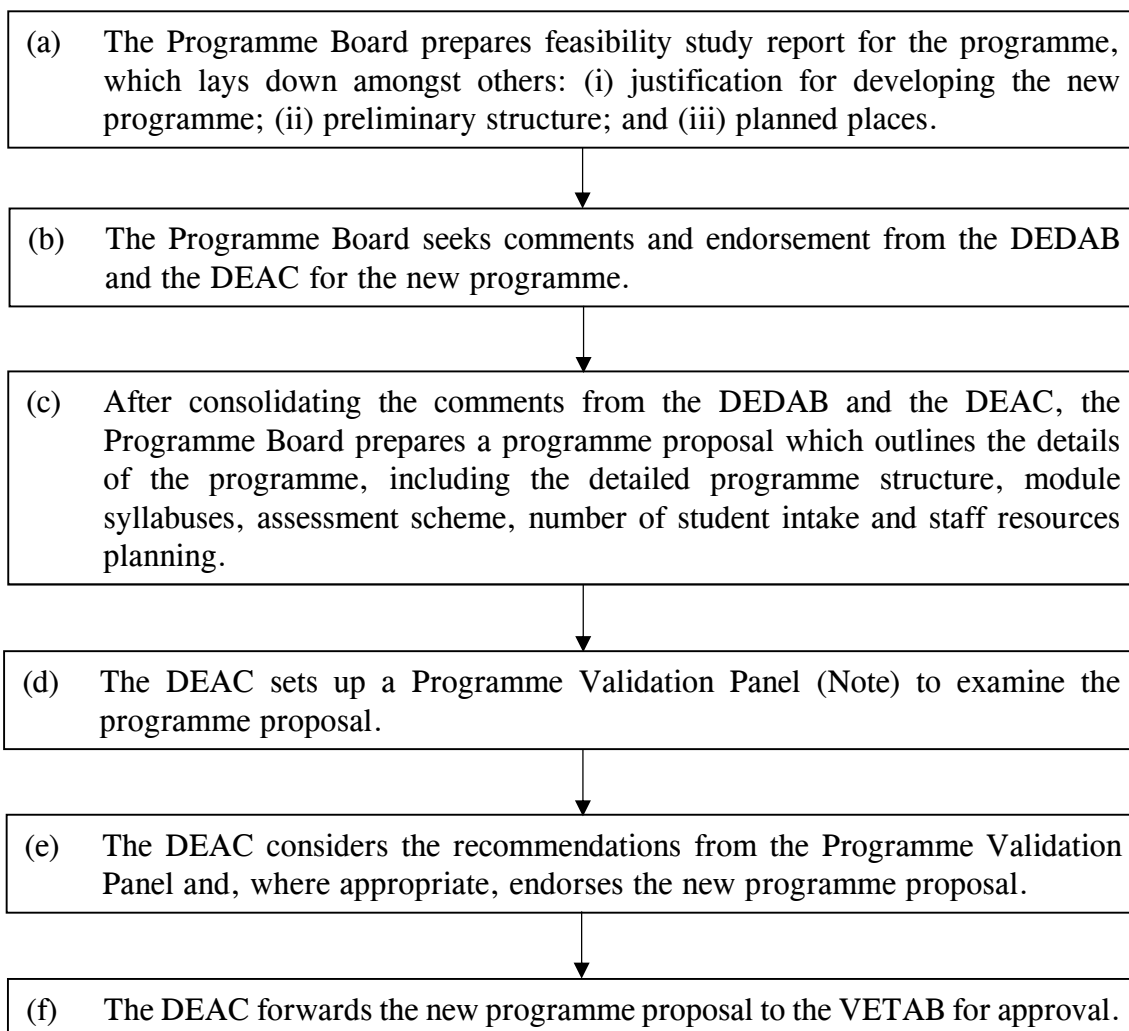
**Design Discipline Boards and Committees
(30 June 2017)**



Legend: ----- Close liaison with each other, but no formal reporting
 ——— Reporting line

Source: HKDI records

Procedures for development of a new programme



Source: Audit analysis of HKDI records

Note: The Programme Validation Panel is set up by the DEAC to assess the appropriateness of the proposed programme. The Panel comprises at least five members, including one external member.

**Programme completion rate
(2012/13 to 2014/15 intake)**

Academic department	2012/13 (%)	2013/14 (%)	2014/15 (%)
DFS	83 %	87 %	77 %
CDM – average – individual programmes	91 % ranged from 88 % to 92 %	85 % ranged from 75 % to 96 %	83 % ranged from 80 % to 85 %
FID – average – individual programmes	84 % ranged from 80 % to 87 %	84 % ranged from 80 % to 90 %	83 % ranged from 81 % to 87 %
PID – average – individual programmes	82 % ranged from 71 % to 88 %	80 % ranged from 58 % to 90 %	75 % ranged from 51 % to 78 %
Overall – average – individual programmes	86 % ranged from 71 % to 92 %	84 % ranged from 58 % to 96 %	80 % ranged from 51 % to 87 %

Source: Audit analysis of HKDI records

Remarks: 1. The programme completion rate is the percentage of students who have fulfilled all the graduation requirements of a programme, and is calculated as follows:

$$\frac{\text{Number of students awarded with HD in an intake year}}{\text{Total number of students enrolled in an intake year}} \times 100\%$$

2. The programme completion rates of 2013/14 and 2014/15 were not the final figures as students were allowed to complete the programme within the maximum period of five academic years. Therefore, the completion rates for 2013/14 and 2014/15 may increase in the next few years.

**Employment rate of graduates
(2014 to 2016)**

Academic department	2014 Graduates (%)	2015 Graduates (%)	2016 Graduates (%)
DFS	73 %	67 %	75 %
CDM – average – individual programmes	87 % ranged from 78 % to 96 %	85 % ranged from 77 % to 89 %	88 % ranged from 78 % to 95 %
FID – average – individual programmes	74 % ranged from 61 % to 84 %	85 % ranged from 75 % to 90 %	84 % ranged from 80 % to 90 %
PID – average – individual programmes	91 % ranged from 83 % to 100 %	82 % ranged from 70 % to 100 %	86 % ranged from 82 % to 100 %
Overall – average – individual programmes	84 % ranged from 61 % to 100 %	84 % ranged from 67 % to 100 %	86 % ranged from 75 % to 100 %

Source: Audit analysis of HKDI records

Remarks: The employment rate was calculated by dividing the number of graduates who were employed by the sum of the number of graduates who were employed and the number of graduates who were seeking employment.

Terms of Reference of the VTC Standing Committee

- (a) To discharge the functions of the Council and to act on its behalf on all matters requiring policy and executive decisions when the Council is not in session, except those items reserved for the full Council.
- (b) To report to the Council at its next regular meeting on all the decisions taken by the Standing Committee.
- (c) To give initial consideration to any strategic planning and development of the Council, formulation of proposals, review of major policies and making recommendations to the Council.
- (d) To keep under review, on behalf of the Council, the conduct of Council business.
- (e) To advise the Council on any matters referred to it by the Council or any committees or boards of the Council.
- (f) To approve new or revised fees and charges with an estimated annual income up to \$50,000,000.
- (g) To approve tenders and to appoint consultants at value up to \$50,000,000.
- (h) To accept donations.
- (i) To accept grants for specific educational and training projects.
- (j) To approve the creation of and appointments to directorate ranks/posts below A3 pay point, including extension of service beyond the normal retirement age.
- (k) To determine disciplinary penalties to be imposed on directorate staff below A3 pay point and to approve removal of such staff.
- (l) To decide on appeal against disciplinary actions from staff on or above pay point B34.

The members of the VTC Standing Committee are appointed by the VTC Council. The Committee comprises up to ten VTC Council members (including the Council Chairman, Deputy Council Chairmen, the Executive Director of the VTC, Chairmen of the functional committees set up under the Council and other Council members) and one elected staff member of the VTC. Not more than three external members may be co-opted as Advisors to the Committee as and when required.

Source: VTC records

Terms of Reference of the VTC Estates Committee

- (a) To formulate policy proposals on the Council's premises and related capital projects for the consideration of the Council and the Standing Committee.
- (b) To advise the Council and the Standing Committee on all matters relating to the purchase, lease, erection, alteration and maintenance of buildings and to the acquisition of land for building new campuses and centres.
- (c) To advise the Council and the Standing Committee on the administration of contracts for building projects including the appointment of architectural and engineering consultants at costs with the financial limits prescribed in the Financial Rules (up to \$10,000,000).
- (d) To examine and approve sketch designs and estimates of building costs.
- (e) To award works tenders within the financial limit prescribed in the Financial Rules (value up to \$10,000,000, but unanimous agreement of members of the Committee is required for tenders of an amount over \$2,000,000).
- (f) To examine works tenders for submission to the Standing Committee or the Council for approval.
- (g) To set up any sub-committees it considers necessary.

The members of the VTC Estates Committee are appointed by the VTC Council. The Committee comprises six to ten members, at least two-thirds of which must be VTC Council members. Membership includes the Director of Architectural Services of the Government or his/her representative, and one elected staff member of the VTC.

Source: VTC records

**Terms of Reference of the Steering Committee
for the TKL Campus development project**

- (a) To steer and oversee the design and construction of the new campuses for the HKDI and IVE(LWL).
- (b) To advise on design optimisation and cost containment options.
- (c) To monitor progress and oversee timely project delivery.
- (d) To monitor project budget management and devise contingency plan for over budget of construction costs.
- (e) To advise on any other issues that may arise in the course of the construction project.
- (f) To report regularly to the VTC Estates Committee.

The Steering Committee was set up under the Estates Committee to steer, oversee and monitor the progress of the project. The membership of the Committee comprised a member of the VTC Estates Committee, an external member, the Executive Director of the VTC and five staff members of the VTC.

Source: VTC records

Appendix K

Acronyms and abbreviations

ArchSD	Architectural Services Department
Audit	Audit Commission
BD	Buildings Department
CCG	Client Consultants Group
CDM	Communication Design and Digital Media
CEC	Campus Executive Committee
CENO	Corporate Environmental Office
CSP	Computer service provider
DEAC	Design Discipline Academic Committee
DEDAB	Design Discipline Advisory Board
DEQAC	Design Discipline Quality Assurance Committee
DFS	Design Foundation Studies
DIAB	Design Institute Advisory Board
EDB	Education Bureau
EVA	Emergency vehicle access
FC	Finance Committee
FID	Fashion and Image Design
HD	Higher Diploma
HKDI	Hong Kong Design Institute
HRD	Human Resources Division
IA	Industrial attachment
IVE	Hong Kong Institute of Vocational Education
IVE(LWL)	Hong Kong Institute of Vocational Education (Lee Wai Lee)
LegCo	Legislative Council
MAA	Memorandum of Administrative Arrangement
m ²	Square metres
PID	Product and Interior Design
RC	Reinforced concrete
TKL Campus	Tiu Keng Leng Campus
VETAB	Vocational Education and Training Academic Board
VTC	Vocational Training Council

CHAPTER 8

Financial Services and the Treasury Bureau Government Property Agency

Provision of government office accommodation and utilisation of government sites

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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PROVISION OF GOVERNMENT OFFICE ACCOMMODATION AND UTILISATION OF GOVERNMENT SITES

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PROVISION OF GOVERNMENT OFFICE ACCOMMODATION AND UTILISATION OF GOVERNMENT SITES

Executive Summary

1. Under the policy directive of the Financial Services and the Treasury Bureau (FSTB), the Government Property Agency (GPA) is responsible for providing administrative support services to all bureaux/departments (B/Ds) in respect of acquisition, allocation and management of government-owned and leased office accommodation. Its functions also include optimising the development potential of government sites through reviewing existing uses. As of December 2016, there was office accommodation of 1,023,110 square metres (m²) under the purview of the GPA, including government owned office accommodation of 715,059 m² in joint-user general office buildings (JUBs) and private developments, and leased office accommodation of 308,051 m². In addition, specialist and departmental buildings (SDBs) of 7,348,976 m² were purposely built for performing specialised functions and/or office use by one or more B/Ds and managed by the concerned B/Ds in accordance with the Accommodation Regulations promulgated by the FSTB. In 2016-17, the GPA incurred \$785.7 million under two programme areas, viz. “Acquisition and allocation” and “Estate utilisation”. Rental expenditure incurred by the GPA and relevant B/Ds on leased office accommodation was \$960 million. The Audit Commission (Audit) has recently conducted a review focusing on the GPA’s work on the provision of government office accommodation and utilisation of government sites with a view to identifying areas for improvement.

Provision of government-owned office accommodation

2. *Need to plan for more JUBs.* Government office accommodation may be provided by construction of government buildings through the Public Works Programme, direct purchase of office premises, provision in private developments under lease, or leasing in the private property market. The Government’s accommodation policy is to house offices in owned buildings as far as practicable because it is more cost-effective than leasing and has security of tenure. According to the Controlling Officer’s Reports of the GPA, the leased accommodation increased by 13% from 271,461 m² in 2006 to 308,051 m² in 2016 while the government-owned office accommodation under the GPA’s purview decreased by 0.4% from 717,679 m²

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to 715,059 m² over the same period mainly due to the decrease in the number of JUBs from 50 to 46. The affected offices of the demolished JUBs had been relocated to new SDBs or leased accommodation. Based on the 2016 returns on the annual review of office accommodation submitted by B/Ds, there were 168 requests for new office space of 94,921 m² from 2017-18 to 2021-22. While office space of 50,462 m² could be met by the release of projected surplus office space, there would still be a shortfall of 44,459 m². According to the GPA's assessment of the requests, there might be a need for a site search for a total office space of 29,591 m². However, no JUBs had been planned other than the three JUBs currently under planning/construction which would be mainly used for reprovisioning the government offices at Wan Chai Government Offices Compound (WCGOC — see para. 3 below). The GPA needs to take measures, including planning for more JUBs, to meet the additional office accommodation needs of B/Ds (paras. 2.2 and 2.4 to 2.8).

3. *Need to monitor progress of reprovisioning WCGOC offices.* As announced in the 2008-09 Budget Speech, the relocation of government offices at the WCGOC (currently providing a total floor area of 175,000 m² for about 10,000 staff of 28 B/Ds and the Judiciary) would release space in the Central Business District (CBD) to meet the demand for Grade A offices. The relocation requires the construction of nine replacement buildings. To facilitate monitoring of the relocation exercise, the FSTB has since September 2014 provided quarterly progress reports to the Financial Secretary's Office. According to the progress report of March 2017, the relocation of the WCGOC as a whole was estimated to be completed in 2025-26 the earliest. Comparing the tentative construction programmes of the replacement building projects as reported in September 2014 with those in March 2017, six projects had encountered delays mainly because of the changes in project scope to meet local needs, technical constraints and the time taken for seeking funding approval. Furthermore, the relocation of the Wan Chai Law Courts was still under planning without a projected completion date. The FSTB, in collaboration with the GPA and the Architectural Services Department (ArchSD), needs to closely monitor the implementation of the nine replacement building projects to ensure their timely completion (paras. 2.11, 2.15 and 2.16).

4. *Long time taken in implementing the West Kowloon Government Offices (WKGO) project.* Among the nine replacement building projects, the WKGO in Yau Ma Tei was an on-going project before the announcement of the WCGOC relocation plan in 2008. In 2002, the WKGO was planned for reprovisioning four government buildings in Yau Ma Tei affected by the Highways Department (HyD)'s Central Kowloon Route (CKR) project, and for de-leasing leased office

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accommodation in various areas. Following the HyD's decision in December 2006 to review the CKR alignment options, the WKGO project was suspended. With the revision of the design of the CKR in January 2008 and June 2010, the demolition of two of the four government buildings would not be required under the CKR project and the earmarked office space in the WKGO could be allocated for reprovisioning offices from the WCGOC. After obtaining funding approval of \$4,742.5 million from the Finance Committee of the Legislative Council, the WKGO contract was awarded in July 2015 for completion in early 2019. Audit examination of the long time taken in implementing the WKGO project revealed the following lessons to be learnt (paras. 2.18 to 2.20, 2.22 and 2.23):

- (a) ***Need to consider advancing part of the WKGO project for deleasing purpose.*** In December 2006, noting that the CKR consultancy study would review the need for reprovisioning the four government buildings, the ArchSD informed the GPA that it was not possible to proceed with the WKGO project as planned. However, a significant part (44% in terms of area) of the WKGO was intended for providing new accommodation and facilitating deleasing leased accommodation in various areas. It was not contingent on the CKR project and could proceed on its own. A phased construction approach for the WKGO was considered physically viable in August 2005. While such phased construction approach would have higher cost implication, the earlier provision of new offices for deleasing purpose could bring about rental saving. However, there was no record to show that the GPA had conducted a cost-benefit analysis for implementing the WKGO project by phases before deciding to defer the whole project in 2006 pending the outcome of the CKR consultancy study. In the event, the reprovisioning requirement of the CKR project was only finalised in 2010 (3.5 years later) and the consequential change in users of the planned accommodation for reprovisioning purpose caused a further delay of over one year in the scheduled implementation date of the WKGO project. Meanwhile, the estimated construction cost had also increased by 170% from \$1,557 million in July 2005 to \$4,199 million in 2011. In any event, a phased approach was adopted in 2010 to address the problem of late possession of some site area for a railway project (paras. 2.20(a) and 2.23(a)); and
- (b) ***Need to conduct public consultation at an early stage.*** According to the Project Administration Handbook issued by the ArchSD, after completing the technical feasibility study, a project team should allow adequate time for public consultations in preparing the outline plan based on the approved

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technical feasibility study, including coordination with and supporting its client to conduct public consultations at an early stage if required, and facilitate resolving public objection in a timely manner. The WKGO project was planned for implementation as a design-and-build project and was ready for conducting public consultation in August 2011 after the ArchSD had completed the revised technical feasibility study report. However, the GPA only commenced public consultation in April 2013 and obtained the support of the District Council in December 2013 after further consultation was conducted to address local concern (para. 2.23(b)).

5. ***Long time taken in identifying sites for reprovisioning two users of the WCGOC.*** Since 2008, the Planning Department (PlanD) had made efforts in identifying suitable sites for reprovisioning the WCGOC offices and the GPA had carried out matching exercises with the affected users for the identified sites. Among the 28 affected B/Ds and the Judiciary, the identification of reprovisioning sites for the Drainage Services Department (DSD) offices and the Wan Chai Law Courts had taken the longest time to finalise, i.e. in 2014 and 2016 respectively. Audit examination of the two cases revealed lessons to be learnt (para. 2.24):

- (a) ***Need to explore sites with residual development potential.*** Since 2008, the GPA had discussed with the DSD on relocating the DSD offices to various locations. In 2014, the DSD proposed to build an SDB at one of its sewage pumping station sites which was found to be technically feasible in 2015 for meeting its reprovisioning needs and maximising the site utilisation. When planning for the reprovisioning of a government-office building in future, the GPA needs to make reference to this good example and request all affected users to review whether their accommodation requirements can be met by making use of the residual development potential of an existing occupied site (Case 1 in para. 2.24); and
- (b) ***Need to consult users on key planning assumptions/parameters in estimating achievable floor area.*** While the GPA assisted the Judiciary in identifying the ex-Western Police Married Quarters site in Sai Ying Pun for relocating the Wan Chai Law Courts as early as 2008, it was only in 2012 that the GPA's estimation of the achievable gross floor area from the site based on the existing 4.5-metre (m) floor height of the Wan Chai Law Courts was found to be different from that under the prevailing law court design standard of a 7-m floor height. The site coverage was also found to be less than the assumed 100%. In the event, the proposed Sai Ying Pun

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site was considered not feasible for the reprovisioning of the Wan Chai Law Courts and another site search had to be conducted. In Audit's view, when assisting users in identifying reprovisioning sites for their offices in future, the GPA needs to consult the users and the works departments at an early stage the planning assumptions/parameters used for estimating the achievable gross floor area/net operational floor area to ensure that any proposed sites can fully meet the accommodation and operational needs of the users concerned (Case 2 in para. 2.24).

Administration of leased government offices

6. According to the GPA Manual, the objectives of leasing office accommodation are to meet short-term, urgent, location-tied accommodation needs or specific operational requirements. In selecting premises to be leased, priority should be given to suitable premises with low-rental implication (paras. 1.9 and 3.2(a)).

7. *Leases with high rental values.* In a comparison of the rentals of 170 leases with the average monthly rents of private office premises of the relevant districts/office grading/lease periods compiled by the Rating and Valuation Department (RVD), Audit found that 60 (35.3%) leases exceeded the average rents. As the RVD's average rents were for general reference only, Audit selected 3 of 6 leases which exceeded the RVD's average rents by more than 40% to examine the specific circumstances under which these leases (Leases A, B and C) were entered into or renewed (para. 3.4):

- (a) *Reasons for rejecting/not recommending leasing offers not documented for Leases A and B.* In March 2014, the Labour and Welfare Bureau (LWB) informed the GPA that a new office of about 4,800 m² for about 500 staff preferably in East Kowloon would be required in July 2014 for administering a new social welfare scheme. With the assistance of estate agents, the GPA in April 2014 identified two potential office premises for the LWB's consideration. The LWB selected the premises with a lower rental in Kwun Tong for which the GPA entered into five leases with the landlord (including Leases A and B) in February 2015 after the LWB had obtained funding approval for the new scheme. Audit noted that the estate agents had also identified seven other office premises of comparable/lower rent in three districts including Kwun Tong for the GPA's consideration but there was no documentation of the reasons for rejecting/not recommending

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these offers to the LWB for its consideration, contrary to the GPA's record-keeping requirement (para. 3.5); and

- (b) ***Alternative premises with lower-rental implication not explored before exercising option for renewal under Lease C.*** The office accommodation of 1,099 m² at a Grade B office building in Kwun Tong under Lease C had been used by the Civil Engineering and Development Department (CEDD) since 2003. The lease was renewed for a 3-year term for four times from July 2006 to July 2015 pending relocation to the WKGO. Audit found that the monthly rent of Lease C had increased significantly since 2006 to a level comparable to the RVD's average monthly rents of Grade B offices in Tsim Sha Tsui (a CBD) and Yau Ma Tei/Mong Kok, and higher than those of Kowloon Bay/Kwun Tong. Audit found that before the lease renewal in July 2009, the fitting-out cost of the CEDD's office had been fully amortised after six years of leasing. There was no record to show that the GPA had explored other alternative premises with lower-rental implication before informing the landlord in January 2009 of its intention to renew Lease C in July 2009 at a rent to be agreed. According to the GPA's valuation report prepared in May 2009 for rental negotiation with the landlord, the monthly rent of the GPA's leased office accommodation of 4,533 m² at a nearby new Grade A office building in January 2009 was \$157.5 per m², which was 43% lower than the then monthly rent of \$275 per m² under Lease C. However, there were no documented reasons for not considering this nearby lower-rental accommodation before renewing Lease C in July 2009 at a monthly rent of \$293 per m² (paras. 3.2 and 3.6).

8. ***Need to improve deleasing arrangements of leased accommodation.*** In line with the Government's accommodation policy of housing offices in owned buildings, it is an ongoing effort of the GPA to relocate B/Ds from leased accommodation through deleasing when opportunities arise. Audit selected two planned deleasing cases for examination and found room for improvement (paras. 1.11 and 3.11):

- (a) ***Planned deleasing not realised under Lease D.*** Leased accommodation of 5,243 m² on four floors of a Grade A office building in Kowloon Bay under Lease D had been used by four sections of the Social Welfare Department (SWD) since December 2003. In 2006, the GPA invited the SWD to relocate the four sections to a new JUB (scheduled for completion in 2015)

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but confirmed in 2008 that only three sections (except the Central Casefile Depository (CCD)) could be relocated. In 2012 and 2013, the SWD proposed to the GPA the relocation of the CCD (without specific location requirement) to lower-cost accommodation in view of the continued increase of case files. The GPA rejected the SWD's proposal as the rent for the Kowloon Bay office was considered low. After the relocation of the three SWD sections in mid-2015, the Kowloon Bay office was taken up by the CCD (76%) and two other SWD sections (24%). Lease D was renewed (at a monthly rent of \$265 per m²) in December 2015. Audit noted from the GPA's records that there was leased accommodation used by other B/Ds for storage purposes at lower monthly rents, ranging from \$94 to \$147 per m². The GPA needs to meet the non-location-tied storage requirements of B/Ds in a more cost-effective manner (paras. 3.12 to 3.14); and

- (b) *Two leased premises left vacant under Leases E and F.* In 2013, two sections of the Labour Department (LD) occupying areas of 344 m² and 159 m² in an office building in Quarry Bay under Leases E and F respectively were included in a relocation plan to a government-owned property in the first quarter of 2017. In 2014 and 2015, Leases E and F were renewed for a three-year fixed term (up to November 2017 and May 2018 respectively) as the GPA's effort to negotiate for a break clause was not successful. Audit noted that the leased premises had been left vacant after relocation of the LD's sections in March 2017. While the removal schedule was confirmed in October 2016, the GPA only invited B/Ds to bid for the vacant office under Lease E in May 2017. No B/Ds showed interest because of the short period of use at such short notice. For the vacant office under Lease F, the LD informed the GPA in October 2016 that it would be used by another section. However, Audit site inspections revealed that the office was still vacant up to late August 2017 (paras. 3.15 and 3.16).

Utilisation of government sites

9. *Identification of under-utilised government sites for optimal development.* According to the Government's land policy, government sites must be developed to the fullest extent possible or put to the best use. In November 2010, the Government adopted a targeted approach to identify government sites that were under-utilised, involving the GPA and the PlanD in conducting site-utilisation reviews and planning

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assessments respectively. Any redevelopment proposals for the identified sites will be submitted to an inter-B/D Property Strategy Group (PSG) for endorsement and monitoring the progress (paras. 1.13 and 4.2 to 4.4).

10. ***Need to document the justifications for site selection.*** After the 2016 site-utilisation reviews, the GPA referred 28 sites to the PlanD for planning assessment in July 2016. Having regard to the planning assessment results, the GPA shortlisted 15 sites for examination and eventually selected 4 priority sites for further action in September 2017 without documenting the justifications. The GPA needs to document the justifications on selecting sites for site-utilisation reviews (paras. 4.11 to 4.13).

11. ***Need to set priority in selecting sites for site-utilisation reviews.*** As of August 2017, there were 1,569 sites pending site-utilisation reviews by the GPA. Given that only 85 sites were selected for review each year, it would take a long time to complete the reviews. The GPA needs to set priority in selecting sites with better development potential for review and follow-up action (para. 4.14).

12. ***Need to identify a project proponent to take forward a redevelopment proposal.*** Of 18 under-utilised government sites identified by the GPA's site-utilisation reviews from 2011 to 2015, 14 were endorsed for redevelopment by the PSG. As of June 2017, one of the 14 sites had been released for redevelopment, 11 were under planning and 2 were accorded low priority. In a case study of one of the 11 sites under planning, Audit found that an ex-laboratory (with a floor area of 2,500 m²) currently used by the Leisure and Cultural Services Department (LCSD) for storage of its museum collections could be redeveloped to provide a floor area of 18,300 m² for both the LCSD and other B/Ds. However, as of September 2017, two years after the PSG's endorsement of the redevelopment of the ex-laboratory in 2015, a project proponent had not yet been determined to take forward the project. The redevelopment proposal also hinged on the identification of a reprovisioning site for the museum collections in the interim. The GPA needs to seek the steer of the PSG in identifying a project proponent and expedite action in assisting the LCSD in identifying a reprovisioning site (paras. 4.8 and 4.9).

13. ***No decision taken in implementing a proposed road project after land acquisition in 1990.*** As of June 2017, the PSG also monitored 11 potential sites brought up by the Committee on Planning and Land Development and PSG members.

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In a case study of one of the 11 sites, Audit found that a four-storey godown acquired by the Government in 1990 had been left vacant since 2008. According to the 1983 transport study, the preferred option of a proposed circumferential road in Kwai Chung would require resumption of the godown site. In 1987, the godown owner objected to the proposed road project and indicated that he planned to redevelop the site. In 1990, the Government acquired the godown site through a land exchange with the godown owner. From 1991 to 2007, the GPA leased out the godown as there was no plan for the road project. However, it was too dilapidated thereafter for short-term uses and had been left vacant for some 10 years up to August 2017. It is unsatisfactory that some 26 years after acquiring the godown in 1990, no decision had been taken on whether the proposed road project would be implemented. According to the GPA, the site was under-utilised as the maximum plot ratio could be revised from 3 to 9.5 should the site be rezoned to “Industrial” use. The Transport and Housing Bureau needs to task the Transport Department to review whether there is still a need from the transport planning perspective to implement the road project and if not, release the site for other uses as soon as possible (para. 4.10).

14. ***Omissions and discrepancies in Government Property Information System (GPIS) records.*** In 2000, the GPA developed a computerised database of government sites which was revamped into the GPIS in 2013. While the GPIS is instrumental in identifying under-utilised sites, Audit sample check revealed that there were omissions and discrepancies. For example, the pertinent site and building records of an unusable property and the site information of eight premises/buildings were missing, and the status of some government sites was not up-to-date. The GPA needs to take measures to ensure that information recorded in the GPIS is accurate and up-to-date (paras. 4.15 and 4.16).

15. ***Vacant or under-utilised specialist and departmental accommodation.*** The GPA regularly reports to the PSG on a half-yearly basis the position of vacant or under-utilised premises of specialist and departmental accommodation under the purview of individual B/Ds (which were surplus to their requirements). According to the GPA’s progress report of April 2017, as of February 2017, there were 27 such vacant or under-utilised premises of specialist and departmental accommodation, comprising one ex-secondary school with a floor area of 6,852 m² and 26 buildings (mostly vacant staff quarters in remote locations) each having a floor area of less than 500 m² (para. 4.23).

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Audit recommendations

16. Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Government should:

- (a) take measures, including planning for more JUBs, to meet the additional office accommodation needs of B/Ds (para. 2.9);
- (b) closely monitor the implementation of the nine replacement building projects for the relocation of the WCGOC to ensure their timely completion (para. 2.25);
- (c) in implementing a JUB project in future, when there is new development affecting the progress of certain separable parts of the project, conduct a cost-benefit analysis to evaluate the possible options for taking forward the project (para. 2.26(a)(i));
- (d) in planning for the reprovisioning of a government-office building in future, critically review whether the users' accommodation requirements can be met within their existing accommodation stock (para. 2.26(b)(i));
- (e) document the reasons for rejecting/not recommending offers in the selection of premises for leasing office accommodation (para. 3.17(a)(i));
- (f) explore suitable alternative premises with lower-rental implication before exercising option for lease renewal, and document the reasons for the decision taken in this regard (para. 3.17(a)(ii));
- (g) meet the non-location-tied storage requirements of B/Ds in a more cost-effective manner (para. 3.17(b));
- (h) improve the planning for the relocation of offices from leased accommodation (para. 3.17(c));
- (i) maintain records of justifications for selecting government sites for site-utilisation review (para. 4.17(b));

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- (j) **take measures to ensure that information recorded in the GPIS is accurate and up-to-date (para. 4.17(d)); and**
- (k) **remind relevant B/Ds to explore other measures to put the 27 vacant or under-utilised premises of specialist and departmental accommodation into gainful use in accordance with the requirements of the Accommodation Regulations (para. 4.27(a)).**

Response from the Government

17. The Government generally agrees with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 The Financial Services and the Treasury Bureau (FSTB) has policy responsibility for government accommodation matters and is the authority for the issue and amendment of the Accommodation Regulations. Under the policy directive of the FSTB, the Government Property Agency (GPA — Note 1) is responsible for providing administrative support services to all bureaux/departments (B/Ds) in respect of acquisition, allocation and management of government-owned and leased office accommodation. Headed by the Government Property Administrator, the GPA's main functions include:

- (a) meeting government accommodation needs for offices through construction, purchase or leasing;
- (b) allocating appropriate accommodation to users and setting space and furniture standards; and
- (c) optimising the development potential of government sites through reviewing existing uses and encouraging joint user development.

1.3 The GPA's operational functions are carried out by five functional divisions. The Acquisition, Allocation and Disposal Division (ADD) is responsible for the acquisition of office accommodation through construction, purchase or leasing; allocation of such accommodation for the use of B/Ds; and de-leasing of leased accommodation. The Site Utilisation Division (SUD) is responsible for examining all matters relating to optimising the utilisation of land resources designated for

Note 1: *In April 1990, the GPA was established to take over the responsibility for dealing with various aspects of government property matters from the Government Secretariat, the then Buildings and Lands Department, and the Rating and Valuation Department.*

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government, institution or community (G/IC) purposes, and letting out of surplus government accommodation. An organisation chart of the GPA is at Appendix A.

1.4 According to its Controlling Officer's Report, the GPA spent a total of \$785.7 million in 2016-17 under the two programme areas, namely "Acquisition and allocation" and "Estate utilisation" (Note 2). As of March 2017, 163 staff were involved in the work under the two programme areas.

Provision of government office accommodation

1.5 According to the Accommodation Regulations, one of the GPA's objectives is to keep an overview of the Government's short-term and long-term office accommodation needs, and meet these needs in an economical and cost-effective manner, typically in government-owned premises supplemented when necessary by leased accommodation. When there is a shortage of office accommodation, the pertinent B/Ds may apply for allocation of accommodation and submit a schedule of accommodation stating their requirements to the GPA for vetting and follow-up action. If a request for additional office accommodation cannot be met by allocation of existing stock of accommodation, it may be provided by one of the following alternatives, subject to the availability of funds:

- (a) ***Construction through the Public Works Programme (PWP).*** For joint-user general office buildings (JUBs), the GPA will assume a coordinating role in seeking funds for the construction of the buildings and allocating the space therein to the user departments. For specialist and departmental buildings (SDBs — Note 3), the proponent/user

Note 2: *The "Estate utilisation" programme covers both the site utilisation and the disposal of surplus quarters. This audit review does not cover the disposal of staff quarters which was covered in a review of "Management of surplus quarters" and the results of which were reported in Chapter 1 of the Director of Audit's Report No. 62 of April 2014.*

Note 3: *SDBs are buildings (e.g. standalone departmental headquarters buildings, law courts, police stations, libraries, museums, clinics, town halls and community centres) and structures (e.g. sewage treatment plants) used to meet the policy objectives and/or operational needs of pertinent B/Ds. While they are generally occupied by a single department for performing specialised functions and/or office use, they may sometimes accommodate more than one department (e.g. the Central Government Offices) and in that event are referred to as multi-user SDBs.*

department/leading department (in the case of a multi-user SDB) is responsible for seeking funds to obtain the accommodation required as well as recurrent and other costs for operating and maintaining the new facilities. A proponent/user department should justify the location, floor space and operational requirements of an SDB (Note 4);

- (b) ***Direct purchase.*** Office accommodation may be acquired from private developments to meet urgent and permanent accommodation needs, where government-owned accommodation cannot cater for such needs and where leasing or construction are not viable alternatives. The proponent/user department is responsible for seeking funding approval through the PWP procedures for the purchase;
- (c) ***Provision through lease conditions in private developments.*** G/IC facilities (e.g. social welfare facilities and government offices) may be provided in private developments under lease conditions imposed by the Lands Department (LandsD) in land sale, land grant or exchange, or by the Planning Department (PlanD) in approved planning brief to meet the needs of government departments; and
- (d) ***Leasing.*** Premises may be leased from the Housing Authority or from the private sector to meet the accommodation needs of government users, which are either short-term, urgent or location-tied, or where owned accommodation is not available or where purchase and construction are less technically or economically feasible alternatives.

1.6 As of December 2016, there were 1,023,110 square metres (m²) of office accommodation under the purview of the GPA, including government-owned office accommodation of 715,059 m² in JUBs and private developments, and leased office accommodation of 308,051 m². In addition, SDBs of 7,348,976 m² were purposely built for performing specialised functions and/or office use by one or more B/Ds and managed by the concerned B/Ds (see Note 3 to para. 1.5(a)). Figure 1 shows the different types of government accommodation for meeting B/Ds' office and operational needs. In 2016-17, the rental expenditure of leased office accommodation

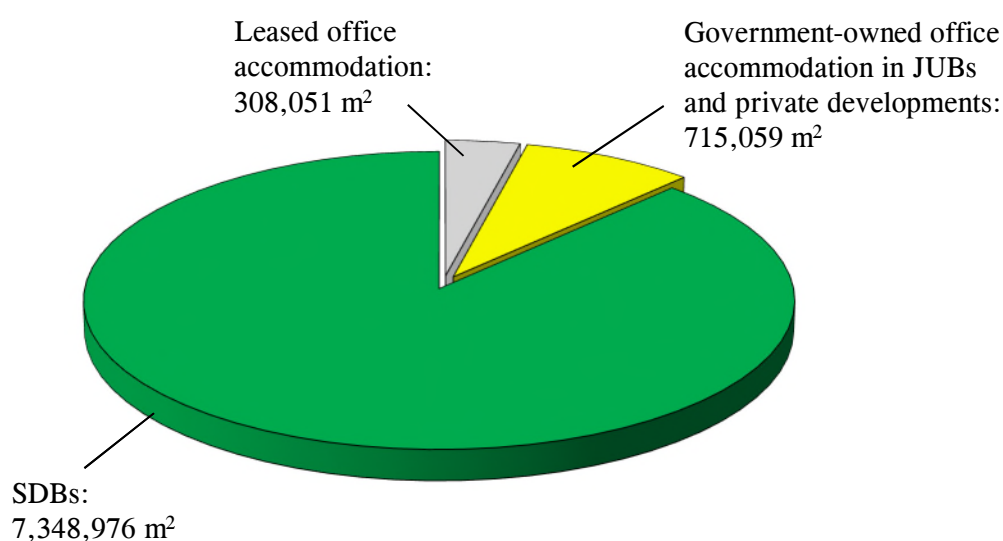
Note 4: *The schedule of accommodation for an SDB is vetted by the Property Vetting Committee which is chaired by an Assistant Director of the Architectural Services Department and comprises representatives of the FSTB and the GPA as members.*

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was \$960 million (see Note 19 to para. 3.2(a)). This review mainly focused on government office accommodation managed by the GPA.

Figure 1

**Types of government accommodation
for meeting B/Ds' office and operational needs
(2016)**



Source: Audit analysis of GPA records

Remarks: The GPA does not maintain records of office areas in an SDB. Based on the relevant B/Ds' classification on the use of their SDBs, some 872,600 m² of the SDBs were designated for office use as of April 2017.

1.7 Annual review and forecast. According to the Accommodation Regulations, B/Ds should see if there is a continued need for all the office accommodation in government-owned and leased accommodation allocated to them once a year. They are required to explore and exhaust all space-saving opportunities through internal rationalisation of space before putting forward a request for additional office accommodation. Based on the annual review of office accommodation (AROA), B/Ds should provide a return on any request for additional office accommodation and surplus accommodation (excluding SDBs which should be

reported separately in the annual stewardship statement exercise — Note 5). Under the AROA exercise, B/Ds are only required to report surplus accommodation exceeding 50 m², which may need to be surrendered to the GPA, and are encouraged to submit proposals on the rationalisation of accommodation or co-location, where feasible, to achieve savings. The GPA will then coordinate and compile annual forecasts on departmental requirements for additional office accommodation for planning purposes. According to the Accommodation Regulations, when government accommodation becomes surplus to requirement and cannot be put to alternative long-term use within the Government, the B/Ds concerned should consider other appropriate means of putting the surplus government accommodation to gainful use, including interim alternative use within the Government, commercialisation and direct leasing. The GPA will try to identify alternative government users. Based on the GPA's work report of 2016, the occupancy rate of office accommodation had been maintained at 99.9%.

1.8 Apart from meeting additional office accommodation demand, the provision of new government-owned premises is necessary from time to time in order to achieve the following government policy initiatives:

- (a) ***Relocation out of high-value areas.*** In 1994, the then Finance Bureau issued a memorandum on the location of general office accommodation specifying the Government's policy to decentralise general office space (i.e. those without specific location requirements) out of high-value areas of Hong Kong Island and Kowloon, and to move the offices to lower-value areas which were well served by public transport. When relocation of government offices was contemplated, various factors such as the operational needs of B/Ds, impact on the delivery of public services and cost-effectiveness would be considered;

Note 5: *The purpose of the exercise is to report, among others, non-financial information (in terms of areas) of government-owned buildings employed by B/Ds for the delivery of public services as at the end of a financial year, which is published together with the Government's annual accrual-based accounts. B/Ds are required to confirm to the Treasury the asset inventory under their control and separately inform the GPA of any surplus SDB accommodation.*

- (b) ***Releasing space in Central Business Districts (CBDs — Note 6) for developing Grade A offices.*** In his 2008-09 Budget Speech, the Financial Secretary said that according to the “Hong Kong 2030: Planning Vision and Strategy” published by the Development Bureau (DEVB) and the PlanD in 2007, the Government should identify more sites for developing Grade A offices (Note 7) in CBDs in order to keep the economy growing. The Government would study the relocation of three government office buildings (i.e. Wan Chai Tower, Immigration Tower and Revenue Tower) at the Wan Chai waterfront (hereinafter referred to as the Wan Chai Government Offices Compound — WCGOC) to other districts so as to release land in the CBD. The WCGOC with a total floor area of 175,000 m² has provided accommodation for about 10,000 staff of 28 B/Ds and the Judiciary. According to the consultancy study entitled “Review of Land Requirement for Grade A Offices, Business and Industrial Uses” completed in 2017 as input to the on-going “Hong Kong 2030+: Towards a Planning Vision and Strategy Transcending 2030” Study, it was estimated that there was a shortfall of about 140,000 m² (in gross floor area (GFA — Note 8)) of CBD Grade A offices in 2013 and the shortfall would increase to 1.06 million m² in GFA in 2041. In July 2017, the Secretary for Development said that the Government would continue to pursue the strategic planning proposals, including the relocation of government office buildings or government offices taking up private office spaces with no requirements for a CBD location so as to free up spaces in the CBDs for private office use; and

Note 6: *For the purpose of the “Hong Kong 2030: Planning Vision and Strategy” published in 2007 by the Development Bureau and PlanD, CBD is defined as the business zones within Central, Wan Chai, Sheung Wan, Causeway Bay, Tsim Sha Tsui and the West Kowloon Reclamation.*

Note 7: *According to the Hong Kong Property Review published by the Rating and Valuation Department, a Grade A office building has the following features: modern with high quality finishes; flexible layout; large floor plates; spacious; well decorated lobbies and circulation areas; effective air-conditioning; good lift services for passengers; professional management and parking facilities normally available.*

Note 8: *GFA refers to the area contained within the external walls of the building measured at each floor level, together with the area of balcony and the thickness of the external walls of the building.*

- (c) ***Providing more facilities for convention and exhibition activities.*** In her Policy Address of October 2017, the Chief Executive of the Hong Kong Special Administrative Region announced that:
 - (i) the Government would demolish and redevelop the WCGOC next to the Hong Kong Convention and Exhibition Centre into a new wing that could be connected to and integrated with the existing Centre; and
 - (ii) hotel facilities, which would complement the convention and exhibition activities, and Grade A office space, which could help alleviate the market shortfall, could be built on top of the new convention and exhibition venue.

Under the AROA (see para. 1.7), B/Ds are required to submit a return on accommodation in CBDs, in which B/Ds should report whether their offices in the CBDs can be relocated to other districts and provide justifications if their offices cannot be relocated outside the CBDs.

Leasing and deleasing of office accommodation

1.9 ***Leasing.*** According to the GPA Manual, the objectives of leasing office accommodation are to:

- (a) meet short-term, urgent, location-tied accommodation needs or specific operational requirements; and
- (b) endeavour to obtain the best overall deal (i.e. achieving the pledged rental level of 5% below the net effective market rent) in respect of the leased premises for the Government.

1.10 ***Selection of premises.*** After a decision is taken to lease from the private sector, the ADD:

- (a) conducts a site search and identifies the premises that meet user's requirements most cost-effectively;

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- (b) inspects and assesses suitability of the target premises and consults the client department and the Architectural Services Department (ArchSD);
- (c) makes a valuation of the premises to assess the reasonableness of the landlord's asking rent and to set a ceiling rent for negotiation, and scrutinises whether the offered service charges are acceptable; and
- (d) negotiates on the rental package, scrutinises and executes the tenancy agreement.

1.11 ***Deleasing.*** The Government's accommodation policy is to house offices in owned buildings and reduce reliance on leasing. According to the GPA, there is an ongoing effort to relocate B/Ds from leased accommodation to government-owned accommodation through deleasing when opportunities arise to reduce recurrent expenditure on commercial leasing.

Utilisation of government sites

1.12 In the 1997 Policy Address, the Government announced a new site utilisation initiative to:

- (a) provide a proactive and systematic approach to the planning of government buildings projects;
- (b) review the existing and planned use of government sites through the setting up of a comprehensive database;
- (c) support government departments in reviewing site requirements and coordinate joint users developments to optimise the use of sites; and
- (d) create a prioritised programme for releasing and redeveloping under-utilised government sites comprising a rolling programme to incorporate a number of new sites each year.

1.13 In 2000, the GPA set up a computerised database of G/IC sites, which was revamped into the Government Property Information System (GPIS) in 2013. In

2010, the Government adopted a targeted approach to identify government sites that were under-utilised, involving the GPA, the PlanD and the Property Strategy Group (PSG — Note 9) which were tasked with different roles. As of May 2017, of the 3,794 sites in the GPIS, 25 sites were under monitoring by the PSG.

Audit review

1.14 In 1997, the Audit Commission (Audit) conducted a review of “The provision of accommodation for government use”. The results were reported in Chapter 8 of the Director of Audit’s Report No. 29 of October 1997. In 2004 and 2008, Audit completed two other reviews, namely “Utilisation of government sites” and “Commercialisation and utilisation of government properties”, the results of which were reported in Chapters 10 and 2 of the Director of Audit’s Reports No. 42 of March 2004 and No. 50 of March 2008 respectively. In May 2017, Audit commenced a review of the GPA’s work on the provision of government office accommodation and utilisation of government sites. The review focuses on the following areas:

- (a) provision of government-owned office accommodation (PART 2);
- (b) administration of leased government offices (PART 3); and
- (c) utilisation of government sites (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

Note 9: *The PSG is chaired by the Permanent Secretary for Financial Services and the Treasury (Treasury). Its members comprise officers from the GPA, the DEVB, the FSTB, the Home Affairs Department, the ArchSD and the PlanD. Appendix B shows the terms of reference of the PSG.*

Acknowledgement

1.15 Audit would like to acknowledge with gratitude the assistance and full cooperation of the staff of the FSTB, the DEVB, the Transport and Housing Bureau, the GPA, the Judiciary, the ArchSD, the Census and Statistics Department (C&SD), the Civil Engineering and Development Department (CEDD), the Drainage Services Department (DSD), the Highways Department (HyD), the LandsD, the Leisure and Cultural Services Department (LCSD), the Labour Department (LD), the PlanD, the Registration and Electoral Office (REO), the Social Welfare Department (SWD), and the Transport Department (TD) during the course of the audit review.

PART 2: PROVISION OF GOVERNMENT-OWNED OFFICE ACCOMMODATION

2.1 This PART examines the provision of government-owned office accommodation, focusing on:

- (a) planning of joint-user general office buildings (paras. 2.2 to 2.10); and
- (b) reprovisioning of offices of the Wan Chai Government Offices Compound (paras. 2.11 to 2.29).

Planning of joint-user general office buildings

2.2 *Government's accommodation policy.* According to the FSTB, the Government's accommodation policy is to house offices in owned buildings as far as practicable. As mentioned in paragraph 1.5, government office accommodation may be provided by construction of government buildings through the PWP, direct purchase of office premises, provision in private developments under lease, or leasing in the private property market. The provision of government-owned office accommodation has a number of advantages over leasing:

- (a) it is more cost-effective;
- (b) it has security of tenure; and
- (c) it can better meet users' special requirements, especially those involving extensive and expensive fittings.

2.3 In line with the Government's accommodation policy, the GPA is responsible for meeting B/Ds' short-term and long-term office accommodation needs typically in government-owned accommodation (e.g. JUBs) supplemented where necessary by leased accommodation.

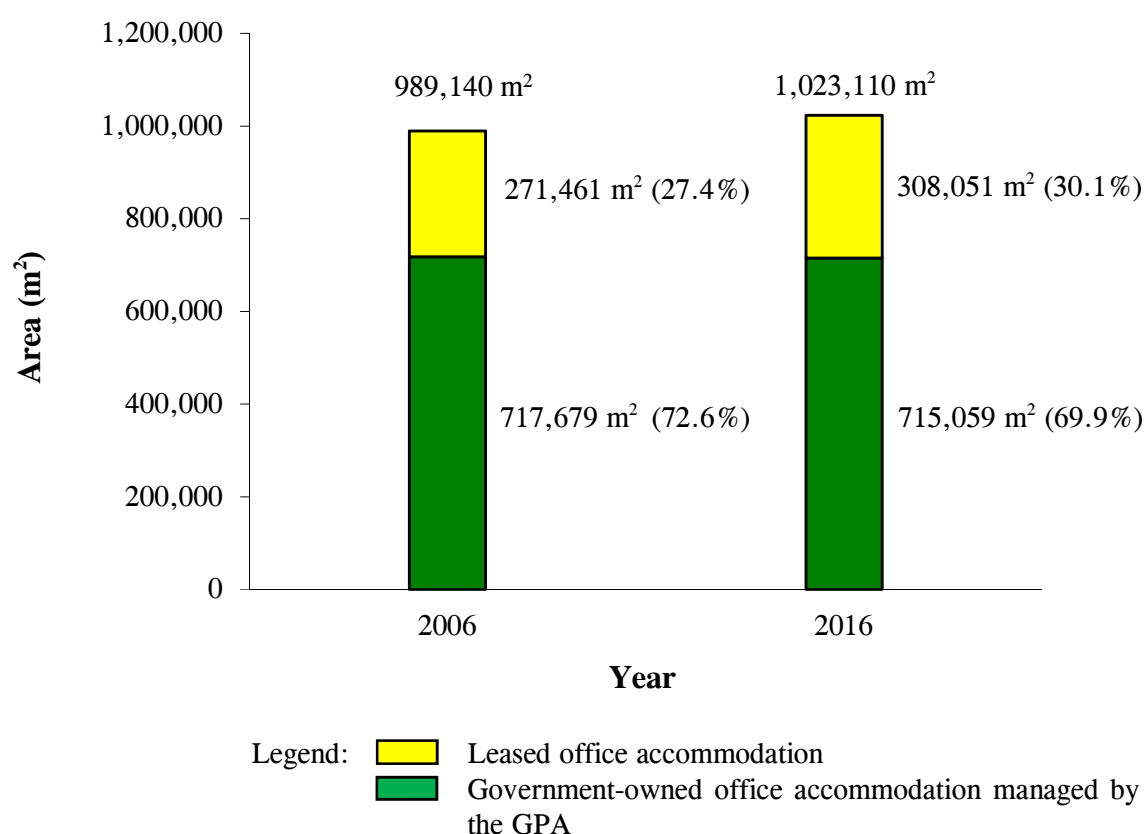
2.4 *Increase in leased office accommodation.* In the 1997 audit review (see para. 1.14), Audit expressed concern over the increase in leased office

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accommodation from 209,042 m² in 1993-94 by 28% to 268,000 m² in 1997-98 (i.e. an increase from 20% to 23% of the total office space). In response, the FSTB and the GPA said that it was the Government's policy to relocate users to government-owned premises whenever possible. However, over the years, the leased office accommodation continued to grow. According to the Controlling Officer's Reports of the GPA, the leased accommodation increased by 13% from 271,461 m² in 2006 to 308,051 m² in 2016 while the government-owned office accommodation under its purview decreased by 0.4% from 717,679 m² to 715,059 m² over the same period (Note 10). As a result, leased office accommodation accounted for 30.1% of the total office space in 2016, up from 27.4% in 2006 (see Figure 2).

Figure 2

**Increase in leased office area
among the office accommodation managed by the GPA
(2006 to 2016)**



Source: GPA records

Note 10: According to the GPA, the reported government-owned office accommodation excludes those SDBs occupied and directly managed by B/Ds.

2.5 Audit examination revealed that the decrease in government-owned office accommodation under the GPA's purview from 2006 to 2016 was mainly attributable to the decrease in the number of JUBs from 50 to 46 (Note 11) resulting in a reduction of office space of some 6,700 m². While the decrease was partly offset by additional office space of some 4,100 m² acquired by the GPA through purchase/exchange of properties in private developments and conversion of surplus government-owned accommodation (e.g. quarters/bungalows) for office/storage use, there was a net reduction of 2,600 (6,700 – 4,100) m². As for the increase in leased accommodation from 2006 to 2016, the GPA informed Audit in September 2017 that it was to meet additional space requirements arising from service expansion and new initiatives. The GPA expected that leased office accommodation would decrease with the completion of the planned JUBs.

Need to plan for more JUBs

2.6 Based on the 2016 AROA returns submitted to the GPA by B/Ds (see para. 1.7), Audit found that there were 168 requests for new office space of 94,921 m² for the five-year period from 2017-18 to 2021-22. While B/Ds' projected surplus office space (Note 12) of 50,462 m² could be released for meeting part of the new office space demand, there would still be a shortfall of 44,459 m².

2.7 Audit noted that in July 2017, the GPA informed the PlanD that:

- (a) having considered B/Ds' accommodation requests in hand in the short and medium terms (in 3 to 5 years) based on the AROA, there were no bids from B/Ds for a stand-alone site; and

Note 11: *From 2006 to 2016, four JUBs (i.e. the Canton Road Government Offices Building, the Middle Road Multi-storey Carpark Building, the ex-Government Flying Services Headquarters Building and the Kwun Tong District Branch Offices Building) were demolished and one JUB (i.e. Trade and Industry Department Tower) was sold while only one JUB (i.e. the Trade and Industry Tower) was built. The offices vacated from the demolished JUBs had been relocated to new SDBs (e.g. Customs Headquarters Building in North Point) or leased accommodation.*

Note 12: *According to the GPA's circular memorandum to B/Ds on the AROA return of October 2016, surplus office space should include accommodation in JUBs and leased premises which might be released, and demand for new office space included those with support from the pertinent policy bureaux.*

Provision of government-owned office accommodation

(b) B/Ds had been advised that no permanent government-owned premises would be available and they were requested to approach the PlanD for a site search for constructing SDBs to meet the long-term accommodation needs, where appropriate. In this connection, the GPA forwarded a list of 29 requests for a total office space of 29,591 m² (Note 13) which might require the PlanD's assistance for site search. According to the GPA, the 29 requests were shortlisted from the 168 requests in the 2016 AROA returns (see para. 2.6) based on the following criteria:

- (i) accommodation requirements exceeding 500 m² each;
- (ii) accommodation plan not rejected by the GPA (e.g. co-location plans would normally be rejected);
- (iii) accommodation requirements on a permanent basis; and
- (iv) site search not yet commenced or outstanding for a prolonged period.

2.8 In other words, no new JUBs nor SDBs had been planned for meeting the additional accommodation needs of B/Ds (29,591 m² — see para. 2.7(b)) for the five-year period from 2017-18 to 2021-22. The GPA needs to take measures, including planning for more JUBs, to meet the additional office accommodation needs of B/Ds.

Audit recommendation

2.9 **Audit has recommended that the Government Property Administrator should take measures, including planning for more JUBs, to meet the additional office accommodation needs of B/Ds.**

Note 13: *The additional space requirements could not be fully met by the three JUBs (i.e. the West Kowloon Government Offices, the Treasury Building and the Tseung Kwan O Government Offices Building) in the pipeline. This was because they would be mainly used for reprovisioning WCGOC offices (see para. 2.11), and could only provide a total area of 8,200 m² to meet new office accommodation demand.*

Response from the Government

2.10 The Government Property Administrator agrees with the audit recommendation. He has said that the GPA will continue to take steps to meet the Government's needs for general office accommodation through construction of new JUBs and/or other alternatives as mentioned in paragraph 1.5.

Reprovisioning of offices of the Wan Chai Government Offices Compound

2.11 In his 2008-09 Budget Speech, the Financial Secretary announced that the relocation of government offices at the WCGOC would release space in the CBD to meet the demand for Grade A offices (see para. 1.8(b)). The relocation of the WCGOC is a mega project as it involves a total floor area of 175,000 m² for about 10,000 staff of 28 B/Ds and the Judiciary. The relocation requires the construction of nine replacement buildings (see Table 1 in para. 2.15). According to the GPA, in planning the replacement building projects, additional space for community facilities and relocation of other government offices currently accommodated in leased premises or government sites have been factored in so as to optimise site utilisation and reduce rental expenditure.

2.12 In March 2008, the GPA issued a circular memorandum to the affected users calling for returns on their office accommodation requirements for vacating the WCGOC and their preference of seven identified replacement sites (three in Kai Tak and another four in various districts, namely Tseung Kwan O, Cheung Sha Wan, Tung Chung and Tin Shui Wai). In November 2009, the GPA completed a study report on the proposed relocation plan. According to the report:

- (a) the Wan Chai Law Courts (comprising the District Court, Family Court, Small Claims Tribunal and other court support services) occupied a net operational floor area (NOFA — Note 14) of 26,834 m² in the WCGOC.

Note 14: *The NOFA refers to the floor area actually allocated to the users for carrying out their intended activities. For example, the NOFA does not include areas for toilets, bathrooms and shower rooms, lift lobbies, stair halls, public/shared corridors, stairwells, escalators and lift shafts, parking spaces, loading and unloading areas and mechanical plant rooms.*

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While noting the Judiciary's requirement on relocating the Wan Chai Law Courts within the CBDs of Hong Kong, the GPA and the PlanD identified two sites for the relocation, namely the ex-Western Police Married Quarters and the ex-Western Magistracy Building, both in Sai Ying Pun, which were outside the CBDs; and

- (b) after consulting the relevant users, the Tin Shui Wai and Tung Chung sites were considered to be remote and not suitable.

2.13 ***Relocation approach and allocation principle.*** In September 2010, the GPA requested the affected users to provide the latest space requirements and the schedules of accommodation. In April 2012, the FSTB issued a memorandum to the affected users on the planning of the phased relocation of users' offices from the WCGOC, specifying that:

- (a) ***Relocation approach.*** The relocation exercise would be taken forward on an incremental basis by relocating offices from the WCGOC in phases as and when government office premises available for reprovisioning came on stream, including the West Kowloon Government Offices (WKGGO — see para. 2.18);
- (b) ***Allocation principle.*** Based on the site preferences of concerned users as indicated in their returns to the GPA in 2008 and taking into account floor space available at the replacement sites, the GPA would work with users concerned on the space allocation in accordance with the following principles:
 - (i) offices providing frontline services would have priority over others in being allocated with space in government-office buildings in urban areas;
 - (ii) accommodation would be allocated to users primarily based on the existing floor space of their offices at the WCGOC. Additional space might be considered subject to justifications for the extra allocation and availability of floor space at the replacement sites;

- (iii) requests for putting together the offices (i.e. co-location of offices) currently housed in non-WCGOC premises would not be considered normally unless there was a strong case for the co-location (such as resulting in deleasing savings or releasing office space in high-value areas) and subject to availability of surplus floor space at the replacement sites; and
 - (iv) to ensure that office space would be put to the best possible use, users were requested to critically review their accommodation needs and put up requests for additional space only where justified; and
- (c) **Way forward.** The GPA would approach the concerned users by phases to discuss details of the relocation exercise, including reprovisioning proposals, space allocation, as well as the necessary preparatory work and schedule for bidding capital works resources (see para. 1.5(a)). Users were requested to render their full support to the relocation exercise and proceed with the preparatory work as necessary to facilitate the delivery of the initiative.

2.14 ***Nine replacement projects proposed.*** As of May 2013, other than the DSD and the Judiciary, the GPA drew up the relocation plan for 27 B/Ds with seven new replacement building projects proposed (see Projects 1 to 7 in Table 1 of para. 2.15). In May 2014, the DSD proposed to the GPA the construction of a new SDB for reprovisioning its Headquarters (HQs) and offices in WCGOC (see Project 8 in Table 1 of para. 2.15). In May 2016, the Judiciary agreed in principle to relocate the Wan Chai Law Courts to a new District Court Complex at a CBD site in Causeway Bay (see Project 9 in Table 1 of para. 2.15).

2.15 *Submission of quarterly progress reports to the Financial Secretary.* The FSTB is responsible for monitoring the implementation of the nine replacement building projects. In April 2014, the FSTB and the GPA submitted a progress report on the relocation exercise to the Financial Secretary. The Financial Secretary did not agree with the proposed timing in the progress report and requested speeding up the process and reducing the time required. The Financial Secretary also said that there should be a monitoring mechanism with key markers so that the FSTB could keep a close watch on the progress. In the same month, the FSTB informed the GPA that in order to facilitate the close monitoring of the WCGOC relocation project, the FSTB, with the input of the GPA, should provide a quarterly progress report to the Financial Secretary setting out the brief details of the replacement building projects, the latest progress and constraints/difficulties encountered. Since September 2014, the FSTB had submitted the quarterly progress reports to the Financial Secretary's Office. Table 1 shows the reported progress of the nine replacement building projects as of March 2017. Figure 3 shows the tentative construction programmes of eight projects (except the District Court Complex project which was under preliminary planning — see Project 9 in Table 1) based on the progress reports of September 2014 and March 2017.

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Table 1

**Progress of nine replacement building projects
for relocation of offices at the WCGOC
(March 2017)**

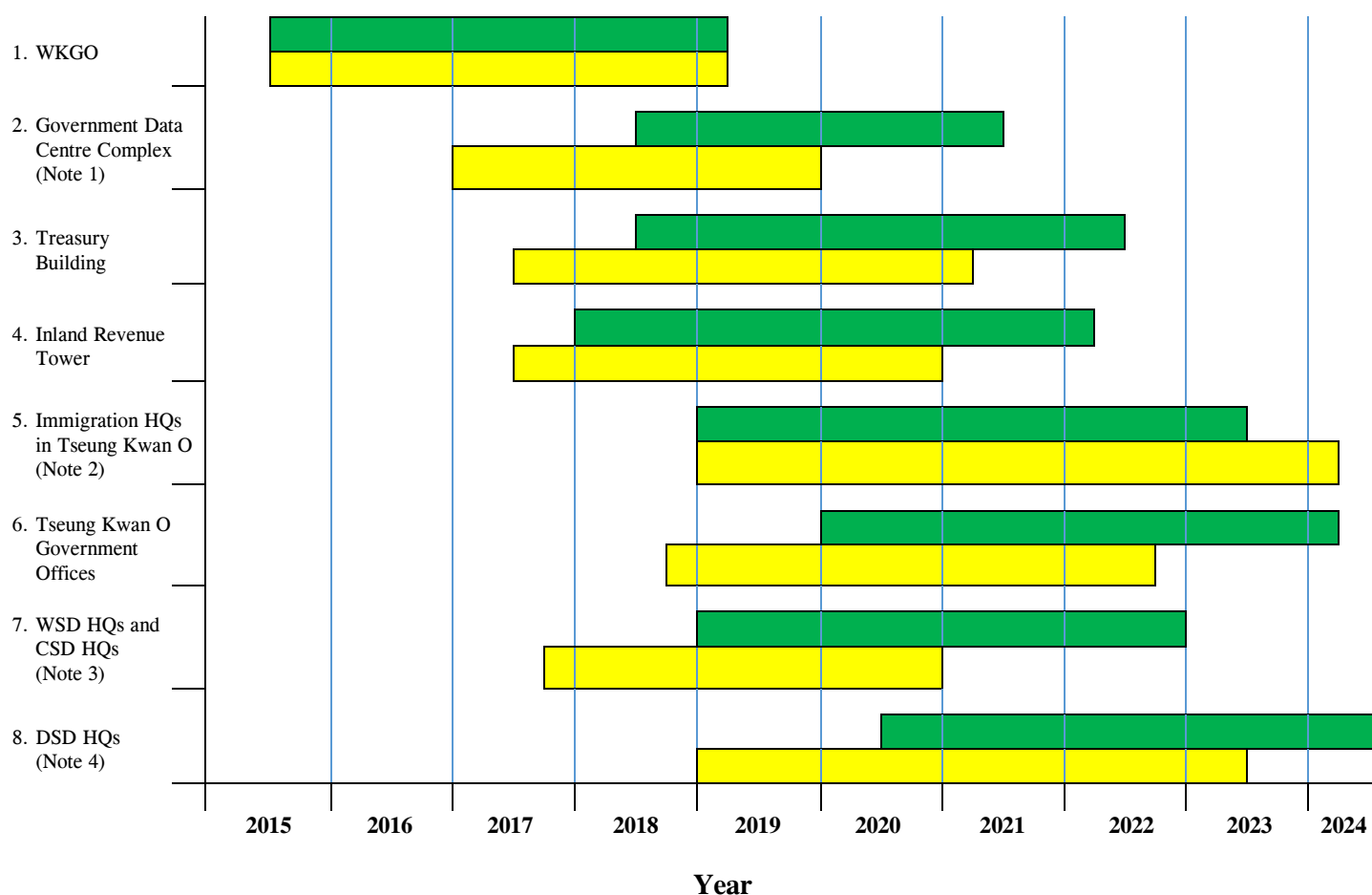
Project	Replacement building projects	Percentage of office space for reprovisioning the WCGOC (Note)	Progress
1 (JUB)	WKGO in Yau Ma Tei	22%	Design-and-build contract awarded in July 2015 and foundation works in progress
2 (SDB)	Government Data Centre Complex in Cheung Sha Wan	54%	Pre-construction consultancy contract awarded in November 2015 and design in progress
3 (JUB)	Treasury Building in Cheung Sha Wan	64%	Pre-construction consultancy contract awarded in March 2016 and design in progress
4 (SDB)	Inland Revenue Tower in Kai Tak	100%	Tenders for design-and-build contract invited in January 2017
5 (SDB)	Immigration HQs in Tseung Kwan O	73%	Prequalification tenders to be invited in April 2017
6 (JUB)	Tseung Kwan O Government Offices in Tseung Kwan O	54%	District Council consultation conducted in January 2017 and planning in progress
7 (SDB)	Water Supplies Department (WSD) HQs and Correctional Services Department (CSD) HQs on Hong Kong Island	58%	Technical feasibility study approved in November 2016 and planning in progress
8 (SDB)	DSD HQs in Kowloon	35%	Technical feasibility study approved in December 2016 and planning in progress
9 (SDB)	District Court Complex in Causeway Bay	Not yet available	Preparation of project definition statement by the Judiciary in progress

Source: GPA records

Note: According to the GPA, the percentage of office space for reprovisioning the WCGOC would be subject to revision. In planning for the replacement building projects, additional space for community facilities and relocation of other government offices currently in leased accommodation has been factored in (see para. 2.11).

Figure 3

Tentative construction programmes of eight replacement building projects based on the progress reports of September 2014 and March 2017



Legend: ■ Tentative construction programme of March 2017
■ Tentative construction programme of September 2014

Source: GPA records

Note 1: According to the Information Technology Bureau, the project would commence in late 2018.

Note 2: According to the Immigration Department, the project would commence in the first quarter of 2019.

Note 3: According to the CSD, the construction programme was tentative only and further progress would depend on various factors. Relevant B/Ds would continue to work together in pursuing the project.

Note 4: According to the DSD, as a result of a review completed in July 2017, the project would commence in September 2019 for completion in September 2023.

Remarks: The tentative construction programme for the District Court Complex project was not yet available because it was still under preliminary planning (see Project 9 in Table 1).

2.16 *Need to monitor progress of reprovisioning WCGOC offices.* According to the progress report of March 2017 submitted to the Financial Secretary, the relocation of the WCGOC as a whole was estimated to be completed in 2025-26 the earliest. As shown in Figure 3 of paragraph 2.15, comparing the tentative construction programmes of the replacement building projects as reported in September 2014 with those in March 2017, six projects had encountered delays. According to the GPA, the changes in tentative completion dates were mainly due to changes in project scope to meet local needs, technical constraints and the time taken for seeking funding approval. The relocation of the Wan Chai Law Courts was still under planning without a projected completion date. The FSTB, in collaboration with the GPA and the ArchSD, needs to closely monitor the implementation of the nine replacement building projects to ensure their timely completion.

2.17 *Audit examination.* Audit examination of the relocation exercise of the government offices in the WCGOC has revealed room for improvement in:

- (a) implementation of the WKGO project (see paras. 2.18 to 2.23); and
- (b) identification of suitable sites for reprovisioning two users of the WCGOC (see para. 2.24).

Implementation of the WKGO project

2.18 Among the nine replacement building projects, the WKGO project (see Project 1 in Table 1 of para. 2.15) was an on-going project before the announcement of the WCGOC relocation plan in 2008 (see para. 2.11). The WKGO, located at Yau Ma Tei, would comprise two blocks of 15 and 17 storeys respectively, providing an estimated total NOFA of around 50,500 m² and an underground car park. In 2002, the ArchSD completed a feasibility study of the WKGO project which was then planned for:

- (a) reprovisioning four blocks of government buildings in Yau Ma Tei (i.e. the Kowloon Government Offices, Yau Ma Tei Multi-storey Carpark Building, Yau Ma Tei Jockey Club Polyclinic and the Department of Health's facilities at Yau Ma Tei Specialist Clinic Extension) which would be

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affected by the construction of the HyD's Central Kowloon Route (CKR — Note 15); and

- (b) providing new government offices to facilitate de-leasing leased office accommodation and meeting new requirements.

2.19 The WKGO project was included in the PWP in July 2003 and funding was earmarked in 2005 for proceeding with the relevant planning work. In July 2005, the GPA informed the FSTB that:

- (a) the four affected government buildings should be vacated by April 2010 when the construction of the CKR was planned to start; and
- (b) in order to meet the overall programme objective of the CKR project, the GPA would explore with the ArchSD and the affected B/Ds on adopting a phased approach to allow for completing part of the WKGO for accommodating the B/Ds' displaced facilities (i.e. 56% of the WKGO office space — see Table 2 in para. 2.22) prior to the overall completion of the whole WKGO project.

While the phased construction approach was subsequently found to be physically viable, in view of the higher overall cost implication as advised by the ArchSD (Note 16), the GPA decided in August 2005 that the WKGO project should proceed in one go.

2.20 ***Changes in the planning of WKGO project.*** Between 2005 and 2011, there had been changes in the planning of the WKGO project, as follows:

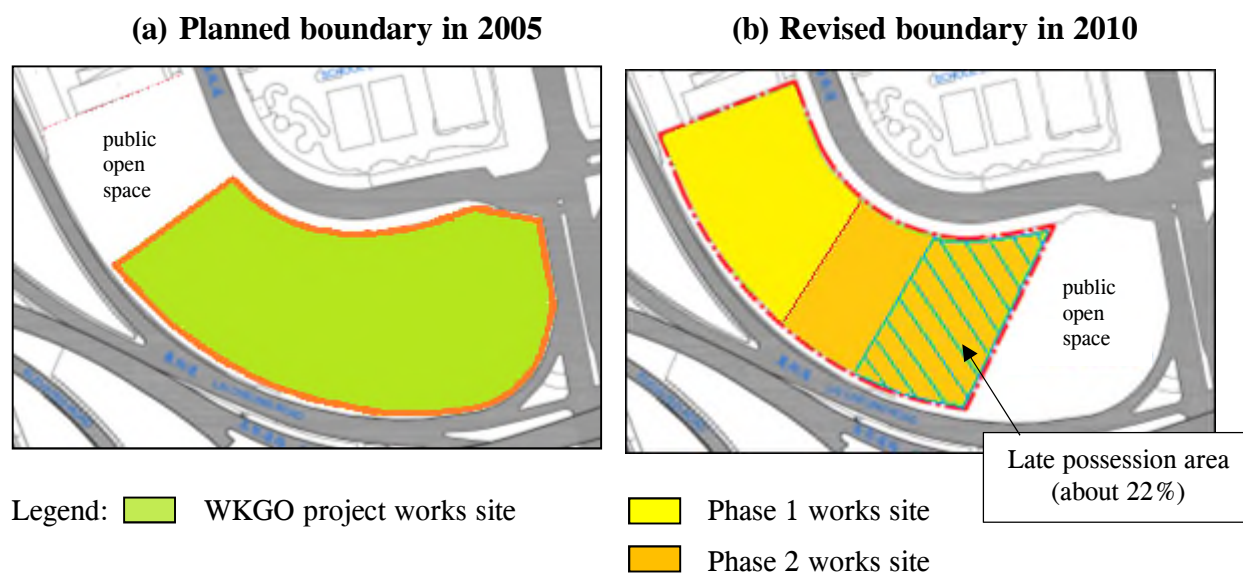
Note 15: *The proposed CKR is a dual 3-lane trunk road connecting the Yau Ma Tei Interchange in West Kowloon with the Kai Tak Interchange in East Kowloon for diverting the traffic along the major east-west corridors in Kowloon to relieve traffic congestion and cope with future traffic demand. In October 2017, the Finance Committee approved funding of \$42,363.9 million for implementing the CKR project.*

Note 16: *According to the ArchSD, as a works agent, it advised on the cost and programme implication on the phased approach, and was not in a position to decide whether the project was to proceed in one go or in phases.*

- (a) ***Suspension of the WKGO project.*** In September 2005, shortly after the earmarking of funding for the WKGO project (see para. 2.19), the HyD informed the GPA that it would commission a consultancy and the review result would be available in the fourth quarter of 2006. According to the HyD, one of the objectives of the consultancy was to review the CKR alignment options with a view to preserving the Yau Ma Tei Police Station and to retaining existing G/IC facilities as far as practicable. In December 2006, noting that the CKR consultancy study (which had not yet started at that time) would review the need for reprovisioning the four blocks of government buildings which in turn would affect the finalisation of scope of the WKGO project and the commencement of technical feasibility study, the ArchSD informed the GPA that it was not possible to proceed with the WKGO project as planned;
- (b) ***Change in site boundary.*** In July 2007, the HyD circulated a railway scheme to the GPA amongst others. In October 2007, the HyD alerted the GPA that part of the site earmarked for the WKGO would be reserved as a works site for the railway project from late 2009 to 2014-15. Since November 2007, the HyD had been exploring with the GPA and other relevant B/Ds on various options for the handing over of the concerned site in phases to mitigate its impacts on the programme of the WKGO project. In September 2009, a land allocation arrangement was agreed, under which the originally planned site boundaries for the WKGO in 2005 and an adjacent public open space were revised in 2010. After the changes, a portion (22%) of the WKGO revised site would only be available at a later stage in March 2015 at the earliest (see Figure 4 for the planned site boundary in 2005 and the revised boundary in 2010). In view of the changes, in April 2010, the ArchSD revised the technical feasibility study report which specified that the WKGO project would be split into two phases, i.e. phase 1 for the construction of one office tower (33% of the total NOFA) was scheduled for completion in May 2015 and phase 2 for the construction of another office tower (the remaining 67% of the NOFA) was scheduled for completion in November 2017; and

Figure 4

Change in site boundary for the WKGO



Source: GPA records

- (c) **Change in users.** In January 2008 and June 2010, the HyD informed the GPA that the demolition of two blocks of government buildings (i.e. the Yau Ma Tei Jockey Club Polyclinic and Kowloon Government Offices Building respectively) would no longer be required under the CKR project. As a result, part of the office space in the WKGO originally earmarked for reprovisioning these two buildings could be allocated for reprovisioning offices from the WCGOC. In August 2011, the ArchSD further revised the technical feasibility study report of the WKGO project to take into account the changes in users. In the event, the scheduled completion of phase 1 was deferred from May 2015 to November 2016 with no change for phase 2 completion (i.e. November 2017).

2.21 In February 2014, the FSTB informed the Legislative Council (LegCo) Panel on Financial Affairs that the scheduled completion dates of phase 1 and phase 2 would be late 2018 and early 2019. According to the funding paper for the construction of the WKGO submitted by the FSTB in April 2015 to the Finance Committee (FC) of LegCo:

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- (a) the construction works would be carried out in two phases as part of the site would only be available at a later stage, i.e. the late possession area (see para. 2.20(b)). Subject to the approval of the FC, construction works would commence in the second half of 2015 for completion in early 2019;
- (b) 58% of the total NOFA would be used for reprovisioning government offices accommodated in leased premises in Wan Chai, Tsim Sha Tsui, Mong Kok and Kwun Tong. The premises to be released would help increase the supply of commercial floor area in various districts and the estimated annual savings in rental expenditure would be about \$160 million (based on December 2014 price level); and
- (c) the GPA had consulted the Yau Tsim Mong District Council and various local stakeholders (including a residential estate and two nearby schools) on the project. Members of the District Council gave support in December 2013 for the project though there were some concerns over possible environmental and traffic impacts.

2.22 In June 2015, the FC approved funding of \$4,742.5 million for implementing the WKGO project. In July 2015, a design-and-build contract for the WKGO was awarded at a sum of \$4,332.8 million for completion in early 2019. As of June 2017, construction works for foundation and other design were in progress. Table 2 summarises the key changes in the planning of the WKGO project from July 2005 to April 2015.

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Table 2

Key changes in the planning of the WKGO project (July 2005 to April 2015)

	July 2005	April 2010 (change in site boundary)	August 2011 (change in users)	September 2012	February 2014 (Panel on Financial Affairs)	April 2015 (FC paper)
Estimated construction cost (\$ million)	1,557 (at September 2005 price level)	3,534 (at September 2009 price level)	4,199 (at September 2011 price level)	4,944 (at September 2012 price level)	— (Note 2)	4,742.5 (including inflation) (or 3,822 at September 2014 price level)
Scheduled completion	July 2010	Phase 1: May 2015 Phase 2: November 2017	Phase 1: November 2016 Phase 2: November 2017	Phase 1: November 2017 Phase 2: April 2018	Phase 1: late 2018 Phase 2: early 2019	By two phases with overall completion in early 2019
Planned allocation of office space (m²)						
(a) office affected by the CKR	28,070 (56%)	16,700 (33%)	4,000 (8%)	4,247 (9%)	6,060 (12%)	6,060 (12%)
(b) deleasing of leased premises	18,755 (37%)	33,300 (67%)	41,550 (83%)	36,114 (72%)	30,300 (60%)	29,290 (58%)
(c) new provision and others	3,325 (7%)	44%			3,030 (6%)	4,040 (8%)
(d) reprovisioning WCGOC	— (Note 1)		4,450 (9%)	9,639 (19%)	11,110 (22%)	11,110 (22%)
Total	50,150	50,000	50,000	50,000	50,500	50,500

66%

Source: GPA records

Note 1: The relocation of the WCGOC was announced in the 2008-09 budget speech. The GPA was informed in January 2008 and June 2010 that the office space earmarked for reprovisioning two government buildings in Yau Ma Tei would not be required (see para. 2.20(c)).

Note 2: According to the panel paper, the estimated cost per unit area would be \$30,000 to \$33,000 per m² (at September 2013 price level).

2.23 *Long time taken in implementing the WKGO project.* As shown in paragraph 2.19 and Table 2 of paragraph 2.22, the WKGO project had taken almost 12 years to progress from project inception (i.e. date of inclusion in the PWP in July 2003) to funding approval in June 2015. The time taken was much longer than 2 to 5 years of two other government-office building projects implemented during the 12-year period (see Appendix C for details). Audit examination of the project development revealed the following lessons to be learnt in the implementation of the WKGO project:

- (a) *Need to consider advancing part of the WKGO project for deleasing purpose.* The WKGO project was planned for reprovisioning government buildings affected by the CKR project and for providing new offices to facilitate deleasing of leased government accommodation (see para. 2.18). In December 2006, noting that the CKR consultancy study would review the need for reprovisioning the government buildings, the ArchSD informed the GPA that it was not possible to proceed with the WKGO project as planned (see para. 2.20(a)). However, a significant part (44% of the planned NOFA — see Table 2 in para. 2.22) of the WKGO for providing new accommodation and facilitating deleasing was not dependent on the CKR project and could proceed on its own given that a phased construction approach for the WKGO was considered physically viable in August 2005 (see para. 2.19). While such phased construction approach would have higher cost implication, the earlier provision of new offices for deleasing purpose could bring about rental saving. There was no record to show that the GPA had conducted a cost-benefit analysis for implementing the WKGO project by phases before deciding to defer the whole project in 2006 pending the outcome of the CKR consultancy study. In the event, the reprovisioning requirement of the CKR project was only finalised in 2010 (3.5 years later) and the consequential change in users of the planned accommodation for reprovisioning purpose caused a further delay of over one year in the scheduled implementation date of the WKGO project (see para. 2.20(c)). Meanwhile, the estimated construction cost had also increased by 170% from \$1,557 million in July 2005 to \$4,199 million in 2011 (see Table 2 in para. 2.22). In any event, a phased approach was adopted in 2010 to address the problem of late possession of some site area for the railway project (see para. 2.20(b)); and
- (b) *Need to conduct public consultation at an early stage.* According to the Project Administration Handbook issued by the ArchSD, after completing the technical feasibility study, a project team should allow adequate time

for public consultations in preparing the outline plan based on the approved technical feasibility study, including coordination with and supporting its client to conduct public consultations at an early stage if required, and facilitate resolving public objection in a timely manner (Note 17). The WKGO project was planned for implementation as a design-and-build project. After completion of the revised technical feasibility study report by the ArchSD (the works agent) in August 2011, the WKGO project was ready for conducting public consultation. However, it was not until July 2012 that the GPA informed the FSTB of its plan (Note 18) to conduct public consultation in March 2013. In the event, public consultation started in April 2013 and the support of the District Council was only obtained in December 2013 after further consultation was conducted to address local concern. In Audit's view, in implementing a JUB project in future, the GPA, in consultation with the ArchSD, needs to conduct public consultation at an early stage to facilitate addressing any public concern/objection in a timely manner.

Long time taken in identifying sites for reprovisioning two users of the WCGOC

2.24 Since 2008, the PlanD had made efforts in identifying suitable sites for reprovisioning the WCGOC offices and the GPA had also carried out matching exercises with the affected users for the identified sites. Audit noted that, among the 28 affected B/Ds and the Judiciary, the identification of reprovisioning sites for the DSD and the Judiciary (see Projects 8 and 9 in Table 1 in para. 2.15) had taken the longest time to finalise, i.e. in 2014 and 2016 respectively. Audit examination of the two cases revealed lessons to be learnt as shown in Cases 1 and 2.

Note 17: *It is also relevant to note that according to Technical Circular (Works) No. 4/2006 (still in force) of the then Environment, Transport and Works Bureau, public consultations for projects should be planned in advance in consultation with the clients and started as soon as possible when the project is upgraded to Category B and a preliminary design is available for the public's discussion.*

Note 18: *According to the GPA, the public consultation plan was based on the works programme as advised by the works agent in June 2012.*

Case 1

Relocation of DSD offices to a sewage pumping station site

1. In April 2008, the DSD informed the GPA that all its offices in the WCGOC could be relocated outside Wan Chai. The DSD considered that the five proposed replacement sites at Cheung Sha Wan, Kai Tak and Tseung Kwan O were acceptable. In December 2013, the GPA informed the DSD that its offices in the WCGOC would be relocated to new JUBs in Tseung Kwan O or Kai Tak.

2. In January 2014, the DSD requested the GPA to reprovision all its WCGOC offices and other offices in various locations in Kai Tak so as to oversee the flood control and sewerage projects and facilities throughout the territories. In February 2014, the GPA replied that since the DSD provided a territory-wide service, there was no operational needs for the DSD's offices to be located in Kai Tak, and proposed to relocate DSD's offices in the WCGOC to Tseung Kwan O.

3. In May 2014, the DSD informed the GPA that it would not take up the Tseung Kwan O JUB office and planned to build an SDB at one of its sewage pumping station sites in Kowloon (Note 1). In February 2015, the DEVB approved the project definition statement for the SDB proposed by the DSD and in September 2015 approved the technical feasibility study prepared by the ArchSD.

4. According to Financial Circular No. 5/2012 (Note 2), new projects are required to achieve at least 90% of the development potential of the allocated sites. According to the ArchSD, although the proposed SDB could achieve more than 90% of the development potential, further endeavours had been made to maximise the site utilisation. From late 2015 to early 2016, the DEVB, in collaboration with the DSD, the GPA, the PlanD and the ArchSD, conducted a review and decided to incorporate the SWD as a joint user (Note 3). Subject to funding approval, the project was scheduled to start in September 2019 for completion in September 2023.

Case 1 (Cont'd)

Audit comments

5. The proposed SDB in a sewage pumping station site was an innovative initiative that could meet the reprovisioning need of the DSD and maximise the utilisation of the site. It is a good example of proactive inter-B/D collaboration in making use of the residual development potential of an existing occupied site. However, such a proposal was only brought up in 2014, some six years after the GPA commenced the relocation project of the WCGOC. This incident indicates that when planning for the reprovisioning of a government-office building in future, the GPA needs to make reference to the DSD's example and request all affected users to critically review whether their accommodation requirements can be met by making use of their existing stock of accommodation, including sites with residual development potential. This is important to ensure that all options available are fully explored at an early stage with a view to meeting the affected users' accommodation needs in a cost-effective and timely manner.

Source: Audit analysis of GPA records

Note 1: According to the DSD, this innovation project aimed to maximise utilisation of the site and promote the concept of co-use of government site for different purposes. The SDB was proposed after critically considering a wide range of factors such as the planned upgrading works of the facilities, operational constraints of the site, planned residential developments in the vicinity and anticipated responses of local residents.

Note 2: In June 2017, the Circular was superseded by Financial Circular No. 4/2017 which contained a similar requirement.

Note 3: According to the DSD, the maximum NOFA that could be provided under the proposed SDB was 18,450 m² whereas the approved schedule of accommodation (in NOFA) was 14,547 m² for the DSD and 4,554 m² for the SWD. The shortfall of 651 m² had to be sorted out among the DSD, the GPA and the SWD.

Case 2

Relocation of Wan Chai Law Courts

1. In April 2008, in response to the GPA's circular memorandum (see para. 2.12), the Judiciary said that:

- (a) its preferred location for reprovisioning the Wan Chai Law Courts (Note 1) should be in a stand-alone law court building in CBDs (Sheung Wan, Central, Wan Chai or Causeway Bay) because legal practitioners and professionals were mainly located in the CBDs on Hong Kong Island; and
- (b) the total NOFA (see Note 14 to para. 2.12(a)) required should be about 20,000 m² and the estimated GFA (see Note 8 to para. 1.8(b)) should be about 56,000 m².

2. ***Proposed relocation site in Sai Ying Pun.*** In October 2008, in response to the GPA's enquiry, the Judiciary considered that the proposed ex-Western Police Married Quarters and the nearby ex-Western Magistracy Building in Sai Ying Pun were acceptable for the relocation. In December 2008, the GPA informed the Judiciary that based on an available area of 5,420 m² for the ex-Quarters site, the maximum GFA that could be constructed was about 50,000 m² which might not fully meet the Judiciary's GFA requirement of 56,000 m². The Judiciary was requested to explore the possibility of trimming down its requirement to 50,000 m². In March and May 2009, the GPA informed the Judiciary that: (a) the architects at a later design stage could assist in utilising the proposed GFA of 50,000 m² to meet the Judiciary's NOFA requirements; and (b) the GFA requirement was estimated to be about 30,753 m² based on the floor plan of the Wan Chai Law Courts (see para. 2.13(b)(ii)).

3. ***Floor height requirement.*** In May 2012, the GPA informed the Judiciary that the site area available was revised to 5,200 m² which according to the GPA's assessment could still provide a GFA of 49,000 m². At a meeting between the GPA and the Judiciary of May 2012, it was brought to light that the GPA's estimation of the GFA was based on the existing floor-to-floor height (or "floor height") of 4.5 metres (m) for the Wan Chai Law Courts whereas a 7-m floor height was required by reference to the West Kowloon Law Courts Building then under construction for accommodating building services installations, structural elements and raised floor. In June 2012, the Judiciary informed the GPA that the proposed site was no longer considered to be suitable because the site area might not be able to provide a GFA of 50,000 m². In the subsequent exchange of correspondence in July and August 2012:

Case 2 (Cont'd)

- (a) the GPA said that accommodation would be allocated to users primarily based on the existing floor areas of their offices in the WCGOC as promulgated by the FSTB in April 2012 (see para. 2.13(b)(ii)) and that the proposed relocation site was not suitable as a result of change in floor height requirement from 4.5 m to 7 m; and
- (b) the Judiciary said that prior to the meeting of May 2012, it had not been consulted on the adequacy of the existing floor height at Wan Chai Law Courts, or whether the existing floor height at Wan Chai Law Courts should be adopted as the benchmark for the new law courts. Moreover, the site coverage was 62.5% according to the Building (Planning) Regulations (Cap. 123F), whereas the GPA's plan was based on 100% site coverage.

In November 2012, on the advice of the PlanD, the GPA informed the Judiciary that there were no other suitable reprovisioning sites on Hong Kong Island which could satisfy the GFA requirement of 50,000 m².

4. From September 2012 to January 2013, the GPA consulted the ArchSD on the achievable floor area if the floor height was reduced from 7 m to 4.5 m. According to the ArchSD:

- (a) based on the designs of a few law court buildings completed/to be completed at various time periods, a higher floor height was employed for new law court buildings, e.g. 6 m for the Fanling Law Courts Building completed in 2001 and 6 m to 7 m for the West Kowloon Law Courts Building then targeted for completion in 2015. With reference to the floor height requirement under the prevailing standard of law court design, a reduced site coverage (Note 2), and assuming a relaxed building height of 88 m, the maximum achievable NOFA at the Sai Ying Pun site was about 9,400 m² (or a GFA of 25,900 m²), which could only meet part of the Judiciary's requirement (about 20,000 m² — see para. 1), and hence the proposed site was not feasible for the reprovisioning of the Wan Chai Law Courts; and
- (b) assuming a 4.5-m floor height, the achievable NOFA would range from 10,900 m² to 12,400 m². The possibility of increasing the potential (i.e. the floor area) through adopting a low floor height of 4.5 m was an unrealistic hypothetical scenario. The ArchSD would not recommend pursuing such a study, as it would yield very misleading results.

Case 2 (Cont'd)

5. **Another site search.** In July 2013, in response to the Judiciary's representations that a holistic approach in mapping out a solution that would address the long-term accommodation needs of the Judiciary was necessary since there was no room for expansion at the High Court and the District Court, the relevant B/Ds conducted another round of site search to identify suitable sites for meeting the long-term accommodation needs of the Judiciary, including the reprovisioning of the Wan Chai Law Courts. In November 2014, the Judiciary informed the Government that the Judiciary would require an NOFA of 26,000 m² for the Wan Chai Law Courts as well as the Lands Tribunal in Yau Ma Tei. In April 2015, the Government offered a CBD site in Causeway Bay which could provide an NOFA of 26,000 m² (subject to detailed assessment) for the development of a District Court Complex (including the reprovisioning of the Wan Chai Law Courts). In May 2016, the Judiciary accepted in principle to use the proposed site.

Audit comments

6. While the GPA assisted the Judiciary in identifying the ex-Quarters site in Sai Ying Pun for relocating the Wan Chai Law Courts as early as 2008, it was only in 2012 that the GPA's estimation of the achievable GFA from the site based on the existing 4.5-m floor height of the Wan Chai Law Courts was found to be different from that under the prevailing law court design standard of a 7-m floor height. The site coverage was also found to be less than the assumed 100%. In the event, the proposed Sai Ying Pun site was considered not feasible and another site search had to be conducted. In Audit's view, when assisting users in identifying reprovisioning sites for their accommodation/offices in future, the GPA needs to consult the users and the works departments at an early stage the planning assumptions/parameters used for estimating the GFA/NOFA achievable to ensure that any proposed sites can fully meet the accommodation and operational needs of the users concerned.

Source: Audit analysis of GPA records

Note 1: Only the District Court and Family Court of the Wan Chai Law Courts (see para. 2.12(a)) together with the Lands Tribunal in Yau Ma Tei were proposed to be reprovisioned to a stand-alone law court building in CBDs. The Small Claims Tribunal was proposed to be reprovisioned to another planned law court building in West Kowloon.

Note 2: In November 2008, the PlanD advised the GPA that no restriction on development intensity was imposed on G/IC zone under the OZP. In September 2012, the PlanD advised the GPA that while according to the Buildings Department's memorandum of the same month, the law court buildings were exempted from the provisions of the Building Ordinance (Cap. 123), in reservation of the subject site, a site coverage of about 80% had all along been assumed.

Audit recommendations

2.25 **Audit has *recommended* that the Secretary for Financial Services and the Treasury, in collaboration with the Government Property Administrator and the Director of Architectural Services, should closely monitor the implementation of the nine replacement building projects for the relocation of the WCGOC to ensure their timely completion.**

2.26 **Audit has also *recommended* that the Government Property Administrator should:**

- (a) in implementing a JUB project in future:**
 - (i) when there is new development affecting the progress of certain separable parts of the project, conduct a cost-benefit analysis to evaluate the possible options for taking forward the project such as adopting a phased implementation approach; and**
 - (ii) in consultation with the Director of Architectural Services, conduct public consultation at an early stage to facilitate addressing any public concerns/objections in a timely manner; and**
- (b) in planning for the reprovisioning of a government-office building in future:**
 - (i) request all affected users to critically review whether their accommodation requirements can be met within their existing accommodation stock, including sites with residual development potential; and**
 - (ii) consult the users and the works departments at an early stage the planning assumptions/parameters used for estimating the achievable GFA/NOFA to ensure that any proposed sites can fully meet the accommodation and operational needs of the users concerned.**

Response from the Government

2.27 The Secretary for Financial Services and the Treasury agrees with the audit recommendation in paragraph 2.25 and will continue to closely monitor the WCGOC relocation exercise in collaboration with the GPA, the ArchSD and the concerned users. He has said that the WCGOC relocation is a mega project involving 28 B/Ds and the Judiciary, and the FSTB:

- (a) has been monitoring the relocation exercise through regular reporting from the GPA with inputs from the ArchSD and other relevant users; and
- (b) keeps track of the progress of the WCGOC relocation exercise through regular housekeeping meetings with the GPA, and helps resolve interfacing issues through inter-departmental meetings with the affected users.

2.28 The Government Property Administrator generally agrees with the audit recommendations in paragraph 2.26. He has said that:

- (a) the GPA will consider conducting a cost-benefit analysis to assess the possible options if sufficient information (e.g. construction costs as advised by the works agent) is available and reasonable assumption can be made. For the WKGO project, its primary objective was to meet the reprovisioning needs of the CKR project. It was technically not viable to conduct a cost-benefit analysis before the finalisation of the delegating plan as it depended on the ultimate reprovisioning needs of the CKR project, which in turn hinged on the CKR alignment;
- (b) the GPA in general will follow the agreed timeframe set out in the construction programme of the technical feasibility study report to conduct public consultation. In fact, the GPA has conducted public consultation at an early planning stage for the two other JUB projects in relation to the relocation of the WCGOC, and will continue to conduct public consultation at an early stage where appropriate;
- (c) the GPA has requested the affected users of the WCGOC to conduct a comprehensive and critical review of their accommodation requirements, taking into account any long-term plan for reorganisation, downsizing and other initiatives when drawing up their reprovisioning requirements;

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- (d) the GPA will continue to consult the users and the works departments at an early stage the planning assumptions/parameters to ensure the suitability of any proposed sites. As regards Case 2 on the relocation of Wan Chai Law Courts (see para. 2.24), the role of the GPA was to assist the Judiciary as a project proponent to identify suitable replacement site for the construction of an SDB. In this connection, the GPA:
 - (i) had at an early stage in 2008 consulted all affected users in the WCGOC relocation exercise their special accommodation requirements. The GPA had also worked closely with the works departments on the planning assumptions and parameters used for estimating the achievable GFA/NOFA of the identified sites so as to assess their suitability;
 - (ii) considered that whether the Sai Ying Pun site could meet the Judiciary's space requirement hinged on the Judiciary's floor height requirements instead of the site area for the footprint of the new law courts. In 2009, the GPA informed the Judiciary that the reprovisioning was on a one-to-one basis under the relocation study (see para. 2.12). It had made reference to the GFA/NOFA requirements provided by the Judiciary when considering the suitability of replacement sites, taking into account any special requirements known to the GPA; and
 - (iii) despite the ArchSD's assessment in early 2013 (see para. 4(a) in Case 2 of para. 2.24), sought further advice from the PlanD and the ArchSD in May 2013 on the technical suitability of the Sai Ying Pun site for reprovisioning purpose, which suggested that the relocation of Wan Chai Law Courts to the reprovisioning site was feasible subject to certain conditions, including relaxation of the building height restriction, and confirmation of space requirements and floor height requirements; and
- (e) as regards the audit recommendation in paragraph 2.25, the GPA has been working closely with project proponents and works agents to implement the nine replacement building projects and address the problems/difficulties encountered. It will continue to report the progress of project implementation to the FSTB with a view to monitoring the implementation to ensure the timely completion of the replacement buildings.

2.29 Regarding Case 2 in paragraph 2.24 on the relocation of the Wan Chai Law Courts, the Judiciary Administrator has said that:

- (a) the 4.5 m of floor height for the Wan Chai Law Courts was adopted in the 1980s and over the years, the floor height requirement for law court buildings had been developed to about 6 m to 7 m for accommodating the building services requirements, structural elements and raised floors; and
- (b) at the time when the relocation of the Wan Chai Law Courts was discussed, the prevailing floor height required was 7 m and the previous 4.5-m floor height requirement was outdated. Hence, there had not been any changes in the floor height requirement.

PART 3: ADMINISTRATION OF LEASED GOVERNMENT OFFICES

3.1 This PART examines the GPA's administration of leased government offices, focusing on:

- (a) leasing and deleasing of office accommodation (paras. 3.2 to 3.21); and
- (b) relocating leased accommodation out of CBDs (paras. 3.22 to 3.26).

Leasing and deleasing of office accommodation

3.2 **Leasing policy.** The Government's accommodation policy is to house offices in owned buildings and reduce reliance on leasing. According to the GPA Manual, leasing office accommodation should be considered if existing government-owned accommodation is not available and the leasing is intended to meet short-term, urgent, location-tied accommodation needs or specific operational requirements. Specifically, the Manual sets out the following procedures:

- (a) **Leasing.** In selecting premises to be leased, priority should be given to suitable premises with low-rental implication such as public housing estates (Note 19). User's location preference should be justified having regard to the policy that departments should be housed as far as possible in government accommodation in less prime area away from the Central and Admiralty. For lease renewal, officers should exercise their judgement to include other pertinent issues for consideration having regard to the circumstances of each case, the objectives of the activity and the general role and function of the GPA. Other considerations should be given to factors such as justification for the continuing need for the leased premises, the proposed rental package and lease terms, the availability of other suitable premises in the market, the economics of a new lease, new fitting-out costs, and removal and unamortised fitting-out costs of the

Note 19: *Rental expenditure for leased accommodation used to be borne by the GPA's rent vote. Since the FSTB imposed a cap on the GPA's rental expenditure in September 2002, new leasing requirements have been funded by user B/Ds.*

existing leased premises (Note 20). According to ADD Divisional Instruction on “Procedures for search of private non-domestic accommodation and engagement of estate agents”:

- (i) upon confirmation of the accommodation requirements of B/Ds, case officers of the ADD should explore possible sourcing methods to identify suitable premises to meet B/Ds’ accommodation needs timely and cost-effectively. These methods include identifying suitable premises from existing records, the building list of government leased accommodation, newspapers and websites of property developers/owners. All site searches should be carried out in a fair and prudent manner;
 - (ii) if it is considered appropriate for sourcing properties through estate agents to meet specific accommodation requirements of B/Ds, case officers of the ADD may consider engaging estate agents to help refer potential properties available in the market; and
 - (iii) it is important that a written record of the site search be maintained in the file. Case officers of the ADD should properly document information such as contact point of the landlords or estate agents, properties offered, suitability of the offered properties and reasons for rejecting the properties; and
- (b) **Deleasing.** Case officers of the ADD need to take the following factors into consideration during the deleasing process:
- (i) where users surrender a part or the whole of the leased accommodation, the practicability of deleasing or reallocation of the vacant space to other users;
 - (ii) whether deleasing may result in nugatory rental payment or compensation to the landlord; and

Note 20: *According to the GPA Manual, a minimum of six years is used for assessing whether the fitting-out work should be considered amortised.*

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- (iii) priority for deleasing to be given to departmental HQs in leased premises, high value leases, where the landlord is uncooperative or unreasonable or leases due to expire in the next six months.

Selection of premises for leasing

3.3 The number and area of leased accommodation handled by the GPA from 2014 to 2016 are shown in Table 3.

Table 3

**GPA's work on leasing/deleasing office accommodation
(2014 to 2016)**

Work	2014		2015		2016	
	Number	Area (m ²)	Number	Area (m ²)	Number	Area (m ²)
Leasing of new premises	50	23,070	33	14,938	36	15,826
Renewal of leases	101	39,282	114	57,084	182	97,571
Deleasing	6	2,034	33	21,638	32	14,292

Source: GPA records

3.4 ***Audit examination of leases with high rental values.*** As stated in the GPA Manual, in selecting premises for leasing, priority should be given to suitable premises with low-rental implication (see para. 3.2(a)). Audit noted that the Rating and Valuation Department (RVD) had compiled average rents on a monthly basis for private office premises designed for commercial/business purposes with a breakdown by districts and by office grading (Note 21). Based on the GPIS records of 170 leases (Note 22) as of April 2017, Audit compared their rentals with the RVD's average rents of the relevant districts/office grading/lease periods. Audit found that:

- (a) the rents of 110 (64.7%) leases were lower than the RVD's average rents (by 1% to 34%); and
- (b) the rents of 60 (35.3%) leases were higher than the RVD's average rents. Of these 60 leases, the rents of 6 (10%) leases exceeded the RVD's average rents by more than 40%. Audit understood that the RVD's average rents were for general reference only. Audit selected 3 of the 6 leases (see Table 4) for examining the specific circumstances under which they were entered into/renewed. The findings on Leases A and B, and Lease C are shown in paragraphs 3.5 and 3.6 respectively.

Note 21: *Districts covered by the RVD included Sheung Wan, Central, Wan Chai/Causeway Bay, North Point/Quarry Bay, Tsim Sha Tsui, Yau Ma Tei/Mong Kok and Kowloon Bay/Kwun Tong. According to the RVD, average rents are analysed for general reference only and their levels at a certain period depend to a large extent on the special characteristics, including quality and location, of the premises which are leased during the period. Therefore, changes in average monthly rents between different periods should not be taken as necessarily indicating a general change in value over the period.*

Note 22: *As of April 2017, there were 629 leases in the GPIS records, of which 459 were either leases with nominal/concessionary rents, leases with buildings without office grading or located at shop level of buildings or at districts in which the RVD's average rents were not available. Therefore, Audit used the remaining 170 (629 less 459) leases for rental comparison.*

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Table 4

**Leases selected for case study
(2015)**

Lease	Building	Current user B/D	Area (m²)	Monthly rent (\$/m²)
<i>New leases (Note 1) commencing March 2015</i>				
A	Grade A office in Kwun Tong (see Note 7 to para. 1.8(b))	Working Family and Student Financial Assistance Agency	988	486
B			974	477
<i>Lease renewed in July 2015</i>				
C	Grade B office (Note 2) in Kwun Tong	CEDD	1,099	501

Source: GPA records

Note 1: The Working Family and Student Financial Assistance Agency occupies five floors of the leased premises under five separate leases. Only the rents of two leases (Leases A and B) exceeded the RVD's average rents by more than 40% while those of the other three leases were 21% to 32% higher than the RVD's average rents.

Note 2: According to the Hong Kong Property Review published by the RVD, Grade B office building has the following features: ordinary design with good quality finishes; flexible layout; average-sized floor plates; adequate lobbies; central or free-standing air-conditioning; adequate lift services; good management and parking facilities not essential.

3.5 Reasons for rejecting/not recommending leasing offers not documented for Leases A and B. In March 2014, the Labour and Welfare Bureau (LWB) informed the GPA that a new office of about 4,800 m² (Note 23) for about 500 staff preferably in East Kowloon would be required in July 2014 for administering the Low-income Working Family Allowance Scheme subject to the FC's funding approval of the Scheme in the same month. With the assistance of estate agents, the GPA in April 2014 identified two potential office premises for the LWB's consideration. The LWB selected the premises with a lower rental (\$30 per square feet (ft²) per month — Note 24) in Kwun Tong (see Building A in Table 5) instead of the other at \$35 per ft² per month in Kwai Chung (see Building F in Table 5). In August 2014, noting that funding approval for the Scheme could not be obtained in July 2014, the GPA recommended another premises (see Building H in Table 5) in Tsuen Wan as a fallback option in case the premises selected by the LWB subsequently became unavailable. In February 2015, after the LWB had obtained funding approval, the GPA entered into five leases for five floors with the landlord of Building A including two floors under Leases A and B (see Note 1 to Table 4 in para. 3.4). Audit noted that, other than the two potential offices offered to the LWB, the estate agents had also identified seven office premises having GFA of over 90,000 ft² (see Note 23) of comparable/lower rent (see Buildings B to E, and G to I in Table 5) for the GPA's consideration. However, as far as Audit could ascertain, there was no documentation of the reasons for rejecting/not recommending these offers to the LWB for its consideration, contrary to the requirement as specified in the ADD Divisional Instruction (see para. 3.2(a)(iii)). Upon Audit's enquiry, the GPA in September 2017 said that the seven office premises had not been selected because of unmatched timing, not preferred location, incompatible land use and insufficient space available. In Audit's view, the GPA needs to remind ADD staff to document the reasons for rejecting/not recommending offers in the selection of premises for leasing office accommodation in accordance with the Divisional Instruction (see para. 3.2(a)(iii)).

Note 23: *The estimated area of 4,800 m² was based on internal floor area, which was equal to approximately 90,000 square feet based on the GFA.*

Note 24: *The rentals were monthly asking rents quoted by estate agents based on the GFA of the potential office premises.*

Table 5

**Potential office premises offered by estate agents
(2014)**

Area	Building	Monthly asking rents based on GFA (\$/ft²)	Availability	Remarks
Kwun Tong	A	30	Immediate	Recommended as suitable in April 2014 by the GPA
	B	30	Oct 2014	Other potential premises identified by estate agents
	C	23.5 – 32	Immediate	
	D	26 – 28	Jul 2014	
	E	22 – 23	Immediate	
Kwai Chung	F	28 – 35 (Note)	Immediate	Recommended as suitable in April 2014 by the GPA
	G	28	Jul 2014	Other potential premises identified by estate agents
Tsuen Wan	H	25	Oct 2014	Recommended by the GPA in August 2014 as a fallback option
	I	11.5 – 19	Immediate	Other potential premises identified by estate agents

Source: GPA records

Note: The GPA had informed the LWB that the monthly asking rental for Building F was \$35 per ft².

3.6 *Alternative premises with lower-rental implication not explored before exercising option for renewal under Lease C.* The office accommodation of 1,099 m² at a Grade B office building in Kwun Tong under Lease C had been used by the CEDD since July 2003. The CEDD's office was among the leased accommodation planned to be relocated to the WKGO for delegating purpose

(see para. 2.18). However, because of the long time taken in implementing the WKGO project (see para. 2.23) and the continued need for leased accommodation, the lease was renewed for a 3-year term for four times from July 2006 to July 2015. As shown in Table 6, the monthly rent of Lease C had increased significantly since 2006 to a level comparable to the RVD's average monthly rents of Grade B offices in Tsim Sha Tsui (a CBD) and Yau Ma Tei/Mong Kok, and higher than those of Kowloon Bay/Kwun Tong (Note 25). According to the GPA Manual, for lease renewal, considerations should be given to a number of factors including rental package, new fitting-out costs and unamortised fitting-out costs of the existing leased premises (see para. 3.2(a)). However, there was no record to show that the GPA had explored other alternative premises with lower-rental implication before informing the landlord in January 2009 of its intention to renew Lease C in July 2009 at an open market rent to be agreed. According to the GPA Manual, the fitting-out cost of the CEDD's office would have been fully amortised after six years in July 2009 (see Note 20 to para. 3.2(a)). Audit also found from a valuation report prepared by the ADD staff in May 2009 for rental negotiation with the landlord for renewing Lease C that the GPA had leased in office accommodation of 4,533 m² at a nearby new Grade A office building in Kwun Tong in January 2009 for the C&SD at a monthly rent of \$157.5 per m², which was 43% lower than the then monthly rent of \$275 per m² under Lease C. However, there were no documented reasons for not considering this nearby lower-rental accommodation before renewing Lease C in July 2009 at a monthly rent of \$293 per m². The GPA needs to remind the ADD staff to explore suitable alternative premises with lower-rental implication before lease renewal, and document the reasons for the decision taken in this regard.

Note 25: *According to the GPA, it does not make reference to the RVD's average rents when assessing the reasonableness of rents of the GPA's leases as: (a) the RVD's average rents are for general reference only (see para. 3.4(b)); and (b) the premises leased by the GPA are likely to be different from other leased premises captured by the RVD. The rent of any premises leased by the GPA is affected by their special characteristics and the prevailing leasing market conditions.*

Table 6

**Comparison of Lease C's monthly rents
with the RVD's average monthly rents of Grade B offices
(2003 to 2015)**

Month	Monthly rent under Lease C (\$/m ²)	RVD average monthly rent		
		Tsim Sha Tsui (\$/m ²)	Yau Ma Tei/ Mong Kok (\$/m ²)	Kowloon Bay/ Kwun Tong (\$/m ²)
July 2003	72 (Note 1)	186	174	No comparable rent for these periods (Note 2)
July 2006	275	265	264	
July 2009	293	283	259	
July 2012	391	399	403	223 (Note 2)
July 2015	501	471	479	291

Source: GPA and RVD records

Note 1: According to the GPA, Lease C was first entered into in mid-2003 at a time of economic downturn and very volatile rental movements. Given the large space leased, the Government was in a strong bargaining position to secure a favourable lease package with exceptionally low rents.

Note 2: The RVD's average monthly rents for Kowloon Bay/Kwun Tong were only available from February 2013 onwards.

Managing periodic accommodation needs

3.7 ***Periodic accommodation needs for conducting elections.*** Within an election cycle, elections (including the District Council ordinary election, the LegCo general election, the Election Committee subsector ordinary elections, and the Chief Executive election) are held in succession, which normally straddle four to five financial years. The REO requires temporary offices in varying periods to accommodate additional staff employed to cope with the increased workload arising from the preparation and conduct of elections and related activities. As reported in Chapter 9 of the Director of Audit's Report No. 47 on "Provision of electoral services" in October 2006, the REO had used long-term leased accommodation to meet part of such periodic demand, resulting in under-utilisation of office space during

non-peak periods of an election cycle. In response to the audit recommendations, the REO used government-owned accommodation (the ex-Electrical and Mechanical Services Department depot and ex-Civil Aid Service HQs) for the 2010-13 election cycle. For the 2014-17 election cycle, Audit noted that the REO again used leased accommodation (in two office buildings in Kwun Tong at a total rental of \$2.6 million per month for different periods ranging from 36 months to 48 months) because the ex-Electrical and Mechanical Services Department depot and ex-Civil Aid Service HQs were not available. In June 2013, the GPA expressed concern that:

- (a) having considered the size, timing and period of the REO's requirement, there would be considerable difficulty to fully meet all the requirements in leased accommodation; and
- (b) the leasing option would incur expensive fitting-out costs repeatedly. The REO should examine whether it would construct its owned accommodation which could be used for multipurpose (e.g. storage space/indoor games hall). The REO could have full control of the premises and re-use the premises on short notice.

According to the GPA, since 2013, it had repeatedly advised the REO to approach the PlanD and the LandsD for site search for the construction of its own SDB to meet its operational needs.

3.8 According to the REO's AROA return for 2017-18 to 2020-21 submitted to the GPA in February 2017, it would have a surplus accommodation of 6,426 m² at the end of the 2014-17 election cycle (in 2017-18) which would require deleasing of office accommodation but an estimated shortfall of 18,529 m² (including 10,874 m² for temporary office and 7,655 m² for temporary storage) for the 2018-24 election cycle. In view of the need to conduct by-election in 2017-18, the REO informed the GPA in April 2017 its intention to renew the existing leases for 3,915 m² out of 6,426 m², which otherwise would expire in 2017 (Note 26).

3.9 ***Periodic accommodation need for conducting censuses.*** Similar to the REO, the C&SD's population census/by-census conducted every five years also require repeated use of short-term leased accommodation for the census staff.

Note 26: *Among the remaining area, the tenancy agreements for 862 m² expired in March 2017 and those for 1,649 m² would expire in December 2018.*

According to the C&SD's AROA return for 2017-18 to 2020-21, it would have a surplus accommodation of 1,917 m² (by phases from December 2016 to March 2018) which would require deleasing but an estimated shortfall of 7,000 m² in 2019 for conducting the 2021 population census.

3.10 *Need for other suitable accommodation arrangements.* Audit shared the GPA's concern on the practical difficulties and the recurring fitting-out costs for the use of short-term leased accommodation to meet the periodic accommodation needs of the REO and the C&SD. In Audit's view, there is a need for the REO and the C&SD, in consultation with the GPA, to explore the feasibility of developing a joint-user SDB in an under-utilised government site (see PART 4) for meeting the periodic accommodation requirements.

Need to improve deleasing arrangements of leased accommodation

3.11 As mentioned in paragraphs 1.11 and 3.2, the Government's accommodation policy is to reduce reliance on leasing. With the commissioning of new government-owned premises, there is an opportunity to relocate some offices in leased accommodation to achieve rental savings. Audit selected two planned deleasing cases (Cases 3 and 4) for examination and found room for improvement in the deleasing arrangements as illustrated in paragraphs 3.12 to 3.16.

3.12 *Case 3: Planned deleasing not realised.* Leased accommodation of 5,243 m² on four floors of a Grade A office building in Kowloon Bay under a single tenancy (Lease D) had been used by four sections of the SWD since December 2003. In 2006, the GPA invited the SWD to relocate the four sections to the new Trade and Industry Tower in Kai Tak (a JUB scheduled for completion in 2015). In 2008, the GPA confirmed that three sections (see Items 1 to 3 in Table 7) excluding the Central Casefile Depository (CCD) (see Item 4 in Table 7) could be relocated to the Trade and Industry Tower. The GPA continued to conduct site search for the relocation of the remaining CCD to other suitable premises. In February 2012, the SWD proposed to the GPA the relocation of the CCD to lower-cost accommodation in Kowloon and Kwai Chung in view of the continued increase of case files. The GPA considered that the SWD's reprovisioning proposal was not cost-effective because: (a) the rental for the SWD's existing premises in Kowloon Bay was on the lower side when compared with the premises in other districts; and (b) relocation from leased premises to other leased premises was not supported as it would incur double fitting-out costs. The GPA then asked the SWD to keep the CCD at the Kowloon Bay premises pending the

Administration of leased government offices

allocation of the space to be vacated by the other three sections in 2015 after their relocation to the new Trade and Industry Tower, to meet its additional space requirement.

Table 7

SWD sections located in a Grade A office building of Kowloon Bay

Item	User section (before commissioning of Trade and Industry Tower in 2015)	Area (m ²)	Current user section in 2017	Area (m ²)
1	Central Para-medical Support Service Unit	1,233	Project Development Office	923
	Special Investigation Section		Target Investigation Team	310
2	Supplies Section	242	CCD	4,010
3	Special Investigation Section	337		
4	CCD	3,431		
Total		5,243		5,243

Source: GPA records

Remarks: The current lease period is from December 2015 to December 2018.

3.13 In April 2013, the SWD proposed the relocation of the CCD again to a lower value location either on Hong Kong Island, in Kowloon or the New Territories in order to meet its imminent space requirement. The GPA rejected the reprovisioning proposal again based on similar consideration as mentioned in paragraph 3.12. In the event, after the relocation of the three SWD sections in mid-2015 (see para. 3.12), the vacated space was taken up by the CCD and two other sections of the SWD. Lease D was renewed for another three years (from December 2015 to December 2018). In late 2015, the GPA proposed and the SWD accepted reprovisioning of the CCD in a new government building then planned for completion in 2023 (see Case 1 in para. 2.24).

Administration of leased government offices

3.14 However, Audit noted from the GPIS records that there was leased accommodation used by other B/Ds for storage purposes at lower monthly rents, ranging from \$94 to \$147 per m² (see Table 8). In Audit's view, the use of some 76% (4,010 m² of the total area of 5,243 m²) of the Grade A office in Kowloon Bay (monthly rent of \$265 per m²) for the storage of case files by the CCD which does not have specific requirement to remain in Kowloon Bay is not good value for money. The GPA needs to meet the non-location-tied storage requirements of B/Ds in a more cost-effective manner.

Table 8

Examples of leased accommodation for storage purposes

Item	B/D	Location	Area (m ²)	Monthly rent (\$/m ²)	Current lease period
1	Government Record Service Office	Tuen Mun	6,989	94 105	10/2014 to 10/2017 9/2016 to 8/2019
2	Customs and Excise Department	Cheung Sha Wan	4,523	147	2/2016 to 2/2019

Source: Audit analysis of GPA records

3.15 **Case 4: Two leased premises left vacant.** In 2013, two sections of the LD occupying office areas of 344 m² and 159 m² in an office building in Quarry Bay under Leases E and F respectively were included in a relocation plan to a Financial Secretary Incorporated-held property in the first quarter of 2017. When considering renewal of the two leases in 2014, the LD requested the GPA to incorporate a break clause so that the actual lease period would tie in with the relocation. However, the GPA's efforts to negotiate with the landlord for a break clause in the leases were in vain. In the event, Leases E and F were renewed for a three-year fixed term (see Table 9). Audit noted that after the eventual relocation of the two sections in March 2017, the leased premises had been left vacant.

Table 9

**Two leased premises previously occupied
by the LD left vacant since March 2017
(September 2017)**

Lease	E	F
Area	344 m ²	159 m ²
Current lease period	18 November 2014 to 17 November 2017	29 May 2015 to 28 May 2018
Monthly net rent	\$141,230	\$67,180
Monthly management fee	\$28,898	\$13,522
Rental to be paid by (see Note 19 to para. 3.2(a))	GPA	LD

Source: GPA records

3.16 Audit examined the efforts made by the GPA to arrange short-term use of the vacant premises during the remaining period of Leases E and F and noted the following:

- (a) **Lease E.** Upon confirmation of the removal schedule in October 2016, the GPA did not issue a memo to invite B/Ds to bid for the vacant office. According to the GPA, action was taken to negotiate with the landlord for an earlier termination of lease. In January 2017, the GPA made a request for an early termination of the tenancy in March 2017 but was turned down by the landlord as there was no break clause under Lease E. After further negotiation, the landlord agreed in April 2017 to accept a lump sum payment of \$560,000 in lieu of reinstatement to be undertaken by the Government (estimated to cost \$1.4 million) and to take over the premises in October 2017. In May 2017, the GPA invited bids from B/Ds for using the vacant office but no B/Ds showed interest because of the short period of use (from May to October 2017) at such short notice. In the event, the leased area of 344 m² had been left vacant since April 2017 with nugatory expenditure in terms of rental and management fee amounting to \$170,000 per month; and

- (b) ***Lease F.*** In October 2016, the LD informed the GPA that the office under Lease F would be used by another section up to the end of February 2018 (i.e. three months before expiry of the tenancy for reinstatement of the premises) and no circulation to B/Ds was required. However, Audit site inspections on 18 and 30 August 2017 revealed that the office was still left vacant. The nugatory expenditure in terms of rental and management fee from April to August 2017 amounted to \$400,000.

According to the GPA Manual, case officers should consider whether de-leasing may result in nugatory rental payment or compensation to the landlord (see para. 3.2(b)(ii)). In Audit's view, the GPA should improve its planning of relocation of offices from leased accommodation (e.g. by identifying potential users at an early stage to take up vacated leased premises for any remaining lease period). To facilitate early termination of a lease to tie in with any relocation plan in future, the GPA needs to negotiate with the landlord on incorporating a break clause in the lease, and failing which, critically consider whether it is still appropriate to enter into/renew such lease or whether there is a need to look for better alternatives. For Lease F which will expire in May 2018, the GPA needs to urge the LD to put the vacant office into gainful use as soon as possible or release the office to meet any short-term need of other B/Ds.

Audit recommendations

3.17 Audit has *recommended* that the Government Property Administrator should:

- (a) **remind ADD staff to:**
 - (i) **document the reasons for rejecting/not recommending offers in the selection of premises for leasing office accommodation in accordance with the Divisional Instruction; and**
 - (ii) **explore suitable alternative premises with lower-rental implication before exercising option for lease renewal, and document the reasons for the decision taken in this regard;**
- (b) **meet the non-location-tied storage requirements of B/Ds (including the CCD) in a more cost-effective manner;**

- (c) **improve the planning for the relocation of offices from leased accommodation by:**
 - (i) **identifying potential users (e.g. by circulation to B/Ds) at an early stage to take up the vacated premises for any remaining lease period; and**
 - (ii) **negotiating with the landlord on incorporating a break clause in the lease, and failing which, critically considering whether it is still appropriate to enter into/renew such lease or whether there is a need to look for better alternatives; and**
- (d) **urge the Commissioner for Labour to put the vacant office under Lease F (see para. 3.16(b)) into gainful use as soon as possible or release the office to meet any short-term need of other B/Ds.**

3.18 **Audit has also *recommended* that the Chief Electoral Officer and the Commissioner for Census and Statistics should, in consultation with the Government Property Administrator, explore the feasibility of developing a joint-user SDB to meet their periodic accommodation requirements.**

Response from the Government

3.19 The Government Property Administrator generally agrees with the audit recommendations. He has said that:

- (a) before committing to lease or renew a lease for any particular premises, the GPA assesses the reasonableness of the offered rent of all cases by conducting a full rental valuation to take account of the special characteristics of the accommodation concerned, such as the location, building quality, size, accessibility, environmental characteristics, etc. These valuations have gone through a due process and are reviewed by the GPA's professional staff to ensure that they are properly carried out;
- (b) while the GPA accords priority to suitable premises with lower-rental implication when leasing new premises, exploring suitable premises with lower-rental implication is only one of the factors to be considered when

conducting a lease renewal. Whether a lease renewal warrants exploration of suitable alternative premises with lower-rental implication would depend on the circumstances of each case, e.g. the proposed rental package, availability of suitable alternative premises, economics of a new lease, etc. The GPA will remind staff to document the considerations before exercising option for a lease renewal and will consider how to implement the audit recommendation of exploring suitable alternative premises with lower-rental implication before exercising option for lease renewal (see para. 3.17(a)(ii)), having regard to a review of operational efficiency and work priorities;

- (c) regarding the audit recommendation in paragraph 3.17(c)(ii), the GPA has strived to secure a break clause in Lease E but the incorporation of such a clause is driven by the market and not entirely at the discretion of the GPA. The GPA will continue to exercise its professional judgment having considered all relevant factors to assess if it is worthwhile to enter into a lease without a break clause;
- (d) regarding the audit recommendation in paragraph 3.17(d), in October 2017, the GPA requested the LD to timely put the vacant office under Lease F into gainful use; and
- (e) regarding the audit recommendation in paragraph 3.18, the GPA will provide assistance to the REO and the C&SD in exploring the feasibility of developing a joint-user SDB.

3.20 The Chief Electoral Officer and the Commissioner for Census and Statistics agree with the audit recommendation in paragraph 3.18. The Chief Electoral Officer has said that the REO will explore with the GPA the feasibility of developing a joint-user SDB for meeting its periodic accommodation requirements having regard to its specific operational needs, including convenience to the public for voter registration and election-related activities, and suitable location for the processing, storage and delivery of electoral materials.

3.21 In the joint reply with the LD, the Secretary for Labour and Welfare has said that:

- (a) the vacated premises under Lease F in paragraph 3.16(b) were designated for use by the Task Force Team and the Claims Support Services Unit of the Employees' Compensation Division of the LD up to the end of February 2018. In the past months, they were yet to move to the vacant premises under Lease F in Quarry Bay because:
 - (i) it would be operationally inconvenient for the Task Force Team to provide secretariat support for meetings of the Task Force and its working groups held in the LD departmental HQs at Harbour Building, Central; and
 - (ii) the Claims Support Services Unit had to provide services to field offices in various locations (i.e. Southorn Centre, Cheung Sha Wan Government Offices, Tsuen Wan Government Offices and Sha Tin Government Offices); and
- (b) notwithstanding the above, the LD had worked out a plan to move the Team/Unit to the vacant premises under Lease F and was taking prompt action to install communication equipment thereat.

Relocating leased accommodation out of Central Business Districts

3.22 *Leased premises in CBDs.* As mentioned in paragraph 1.8(a), it is the Government's policy to decentralise general office space (i.e. those without specific location requirements) out of high-value areas located in the CBDs of Hong Kong Island and Kowloon, and to move the offices to lower-value areas which are well served by public transport. According to the GPA, leasing of office accommodation in the CBDs was very costly, in particular in core areas such as Central and Admiralty. Table 10 shows the areas of leased government offices in CBDs as of April 2017.

Table 10**Areas of leased government offices in CBDs
(April 2017)**

CBD	Area of leased offices (m²)
Sheung Wan	2,545
Central	228
Admiralty	1,368 (Note)
Wan Chai	17,667
Causeway Bay	337
Tsim Sha Tsui	4,341
Tsim Sha Tsui East	2,888
Total	29,374

Source: GPA records

Note: As of August 2017, the leased area in Admiralty decreased to 263 m² after releasing an office of 1,105 m².

3.23 Over the years, the GPA had made efforts to relocate leased government offices out of the CBDs, taking into account the justifications for retaining leased offices in CBDs put forth by B/Ds. According to the AROA returns submitted by B/Ds, the justifications for retaining leased offices in CBDs included:

- (a) location-bound to provide district or community services;
- (b) proximity to the B/Ds' HQs or related sections; and
- (c) other operational reasons.

In high-rental CBDs such as Central and Admiralty, the area of office premises leased by the Government had been reduced from 11,450 m² in 2006 to 1,596 (228+1,368) m² in April 2017 (see Table 10 in para. 3.22). As it is the Government's policy to decentralise general office space out of CBDs and to move the offices to lower rental areas, the GPA should continue its efforts to relocate the leased accommodation out of CBDs.

Need to continue assisting the SWD in relocating offices out of CBDs

3.24 As shown in Table 10 in paragraph 3.22, as of April 2017, among the CBDs, most leased government premises were located in Wan Chai. Audit noted that in 2012, the SWD had indicated its willingness to move its offices (including three sections occupying 1,581 m² in leased accommodation and its HQs occupying 6,878 m² in a Financial Secretary Incorporated-held property) out of Wan Chai but there was a need to co-locate one of the three sections (occupying 1,031 m²) with the HQs. Apart from advising the SWD to liaise with the PlanD for reserving a site for the planning of an SDB to meet its long-term accommodation needs (including releasing from CBDs), the GPA advised the SWD in November 2016 and March 2017 respectively to consider reprovisioning of its leased offices from Wan Chai to two planned facilities, one in Hung Hom and the other in Shum Shui Po. In September 2017, the SWD informed the GPA that it was considering including two of the three leased offices (occupying 550 m²) in Wan Chai in another planned project located outside CBDs. In line with the Government policy to relocate offices out of CBDs, the GPA needs to continue assisting the SWD in identifying suitable accommodation for meeting its relocation requirements.

Audit recommendation

3.25 **Audit has recommended that the Government Property Administrator should continue to assist the SWD in identifying suitable accommodation for meeting its relocation requirements out of Wan Chai.**

Response from the Government

3.26 The Government Property Administrator agrees with the audit recommendation.

PART 4: UTILISATION OF GOVERNMENT SITES

4.1 This PART examines the Government's efforts in improving the utilisation of government sites, focusing on:

- (a) identification of under-utilised government sites for optimal development (paras. 4.2 to 4.21); and
- (b) utilisation of vacant or under-utilised specialist and departmental accommodation (paras. 4.22 to 4.29).

Identification of under-utilised government sites for optimal development

4.2 Land is a valuable asset. The Government is facing competing demands for land for housing and other purposes. According to the Government's land policy, government sites must be developed to the fullest extent possible or put to the best use. The GPA is responsible for overseeing the government accommodation usage with a view to optimising the utilisation of government sites and surplus properties with potential for alternative government uses or commercialisation. In the 2004 audit review, Audit recommended that the Secretary for the Financial Services and the Treasury should ask the PSG to take stock of what needed to be done on the under-utilised government sites and review its strategy and set targets for optimising the utilisation of government sites. In response, the PSG reviewed its strategy for ensuring the optimal utilisation of government sites and held regular meetings to enhance the utilisation of government sites. In November 2010, the Government refined its strategy by adopting a targeted approach to identify government sites that were under-utilised, involving the GPA, the PlanD and the PSG which were tasked with different roles. According to a memorandum issued by the FSTB in November 2010:

- (a) the PlanD and the GPA would, on an annual basis, jointly identify for the PSG's consideration a number of priority sites for release having regard to, among others, the alternative use and redevelopment need/potential of the government sites, the extent of their under-utilisation and the condition of existing facilities;

- (b) subject to the PSG's endorsement of the priority sites identified in (a), B/Ds occupying the identified sites would be tasked to lead and oversee the planning and delivery of reprovisioning projects, with participation from the PlanD and the GPA as appropriate. The PlanD would identify alternative sites for reprovisioning of facilities. The GPA would advise on site-utilisation matters and identify partners to jointly develop the site or alternative premises for reprovisioning; and
- (c) the lead B/Ds would be requested to provide the PSG with progress reports on the reprovisioning exercises. The PSG would maintain an oversight of the progress and provide a steer on unresolved issues. The PSG would also consider and prioritise the reprovisioning projects.

Site-utilisation reviews

4.3 Since 2013, the SUD has selected 85 sites (17 by each of its 5 teams responsible for different areas) each year for conducting site-utilisation reviews to identify under-utilised government sites for redevelopment, alternative uses or disposal options with a view to optimising their utilisation. For each site, the SUD examines its existing uses, redevelopment potential, disposal options and reprovisioning requirements. According to the GPA Manual, the following factors will be considered:

- (a) sites with low utilisation ratio (Note 27);
- (b) sites located in valuable urban area;
- (c) sites with old or obsolete structures;
- (d) an occupier who is willing or able to be relocated;

Note 27: *The actual utilisation ratios of existing sites as against those recorded in GPIS will be known when there is a detailed proposal for redevelopment (see Note to Table 11 in para. 4.8).*

Utilisation of government sites

- (e) the capability to be rezoned and sold or to accommodate a higher development capacity for G/IC use; and
- (f) demand for the site.

On a cross-B/D level, the PSG serves as a forum to deal with utilisation of government sites.

4.4 After identification of potential sites, the GPA will refer them to the PlanD for planning assessment which may include advice on possible alternative long-term uses and redevelopment need/potential of the government sites. The PlanD will conduct assessment for each site on the land use planning and development proposal based on parameters such as plot ratios and building height control (i.e. planning assessment). Upon receipt of the PlanD's comments, the GPA will review redevelopment/reprovisioning proposals for shortlisted sites and submit them to the PSG for endorsement. The PSG will monitor the progress and provide a steer on unresolved issues.

4.5 The GPA maintains records of government sites in the GPIS (see para. 1.13), including information on site areas and utilisation ratios. According to the GPA, of the 3,794 sites in the GPIS, 1,793 sites were excluded from the site-utilisation reviews (Note 28). The status of the remaining 2,001 sites as of May 2017 was as follows:

- (a) 25 were under monitoring by the PSG;
- (b) 322 had been reviewed by the GPA (with the PlanD's assistance) from 2012 to 2016; and
- (c) 1,654 had yet to be reviewed.

Note 28: *These included: (a) 904 reserved sites (e.g. vacant school premises sites) for which the DEVB issued a circular in 2016 requesting the B/Ds concerned to periodically review and confirm their need for retaining these sites; (b) 508 sites classified as low-priority sites due to reprovisioning difficulties; and (c) 381 sites with an area less than 500 m² each and limited development potential.*

Identification of under-utilised government sites from 2011 to 2015

4.6 ***Six priority sites identified in 2011.*** Based on the GPA's utilisation review of 109 sites completed in 2010 and the PlanD's planning assessment, the GPA and the PlanD jointly identified six priority sites which were subsequently endorsed by the PSG for redevelopment. These six sites (3 G/IC sites and 3 departmental-quarters sites — see Items 1 to 6 in Table 11 of para. 4.8) were identified on the basis of the site utilisation information in the GPA's progress report submitted to the PSG in August 2010 and the PlanD's latest review of existing G/IC sites in July 2010, taking into account the need for according a higher priority to:

- (a) under-utilised sites that had development potential for residential use as there was an imminent need for housing sites;
- (b) under-utilised sites that were located in close proximity, thus possessing greater potential for consolidation in reprovisioning and releasing some existing sites for alternative suitable uses; and
- (c) sites not requiring reprovisioning or with more flexible reprovisioning requirements.

4.7 ***12 priority sites identified from 2012 to 2015.*** In the site-utilisation reviews conducted from 2012 to 2015, the SUD further examined 356 sites (Note 29) and referred 350 sites to the PlanD for planning assessment (see para. 4.4). Based on the planning assessment results of the 267 sites (Note 30), the GPA drew up redevelopment proposals for 12 sites for the PSG's consideration, with 8 redevelopment proposals subsequently endorsed by the PSG from 2014 to 2017 (see Table 11 in para. 4.8).

Note 29: *From 2012 to 2016, the GPA completed reviews of 441 sites (356 from 2012 to 2015 (see para. 4.7) + 85 in 2016 (see para. 4.11)), including 119 sites which were subsequently classified as low-priority sites (see Note 28 to para. 4.5) and excluded from the 322 reviewed cases referred to in paragraph 4.5(b)).*

Note 30: *The PlanD had not carried out planning assessment for 83 of the 350 sites mainly because they had been identified for alternative uses, covered by other planning studies or monitored by the PSG.*

Progress of redevelopment of under-utilised sites monitored by the PSG

4.8 ***Progress of redevelopment of 14 under-utilised sites endorsed by the PSG.*** Of the 18 under-utilised government sites identified in the site-utilisation reviews from 2011 to 2015 (see paras. 4.6 and 4.7), 14 were endorsed for redevelopment by the PSG. Audit examined the redevelopment progress of these 14 sites (see Table 11) and noted that as of June 2017:

- (a) 1 site had been released for redevelopment (see Item 6 in Table 11);
- (b) 11 sites were under planning; and
- (c) 2 sites were accorded a low priority for redevelopment (see Items 4 and 5 in Table 11).

Table 11

**Progress of redevelopment of 14 under-utilised sites
endorsed by the PSG
(June 2017)**

Item	Site	Site area (m ²)	Utilisation ratio (Note)	Date of endorsement by PSG	Progress as of June 2017
6 sites identified in 2011					
1	Lui Kee Education Services Centre, Wan Chai	1,320	40%	January 2011	The site was zoned for residential use on the draft Wan Chai Outline Zoning Plan (OZP). The implementation of the proposed residential use was pending the resolution of three outstanding judicial reviews on the draft Wan Chai OZP. The Education Bureau and the GPA would continue to arrange temporary uses of the existing building.
2	Lady Trench Training Centre, Wan Chai	1,330	21%	January 2011	The ArchSD was preparing a revised proposal which would further optimise the site utilisation, with the support of relevant technical assessments for the reprovisioning of the Wan Chai Polyclinic (Item 3). The PlanD would process the planning application for the proposal.
3	Wan Chai Polyclinic, Wan Chai	1,248	42%	January 2011	The site was zoned for residential use on the draft Wan Chai OZP. The implementation of the proposed residential use was pending the reprovisioning of facilities to nearby site (see Item 2) and the resolution of three outstanding judicial reviews on the draft Wan Chai OZP.
4	Ho Man Tin Hill Road Government Quarters, Kowloon City	6,354	37%	January 2011	The site was subsequently accorded a low priority for redevelopment.

Utilisation of government sites

Table 11 (Cont'd)

Item	Site	Site area (m ²)	Utilisation ratio (Note)	Date of endorsement by PSG	Progress as of June 2017
5	Ha Hang Government Staff Quarters, Tai Po	1,885	78.26%	January 2011	The site was subsequently accorded a low priority for redevelopment.
6	650 Cheung Sha Wan Road, Cheung Sha Wan	1,500	65%	January 2011	The site was sold in April 2014.
8 sites identified from 2012 to 2015					
7	Shek Wu Hui Post Office, Sheung Shui	838	10.1 %	April 2014	With the pertinent Post Office identified by the GPA for relocation, the Hongkong Post requested the Housing Authority to consider incorporating a Post Office into the proposed public housing developments in Sheung Shui. Under the on-going planning and engineering study for rezoning of land for the public housing developments, the Housing Authority was exploring the feasibility of incorporating the Post Office for technical studies and planning brief. The study was targeted for completion in early 2018.
8	Ex-Harbour Hydraulics Laboratory, Tuen Mun (Case 5)	6,860	7.29%	August 2015	An alternative site was being identified for storing the museum exhibits of the LCSD and for reprovisioning the museum workshops.
9	Tuen Mun Clinic, Tuen Mun	4,400	12.11%	August 2015	B/Ds concerned were exploring the redevelopment of the Tuen Mun Clinic Site. Initial assessment on proposed facilities to be accommodated was being coordinated by the GPA.

Utilisation of government sites

Table 11 (Cont'd)

Item	Site	Site area (m ²)	Utilisation ratio (Note)	Date of endorsement by PSG	Progress as of June 2017
10	HyD's Depot and Training Centre Site, Hung Hom	2,054	34.15%	July 2016	The accommodation requirements from B/Ds' office use were being discussed by the GPA and the B/Ds concerned.
11	Tai Po Government Offices, Tai Po	6,484	25.45%	December 2016	Since the facilities in Wong Siu Ching Clinic (Item 12) would not be relocated to the Tai Po Government Offices, there was no imminent need to put forward a comprehensive redevelopment proposal.
12	Wong Siu Ching Clinic, Tai Po	2,599	24.11%	December 2016	The GPA would monitor the progress of reprovisioning the clinical facilities at the site.
13	Madam Yung Fung Shee Health Centre, Yuen Long	2,576	21.58%	July 2017	The GPA would follow up with the PlanD and the ArchSD for detailed assessment on the redevelopment proposal.
14	Yuen Long District Office Building and Clinic, Yuen Long	10,210	8.06%	July 2017	

Source: GPA records

Note: Utilisation ratio = $\frac{\text{Existing GFA}}{\text{Maximum GFA allowed to be built}^} \times 100\%$*

** According to the GPA, maximum GFA was based on statutory planning restrictions or the PlanD's advice, or if such information was not available, an estimation with reference to the development density of adjacent private land.*

4.9 Audit examination. Among the 11 sites under planning, Audit selected the ex-Harbour Hydraulics Laboratory (see Item 8 in Table 11 of para. 4.8) with the lowest site utilisation rate for case study (see Case 5).

Case 5

Ex-Harbour Hydraulics Laboratory site in Tuen Mun

1. The ex-Harbour Hydraulics Laboratory located at the west of Tuen Mun near Pillar Point occupies a site area of 6,860 m². The laboratory itself is a single-storey building with a floor area of about 2,500 m² (see Photograph 1). In 2001, the then Civil Engineering Department (now the CEDD) ceased operation of the laboratory and returned the building to the GPA. In March 2003, the GPA allocated the vacated building to the LCSD for storage of museum collections. Part of the site was also used as a workshop and storage for the Hong Kong Science Museum and the Space Museum.

Photograph 1

Ex-Harbour Hydraulics Laboratory used by the LCSD for storage



Source: Photograph taken by Audit staff on 25 August 2017

2. In the 2014 site-utilisation review, the site was identified by the GPA as a priority site for redevelopment. In August 2015, the PSG endorsed the GPA's proposal to develop the site as a government storage centre so as to maximise the site utilisation (Note 1). In December 2015, the GPA reported to the PSG that there was scope to enhance the site utilisation through a joint development of the subject site and an adjacent site, namely the Tuen Mun Government Depot, which was used mainly by the Electrical and Mechanical Services Department for vehicle maintenance and other departments for storage purposes.

Case 5 (Cont'd)

3. In September and December 2016, the GPA informed the LCSD that:

- (a) the redevelopment proposal could offer a total floor area of about 18,300 m². Taking into account the users' space requirements of 14,900 m² (Note 2), there would be a surplus space of about 3,400 m² available for further allocation; and
- (b) the LCSD as the "owner" department of the ex-Harbour Hydraulics Laboratory had the primary responsibility to ensure the optimal utilisation of the site. The LCSD should take up the role of a project proponent.

4. In March 2017, the LCSD informed the GPA that it had reservations on assuming the project proponent role for the redevelopment. At its meeting of April 2017, the PSG noted that the proposed redevelopment of the site would hinge on the LCSD's reprovisioning plan of the museum collections (see Note 1). The PSG then requested the GPA to explore an alternative reprovisioning site in the interim. As of June 2017, the GPA was exploring the possibility of reprovisioning the LCSD's museum collections to the Siu Ho Wan Government Depot.

Audit comments

5. As of September 2017, two years after the endorsement of the redevelopment proposal by the PSG in 2015, a project proponent had not yet been determined. In this connection, Audit noted a similar problem in identifying a project proponent for another PSG-endorsed redevelopment project (see Item 10 in Table 11 of para. 4.8). According to the Accommodation Regulations, for multi-user SDBs: (a) the major user department should perform the role of the project proponent; (b) where there is no major user department, all user departments should agree on the designation of a lead department as the project proponent; and (c) if no consensus can be reached, they should escalate the issue to the policy bureaux concerned for a decision. In accordance with the circular memorandum issued by the FSTB in November 2010, the GPA should consider seeking the PSG's steer on project proponent disputes at an appropriate juncture (see para. 4.2(c)), and invite the user departments to seek their policy bureaux'

Case 5 (Cont'd)

decisions having regard to the PSG's views if the issue remains unresolved after the PSG's intervention. In addition, the GPA needs to expedite action in assisting the LCSD in identifying a reprovisioning site for the museum collections.

Source: Audit analysis of GPA records

Note 1: According to the PSG paper of August 2015, the LCSD had no objection to the redevelopment proposal provided that: (a) the museum collections could be relocated to the planned Heritage Conservation and Resource Centre; and (b) alternative accommodation could be provided for reprovisioning the workshop and storage for the Science Museum and the Space Museum. Based on the GPA's assessment, the workshop and storage of the two museums could be reprovisioned in-situ through phased redevelopment.

Note 2: According to the LCSD, it would take up 5,400 m² (36%) of the 14,900 m². The remaining 9,500 m² (64%) would be taken up by other government departments.

4.10 ***Other referral sites under the monitoring of the PSG.*** Other than the sites identified by the GPA's site-utilisation reviews, the Committee on Planning and Land Development (CPLD — Note 31) and PSG members may also refer potential sites to the PSG for consideration. As of June 2017, there were 11 such cases under the monitoring of the PSG (see Appendix D). Among these 11 cases, Audit has reviewed one case (Case 6) relating to a godown acquired by the Government in early 1990s which had been left vacant since 2008.

Note 31: *The CPLD is chaired by the Secretary for Development and comprises representatives from the relevant B/Ds as members. One of its functions is to consider and review policies on production, acquisition, use and disposal of land.*

Case 6

A government-owned godown at No. 5-7 Yip Shing Street, Kwai Chung

1. The subject godown is a four-storey building with a floor area of about 4,562 m² (see Photograph 2). The godown occupying a site area of about 1,505 m² was previously privately-owned. It is at present unallocated government land mainly falling within an area shown as “Road” on the draft Kwai Chung OZP.

Photograph 2

Vacant godown in Kwai Chung



Source: Photograph taken by Audit staff on 25 August 2017

2. **Acquisition of the godown site.** According to the recommendation of a transport study for Tsuen Wan completed in 1983, the preferred option of a proposed Kwai Chung Circumferential Road (road project) would require resumption of the godown site. In 1987, the godown owner raised objection to the routing of the Kwai Chung Circumferential Road and indicated that he planned to redevelop the site. The then Territory Development Department (TDD —Note 1) informed the LandsD in 1988 that although the implementation programme of the proposed road project had yet to be confirmed, it shared the LandsD’s view that acquiring the godown site before it was redeveloped to a higher density development was the most economical option. In July 1989, the

Case 6 (Cont'd)

proposed Kwai Chung Circumferential Road was incorporated in the pertinent OZP forming a statutory basis for preservation of the road route and for continued negotiation with the godown owner. In 1990, the godown owner surrendered the godown site together with a premium payment assessed at full market value of \$5 million in exchange for the grant of another site in Kwai Chung of about 1,875 m².

3. In March 1991 the Government took possession of the godown site. The godown site was subsequently handed over to the GPA for management. In 1994, in response to the GPA's enquiry, the TDD said that the project was scheduled to commence in 1998-99 for completion in 2001-02. In March 1995, the TDD informed the GPA that there was no definite programme for the road project and suggested that the TD comment on the potential need of the project. In April 1995, the TD informed the GPA that there was no fixed programme for the road project in the next five years. From 1999 to 2002, the TDD and the TD discussed the need for the road project (Note 2).

4. *Interim use.* From 1991 to 2007, the GPA leased out the godown in the market for industrial use or use as a non-dangerous goods logistics centre. Thereafter, the building was too dilapidated for short-term uses. Over the years, various B/Ds had expressed interest in using the godown as storage, data centre and file repository. However, they all withdrew their proposals after considering the costs involved, the requirements for conducting a traffic study, the need for rezoning the site and the uncertainty of occupation period.

5. In April 2012, in response to the GPA's enquiry for using the site as a new data centre, the TD advised that although there would be no need for the road project, the project proponent of the new data centre should carry out studies and arrange the necessary amendment to the relevant OZP (see para. 1). In November 2012, the GPA informed the PSG that the site was substantially under-utilised and should the site be rezoned to "Industrial" use, the development potential (the maximum plot ratio could be revised from 3 to 9.5) would increase. The PSG then requested the TD to carry out a broad assessment which confirmed that there was no immediate need for the road project. In October 2014, the TD confirmed to the GPA again that there was no need for the road project up to 2026 and the CEDD (see Note 1) said that there was no active project at that location. In May 2017, the ArchSD obtained funding for demolishing the godown and the demolition works were planned to commence before November 2017.

Case 6 (Cont'd)

Audit comments

6. Audit considers it unsatisfactory that some 26 years after acquiring the godown in 1990, no decision had been taken on whether the proposed road project would be implemented. While the GPA had put the godown into short-term uses from 1991 to 2007, it had been left vacant for some 10 years up to August 2017. In Audit's view, the Transport and Housing Bureau needs to task the TD to review whether there is still a need from the transport planning perspective to implement the road project and if not, release the site for other uses as soon as possible. To prevent recurrence of similar problem, the CEDD, in consultation with the DEVB, also needs to consider issuing guidelines reminding project offices to acquire sites/properties for their projects after confirming the project implementation programmes. Where there are exceptional circumstances warranting the acquisition of a site/property before there is a firm project implementation programme, the project offices should keep the project under regular review to ensure the best use of the acquired site/property.

Source: Audit analysis of GPA records

Note 1: In July 2004, the former Civil Engineering Department and the former TDD merged into the CEDD.

Note 2: In July 1999, the TDD informed the TD that if the road project should remain indefinite, it should be deleted from the OZP. In 2000, the TD informed the TDD that in view of the high project cost and the potential environmental impact of a long elevated road from Kwai Chung Road to Castle Peak Road, the TD was doubtful of its chance of getting policy/funding support even for conducting a feasibility study and decided to shelve the project for the time being. In 2002, the TD said that there was no implementation programme for the road project.

Shortlisted sites in the 2016 site-utilisation reviews

4.11 Same as previous years, the SUD selected 85 sites for studies in the 2016 site-utilisation reviews. In July 2016, the GPA referred 28 sites to the PlanD for planning assessment with a view to recommending priority sites for the PSG's consideration by October 2016. After reviewing the planning assessment results of all the 28 sites provided by the PlanD in September 2016, the GPA shortlisted 15 sites for examination (see Table 12).

Table 12

15 shortlisted sites in 2016 site-utilisation reviews

Item	Site	Site area (m ²)	Utilisation ratio per GPIS	Scope for increasing building height/intensity as assessed by PlanD
1	Public Open Carpark and Bus Terminus at Fung Nam Road, North District	7,251	0 %	Yes (minor increase)
2	Kai Tak Airport Sewage Pumping Station and Open Carparks, Wang Kwong Road (South Portion)	6,670	0 %	Yes
3	DSD Sham Shui Po Nos.1 and 2 Sewage Screening Plant, South West Kowloon Reclamation Area	5,031	97.85 %	No
4	Former reserved G/IC site for Parking Area, Tai Yip Street, Kwun Tong	4,901	0 %	N/A (Note)
5	Tsz Wan Shan Yuk Wah Street Bus Terminus and Open Carpark	3,355	0 % (Bus Terminus) 0 % (Open Carpark)	Yes (minor increase)
6	Ap Lei Chau Sewage Screening Plant, Lee Nam Road	2,561	100 %	No
7	Wing Shun Street HyD Maintenance Depot, Kwai Chung	2,238	61 %	Yes (minor increase)
8	Car Park (Open) at Man Tung Road, Lantau Island	2,079	100 %	No
9	HyD Depot and ArchSD's Works Area, Heung Yip Road	2,044	0 %	No
10	Kai Tak Airport Sewage Pumping Station and Open Carparks, Wang Kwong Road (Middle Portion)	913	100 %	No
11	Kwai Fong Community Hall, Lai Fong Street	896	27.95 %	Yes
12	DSD Wah Fu Sewage Screening Plant, Waterfall Bay Road	875	100 %	No

Table 12 (Cont'd)

Item	Site	Site area (m ²)	Utilisation ratio per GPIS	Scope for increasing building height/intensity as assessed by PlanD
13	Reserved Waterworks Depot, Cheung Tung Road, Tung Chung	654	0%	Yes (minor increase)
14	Kai Tak Airport Sewage Pumping Station and Open Car parks, Wang Kwong Road (North Portion)	573	0%	Yes
15	DSD Mui Wo Sewage Pumping Station, Ngan Kwong Wan Road	556	100%	No

Source: GPA records

Note: Site committed for alternative use and taken out from planning assessment.

4.12 ***Need to document the justifications for site selection.*** According to the GPA, the objective of the site-utilisation reviews was to release G/IC sites for optimum development. In September 2017, in response to Audit's enquiry on the status of the 15 shortlisted sites (para. 4.11), the GPA said that 4 sites (Items 1, 3, 7 and 10 in Table 12 of para. 4.11) had been selected for further action. However, there were no documented justifications for selecting the 4 sites. Audit noted that the 4 sites had included 2 sites with a utilisation ratio exceeding 90% each and assessed by the PlanD as not having scope for increasing development intensity (Items 3 and 10 in Table 12 of para. 4.11). On the other hand, 2 of the remaining 11 sites with a utilisation ratio of 0% each and scope for increasing the existing building height up to the statutory restriction (Items 2 and 14 in Table 12 of para. 4.11) were not selected for further action.

4.13 In October 2017, the GPA informed Audit that:

- (a) the two DSD's sewage screening plant/pumping station (Items 3 and 10 in Table 12 of para. 4.11) warranted further studies despite the high utilisation ratios in light of the successful new initiative of relocating DSD offices to a sewage pumping station in Kowloon (see Case 1 in para. 2.24); and

Utilisation of government sites

- (b) as regards the two sites with a utilisation ratio of 0% (Items 2 and 14 in Table 12 of para. 4.11), the former had been earmarked for another purpose by a B/D, whereas in the latter, there were constraints in realising its development potential in view of its elongated shape, the existence of a drainage reserve and the need for reserving an access road in the site.

In Audit's view, the GPA needs to document the justifications for selecting sites for site-utilisation reviews.

4.14 *Need to set priority in selecting sites for site-utilisation reviews.* As mentioned in paragraph 4.3, each of the SUD's 5 teams selects annually 17 government sites, making a total of 85 sites for conducting site-utilisation reviews to identify under-utilised sites in accordance with the guidelines specified in the GPA Manual. In May 2017, the SUD commenced another 85 site-utilisation reviews for 2017. As of August 2017, there were 1,569 (1,654 less 85) sites pending site-utilisation reviews by the GPA, which would take a long time to complete the reviews. In Audit's view, the GPA needs to set priority in selecting sites with better development potential for review and follow-up action.

Maintenance of GPIS records

4.15 *Omissions and discrepancies in GPIS records.* The computerised database was developed in 2000 and revamped into the GPIS in 2013 to record the government-owned site, building and premises information in a database (see para. 1.13). The GPIS captured relevant information such as existing GFA and maximum plot ratio, and could generate management reports based on different sorting criteria. Audit sample check revealed that there were omissions and discrepancies, as follows:

- (a) the pertinent site and building records of an unusable property at 405-406 Victoria Road, Mount Davis were missing;
- (b) site information of eight premises/buildings was missing (see Table 13); and

Table 13

**Premises/buildings without site information recorded in the GPIS
(July 2017)**

Item	Premises
1	Cyberport Sewage Treatment Works
2	Sai Ying Pun Jockey Club General Out-patient Clinic
3	Luard Road Refuse Collection Point
4	Gloucester Road Refuse Collection Point
5	Tai Po Tau Water Treatment Works Filtration Plant Building
6	Pak Tin Bungalow (currently used as a social welfare facility)
7	Lower Shing Mun Bungalow (currently used as an office)
8	Lower Shing Mun Village Refuse Collection Point

Source: GPA records

- (c) the status of some government sites was not up-to-date. Examples included:
- (i) the Harbour Road Sport Centre (3 storeys) and the Wan Chai Swimming Pool (Outdoor) which had been demolished for railway development;
 - (ii) Yuet Wah Street Bus Terminus which had been redeveloped into private residential use; and
 - (iii) Kwun Tong District Branch Office and Hip Wo Street Hawker Bazaar which had been demolished for urban redevelopment.

4.16 The GPIS is instrumental in maintaining proper government-owned site, building and premises information which will assist the GPA to identify under-utilised sites. Audit considers that the GPA needs to take measures to ensure that information recorded in the GPIS is accurate and up-to-date.

Audit recommendations

4.17 **Audit has *recommended* that the Government Property Administrator should:**

- (a) **for the redevelopment of the ex-Harbour Hydraulics Laboratory site in Tuen Mun (i.e. Case 5 in para. 4.9):**
 - (i) **seek the steer of the PSG on the unresolved issue of identifying a project proponent and invite the relevant departments to consult their policy bureaux for a decision having regard to the PSG's views if the issue remains unresolved after the PSG's intervention; and**
 - (ii) **expedite action in assisting the LCSD to identify a reprovisioning site for its museum collections in order to speed up the site redevelopment;**
- (b) **maintain records of justifications for selecting government sites for site-utilisation review;**
- (c) **for the 1,569 government sites pending site-utilisation reviews (see para. 4.14), set priority in selecting sites with better development potential for review and follow-up action; and**
- (d) **take measures to ensure that information recorded in the GPIS is accurate and up-to-date.**

4.18 **Audit has also *recommended* that:**

- (a) **the Secretary for Transport and Housing should task the Commissioner for Transport to review whether there is still a need to implement the Kwai Chung Circumferential Road project and if not, release the site for other uses as soon as possible; and**
- (b) **the Director of Civil Engineering and Development should, in consultation with the Secretary for Development:**

- (i) **consider issuing guidelines reminding project offices to acquire sites/properties for their projects after confirming the project implementation programmes; and**
- (ii) **if there are exceptional circumstances warranting the acquisition of a site/property before there is a firm project implementation programme, keep the project under regular review to ensure the best use of the acquired site/property.**

Response from the Government

4.19 The Government Property Administrator agrees with the audit recommendations in paragraph 4.17. He has said that:

- (a) starting from the 2017 site-utilisation review, the GPA has documented the justifications on selecting sites and drawn up guidelines to facilitate the setting of priority in selecting sites with better development potential; and
- (b) the utilisation of a site depends on a range of factors including land use, zoning, topography, availability of vehicular access, reprovisioning feasibility, presence of conservation elements, changes to neighbouring developments, etc. Selection of suitable sites for review involves a holistic consideration of a combination of factors mentioned in paragraph 4.3 and cannot rely simply on one or two factors such as the utilisation ratio or potential for increasing building height.

4.20 The Secretary for Transport and Housing agrees with the audit recommendation in paragraph 4.18(a). The Commissioner for Transport has said that, since 1995, the TD had been informing the GPA that there was no fixed programme for the proposed road project.

4.21 The Secretary for Development and the Director of Civil Engineering and Development agree with the audit recommendation in paragraph 4.18(b).

Utilisation of vacant or under-utilised specialist and departmental accommodation

4.22 ***Surplus accommodation.*** In the 2008 audit review (see para. 1.14), Audit urged the PSG to provide the GPA with strategic direction and support for handling surplus SDBs. In April 2008, the GPA promulgated a circular setting out the arrangements for handling surplus SDBs as agreed by the PSG, which have been incorporated in the Accommodation Regulations, as follows:

- (a) ***Options of alternative use.*** The GPA will consider and decide the alternative use of surplus JUBs or leased premises. Other surplus specialist and departmental accommodation (without long-term use) under the purview of individual B/Ds should be put to gainful use in the following order of priorities:
 - (i) interim alternative use within the Government;
 - (ii) commercialisation; and
 - (iii) direct leasing supported by pertinent B/Ds.

Where appropriate and justified, B/Ds may also consider and explore sale or demolition as the ultimate option of dealing with the surplus accommodation or buildings;

- (b) ***JUBs and leased premises.*** For JUBs or leased premises, departments should notify the GPA upon identifying any part or whole of their accommodation which is or will become surplus in the short or long-term. The GPA will consider and decide whether any alternative use of such surplus accommodation should be approved; and
- (c) ***SDBs.*** The proponent/user departments of SDBs have the primary responsibility and are accountable for the proper use and optimal utilisation of their accommodation. They should explore and exhaust possible alternative uses within the respective departments before considering giving up the surplus accommodation. If no new user departments can be identified to take over the whole surplus accommodation and assume the role of the land allocatees or the owner department, the original

proponent/user department shall remain as the owner of the surplus accommodation responsible for all matters arising directly or indirectly from it. As the allocatees of an accommodation, the proponent/user departments may request the GPA to assist in identifying other departments to make long-term use of their surplus accommodation.

4.23 The GPA regularly reports to the PSG on a half-yearly basis the position of vacant or under-utilised premises of specialist and departmental accommodation under the purview of individual B/Ds (which were surplus to their requirements). According to the GPA's progress report of April 2017, as of February 2017, there were 27 such vacant or under-utilised premises of specialist and departmental accommodation. Among the 27 premises:

- (a) one had a floor area of 6,852 m² (an ex-secondary school in Mui Wo, Lantau). The ex-school site had been left vacant for more than 5 years and in 2016, the CPLD considered that the future use of the site should be reviewed upon the publication of Lantau Development and Conservation Blueprint for Lantau in 2017 (Note 32). According to the Education Bureau, it had informed the PlanD and other relevant departments (including the LandsD and the GPA) for their consideration of other suitable alternative long-term uses of the vacant school premises under the established mechanism in handling these premises; and
- (b) 26 each had a floor area of less than 500 m². Most of them were vacant staff quarters in remote locations. In terms of vacant period:
 - (i) 19 (73%), including the 6 historic buildings with preservation value (1 declared monuments by the Antiquities Authority and 5 graded buildings by the Antiquities Advisory Board) had been left vacant for over 5 years; and
 - (ii) the remaining 7 (27%) had been left vacant for 5 years or less.

Note 32: *In June 2017, the Blueprint was published which stated that Mui Wo could be revitalised as an enhanced township with small amount of low-density residential developments as well as recreational and tourism-related uses.*

Utilisation of government sites

4.24 To assist the pertinent B/Ds in identifying alternative uses, upon request, the GPA circulates on a quarterly basis surplus specialist and departmental accommodation to B/Ds for identifying possible permanent and temporary uses. Apart from circulating such accommodation to B/Ds, the GPA also posted on its website in March and August 2017 the information of 13 of the 27 vacant or under-utilised premises (including the 6 historic buildings) for bidding by the non-governmental organisations. However, as of August 2017, none of these 13 premises had been allocated to B/Ds or non-governmental organisations for use.

4.25 According to the Accommodation Regulations, if no users can be identified for surplus specialist and departmental accommodation, the original proponent/user department shall remain as the owner of the surplus accommodation responsible for all matters arising directly or indirectly from it (see para. 4.22(c)). Given that no alternative use for the 27 vacant or under-utilised premises within the Government could be identified despite efforts made by the GPA, the relevant B/Ds need to explore other measures to put the premises into gainful use in accordance with the requirements of the Accommodation Regulations (i.e. commercialisation, direct leasing and sale or demolition where permitted (see para. 4.22(a)), seeking the assistance from the GPA if required.

4.26 According to the progress report of April 2017 (see para. 4.23), there were four unusable properties (with floor areas ranging from 105 m² to 1,212 m²). They were classified as condemned buildings pending review/demolition. The GPA should, in collaboration with the PlanD and the relevant owner B/Ds, determine the long-term use of the sites, and work out a suitable disposal option in accordance with the Accommodation Regulations (e.g. sale or demolition).

Audit recommendations

4.27 **Audit has *recommended* that the Government Property Administrator should:**

- (a) **remind relevant B/Ds to explore other measures to put the 27 vacant or under-utilised premises of specialist and departmental accommodation into gainful use in accordance with the requirements of the Accommodation Regulations; and**

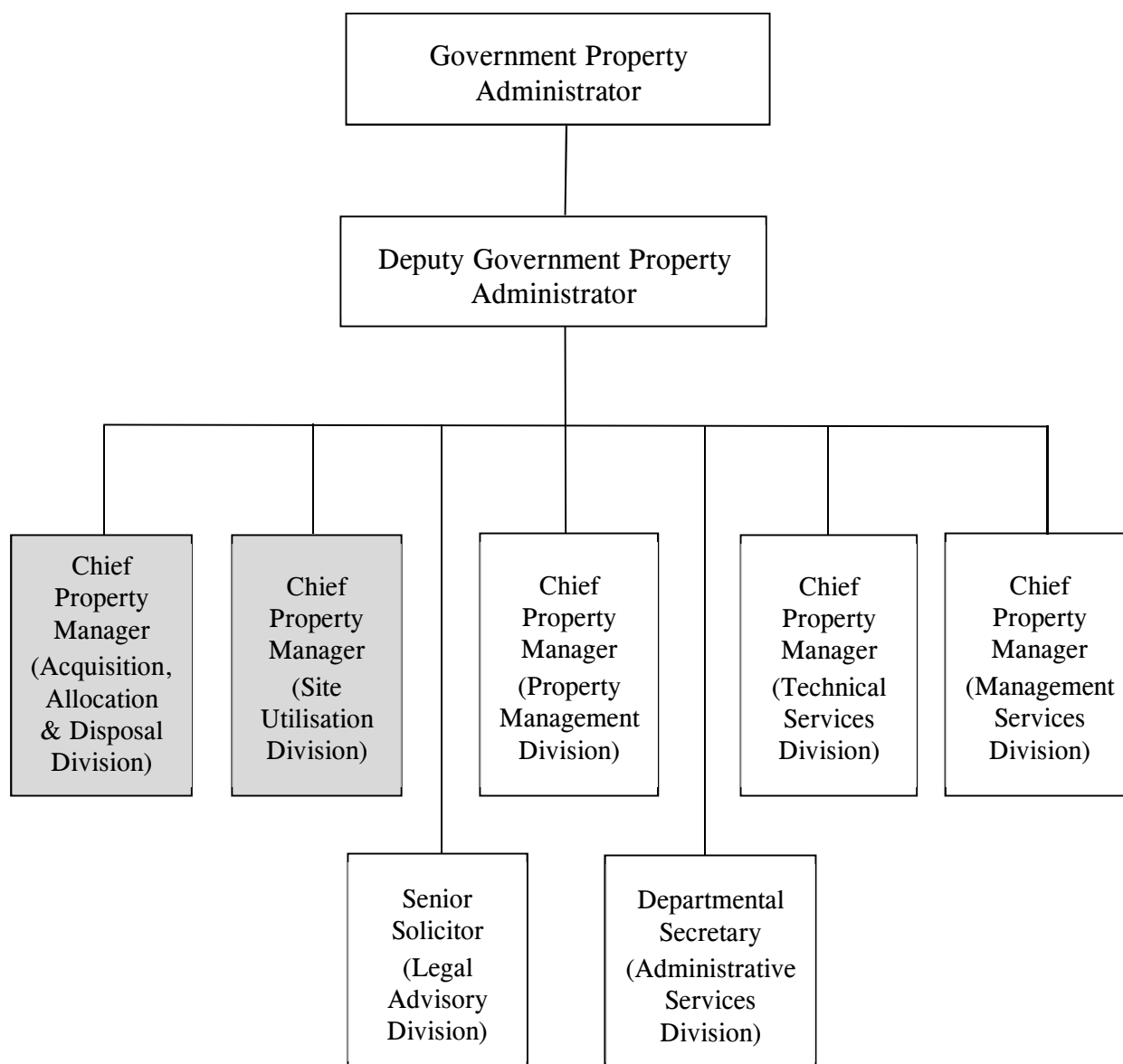
- (b) **in collaboration with the Director of Planning and the relevant owner B/Ds, determine the long-term use of the sites of the four unusable properties and work out a suitable disposal option.**


Response from the Government

4.28 The Government Property Administrator generally agrees with the audit recommendations. He has said that the GPA regularly reminds B/Ds to put their vacant premises to gainful use in the annual stewardship statement exercise (see para. 1.7) and the periodic departmental circulation of surplus accommodation. The GPA will continue to remind the relevant B/Ds to explore other measures to put the 27 vacant or under-utilised premises into gainful use.

4.29 The Director of Planning agrees with the audit recommendation in paragraph 4.27(b).

**Government Property Agency:
Organisation chart
(July 2017)**



Legend:  Divisions mainly responsible for handling matters relating to provision of government office accommodation and utilisation of government sites

Source: *GPA records*

Terms of reference of the Property Strategy Group

The terms of reference of the PSG are to:

- (a) consider and decide on issues or cases for the optimal utilisation of government sites (i.e. G/IC sites which have been allocated or reserved for government uses), and the incorporation of government uses into private development;
- (b) develop guidelines, and identify and promote programmes or projects, for the optimal utilisation of government sites as well as to maintain an oversight on their implementation;
- (c) consider and decide on issues or cases for management, alternative use and release as appropriate of under-utilised or surplus government properties and the sites involved;
- (d) consider and decide on departmental appeals on issues or cases related to optimum site utilisation, including those on reprovisioning arrangements, joint-user developments and government uses in private developments; and
- (e) consider and decide on whether PWP projects using less than full development potential of G/IC sites can be allowed to proceed to Public Works Subcommittee submission.

Source: FSTB records

**A comparison of the time taken in
implementing three government-building projects**

	Project		
	Central Government Complex at Tamar	Trade and Industry Tower at Kai Tak	WKGO at West Kowloon
Date of inclusion in PWP	February 2004	November 2007	July 2003
Date of funding approval	June 2006	January 2012	June 2015
Time taken from inclusion in PWP to funding approval	2 years 4 months	4 years 2 months	11 years 11 months
Date of project completion	July 2011	April 2015	Early 2019 (estimate)
Total NOFA (m ²)	62,340	33,000	50,500
Area for reprovisioning accommodation in leased premises (m ²)	5,520 (8.9% of 62,340 m ²)	16,500 (50% of 33,000 m ²)	29,290 (58% of 50,500 m ²)

Source: GPA records

**Other redevelopment cases monitored by
the Property Strategy Group
(June 2017)**

Item	Site	Site area (m ²)
6 cases referred by the CPLD		
1	General Post Office	3,900
2	Whitfield Depot cum offices and quarters	6,600
3	Ex-Ma Kok Street Cooked Food Hawker Bazaar	2,400
4	Chak On Road Driving Test Centre and its adjoining area	9,458
5	Wong Tai Sin Community Centre	2,000
6	Ex-Yu Chau West Street Cooked Food Hawker Bazaar	800
5 other cases referred by PSG members		
7	5-7 Yip Shing Street, Kwai Chung (Case 6)	1,400
8	Kowloon West Regional Police Headquarters	10,475
9	Tuen Mun Water Treatment Works Staff Quarters, Lam Tei Raw Water Pumping Station and adjoining Staff Quarters	1,930 2,800
10	Ex-Western Police Married Quarters (Sai Ying Pun)	3,800 (Note)
11	Ex-Mui Fong Street Cooked Food Bazaar	600

Source: GPA records

Note: The ex-Western Police Married Quarters (occupying about 3,800 m²) were situated in the compound of the Western Police Station with a total site area of 6,900 m².

Remarks: Other than the 11 sites (as of June 2017) monitored by the PSG, the GPA also monitors 22 identified sites with redevelopment potential and reports to the PSG on the positions of these sites on a half-yearly basis.

Acronyms and abbreviations

ADD	Acquisition, Allocation and Disposal Division
ArchSD	Architectural Services Department
AROA	Annual review of office accommodation
Audit	Audit Commission
B/D	Bureau/department
C&SD	Census and Statistics Department
CBD	Central Business District
CCD	Central Casefile Depository
CEDD	Civil Engineering and Development Department
CKR	Central Kowloon Route
CPLD	Committee on Planning and Land Development
CSD	Correctional Services Department
DEVB	Development Bureau
DSD	Drainage Services Department
FC	Finance Committee
FSTB	Financial Services and the Treasury Bureau
ft ²	Square feet
GFA	Gross floor area
G/IC	Government, institution or community
GPA	Government Property Agency
GPIS	Government Property Information System
HQs	Headquarters
HyD	Highways Department
JUB	Joint-user general office building
LandsD	Lands Department
LCSD	Leisure and Cultural Services Department
LD	Labour Department

Appendix E
(Cont'd)

LegCo	Legislative Council
LWB	Labour and Welfare Bureau
m	Metres
m ²	Square metres
NOFA	Net operational floor area
OZP	Outline Zoning Plan
PlanD	Planning Department
PSG	Property Strategy Group
PWP	Public Works Programme
REO	Registration and Electoral Office
RVD	Rating and Valuation Department
SDB	Specialist and departmental building
SUD	Site Utilisation Division
SWD	Social Welfare Department
TD	Transport Department
TDD	Territory Development Department
WCGOC	Wan Chai Government Offices Compound
WKGO	West Kowloon Government Offices
WSD	Water Supplies Department

CHAPTER 9

Labour Department

Occupational safety and health

**Audit Commission
Hong Kong
27 October 2017**

This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.

Report No. 69 of the Director of Audit contains 9 Chapters which are available on our website at <http://www.aud.gov.hk>

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OCCUPATIONAL SAFETY AND HEALTH

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OCCUPATIONAL SAFETY AND HEALTH

Executive Summary

1. “Safety and Health at Work” is one of the Labour Department (LD)’s programme areas. The aim of the programme area is to ensure that risks to the safety and health of people at work are properly managed by legislation, enforcement, education and publicity efforts. For 2017-18, the estimated expenditure for the programme area is \$510 million.

2. Occupational safety and health is regulated mainly through: (a) the Factories and Industrial Undertakings Ordinance (FIUO – Cap. 59); and (b) the Occupational Safety and Health Ordinance (OSHO – Cap. 509). The FIUO was enacted in 1955 to provide for the safety and health protection for workers in the industrial sector. It applies to industrial undertakings such as factories, construction sites and catering establishments. The OSHO was enacted in 1997 to extend the safety and health protection of employees to the majority of economic activities. It covers almost all workplaces.

3. The Occupational Safety and Health Branch (OSHB) of the LD is responsible for work related to occupational safety and health. As at 31 March 2017, the OSHB had a staff establishment of 642. The Audit Commission (Audit) has recently conducted a review of the LD’s work in occupational safety and health.

Occupational safety: inspection and enforcement

4. *Need to strengthen enforcement of notification requirement for Notifiable Workplaces.* The OSHB is responsible for carrying out inspections of workplaces and initiating enforcement action where necessary. There are two types of workplaces, namely building and engineering construction (BEC) workplaces (i.e. construction sites) and non-BEC workplaces. As at September 2017, information on 36,692 BEC workplaces and 141,206 non-BEC workplaces was kept in the OSHB’s database. The LD’s focus of inspection is placed on: (a) BEC workplaces; and (b) non-BEC workplaces subject to statutory workplace notification requirements

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(hereinafter referred to as Notifiable Workplaces). The person having the management or control of a Notifiable Workplace is required to notify the LD of the workplace before commencement of operation. Audit examined the LD's investigations of 20 accident cases that occurred in 2016 at Notifiable Workplaces and found that the persons concerned of eight (40%) Workplaces had not submitted the required statutory notifications to the LD before the LD's investigations. These eight Workplaces had commenced operation for 90 days to 18 years and 5 months. Audit checked the records for the period January 2012 to July 2017 and noted that no prosecution had been taken by the LD against non-compliance of the notification requirement (paras. 2.2 to 2.5).

5. ***Need to review notification requirement for BEC workplaces.*** Although the construction industry is accident-prone, unlike the notification requirement for Notifiable Workplaces, notification of BEC workplaces is only required to be submitted within seven days after commencement of the construction work. The current notification requirement for BEC workplaces leaves a time gap between the commencement of work and the notification submitted to the LD (para. 2.8).

6. ***Need to review the list of hazardous trades.*** The LD gives inspection priorities to workplaces of 23 hazardous non-BEC trades, which are identified by the LD according to the assessment of the prevailing risks. The last review of the list of hazardous trades was completed in January 2013. The review recommended that similar review should be conducted at a three-year interval. Not until July 2017 did the LD commence a new round of review, which may take about one and a half years to complete (paras. 2.3, 2.9 and 2.10).

7. ***Need to clear backlog and improve documentation for inspection work.*** The LD has a bring-up system for workplace files to be brought up for inspections. If the file is not brought up and assigned to an inspecting officer on the scheduled date, it is counted as a backlog. Audit noted that, as at 31 March 2017, there were 6,074 backlog cases of inspection on inactive BEC workplaces (i.e. construction sites where works were carried out intermittently or sites under defects liability period), and 23,414 backlog cases on non-BEC workplaces. The LD had not monitored whether inspections were carried out according to schedule. Audit examined 80 inspections carried out by the LD in the period from 1 April 2016 to 31 March 2017 and found that 24 (30%) inspections were conducted more than 90 days after the workplace files were brought up. Audit also noted that inspecting officers only documented the irregularities identified during

Executive Summary

inspections, but not the details of inspection work carried out, such as the work processes examined and the results of such examinations. Moreover, the LD reported in its Controlling Officer's Report (COR) the number of inspections conducted by the Operations Division of the OSHB under the FIUO and the OSHO. In the period from 2012 to 2016, the reported number of inspections carried out per year ranged from 123,115 to 131,339. Audit examination revealed that if an inspection was conducted jointly by more than one inspecting officer, the LD counted the number of inspecting officers as the number of inspections conducted. Had an inspection been counted as one irrespective of how many inspecting officers took part in the inspection work, the number of inspections carried out per year during the period would have ranged from 44,756 to 73,565 (paras. 2.15 to 2.17, 2.19, 2.22 and 2.24).

8. ***Need to strengthen deterrent effect of occupational safety legislation.*** In the period from 2012 to 2016, the average amount of fines imposed by the court on cases convicted under the FIUO and the OSHO had increased by 47% from \$7,723 in 2012 to \$11,390 in 2016. Audit analysis of the highest amount and the average amount of fines under the five most common offences of the FIUO and the OSHO revealed that notwithstanding the increase in amount of fines, the highest amount and the average amount were significantly below the maximum amount stipulated in the legislation (para. 2.30).

Occupational safety: training

9. ***Need to improve planning of inspection on mandatory safety training courses.*** Every person engaged in specific high risk sectors, activities or machine operations is required to complete the relevant mandatory safety training (MST) course organised by a training course provider (TCP). In 2016, there were 146 TCPs providing 704 MST courses. The LD conducted 225 inspections on the 146 TCPs and issued 17 warning letters and 5 directions. Of the 225 inspections, 182 (81%) were conducted at the time when there was no course session. As a result, many aspects of the courses could not be observed. Instead, the LD inspected the TCP's documentation (paras. 3.2, 3.4 and 3.6).

10. ***Need to expedite implementation of improvement measures recommended by the 2009 review on MST courses.*** In 2009, the LD conducted a review to devise improvement measures on recognition and monitoring of MST courses. In April 2011, the LD proposed to the Legislative Council Panel on Manpower a

Executive Summary

two-phase approach to implement the improvement measures. Up to August 2017, two of the three Phase One improvement measures, namely the standardisation of course contents and the centralisation of issuance of examination papers for the MST courses, had not been fully implemented. Furthermore, there was also no timetable to implement these measures and the Phase Two measures (paras. 3.7 to 3.9).

11. ***Some Registered Safety Auditors are not Registered Safety Officers.*** The FIUO and its subsidiary regulations stipulated that the contractors or proprietors of some workplaces are required to employ an Registered Safety Officer (RSO) to assist in the promotion of the occupational safety and health, and/or an Registered Safety Auditor (RSA) to audit the required safety management system. To register as an RSA, a person shall be an RSO and fulfil the specified requirements. The designation of an RSA is valid for life while the registration of an RSO is valid for a period of four years subject to renewal or revalidation. Some RSAs will cease to be RSOs after they have become RSAs if they choose not to apply for renewal or revalidation of the RSO registration upon expiry. The lists of RSOs and RSAs as at 31 May 2017 indicated that 29 (2.3%) of the 1,273 RSAs were not RSOs (paras. 3.12, 3.14 to 3.16 and 3.18).

Occupational health

12. ***Need to improve arrangements for medical examination of radiation workers.*** Every year, the Kwun Tong Occupational Health Clinic (KTOHC) reserves a number of sessions exclusively for carrying out medical examinations of workers prone to exposure to radiation. For each session, 30 examinations can be carried out. Audit found that the utilisation of the reserved sessions was decreasing in the period from 2012 to 2017 (up to June): (a) the annual average number of no-show cases per session ranged from 2.7 to 4.2 (11% to 15% of the booked slots); and (b) the average number of booked examinations in each session decreased from 27.8 to 22.9 and the number of sessions in which not more than 20 examinations were carried out increased from 17% to 56% of the total number of sessions. Moreover, the law stipulates that the examinations carried out for the workers' first employment would be provided free of charge, but it does not stipulate that the periodic examinations after the workers' first employment would be provided at a charge or free of charge. Audit noted that workers and their employers were not required to pay any fee for the periodic examinations (paras. 4.4, 4.6 to 4.8, 4.10 and 4.11).

Executive Summary

13. *Need to monitor progress of workplace inspections.* The LD did not monitor the number of outstanding inspections and the delay in carrying out inspections after they were brought up for inspection. Audit reviewed 30 outstanding inspections on occupational health as at 30 June 2017 and found that all of them had been outstanding for more than six months after they were brought up. The outstanding periods ranged from 7 months to 4.25 years, averaging 2.17 years. Audit also reviewed 24 inspections conducted by the LD in the period from July 2016 to June 2017 and found that there were delays in 13 (54%) of the 24 inspections. The delay ranged from 4 days to 3 years, averaging 11 months (paras. 4.18 to 4.20).

14. *Need to improve reporting of performance indicators in COR.* For 2016, the LD reported in the COR that it had achieved 22,629 “investigations/surveys/examinations/assessments/clinical consultations” without the breakdown information. Audit noted that the number comprised 2,983 investigations, 7,018 surveys, 1,471 medical examinations, 713 assessments and 10,444 clinical consultations (para. 4.23).

Audit recommendations

15. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Commissioner for Labour should:**

Occupational safety: inspection and enforcement

- (a) **step up measures to strengthen the enforcement of the notification requirement for Notifiable Workplaces (para. 2.11(a));**
- (b) **review the reasonableness of the submission deadline for notification of construction work and if necessary, tighten the deadline (para. 2.11(c));**
- (c) **closely monitor the progress of the review of the list of hazardous trades to ensure that it is completed in a timely manner (para 2.11(d));**

Executive Summary

- (d) **take measures to ensure that there is no delay in bringing up cases for inspection and conducting inspections after the cases were brought up for inspection (para. 2.26(a));**
- (e) **take measures to clear the existing backlog of inspections as soon as practicable (para. 2.26(b));**
- (f) **improve the documentation of the inspection work performed (para. 2.26(c));**
- (g) **separately disclose in the COR the number of workplaces inspected (para. 2.26(g));**
- (h) **monitor closely the need to review the labour legislation with a view to strengthening the deterrent effect of the legislation (para. 2.32);**

Occupational safety: training

- (i) **arrange inspections on the TCPs during time period when there are course sessions taking place as far as practicable (para. 3.10(a));**
- (j) **expedite the implementation of the improvement measures recommended by the 2009 review on MST courses (para. 3.10(b));**
- (k) **review whether there is a need to revise the Factories and Industrial Undertakings (Safety Management) Regulation to address the shortcomings that some RSAs are not RSOs (para. 3.25(a));**

Occupational health

- (l) **in collaboration with the Director of Health, take measures to reduce the no-show rate of radiation workers for medical examinations (para. 4.16(a));**
- (m) **monitor the utilisation of time slots reserved for medical examinations for radiation workers to ensure that the clinical resources are optimally utilised as far as practicable (para. 4.16(b));**

Executive Summary

- (n) **in collaboration with the Director of Health, review the justifications for not charging radiation workers or their employers for periodic medical examinations carried out at the KTOHC after the workers' first employment (para. 4.16(c));**
- (o) **closely monitor the progress of workplace inspections (para. 4.21(a));**
- (p) **take measures to minimise the number of outstanding inspections in future (para. 4.21(c));**
- (q) **ascertain the number of existing backlog inspections and take effective measures to clear the backlog as soon as practicable (para. 4.21(d)); and**
- (r) **with a view to enhancing transparency, consider reporting separately in the COR the number of investigations, surveys, examinations, assessments and clinical consultations (para. 4.25(a)).**

Response from the Government

16. The Commissioner for Labour agrees with the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 “Safety and Health at Work” is one of the Labour Department (LD)’s programme areas. The aim of this programme area is to ensure that risks to the safety and health of people at work are properly managed by legislation, enforcement, education and publicity efforts. For 2017-18, the estimated expenditure for the programme area is \$510 million.

Major legislations

1.3 Occupational safety and health is regulated mainly through the following legislations:

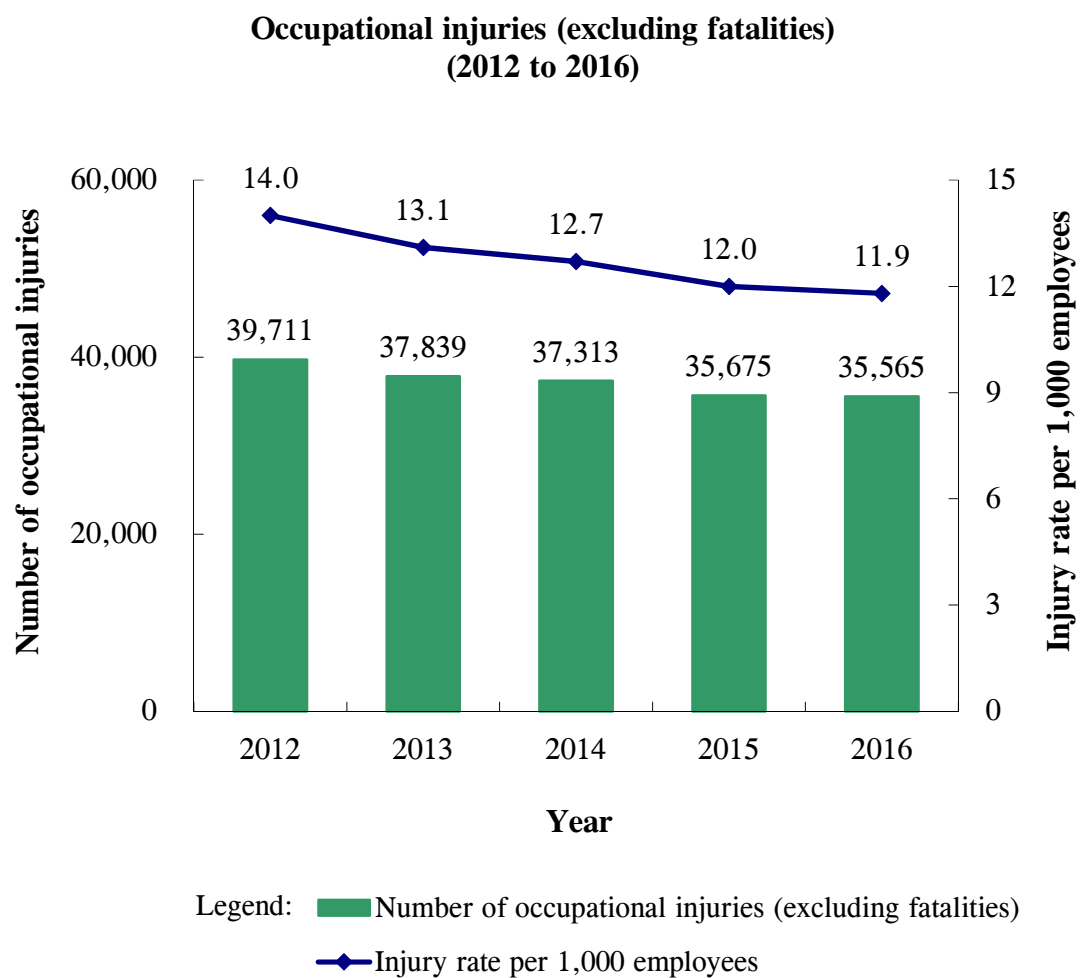
- (a) ***Factories and Industrial Undertakings Ordinance (FIUO — Cap. 59).*** The FIUO was enacted in 1955 to provide for the safety and health protection for workers in the industrial sector. It applies to industrial undertakings, such as factories, construction sites, catering establishments, cargo and container handling undertakings, repair workshops and other industrial workplaces. Under the FIUO, there are 31 sets of subsidiary regulations covering various aspects of work activities in industrial undertakings. The subsidiary regulations prescribe detailed safety and health standards on work situations, plant and machinery, processes and substances; and
- (b) ***Occupational Safety and Health Ordinance (OSHO — Cap. 509).*** The OSHO was enacted in 1997 to extend the safety and health protection of employees to the majority of economic activities. It empowers the Commissioner for Labour to make regulations prescribing occupational safety and health standards for working environment. It covers almost all workplaces. In addition to factories, construction sites and catering establishments, other places, such as offices, laboratories, shopping arcades

and educational institutions also come under the ambit of the OSHO. Two sets of subsidiary regulations were made under the OSHO setting out the basic requirements for accident prevention, fire precaution, workplace environment control, hygiene at workplaces, first aid, proper use of display screen equipment as well as what employers and employees are expected to do in manual handling operations.

Occupational injuries and fatalities and occupational diseases

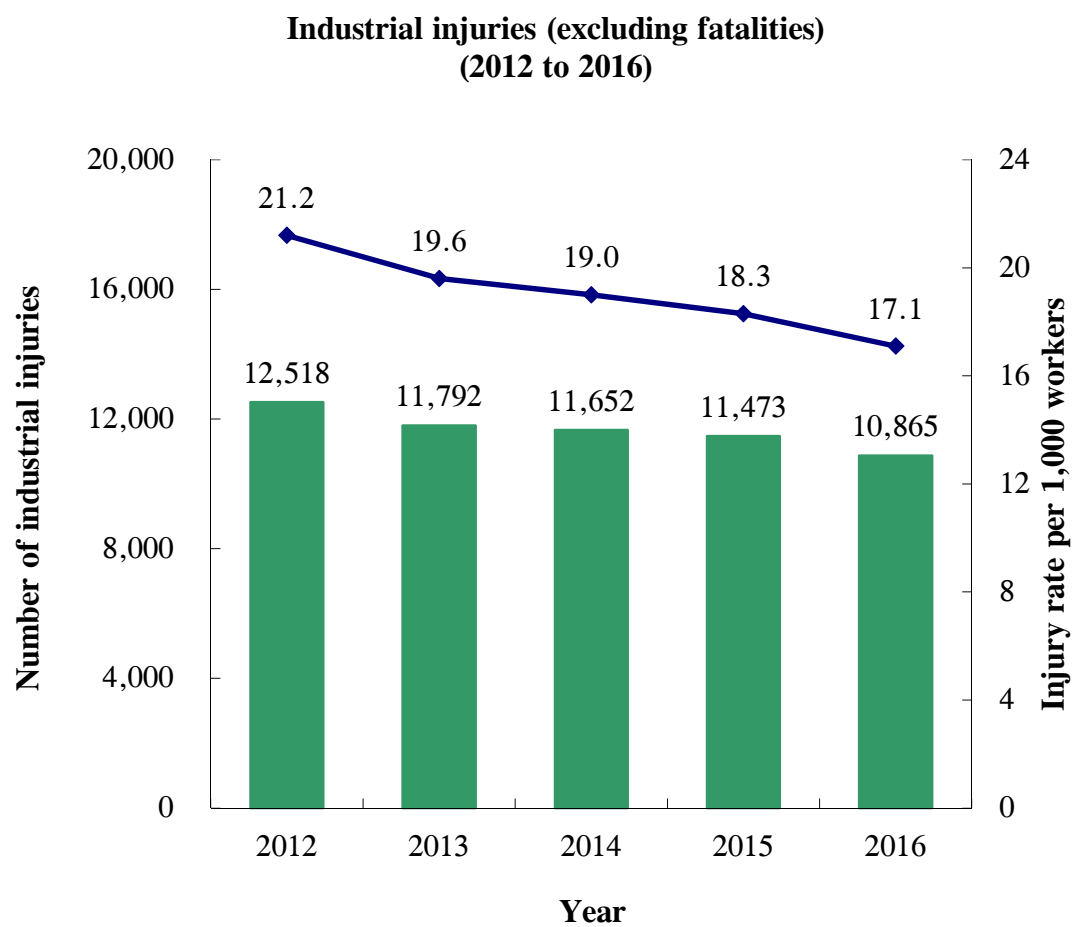
1.4 Figure 1 shows the statistics on occupational injuries (excluding fatalities) for the period from 2012 to 2016. The statistics refer to the numbers of occupational injuries (excluding fatalities) resulting in incapacity for work for a period exceeding three days reported under the Employees' Compensation Ordinance (ECO — Cap. 282). The number of occupational injuries (excluding fatalities) includes industrial injuries (excluding fatalities), which refer to injuries arising from industrial activities in industrial undertakings as defined under the FIUO. Other occupational injuries (excluding fatalities) are cases including non-industrial injuries (excluding fatalities), cases outside Hong Kong, and cases that happened on vessel. Figure 2 shows the statistics on industrial injuries (excluding fatalities) for the same period. As shown in Figures 1 and 2, the number of occupational injuries (excluding fatalities) decreased by 10.4% from 39,711 in 2012 to 35,565 in 2016 and the number of industrial injuries (excluding fatalities) decreased by 13.2% from 12,518 in 2012 to 10,865 in 2016.

Figure 1



Source: LD records

Figure 2



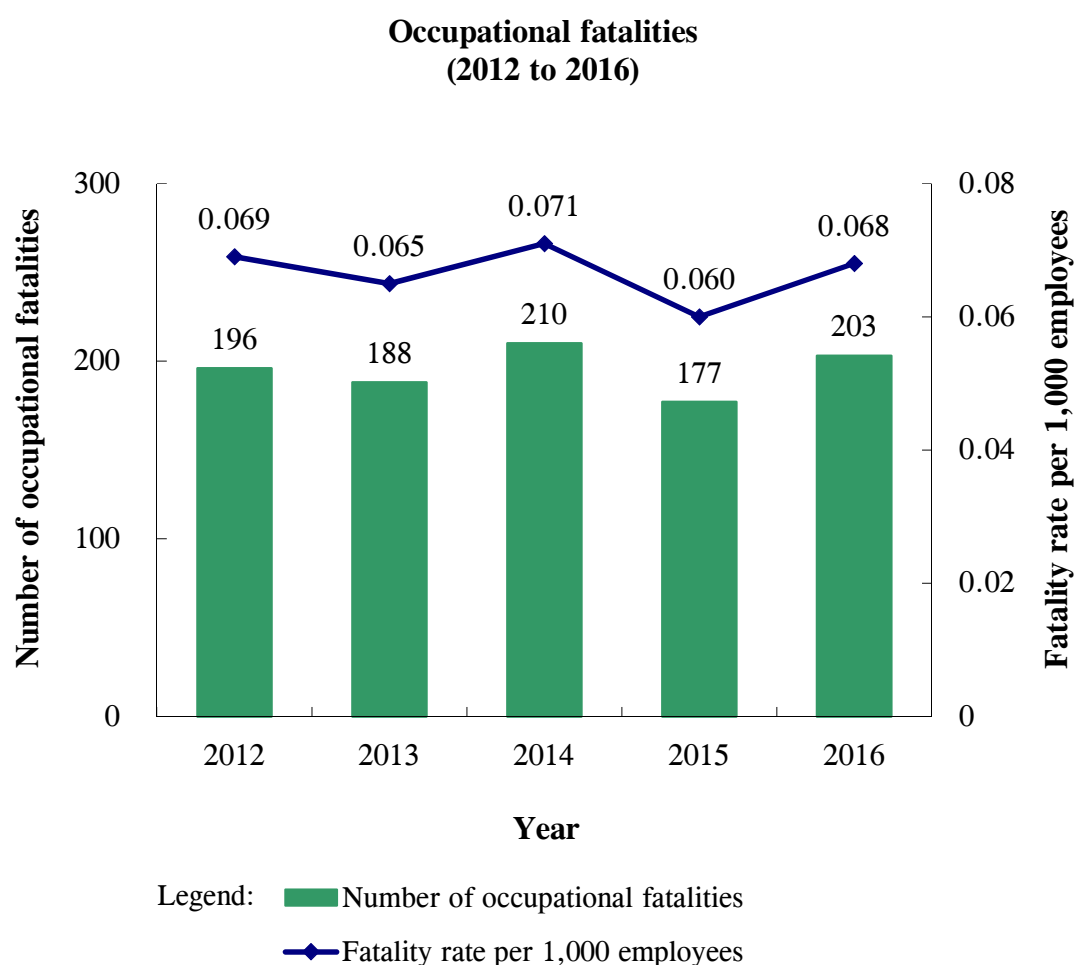
Legend: ■ Number of industrial injuries (excluding fatalities)

◆ Injury rate per 1,000 workers

Source: LD records

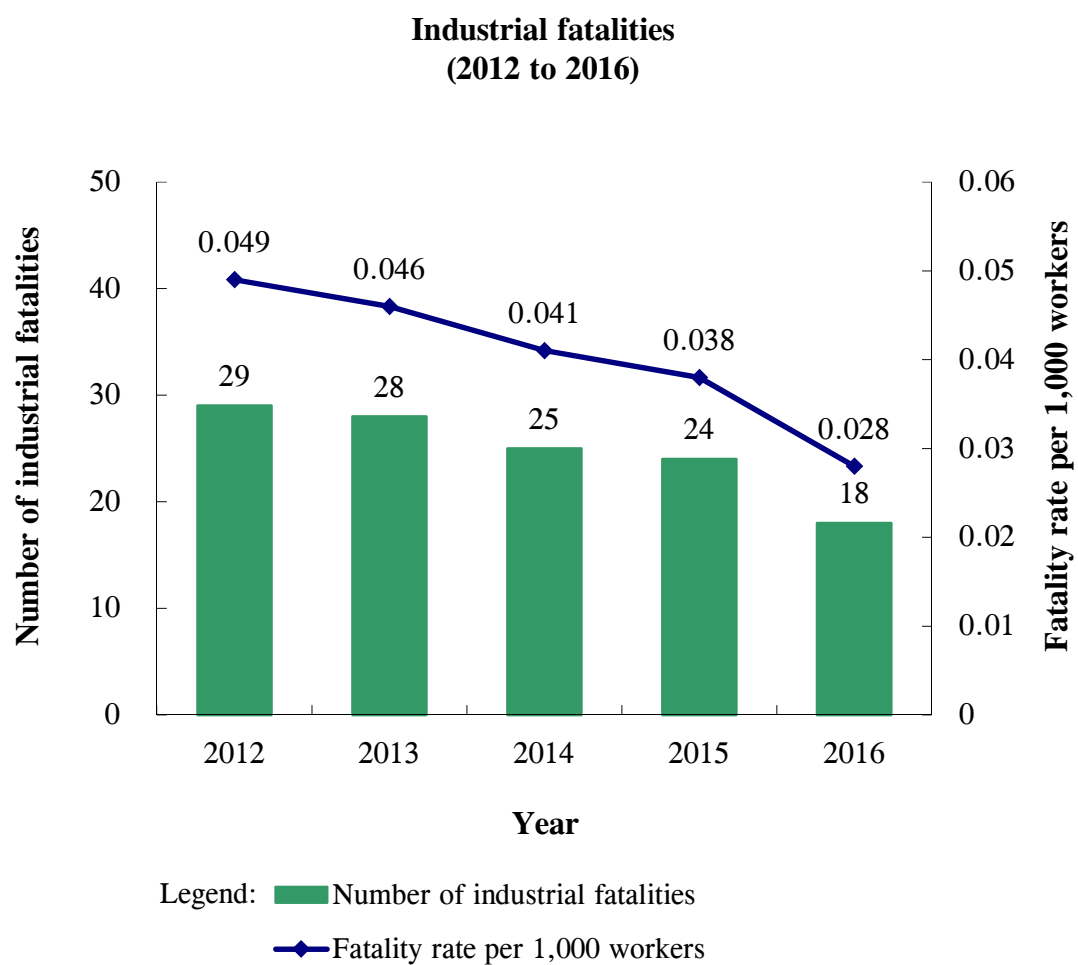
1.5 Figure 3 shows the statistics on occupational fatalities for the period from 2012 to 2016. The statistics refer to the numbers of occupational fatalities reported under the ECO. The number of occupational fatalities includes industrial fatalities, which refer to fatalities arising from industrial activities in industrial undertakings as defined under the FIUO. Other occupational fatalities are cases including non-industrial fatalities, natural deaths, cases outside Hong Kong, and cases that happened on vessel. Figure 4 shows the statistics on industrial fatalities for the same period. As shown in Figures 3 and 4, the number of occupational fatalities slightly increased by 3.6% from 196 in 2012 to 203 in 2016 whereas the number of industrial fatalities decreased by 37.9% from 29 in 2012 to 18 in 2016. Figure 5 shows the statistics for the same period on 52 types of occupational diseases as prescribed under the ECO, the Occupational Deafness (Compensation) Ordinance (Cap. 469) and the Pneumoconiosis and Mesothelioma (Compensation) Ordinance (Cap. 360) (see Appendix A).

Figure 3



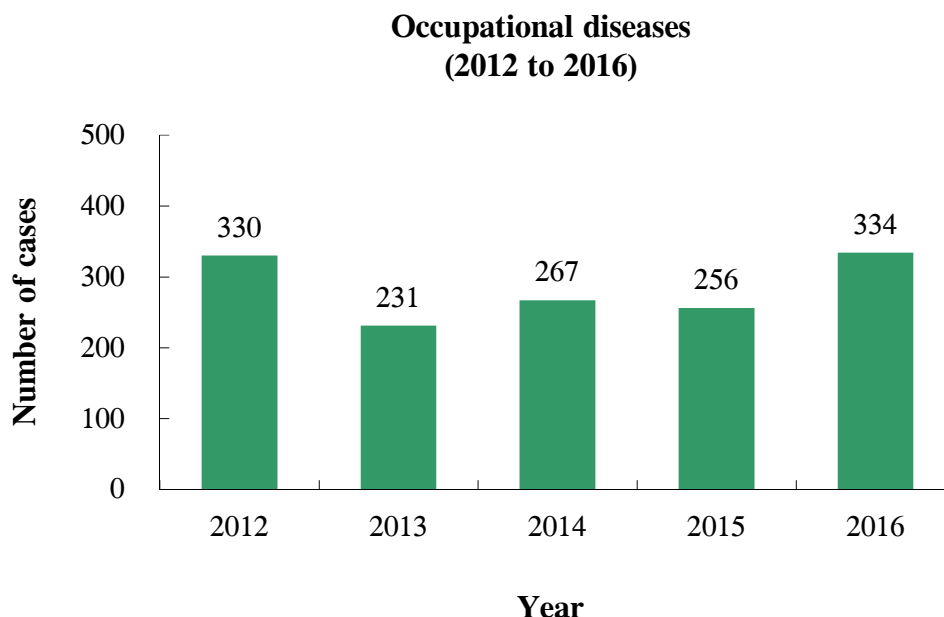
Source: LD records

Figure 4



Source: LD records

Figure 5



Source: LD records

Remarks: The statistics refer to the number of confirmed cases of occupational diseases under the ECO, the Occupational Deafness (Compensation) Ordinance and the Pneumoconiosis and Mesothelioma (Compensation) Ordinance (see Appendix A).

Work of the LD on occupational safety and health

1.6 The Occupational Safety and Health Branch (OSHB) of the LD is responsible for work related to occupational safety and health. It is headed by a Deputy Commissioner for Labour. As at 31 March 2017, the OSHB had a staff establishment of 642. The organisation chart of the OSHB is shown at Appendix B. The OSHB is responsible for two types of work:

- (a) ***Occupational safety.*** The major work relating to occupational safety includes:
 - (i) enforcing the OSHO, the FIUO and their subsidiary regulations through carrying out inspections of workplaces to ensure the compliance of the occupational safety requirements under the legislation;

Introduction

- (ii) carrying out accident investigations and giving advice to employers, employees and other stakeholders on measures to minimise workplace safety hazards;
 - (iii) offering advice to owners in the planning and layout of factories and workplaces, and in-plant or in-house safety programmes;
 - (iv) providing support services to instil safety concepts to the public at large with a view to inculcating a safety culture among employers, employees and other stakeholders, and to securing their commitment to self-regulation to bring in a safety management approach; and
 - (v) operating the Occupational Safety and Health Training Centre which provides training on occupational safety and health for employees in public and private sectors, gives recognition to mandatory safety training courses, and processes registration of Safety Officers, Safety Auditors and Safety Auditor Training Scheme Operators; and
- (b) ***Occupational health.*** The work relating to occupational health includes:
- (i) providing advisory services to the public on health and hygiene aspects of occupational health problems such as prevention of occupational diseases in workplaces;
 - (ii) conducting field surveys to ensure that the requirements of health and hygiene at workplaces are complied with;
 - (iii) enforcing legislation relating to occupational health and hygiene;
 - (iv) investigating and providing treatment to suspected occupational disease cases; and
 - (v) others (e.g. conducting sick leave clearance interview of employees with compensation claims, organising exhibitions and delivering talks).

1.7 Table 1 shows the performance indicators of the LD's work on occupational safety and health and the related performance reported by the LD in the Controlling Officer's Report (COR) for the period from 2012 to 2016.

Table 1

**Performance on occupational safety and health
(2012 to 2016)**

Major performance indicator	2012	2013	2014	2015	2016	Change between 2012 and 2016 (percentage)
<i>Occupational safety</i>						
Inspections	128,821	123,115	124,907	130,173	131,339	+2,518 (+2.0%)
Investigations of accidents at workplaces	13,442	13,266	14,758	15,046	14,730	+1,288 (+9.6%)
Promotional visits to workplaces	5,373	5,901	5,837	5,994	5,436	+63 (+1.2%)
Talks, lectures and seminars	2,023	1,944	2,047	2,106	2,097	+74 (+3.7%)
<i>Occupational health</i>						
Investigations/ surveys/ examinations/ assessments/ clinical consultations	26,437	25,286	22,164	21,592	22,629	-3,808 (-14.4%)

Source: Audit analysis of LD records

Introduction

Audit review

1.8 In March 2005, the Audit Commission (Audit) completed an audit review of the LD's work in work safety at construction sites. The results were reported in Chapter 8 of the Director of Audit's Report No. 44 of March 2005.

1.9 In March 2017, Audit commenced a review of the LD's work in occupational safety and health. The audit has focused on the following areas:

- (a) occupational safety: inspection and enforcement (PART 2);
- (b) occupational safety: training (PART 3); and
- (c) occupational health (PART 4).

Audit has found room for improvement in the above areas and has made a number of recommendations to address the issues.

General response from the Government

1.10 The Commissioner for Labour agrees with the audit recommendations. He finds the Audit Report constructive and thanks Audit for its advice.

Acknowledgement

1.11 Audit would like to acknowledge with gratitude the full cooperation of the staff of the LD during the course of the audit review.

PART 2: OCCUPATIONAL SAFETY: INSPECTION AND ENFORCEMENT

2.1 This PART examines the LD's inspection and enforcement effort to improve occupational safety. Audit has found that there is scope for improvement in the following areas:

- (a) identification of workplaces for inspection (paras. 2.3 to 2.12);
- (b) inspection work (paras. 2.13 to 2.27); and
- (c) enforcement action (paras. 2.28 to 2.33).

Background

2.2 The Operations Division of the OSHB is responsible for carrying out inspections of workplaces and initiating enforcement action where necessary. As at 31 March 2017, the Operations Division had a staff establishment of 351 and a staff strength of 314. The Division comprises:

- (a) ***Operational Regions.*** There are four Operational Regions, namely Hong Kong and Islands, Kowloon, New Territories East, and New Territories West. They are responsible for carrying out inspections of workplaces within their geographical boundaries. Each Region is sub-divided into two streams, one for the building and engineering construction (BEC) workplaces (i.e. construction sites), and the other for non-BEC workplaces (i.e. workplaces other than construction sites). In the four Regions, there are a total of 22 BEC offices and 20 non-BEC offices; and
- (b) ***Integrated Services Group (ISG).*** The ISG consists of 11 Offices/Teams:
 - (i) three Mega Infrastructure Project (MIP) Offices responsible for overseeing the safety of construction work of MIPs such as the Hong Kong-Zhuhai-Macao Bridge project and the Shatin to Central Link project;

- (ii) three Airport and Railways Offices responsible for overseeing the safety of all workplaces in relation to the airport and railway construction and operation (including properties managed by the railway operator);
- (iii) four Integrated Services Teams responsible for carrying out inspections of large chain establishments (such as supermarkets) by adopting a multi-disciplinary approach (i.e. tackling problems relating to both occupational safety and occupational health); and
- (iv) one temporary Surveillance Team responsible for overseeing the high pressure compressed air work associated with the Hong Kong-Zhuhai-Macao Bridge project.

Identification of workplaces for inspection

Inspection strategy

2.3 There are two types of workplaces, namely BEC workplaces and non-BEC workplaces (see para. 2.2(a)). As at September 2017, information on 177,898 workplaces was kept in the OSHB's database. These workplaces comprise 36,692 BEC workplaces and 141,206 non-BEC workplaces. The LD adopts a risk-based inspection strategy as follows:

- (a) focus of inspection work is placed on:
 - (i) BEC workplaces; and
 - (ii) non-BEC workplaces which are subject to statutory workplace notification requirement (see para. 2.4(b)); and
- (b) inspection priorities are also given to workplaces of 23 hazardous non-BEC trades (see Appendix C and para. 2.9). The list of 23 hazardous trades was drawn up according to the assessment of the prevailing risks.

Statutory workplace notification requirements

2.4 The FIUO and its subsidiary regulations stipulate requirements for the proprietors and contractors of some workplaces to give the LD notifications of their workplaces. The requirements are:

- (a) ***BEC workplaces.*** According to the Construction Sites (Safety) Regulations (Cap. 59I), a contractor undertaking construction work shall furnish the Commissioner for Labour with information (Note 1) on the construction work within seven days after commencement of the work. A contractor is not required to give notification of the work he undertakes if:
 - (i) he has reasonable grounds for believing that the work will be completed in a period of less than six weeks; or
 - (ii) not more than ten workmen are or will be employed on the work at any one time; and
- (b) ***Non-BEC workplaces.*** According to the FIUO, the person (i.e. the proprietor) having the management or control of a Notifiable Workplace shall give the Commissioner for Labour notification of the workplace before commencement of operation. Notifiable Workplace means:
 - (i) any factory, mine or quarry; and

Note 1: *Information that should be furnished includes: (a) the contractor's name and address; (b) the name and address of every subcontractor employed on the work; (c) the location of the construction site; (d) the nature of the work; (e) the date upon which the work was commenced; (f) whether any mechanical power is being or will be used in connection with the work and its nature; and (g) the expected duration of the work.*

- (ii) any premises or place in which a Dangerous Trade (Note 2) or Scheduled Trade (Note 3) is carried on or is proposed to be carried on.

A proprietor or contractor who fails to comply with the requirements is liable to a maximum fine of \$10,000.

Need to strengthen enforcement of notification requirement for Notifiable Workplaces

2.5 A proprietor who fails to give the notification under the FIUO not only commits an offence and may be prosecuted, but may also deprive himself of an opportunity of being advised by the LD to improve the safety and health conditions of his workplace in the early stage of operation. In order to ascertain if effective action had been taken by the LD to ensure compliance with the notification requirement, Audit examined the LD's investigations of 20 accident cases that occurred in 2016 at Notifiable Workplaces. Audit found that the proprietors of eight (40%) Notifiable Workplaces had not submitted the required statutory notifications to the LD before the LD's investigation. According to the FIUO, the notifications should be submitted before commencement of operation. These eight Workplaces had commenced operation for 90 days to 18 years and 5 months prior to the LD's investigations (see Table 2). Audit checked the records of the LD for the period from January 2012 to July 2017 and noted that no prosecution had been taken by the LD against non-compliance of the notification requirement. Audit considers that the LD needs to step up measures to strengthen the enforcement of the notification requirement for Notifiable Workplaces.

Note 2: *Examples of Dangerous Trade defined under the FIUO include: (a) boiler chipping; (b) vermillion manufacture; (c) chromium plating; and (d) the manufacture of hydrochloric, nitric or sulphuric acids.*

Note 3: *Examples of Scheduled Trade defined under the FIUO include: (a) any industrial undertaking involving the use of any dangerous goods specified in Category 5 in the Schedule to the Dangerous Goods (Application and Exemption) Regulations (Cap. 295A) and for which a licence is required under the Dangerous Goods Ordinance (Cap. 295); and (b) any industrial undertaking involving the use of any X-ray or radioactive substance.*

Table 2

**Time lapse between operation commencement date
and LD's investigation date**

Time lapse	Number of workplaces
90 days to 1 year	2 (25%)
> 1 year to 2 years	1 (12.5%)
> 2 years to 3 years	3 (37.5%)
> 3 years	2 (25%) (Note)
Total	8 (100%)

Source: Audit analysis of LD records

Note: The time lapses between the operation commencement date of the workplace and the LD's investigation date of these two cases were 6 years and 4 months, and 18 years and 5 months respectively.

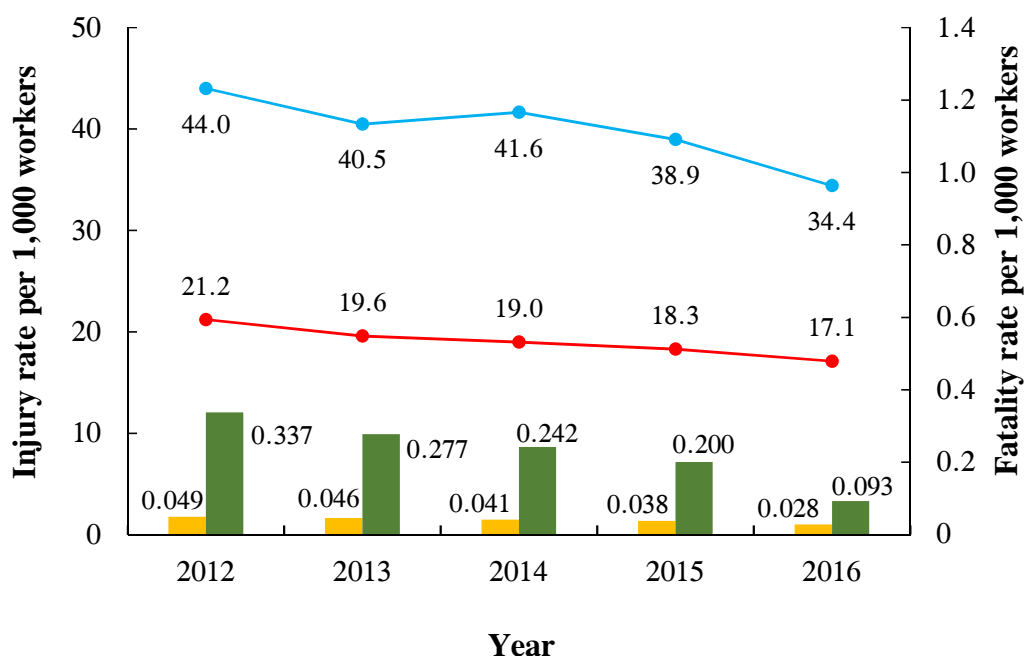
Need to review notification requirement for BEC workplaces and non-BEC workplaces

2.6 Although workplaces may be identified by the LD's action (e.g. enforcement campaigns), it is important for the contractors or proprietors to give the LD notifications of their BEC workplaces or non-BEC workplaces so that these workplaces are subject to the LD's inspection and advice. Audit reviewed the notification requirement for BEC workplaces and non-BEC workplaces and identified areas for improvement, as detailed in paragraphs 2.7 to 2.8.

2.7 *Notification by small BEC workplaces exempted.* A contractor of a BEC workplace is not required to give notification of the work he undertakes if he has reasonable grounds for believing that the work will be completed in a period of less than six weeks or not more than ten workmen are or will be employed on the work at any one time (see para. 2.4(a)). In the period from 2012 to 2016, although the fatality rates and the injury rates (excluding fatalities) per thousand workers of the construction industry decreased from 0.337 to 0.093 and 44.0 to 34.4 respectively (see Figure 6), the number of fatal industrial accidents and the industrial accident rate per thousand workers of the construction industry had been the highest among all trades. In view of the accident-prone nature of the construction industry, there is merit for the LD to consider reviewing the need to tighten the exemption criteria.

Figure 6

**Fatality rate and injury rate of construction industry
(2012 to 2016)**



Legend:

- Industrial fatality rate per 1,000 workers of all trades
- Industrial fatality rate per 1,000 workers of construction industry
- Industrial injury rate (excluding fatalities) per 1,000 workers of all trades
- Industrial injury rate (excluding fatalities) per 1,000 workers of construction industry

Source: Audit analysis of LD records

2.8 Seven-day submission deadline for notification of construction work. According to the FIUO, notification of Notifiable Workplaces should be given to the Commissioner for Labour before the commencement of operation. However, according to the Construction Sites (Safety) Regulations made under the FIUO, notification of construction work is only required to be submitted within seven days after commencement of the work. The current notification requirement leaves a time gap between the commencement of work and the submission of notification to the LD. Given that the construction industry is accident-prone, the LD needs to review the reasonableness of the submission deadline for notification of construction work.

Need to review the list of hazardous trades

2.9 The last review of the list of hazardous trades was conducted by the LD in the period from August 2011 to January 2013. According to the results of the review, 23 trades were identified as hazardous trades (see Appendix C) taking into account:

- (a) the then prevailing accident profiles, technological advancement and socio-economic development; and
- (b) the probability and consequence of accidents in the trades. Trades that were more prone to accidents were included in the list.

The review suggested targetting the workplaces of the 23 trades for proactive monitoring. The review also recommended that similar review should be conducted at a three-year interval to cope with future changes.

2.10 Audit noted that the LD had not commenced a new round of review of hazardous trades until July 2017, more than four years after the completion of the last review. Basing on the experience of the last review, the LD may take about one and a half years to complete the review. Audit considers that the LD needs to complete the review of the list of hazardous trades as soon as practicable and take measures to ensure that such review is conducted regularly in future.

Audit recommendations

2.11 **Audit has *recommended* that the Commissioner for Labour should:**

- (a) **step up measures to strengthen the enforcement of the notification requirement for Notifiable Workplaces;**
- (b) **consider reviewing the need to tighten the exemption criteria of the notification requirement for BEC workplaces with work that will be completed in a period of less than six weeks or not more than ten workmen are or will be employed on the work at any one time;**

- (c) **review the reasonableness of the submission deadline for notification of construction work and if necessary, tighten the deadline;**
- (d) **closely monitor the progress of the review of the list of hazardous trades to ensure that it is completed in a timely manner; and**
- (e) **take measures to ensure that the list of hazardous trades is reviewed regularly in future.**

Response from the Government

2.12 The Commissioner for Labour agrees with the audit recommendations. He has said that:

- (a) the workplace notification mechanism is complemented by other risk identification approaches in guiding the LD's inspection and enforcement actions. For instance, the LD monitors prevailing risks and conducts enforcement campaigns accordingly targeting at particular trades and particular occupational risks. Through area patrol and various referral schemes under which organisations (e.g. the Housing Authority) inform the LD of construction works carried out at the premises under their management, the LD is able to identify small BEC workplaces which potentially carry higher risks. The LD will review the notification mechanism to expand its coverage to more BEC workplaces; and
- (b) the list of hazardous trades serves as a general reference for the LD to set its work priorities. In addition to the list, the LD also makes reference to the prevailing occupational risks and accident statistics in setting its work priorities. The LD will complete the current review of the list as soon as possible and will take the opportunity to rename the list to better reflect its purpose.

Inspection work

Frequency of inspection

2.13 ***BEC workplaces.*** It was stipulated in the LD's Standing Order that as far as practicable, each construction site (i.e. BEC workplace) should be inspected approximately once every one to three months. Where such a frequency of inspections cannot be maintained, priority should be given to the sites that are more risk-prone (e.g. sites where many workers are often engaged in higher-risk work processes such as work at height, or sites where the contractors have not responded to advice given by the LD previously). Following the principle of the Standing Order, the OSHB sets out the inspection frequency as follows:

- (a) ***Active sites.*** These are sites where works are in progress. They should be inspected at intervals of one to three months; and
- (b) ***Inactive sites.*** These are sites where works are only carried out intermittently (e.g. landscape works) or sites under defects liability period, where further works may have to be carried out. Inactive sites should be inspected at intervals of six to twelve months.

After an inspection was conducted, the Divisional Occupational Safety Officer (DSO) determines the date of the next inspection.

2.14 ***Non-BEC workplaces.*** It was stipulated in the LD's Standing Order that the priority of inspection work is determined according to its nature and urgency. Inspections are divided into two categories:

- (a) ***Inspections of priority cases.*** These are cases that shall be dealt with as soon as possible. Examples of inspections of priority cases are inspections in relation to accident/complaint investigations and follow-up of legal notices. Subsequent to the inspection, the DSO may consider a follow-up inspection necessary and determine the next inspection date (e.g. the inspecting officer could not gain access to the workplace); and
- (b) ***Rated inspections.*** These are cases that are subject to regular inspections. Regular inspections will only be made to workplaces under the hazardous trades. A point rating system is used to determine the inspection frequency of individual workplaces, ranging from once every 6 to 54 months. Each

workplace is assessed in accordance with a set of 11 elements (e.g. the size of premises and the number of employees) and points will be assigned to each of the 11 elements. Workplaces with higher points will be inspected more frequently.

Backlog in bringing up files for inspections

2.15 The LD has a bring-up system for workplace files to be brought up for inspections. When a workplace file is brought up to the attention of the DSO on the scheduled bring-up date, the DSO will assign the file to the inspecting officers for carrying out inspection. If a workplace file is not brought up to the attention of the DSO on the scheduled bring-up date and not assigned to the inspecting officers, the LD will count it as a backlog. The DSO reports the file backlog situation to the LD Headquarters through the submission of Monthly Progress Reports (MPRs). Table 3 shows the backlog situation at 20 Offices on 31 March 2016 and 31 March 2017. These 20 offices comprised all the 3 MIP Offices of the ISG (see para. 2.2(b)(i)), all the 6 BEC Offices of Hong Kong and Islands Region, all the 5 non-BEC Offices of Kowloon Region and all the 6 non-BEC Offices of New Territories West Region (see para. 2.2(a)).

Table 3
Backlog in bringing up inspections at 20 Offices
(31 March 2016 and 31 March 2017)

Stream	Office	Type of inspection	Number of backlog files		Change (percentage)
			31 March 2016	31 March 2017	
BEC	3 MIP Offices of ISG and 6 BEC Offices of Hong Kong and Islands Region	Active site inspection	0	24	+24 (N/A)
		Inactive site inspection	5,338	6,074	+736 (+14%)
Non-BEC	5 non-BEC Offices of Kowloon Region and 6 non-BEC Offices of New Territories West Region	Follow-up inspection of priority case	0	0	—
		Rated inspection	20,078	23,414	+3,336 (+17%)

Source: Audit analysis of LD records

Need to monitor time lapse between bring-up date and inspection date

2.16 Audit noted that the LD only monitors the backlog in bringing up the workplace files but not whether inspections are carried out according to schedule. Audit examined 80 inspections conducted by the LD in the period from 1 April 2016 to 31 March 2017 comprising 20 active site inspections, 20 inactive site inspections, 20 follow-up inspections of priority cases and 20 rated inspections conducted by these Offices. Audit found that 24 (30%) of 80 inspections were conducted more than 90 days after the workplace files were brought up (see Table 4). On average, the inspections were conducted 82 days after the bring-up date (see Table 5). According to the MPRs of the 20 Offices, 8 of the 9 BEC/MIP Offices reported no backlog of bringing up active site inspections (Note 4) and all the 11 non-BEC Offices reported no backlog of bringing up follow-up inspections of priority cases in the period from 1 April 2016 to 31 March 2017. In Audit's view, apart from monitoring whether the workplace files are brought up on time, it is more important for the LD to develop a computer system to monitor whether there are delays in carrying out the inspections.

Table 4
Time lapse between bring-up date
and inspection date
(1 April 2016 to 31 March 2017)

Time lapse (days)	Number of inspections (percentage)				
	Active site inspection	Inactive site inspection	Follow-up inspection of priority case	Rated inspection	Total
0 to 14 days	4 (20%)	12 (60%)	3 (15%)	6 (30%)	25 (31%)
15 to 30 days	4 (20%)	2 (10%)	0 (0%)	1 (5%)	7 (9%)
31 to 60 days	6 (30%)	1 (5%)	5 (25%)	3 (15%)	15 (19%)
61 to 90 days	3 (15%)	4 (20%)	1 (5%)	1 (5%)	9 (11%)
91 to 180 days	2 (10%)	1 (5%)	6 (30%)	1 (5%)	10 (13%)
181 to 260 days	1 (5%)	0 (0%)	5 (25%)	2 (10%)	8 (10%)
261 to 455 days	0 (0%)	0 (0%)	0 (0%)	6 (30%)	6 (7%)
Total	20 (100%)	20 (100%)	20 (100%)	20 (100%)	80 (100%)

} 24
(30%)

Source: Audit analysis of LD records

Note 4: One MIP Office reported backlogs in February and March 2017.

Table 5

**Average time lapse between bring-up date
and inspection date for 80 inspections
(1 April 2016 to 31 March 2017)**

Type of inspections	Number of inspections	Average time lapse (days)
Active site inspection	20	54
Inactive site inspection	20	30
Follow-up inspection of priority case	20	107
Rated inspection	20	137
Overall	80	82

Source: Audit analysis of LD records

***Need to clear the backlog
in bringing up workplace files for inspections***

2.17 Audit reviewed the MPRs of the 20 Offices as at 31 March 2016 and 31 March 2017 and found that:

- (a) of the 6 BEC Offices and 3 MIP Offices that are responsible for conducting inspections on inactive construction sites (i.e. sites where works are only carried out intermittently or sites under defects liability period), seven Offices had a total of 6,074 backlog files as at 31 March 2017 (see Table 6). The oldest backlog file was over six years (January 2011). As the typical duration of a defects liability period ranges from six months to one year, many of the inactive construction sites may no longer exist and the inspections on them are no longer possible. Audit considers that the LD needs to endeavour to clear the backlog as soon as possible; and

Table 6**Backlog in bringing up inactive site inspections
(31 March 2017)**

Office		Number of backlog files	Longest delay (no. of months)
BEC Office of Hong Kong and Islands Region	1	1,497	74
	2	1,129	62
	3	1,251	67
	4	1,230	69
	5	797	38
	6	111	31
MIP Office of ISG	1	59	2
Overall		6,074	74

Source: Audit analysis of LD records

- (b) of the 11 non-BEC Offices that are responsible for conducting rated inspections (see para. 2.14(b)), the number of backlog files increased by 17% from 20,078 on 31 March 2016 to 23,414 on 31 March 2017. As at 31 March 2017, the number of backlog files of individual Offices ranged from 471 to 4,445, with an average of 2,129 files (see Table 7). Audit considers that the LD needs to critically review the problem of backlog and take measures to clear the backlog as soon as possible.

Table 7

**Backlog in bringing up rated inspections
(31 March 2016 and 31 March 2017)**

Region	Non-BEC Office	Number of backlog files		Change (percentage)
		31 March 2016	31 March 2017	
Kowloon	1	4,065	4,445	+380 (+9%)
	2	1,379	1,916	+537 (+39%)
	3	2,577	2,796	+219 (+8%)
	4	2,606	2,666	+60 (+2%)
	5	1,492	1,534	+42 (+3%)
New Territories West	1	1,530	1,785	+255 (+17%)
	2	476	471	-5 (-1%)
	3	1,486	2,859	+1,373 (+92%)
	4	1,820	2,095	+275 (+15%)
	5	1,093	1,116	+23 (+2%)
	6	1,554	1,731	+177 (+11%)
Overall		20,078	23,414	+3,336 (+17%)
Average		1,825	2,129	+304 (+17%)

Source: Audit analysis of LD records

Need to improve documentation to cover all important areas of inspection work

2.18 It was stipulated in the OSHB Orders that one of the principles underpinning field operation's approach to inspection is that inspecting officers will strive for a consistent and demonstrably fair approach, i.e. demand similar action for similar circumstances.

2.19 After conducting an inspection, the inspecting officer documents his observations arising from the inspection in a workplace file and submit the file to his DSO for review. Audit noted that apart from updating the particulars of workplaces such as details of management, premises, work process, machinery and materials used, the inspecting officer only documented in the file the irregularities identified during the inspection. The officer did not document details of inspection work carried out, such as the work processes examined and the results of such examinations. Audit considers that in the absence of detailed documentation of inspection work, it would be difficult for the DSOs to ensure that:

- (a) adequate inspection work had been carried out;
- (b) important areas were not overlooked;
- (c) due professional judgement had been exercised to determine whether a situation was irregular; and
- (d) standard of inspection had been consistently applied.

The LD needs to improve the documentation of the inspection work performed to ensure that all important areas are covered. For instance, the LD may consider designing a comprehensive checklist covering all important areas of inspection to document the inspection work. The checklist can also facilitate DSOs' review of inspecting officers' work to ensure that inspections conducted by different officers are carried out properly and consistently.

Need to improve the frequency and sufficiency of supervisory visit

2.20 It was stipulated in the OSHB Guidelines that the following two types of supervisory visits should be conducted:

- (a) ***Re-inspection.*** DSOs are required to randomly re-inspect the workplaces that have been inspected by their inspecting officers to check and verify physically the reliability of the documented events and observations in the workplace files. The number of such re-inspections should not be less than 20% of the total number of supervisory visits; and
- (b) ***Joint inspection.*** DSOs are required to regularly carry out joint inspections with their inspecting officers to appraise their performance and to give them coaching.

2.21 Audit analysed the number of supervisory visits conducted by the DSOs of the 20 Offices (see para. 2.15) in the period from 1 April 2016 to 31 March 2017 (see Table 8) and found areas for improvement in the frequency and sufficiency of the supervisory visits, as follows:

- (a) ***Frequency of supervisory visits not stipulated in guidelines.*** Audit noted that the LD's guidelines only required that the number of re-inspections should not be less than 20% of the total number of supervisory visits. The guidelines did not stipulate the frequency of supervisory visits to be conducted (e.g. as a percentage of the total inspections). The number of supervisory visits conducted by the 20 Offices varied from 13 to 165 and accounted for 0.6% to 6.2% of the total number of inspections conducted. Audit considers that the LD needs to stipulate in the guidelines the frequency of supervisory visits; and
- (b) ***Insufficient re-inspections conducted.*** Audit examined the inspection records of 20 Offices. Of these 20 Offices, 12 (60%) Offices did not comply with the requirement that the number of re-inspections should not be less than 20% of the total number of supervisory visits. Among the 12 Offices, 6 Offices did not conduct re-inspections during the period. Audit considers that the LD needs to take measures to ensure that all Offices comply with the requirement on supervisory visit.

Occupational safety: inspection and enforcement

Table 8

**Supervisory visits conducted
(1 April 2016 to 31 March 2017)**

Office	Number of supervisory visits			Meeting minimum requirement on re-inspection	Number of inspections (b)	Percentage of supervisory visits (c) = (a) ÷ (b) × 100%
	Re-inspection (percentage of total supervisory visits)	Joint inspection (percentage of total supervisory visits)	Total (a)			
1	0	13 (100%)	13	✗	2,317	0.6%
2	8 (25%)	24 (75%)	32	✓	2,534	1.3%
3	0	69 (100%)	69	✗	3,034	2.3%
4	5 (9%)	51 (91%)	56	✗	2,235	2.5%
5	70 (77%)	21 (23%)	91	✓	3,233	2.8%
6	4 (7%)	53 (93%)	57	✗	1,873	3.0%
7	0	60 (100%)	60	✗	1,976	3.0%
8	0	55 (100%)	55	✗	1,773	3.1%
9	57 (55%)	47 (45%)	104	✓	3,381	3.1%
10	15 (15%)	83 (85%)	98	✗	3,023	3.2%
11	9 (18%)	40 (82%)	49	✗	1,414	3.5%
12	0	78 (100%)	78	✗	2,070	3.8%
13	26 (25%)	80 (75%)	106	✓	2,366	4.5%
14	40 (24%)	125 (76%)	165	✓	3,594	4.6%
15	70 (49%)	73 (51%)	143	✓	3,012	4.7%
16	11 (9%)	112 (91%)	123	✗	2,502	4.9%
17	65 (42%)	91 (58%)	156	✓	3,093	5.0%
18	15 (13%)	104 (87%)	119	✗	2,270	5.2%
19	51 (32%)	109 (68%)	160	✓	3,008	5.3%
20	0	150 (100%)	150	✗	2,428	6.2%

Source: Audit analysis of LD records

Need to set suitable performance targets

2.22 The LD reported in its COR two key performance indicators in relation to the field operations conducted by the Operations Division, namely “Inspections under the FIUO and the OSHO” and “Promotional visits to workplaces under the FIUO and the OSHO”. Promotional visits are mostly conducted by the inspecting officers when they visit workplaces for inspections. Inspecting officers would normally conduct promotional visits to sizeable establishments/construction sites. Table 9 shows the targets and actual performance of field operations in the period from 2012 to 2016.

Table 9
Targets and actual performance of field operations
(2012 to 2016)

	2012	2013	2014	2015	2016	Total
<i>Inspections under the FIUO and the OSHO</i>						
Target	113,400	113,400	113,400	114,700	114,700	569,600
Actual	128,821	123,115	124,907	130,173	131,339	638,355
Difference	15,421 (13.6%)	9,715 (8.6%)	11,507 (10.1%)	15,473 (13.5%)	16,639 (14.5%)	68,755 (12.1%)
<i>Promotional visits to workplaces under the FIUO and the OSHO</i>						
Target	4,800	4,800	4,800	4,860	4,860	24,120
Actual	5,373	5,901	5,837	5,994	5,436	28,541
Difference	573 (11.9%)	1,101 (22.9%)	1,037 (21.6%)	1,134 (23.3%)	576 (11.9%)	4,421 (18.3%)

Source: Audit analysis of LD records

Occupational safety: inspection and enforcement

2.23 Performance measures aim at setting specific goals, challenging an organisation to improve. As shown in Table 9, the LD had over-performed in the period from 2012 to 2016 by a significant margin. During the period, the actual performance of the indicator “Inspections under the FIUO and the OSHO” averaged 127,671 per year and exceeded the target by 8.6% to 14.5% while the performance of the indicator “Promotional visits to workplaces under the FIUO and the OSHO” averaged 5,708 per year and exceeded the target by 11.9% to 23.3%. Audit noted that the targets of the two indicators for 2017 remained at the same levels for 2016 (i.e. 114,700 inspections and 4,860 promotional visits). Audit considers that the LD needs to set performance targets at a level that is challenging and yet achievable.

Need to provide adequate elaboration on performance measures

2.24 The inspections conducted by an inspecting officer are reported as his output in the MPR (see para. 2.15). Audit found that:

- (a) if an inspection is conducted jointly by more than one inspecting officer, each individual officer would separately report the inspection as his output. The LD added up their total output for reporting in the CORs. Audit analysis of the LD’s records on inspections conducted from 2012 to 2016 revealed that the numbers of workplaces inspected per year ranged from 44,756 to 73,565 (i.e. one inspection visit to one workplace was counted as one irrespective of how many inspecting officers took part in the inspection work) (see Table 10); and

Table 10

Number of inspections to workplaces (2012 to 2016)

Year	Number of workplaces inspected	Number of inspections reported in COR
2012	73,565	128,821
2013	67,010	123,115
2014	58,897	124,907
2015	61,127	130,173
2016	44,756	131,339

Source: Audit analysis of LD records

- (b) the numbers of inspections reported in the CORs included cases where the workplaces were locked, removed or not in operation. The LD has not kept separate statistics on the numbers of these incidents.

2.25 The LD needs to separately disclose in the COR the number of cases where the workplaces were locked, removed or not in operation, and the number of workplaces inspected.

Audit recommendations

2.26 Audit has *recommended* that the Commissioner for Labour should:

- (a) take measures to ensure that there is no delay in:
 - (i) bringing up cases for inspection; and
 - (ii) conducting inspections after the cases were brought up for inspection;
- (b) take measures to clear the existing backlog of inspections as soon as practicable;
- (c) improve the documentation of the inspection work performed;
- (d) stipulate in the guidelines the frequency of supervisory visits (for example, as a percentage of the total number of inspections conducted);
- (e) take measures to ensure that the requirements on supervisory visit are complied with;
- (f) set suitable performance targets for the inspections and promotional visits conducted by the Operations Division at a level that is challenging and achievable; and

- (g) separately disclose in the COR the number of cases where the workplaces were locked, removed or not in operation, and the number of workplaces inspected.

Response from the Government

2.27 The Commissioner for Labour agrees with the audit recommendations. He has said that:

- (a) the LD's inspection strategy is risk-based. The LD places priority on workplaces with higher risk, such as workplaces subject to the statutory notification requirements, active construction sites, priority non-BEC cases, complaint cases, and workplaces carrying prevailing occupational risks at different times. While noting that the backlog cases in bringing up for inspection are low-risk ones, the LD agrees that the backlog situation needs to be addressed in accordance with the risk-based inspection approach. The LD will refine the bring-up system to align it with the LD's risk-based inspection approach;
- (b) inspecting officers are currently required to complete various inspection records and reports after each inspection. The current system also requires the DSOs to sign off every workplace file to ensure that each inspection is conducted properly. The LD will devise a checklist to further strengthen the DSOs' monitoring work;
- (c) the LD will set performance targets for inspections and promotional visits with reference to the manpower situation and the prevailing enforcement strategy; and
- (d) conditions of workplaces can only be ascertained at the point of inspection. In cases where the original workplace is taken up by another business (i.e. removal) or the workplace is accessible although not in operation, the inspecting officer can still conduct an inspection. The LD will include the number of such inspections in the COR.

Enforcement action

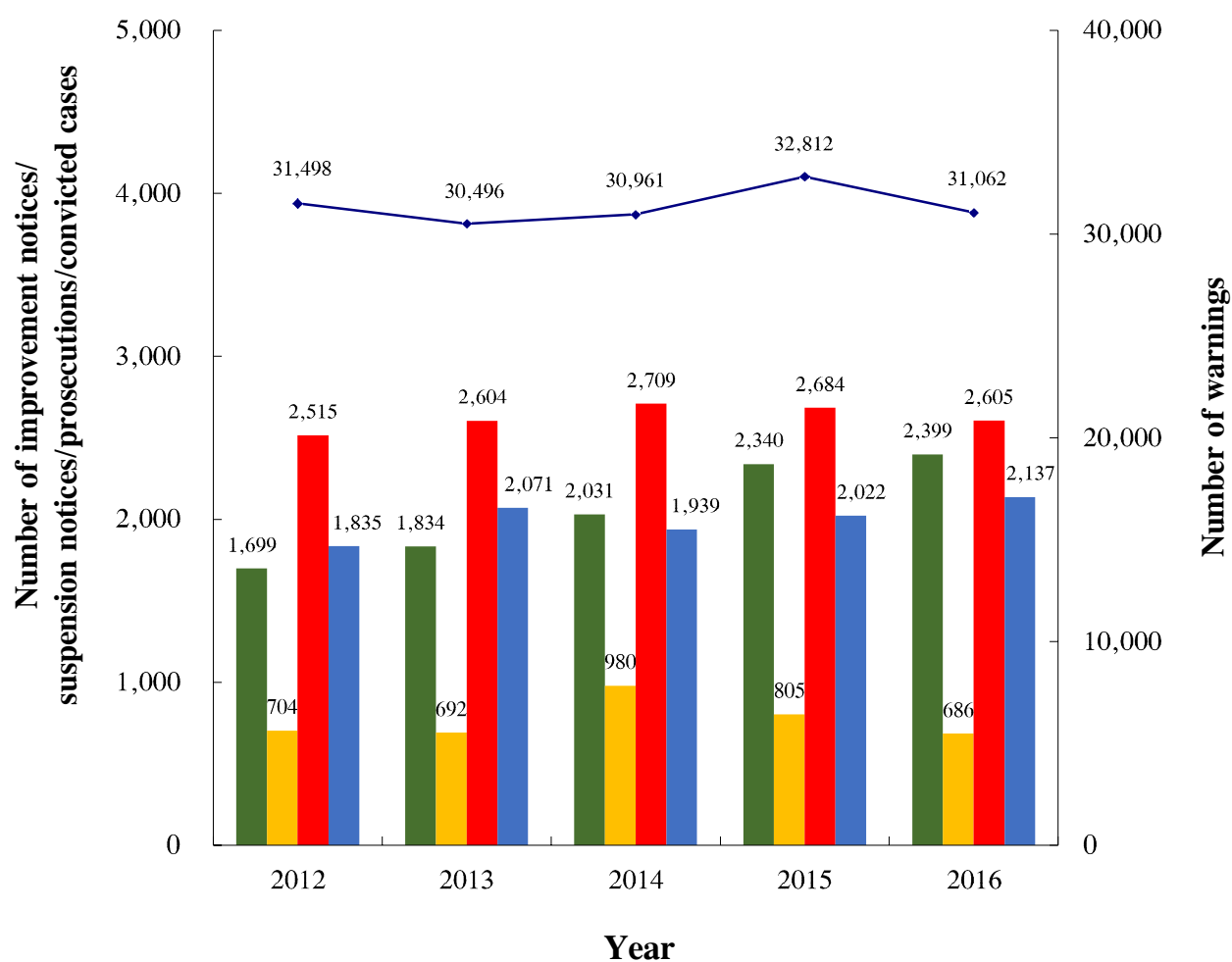
2.28 According to the LD's Standing Order, inspecting officers may take the following enforcement action against any irregularity identified during inspections:

- (a) **Warning.** This is for breaches of safety and health regulations that do not normally give rise to imminent or serious risks of bodily injury (for example, lack of first-aid equipment and persons trained in first-aid);
- (b) **Improvement notice.** This is for breaches of safety and health regulations which are related to risks less serious in nature or where some actions have been taken to reduce the risk substantially despite the fact that the relevant regulations have not been fully complied with (for example, improper use of personal protection equipment);
- (c) **Suspension notice.** This is for suspension of any hazardous work or process or the use of any dangerous equipment which may cause an imminent risk of death or serious bodily injury to workers (for example, lifting appliance being used to carry goods well in excess of its capacity); and
- (d) **Prosecution.** This is for breaches of safety and health regulations that will pose risks of serious bodily injury/ill health or considerable fire hazards.

Figure 7 shows the statistics on the enforcement action taken by the LD and cases convicted for the period from 2012 to 2016.

Figure 7

Enforcement action on irregularities identified during inspections and cases convicted (2012 to 2016)



Legend:

- Improvement notices
- Suspension notices
- Prosecutions
- Convicted cases
- Warnings

Source: *Audit analysis of LD records*

Remarks: *The number of convicted cases in a year includes those cases on which prosecution began in previous years.*

Need to strengthen deterrent effect of occupational safety legislation

2.29 During the period 2013 to 2015, the LD considered the issue of the deterrent effect against non-compliance with the legislation related to occupational safety. Since then, the LD:

- (a) had submitted information to the court for reference in sentencing. Such information included the serious consequences arising from the accidents in question, the upward trend of the number of accidents concerned, and the highest penalty imposed on similar cases in the past; and
- (b) depending on the circumstances of individual cases, had requested the Department of Justice (DoJ) to consider filing a review or an appeal to the court in respect of the conviction and the penalty.

2.30 Audit analysed the cases convicted under the FIUO and the OSHO in the period from 2012 to 2016 and found that the average amount of fines imposed by the court on convicted cases had increased by 47% from \$7,723 in 2012 to \$11,390 in 2016 (see Table 11). However, Audit analysis of the highest amount and the average amount of fines under the five most common offences of the FIUO and the OSHO revealed that notwithstanding the increase in amount of fines, the highest amount and the average amount were significantly below the maximum amount stipulated in the legislation (see Table 12).

Table 11**Average amount of fine for
convicted cases under FIUO and OSHO
(2012 to 2016)**

Year	Fatal cases		Non-fatal cases		All cases	
	No. of convicted cases	Average fine (\$)	No. of convicted cases	Average fine (\$)	No. of convicted cases	Average fine (\$)
2012	59	14,212	1,776	7,508	1,835	7,723
2013	56	15,959	2,015	7,821	2,071	8,041
2014	143	21,962	1,796	9,419	1,939	10,344
2015	104	19,231	1,918	10,305	2,022	10,764
2016	138	28,022	1,999	10,242	2,137	11,390

Source: Audit analysis of LD records

Remarks: In addition to fines imposed by the court under the FIUO and OSHO, employers are also liable for compensation under the ECO for work injuries and fatalities as well as prescribed occupational diseases of their employees. As the ECO does not limit the civil liability of employers, when the injury or death is caused by the negligence or other wrongful acts of the employers, the employees and family members of the deceased employees may recover compensation and sue for damages as well.

Table 12

**Highest amount and average amount of fine for
five most common offences under FIUO and OSHO
(2012 to 2016)**

Offence		Number of convicted cases	Maximum statutory fine (\$)	Highest fine imposed (\$)	Average fine (\$)
1	Failure to ensure that suitable and adequate access to and egress from the construction site is provided and properly maintained	545	200,000	80,000	11,633
2	Failure to take adequate steps to prevent any person on the construction site from falling from height (for contractor responsible for the construction site)	1,054		90,000	16,315
3	Failure to take adequate steps to prevent any person on the construction site from falling from height (for contractor who has direct control over the construction work)	922		120,000	11,211
4	Failure to maintain in good condition and free from obstruction the means of escape from the workplace in case of fire	847		70,000	9,674
5	Failure to ensure that all means of escape from the workplace are maintained in a safe condition and kept free from obstruction	577		100,000	12,642

Source: Audit analysis of LD records

Occupational safety: inspection and enforcement

2.31 According to the LD:

- (a) it had already implemented the measures to enhance the deterrent effect against non-compliance with the legislation related to occupational safety (see para. 2.29); and
- (b) legislative amendment would be the remaining way to increase penalty in a substantial manner.

Audit recommendation

2.32 Audit has *recommended* that the Commissioner for Labour should monitor closely the need to review the labour legislation with a view to strengthening the deterrent effect of the legislation.

Response from the Government

2.33 The Commissioner for Labour agrees with the audit recommendation.

PART 3: OCCUPATIONAL SAFETY: TRAINING

3.1 This PART examines the LD's work on training on occupational safety. Audit found room for improvement in the following areas:

- (a) mandatory safety training courses (paras. 3.2 to 3.11);
- (b) Registered Safety Officers and Registered Safety Auditors (paras. 3.12 to 3.26); and
- (c) performance reporting (paras. 3.27 to 3.30).

Mandatory safety training courses

3.2 According to the FIUO and its subsidiary regulations, every person engaged in specific high risk sectors, activities or machine operations is required to complete the relevant mandatory safety training (MST) course organised by a training course provider (TCP) and obtain a relevant certificate. There are six types of MST courses. In 2016, there were 146 TCPs providing 704 MST courses. These 146 TCPs issued a total of 349,056 certificates (see Table 13).

Table 13**Number of TCPs, MST courses provided and certificates issued
(2016)**

Type of MST course		Number of TCPs	Number of MST courses provided	Number of certificates issued
1	Confined Spaces Operation Safety Training Course	47	150	43,157
2	Crane Operator Safety Training Course	37	112	5,163
3	Gas Welding Safety Training Course	22	37	7,909
4	Loadshifting Machine Operator Safety Training Course	45	159	13,524
5	Mandatory Basic Safety Training Course	112	243	277,734
6	Person Working on Suspended Working Platform Safety Training Course	2	3	1,569
Overall		146 (Note)	704	349,056

Source: LD records

Note: The numbers of TCPs do not add up because some TCPs provided more than one type of courses.

Monitoring of TCPs

3.3 MST courses provided by TCPs must be recognised by the LD. To assure the quality of the MST courses, the LD promulgated the Approval Conditions setting out the requirements (e.g. course contents and qualification of trainers) for all TCPs to follow.

3.4 The LD has promulgated a set of Guidelines on monitoring the performance of TCPs. Surprise inspections are carried out on TCPs to inspect their conduct of MST courses. To maintain consistency, objectivity and fairness, the LD uses a standard inspection checklist during the inspections. The checklist contains ten aspects (Note 5). Furthermore, the LD complements its TCP inspections with regular undercover inspections which involve inspecting officers in the guise of a course participant (i.e. covert operation). When a breach of the Approval Conditions is found, enforcement action (e.g. issuing warnings or directions or withdrawal of course recognition) will be taken according to the severity of the breach. In 2016, the LD issued 17 warning letters and 5 directions.

Need to improve planning of inspection

3.5 As stipulated in the LD's Guidelines, every TCP should be inspected by the LD at least once a year. The inspection interval of individual TCPs is determined by their business nature:

- (a) commercial operators providing MST courses to the public should be inspected once every three months;
- (b) organisations providing in-house training as well as trade unions and associations should be inspected once every nine months; and
- (c) professional institutions, universities and statutory training bodies should be inspected annually.

Note 5: *The ten aspects are: (a) delivery of course contents; (b) course duration; (c) performance of trainers; (d) training venue and training facilities; (e) trainer to trainees ratio; (f) conduct of examination; (g) keeping of training records; (h) issuing of certificates; (i) enrolment of trainees and complaint procedures; and (j) medium of training.*

3.6 *Many inspections conducted when there were no course sessions.* Seven of the ten aspects of the inspection checklist can only be observed during course sessions, namely:

- (a) delivery of course contents;
- (b) course duration;
- (c) performance of trainers;
- (d) training venue and training facilities;
- (e) trainer to trainees ratio;
- (f) conduct of examination; and
- (g) medium of training.

In 2016, the LD conducted 225 inspections on 146 TCPs. Audit examination of the inspection records revealed that of the 225 inspections, 182 (81 %) were conducted at the time when no course session was available for observation. As a result, many aspects of the courses could not be observed. In these inspections, the LD conducted checking on the TCPs' documentation. Audit noted that it is stipulated in the Approval Conditions that a TCP should submit the course schedule, including the examination timetable, to the LD at least three working days before the commencement of the course. Audit considers that the LD needs to make good use of the information in planning its inspections to arrange as far as practicable more inspections when there is a course session.

Review of MST courses

3.7 In 2009, the LD conducted a review to devise improvement measures on recognition and monitoring of MST courses. The review identified a number of problems such as:

- (a) discrepancies in course contents among the same type of MST courses provided by different TCPs;
- (b) removing part of the course contents by the TCPs without obtaining prior approval from the LD; and
- (c) leakage of examination contents by the TCPs.

3.8 In April 2011, the LD proposed to the Legislative Council (LegCo) Panel on Manpower a two-phase approach to implement the improvement measures. The LD informed the Panel that:

- (a) ***Phase One.*** In Phase One, three improvement measures would be introduced to all MST courses:
 - (i) standardisation of course contents;
 - (ii) consolidation of the Guidance Notes, which sets out the procedures for a TCP to apply for recognition of a MST course; and
 - (iii) centralisation of issuance of examination papers by the LD; and
- (b) ***Phase Two.*** Subject to the effectiveness of the improvement measures implemented in Phase One, consider to implement the following improvement measures in Phase Two:
 - (i) accreditation of the TCPs' governance and quality assurance capability;
 - (ii) introduction of a validity period for recognised courses; and

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- (iii) introduction of a demerit point system for the TCPs and strengthening disciplinary action against TCPs with poor performance.

The Panel supported the LD to implement the improvement measures in Phase One and considered that the LD should continue to examine other measures with a view to enabling their early implementation in Phase Two.

3.9 In October 2011, the LD reported the progress of the implementation of improvement measures to the LegCo Panel on Manpower. The LD informed the Panel that:

- (a) the Guidance Notes of all the six types of MST courses were consolidated and came into effect in September 2011; and
- (b) with effect from September 2011, the course contents of the Mandatory Basic Safety Training Course had been standardised and its examination papers had been issued by the LD centrally.

Audit noted that up to August 2017, two of the three Phase One improvement measures, namely the standardisation of course contents and the centralisation of issuance of examination papers for the remaining five types of MST courses had not been implemented. Furthermore, there was also no timetable to implement these measures and the Phase Two measures. Audit considers that the LD needs to expedite the implementation of the improvement measures.

Audit recommendations

3.10 **Audit has *recommended* that the Commissioner for Labour should:**

- (a) **arrange inspections on the TCPs during time period when there are course sessions taking place as far as practicable; and**
- (b) **expedite the implementation of the improvement measures recommended by the 2009 review on MST courses.**

Response from the Government

3.11 The Commissioner for Labour agrees with the audit recommendations. He has said that:

- (a) of the 182 TCP inspections conducted when there were no course sessions, 95 were not only typical inspections but also follow-up on warning/withdrawal cases and complaint investigations. Covert operations are proven to be an effective approach to monitor the effectiveness of MST courses. The LD will review its relevant guidelines with a view to arranging more during-class inspections in conjunction with other surprise inspections and covert operations to achieve the optimal impact; and
- (b) the LD has been focusing its efforts in refining the course content and the Approval Conditions of the Mandatory Basic Safety Training Course, which is required to be taken by all construction workers. The LD will draw up a timetable to guide implementation of the improvement measures on MST courses.

Registered Safety Officers and Registered Safety Auditors

3.12 Under the FIUO, proprietors of industrial undertakings have a general duty to ensure the safety and health conditions of their employees. To further promote occupational safety, the subsidiary regulations set out the following requirements for those more risk-prone industries:

- (a) **Registered Safety Officers (RSOs).** It was stipulated in the Factories and Industrial Undertakings (Safety Officers and Safety Supervisors) (FIU (SOSS)) Regulations (Cap. 59Z) that a proprietor of a construction site who is a principal contractor shall employ an RSO on a full time basis when the total number of persons employed on his construction site or sites is 100 or more. The same requirement applies to a proprietor of a shipyard or a container handling workplace if the proprietor employs 100 or more persons in one or more of his shipyards or container handling workplaces. The duties of an RSO are to assist the proprietor of an industrial undertaking in promoting the safety and health of employees, for example:

- (i) inspecting the workplace to identify potential hazards and reporting the findings with recommendations for correction to the proprietor; and
 - (ii) investigating accidents and dangerous occurrences, and reporting with recommendations for prevention to the proprietor; and
- (b) **Registered Safety Auditors (RSAs).** It was stipulated in the Factories and Industrial Undertakings (Safety Management) (FIU (SM)) Regulation (Cap. 59AF) that a contractor of a single or multiple construction sites having 100 or more workers, or having a construction project with a contract value of \$100 million or more, shall implement a safety management system (Note 6) and appoint an RSA to conduct safety audits on the system at specified regular intervals. The same requirement applies to a proprietor of a single or multiple factories, shipyard business and designated industrial undertaking (i.e. those involved in the generation, transformation and transmission of electricity, town gas or liquefied petroleum gas and in the handling of containers) with 100 or more workers.

Note 6: *The safety management system contains 14 elements. Examples of the elements are: (a) a safety policy which states the commitment of the proprietor or contractor to safety and health at work; and (b) a programme of inspection to identify hazardous conditions and for the rectification of any such conditions at regular intervals or as appropriate.*

3.13 Table 14 shows the numbers of RSOs and RSAs as at the year end of 2012 to 2016.

Table 14

**Number of RSOs and RSAs
(2012 to 2016)**

Year (as at 31 December)	RSO	RSA
2012	2,546	1,094
2013	2,846	1,137
2014	2,977	1,179
2015	3,260	1,225
2016	3,607	1,261

Source: LD records

Eligibility of RSOs and RSAs

3.14 The LD is responsible for the registration of Safety Officers and Safety Auditors. The eligibility criteria of RSOs and RSAs are set out as follows:

- (a) **RSOs.** To register as an RSO, a person shall possess one of the specified academic qualifications and other specified requirements (e.g. relevant experience of not less than one year); and
- (b) **RSAs.** To register as an RSA, a person shall be an RSO and fulfil the specified requirements (e.g. having successfully completed a scheme conducted by a registered Scheme Operator).

Some RSAs are not RSOs

3.15 Prior to June 2002, the designation of an RSO was valid for life. The FIU (SOSS) Regulations were amended in 2002. The amendments provide that the registration of RSOs shall be valid for a period of four years subject to renewal or revalidation. An application for renewal or revalidation of registration shall only be

approved by the Commissioner for Labour if he is satisfied that the applicant has completed a total of not less than 100 hours of Continuing Professional Development Programmes in occupational safety and health in the four years immediately preceding the application.

3.16 One of the qualifications for registration as an RSA is that the person shall be an RSO. Under the renewal/revalidation requirement for the RSOs, there is a possibility that some RSAs who cease to be RSOs after they have become RSAs. This is because some RSAs, who at the time of registration were RSOs, may choose not to apply for renewal or revalidation after the expiry of the four-year period. In September 2000, the LD consulted the DoJ whether the status of these RSAs would be affected. According to the legal opinion:

- (a) there was no express provision in the FIU (SM) Regulation which nullified the validity of the registration of an RSA when he ceased to be an RSO. It might however be argued that the requirement of being an RSO was a necessary condition for being an RSA; and
- (b) there was no clear authority on the question as to whether the validity of the designation of an RSA would be affected if he was no longer an RSO.

3.17 In response to Audit enquiry, the DoJ advised in October 2017 that:

- (a) according to the FIU (SM) Regulation, where the Commissioner for Labour has ceased to be satisfied that an RSA is competent to be so registered or fit and proper to be so registered, he may refer the matter for hearing by a disciplinary board. After concluding its hearing, the disciplinary board may exonerate the registered person concerned or may do one or more of the following:
 - (i) reprimand the registered person;
 - (ii) cancel the registration of the registered person; and
 - (iii) suspend the registered person's registration for a specified period of time; and

- (b) it appeared that although the Regulation did not expressly enable the Commissioner for Labour to cancel the registration of an RSA if he was no longer an RSO, the Regulation may be resorted to which may result in cancellation of registration of an RSA if the disciplinary board considered it appropriate to do so.

3.18 It was the LD's policy intention that RSAs should also be RSOs. Audit compared the lists of RSOs and RSAs as at 31 May 2017 and noted that 29 (2.3%) of a total number of 1,273 RSAs were not on the RSO list. Unlike RSO, the designation of an RSA is valid for life and an RSA is not required to receive continuous training to ensure that he possesses up-to-date knowledge in promoting safety and health in a workplace. The LD needs to review whether there is a need to revise the FIU (SM) Regulation and, where necessary, consider initiating action to revise the Regulation.

Safety Auditor Training Scheme Operators

3.19 To register as an RSA, one of the specified requirements is that a person shall have successfully completed a scheme conducted by a registered Scheme Operator recognised by the LD (see para. 3.14(b)). The LD has promulgated the Guidance Notes for Registration as a Safety Auditor Training Scheme Operator setting out the criteria and procedures for registration as a Scheme Operator. The LD publishes a list of registered Scheme Operators on its website. As at 30 June 2017, there were 15 registered Scheme Operators.

3.20 According to the Guidance Notes for Registration as a Safety Auditor Training Scheme Operator, Scheme Operators should collect feedback or evaluation of the training schemes from the students and submit a summary with the Scheme Operator's comments to the LD for reference. The Guidance Notes also state that the LD may inspect the conduct of schemes. As stipulated in the LD's Guidelines, the LD should:

- (a) conduct at least one monitoring visit for each round of intake and complete a standard checklist;

- (b) issue a copy of the completed checklist to Scheme Operators within seven working days after the monitoring visits; and
- (c) conduct at least two independent follow-up inspections to two Scheme Operators selected at random within a year.

3.21 *Need to improve monitoring of Scheme Operators.* In 2016, there were four Scheme Operators who conducted training schemes with a total of seven rounds of intakes. The LD conducted one monitoring visit to each of the seven rounds of intakes. Audit found the following areas for improvement:

- (a) although none of the four Scheme Operators had submitted the summary of students' feedback, the LD did not follow up with the Operators;
- (b) during monitoring visits, the visiting officer should inspect seven aspects according to the checklist (Note 7). However, in all the seven visits only four aspects were inspected. The "examination session", "issuing of certificates" and "security steps" aspects had not been checked;
- (c) the LD only issued the completed checklists to three Operators after three of the seven visits within seven working days; and
- (d) no follow-up inspections were conducted by the LD.

Audit considers that the LD needs to take measures to strengthen monitoring of the Scheme Operators.

Safety Officer course providers

3.22 To qualify as an RSO, a person shall possess an academic qualification recognised by the LD. An organisation may apply for its academic course to be recognised by the LD by submitting a proposal of the course and a full set of

Note 7: *The seven aspects are: (a) venue features; (b) teaching aids; (c) presentation skills; (d) administration system; (e) examination session; (f) issuing of certificates; and (g) security steps.*

course materials for the LD's vetting. The LD publishes a list of courses as recognised academic qualifications for RSOs on its website. As at 30 June 2017, there were 29 recognised courses provided by ten institutions. Of the 29 courses, 16 were open for enrolment in 2016. The remaining 13 courses were ceased to be provided by the concerned institutions.

3.23 *Guidance Notes on application for recognition of academic course not promulgated.* The LD promulgates Guidance Notes to facilitate the applications. For instance, the LD has promulgated Guidance Notes for application for recognition of MST courses and Guidance Notes for Registration as Safety Auditor Training Scheme Operator. However, Guidance Notes on applications for academic courses as recognised qualifications for RSOs were not promulgated. Audit considers that the LD needs to consider the need to promulgate such Guidance Notes.

3.24 *No guidelines on inspection on recognised academic courses.* The LD had not devised guidelines on conducting inspections on recognised academic courses as qualification for RSOs. In 2016, there were 14 rounds of intakes for the 16 recognised courses. The LD had conducted 13 monitoring visits to the 14 rounds of intakes (Note 8). The LD documented the results of the visits in the same standard checklist used for monitoring visit to Safety Auditor Training Scheme Operator. However, only four of the seven aspects were inspected (i.e. venue features, teaching aids, presentation skills and administration system). Audit considers that the LD needs to devise inspection guidelines on recognised academic courses, specifying detailed inspection procedures such as the inspection frequency and the areas to be inspected (e.g. examination session).

Audit recommendations

3.25 *Audit has recommended that the Commissioner for Labour should:*

- (a) *review whether there is a need to revise the FIU (SM) Regulation to address the shortcomings that some RSAs are not RSOs and, where necessary, consider initiating action to revise the Regulation;***

Note 8: *One of the 14 rounds of intakes is a two-year programme. According to the LD, monitoring visit will be arranged in the second year of the programme (i.e. 2017).*

- (b) take measures to strengthen the monitoring of the Safety Auditor Training Scheme Operators;
- (c) promulgate guidelines on applications for academic courses as recognised qualifications for RSOs with a view to facilitating applications; and
- (d) devise internal guidelines on inspections on recognised academic courses for RSOs with a view to enhancing the effectiveness and efficiency of the inspections.

Response from the Government

3.26 The Commissioner for Labour agrees with the audit recommendations. He has said that:

- (a) the LD will take action to ensure that RSAs are RSOs; and
- (b) LD officers sit on the Board of Examination convened for each of the intakes of the Safety Auditor Training schemes where examination papers and certificates issued can be examined. The LD will refine the relevant Guidelines to strengthen monitoring of Safety Auditor Training Scheme Operators.

Performance reporting

3.27 *Documents not available to substantiate actual performance.* The LD has published on its website three performance pledges, namely completion of processing applications within two weeks upon receipt and verification of all relevant information and documentation for:

- (a) registration as Safety Officers or Safety Auditors;
- (b) renewal or revalidation as Safety Officers; and
- (c) recognition of MST courses.

The LD reported on its website that the three pledges were fully met in 2016. However, no supporting documents were available to substantiate that the pledges had been achieved. Audit considers that the LD needs to keep supporting documents to substantiate the levels of performance achieved.

3.28 *Need to develop more performance pledges.* Audit noted that the LD has set two performance pledges on the processing of applications for registration/renewal/revalidation as RSOs and registration as RSAs. However, there was no performance pledge on the processing of applications for:

- (a) the recognition of Safety Auditor Training Scheme Operator; and
- (b) the recognition of academic course for Safety Officers.

Audit considers that the LD needs to consider developing performance pledges in this regard.

Audit recommendations

3.29 **Audit has recommended that the Commissioner for Labour should:**

- (a) **strengthen the monitoring of the processing time of applications for:**
 - (i) **registration as RSOs or RSAs;**
 - (ii) **renewal or revalidation as RSOs; and**
 - (iii) **recognition of MST courses;**
- (b) **keep proper records to substantiate the achievement of performance pledges; and**
- (c) **consider developing performance pledges for processing of applications for the recognition of Safety Auditor Training Scheme Operator and academic course for Safety Officers.**

Response from the Government

3.30 The Commissioner for Labour agrees with the audit recommendations. He has said that there is a mechanism in place to ensure the performance pledges are met. The LD has checked the concerned applications processed in the second half of 2016 and confirmed that the processing time of all applications met the performance pledges. The LD agrees that proper record should be kept in future to strengthen monitoring of meeting the pledges.

PART 4: OCCUPATIONAL HEALTH

4.1 This PART examines the work of the LD on occupational health, focusing on the following areas:

- (a) medical examination of radiation workers (paras. 4.4 to 4.17);
- (b) workplace inspection (paras. 4.18 to 4.22); and
- (c) performance reporting (paras. 4.23 to 4.26).

Background

4.2 The two Occupational Medicine Divisions, and the three Occupational Hygiene Divisions (OHDs) of the OSHB (see Appendix B) are responsible for preventing occupational diseases and promoting health at work (Note 9).

4.3 The work of the divisions mainly includes:

- (a) providing occupational clinical services at the Kwun Tong Occupational Health Clinic (KTOHC) and the Fanling Occupational Health Clinic (Note 10);

Note 9: *Under the OSHB, there are four Integrated Services Teams. These Teams carry out inspections of workplaces to enforce legislation relating to occupational health in addition to occupational safety (see para. 2.2(b)(iii)).*

Note 10: *Consultation at the clinics is by appointment in person or by phone. Doctors' referrals are not required. Consultation fees are set at the same level as other government specialist clinics.*

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- (b) providing medical examination services (Note 11) for workers prone to exposure to radiation;
- (c) providing medical examination services for civil servants who are exposed to occupational hazards (Note 12);
- (d) conducting sick leave clearance interview of employees with compensation claims;
- (e) providing advisory services to the public, organising exhibitions and delivering talks on health and hygiene aspects of occupational health issues; and
- (f) conducting inspections and surveys to enforce legislation relating to occupational health and hygiene.

Table 15 shows their outputs in the period from 2012 to 2016.

Note 11: *Under the subsidiary regulations of the Radiation Ordinance (Cap. 303), workers prone to exposure to radiation are required to undergo medical examinations.*

Note 12: *The examinations are conducted at the request of some government departments to safeguard the health of workers prone to exposure to specific occupational hazards (e.g. asbestos and noise).*

Table 15

**Outputs of occupational health work
(2012 to 2016)**

Nature of work	2012 (No.)	2013 (No.)	2014 (No.)	2015 (No.)	2016 (No.)
Clinical consultation	13,007	11,855	10,396	9,054	10,444
Survey (Note 1)	6,676	6,577	6,258	5,978	7,018
Inspection	3,755	3,616	3,492	3,664	4,205
Investigation (Note 2)	2,979	2,884	3,093	3,433	2,983
Medical examination	1,364	1,692	1,929	1,639	1,471
Talk	1,178	1,069	1,186	1,239	1,243
Assessment (Note 3)	2,411	2,278	488	1,488	713

Source: Audit analysis of LD records

Note 1: A survey is an activity which involves detailed examination at the workplace on a particular potential health hazard (e.g. lighting and thermal) or an unhealthy work process which requires detailed scientific measurement. Surveys form part of the work undertaken by LD staff in workplace inspections.

Note 2: These were investigations on occupational diseases or work-relatedness of workers' health problems by doctors of the OSHB.

Note 3: These were assessments of medical fitness for pilots and air traffic control officers.

Medical examinations of radiation workers

4.4 Under the subsidiary regulations of the Radiation Ordinance (Cap. 303), workers prone to exposure to radiation are required to undergo medical examinations for their first employment and subsequently at an interval not exceeding 14 months during the continuance of such employment. The objective is to safeguard the health of the workers and to ensure that they are medically fit for the work.

4.5 The Radiation Board formed under the Radiation Ordinance appoints the Radiation Board Medical Panel to examine workers handling radioactive substances and irradiating apparatus. The Board is chaired by the Director of Health. Panel members are occupational health officers from the Occupational Medicine Division (Clinical Services). In 2016, a total of 834 examinations were carried out at the KTOHC of the Occupational Medicine Division (Clinical Services) (Note 13).

Many reserved time slots not used

4.6 Every year in September, based on the estimated number of radiation medical examinations to be carried out, the KTOHC reserves a consultation room for a number of morning sessions of the forthcoming year exclusively for carrying out the examinations. A medical doctor mans each of the reserved sessions. No other clinical service will be provided by the doctor during the reserved sessions.

4.7 *Some time slots not used due to no-show cases.* For each reserved session, 30 radiation medical examinations can be carried out. Staff of the Department of Health (as secretariat for the Radiation Board) would remind all workers of their appointments three days in advance. The KTOHC's records showed that for each year in the period from 2012 to 2017 (up to June), there were on average 2.7 to 4.2 no-show cases per session. The no-show rates ranged from 11% to 15% (see Table 16).

Note 13: *Upon receipt of applications from hospitals and universities, the Radiation Board Medical Panel may grant approval for them to conduct the concerned medical examinations for their staff at their facilities.*

Table 16

**Analysis of radiation examinations conducted
(2012 to 2017)**

	2012	2013	2014	2015	2016	2017 (Jan to June)
Total						
No. of sessions (a)	30	33	36	38	37	18
No. of examinations (b)	707	787	858	860	834	350
Number of workers booked per session						
Average (c)	27.8	27.2	27.0	25.6	25.2	22.9
Range (d)	21-30	23-30	19-30	21-30	10-30 (Note)	16-29
Number of workers examined per session						
Average (e) = (b) ÷ (a)	23.6	23.8	23.8	22.6	22.5	19.4
Range (f)	18-28	20-29	17-29	15-29	8-29 (Note)	15-24
Number of no-show cases per session						
Average number of cases (g) = (c) – (e)	4.2	3.4	3.2	3.0	2.7	3.5
Percentage of booked slots (h) = (g) ÷ (c) × 100%	15%	13%	12%	12%	11%	15%

Source: Audit analysis of LD records

Note: In one session, there were ten workers booked for examinations and eight workers examined. For each of the other sessions, the number of workers booked ranged from 15 to 30 and the number of workers examined ranged from 14 to 29.

4.8 *Room for reducing the number of reserved sessions.* As indicated in Table 16 (see para. 4.7), the average number of workers booked for medical examinations in each session decreased from 27.8 in 2012 to 22.9 in the first six months of 2017. Further analysis revealed that the number of sessions in which not more than 20 medical examinations of radiation workers were carried out increased from 17% in 2012 to 24% in 2016 and further to 56% (10 of 18 sessions) in the first six months of 2017 (see Table 17).

Table 17

**Analysis of radiation examinations conducted in each session
(2012 to 2017)**

Number of examinations conducted per session	Number of sessions					
	2012	2013	2014	2015	2016	2017 (up to June)
1 – 20	5 (17%)	3 (9%)	5 (14%)	12 (32%)	9 (24%)	10 (56%)
21 – 30	25 (83%)	30 (91%)	31 (86%)	26 (68%)	28 (76%)	8 (44%)
1 – 30	30 (100%)	33 (100%)	36 (100%)	38 (100%)	37 (100%)	18 (100%)

Source: Audit analysis of LD records

4.9 In 2016, the waiting time for clinical consultations at the two occupational health clinics ranged from 7 to 14 days. Tables 16 and 17 indicate that the clinical resources reserved for radiation medical examinations were not optimally utilised. The LD needs to, in collaboration with the Department of Health, monitor the situation and make necessary arrangements with a view to ensuring that occupational clinical resources reserved for radiation medical examinations are optimally utilised as far as practicable. Where resources are available, they should be redeployed to shorten the waiting time for clinical consultations.

Need to review the recovery of examination costs

4.10 Under the subsidiary regulations of the Radiation Ordinance, radiation workers are required to undergo pre-employment medical examinations and periodic examinations thereafter. The regulations stipulate that the examinations carried out for their first employment would be provided free of charge. The regulations do not stipulate that the periodic examinations carried out after their first employment would be provided at a charge or free of charge.

4.11 Audit noted that workers and their employers were not required to pay any fee for the radiation medical examinations conducted at the KTOHC, both for the workers' first employment and after their first employment. The LD had no readily available statistics for the number of pre-employment medical examinations and that of periodic examinations thereafter.

4.12 According to Financial Circular No. 6/2016 issued by the Financial Services and the Treasury Bureau in July 2016, it is Government's policy that fees charged should in general be set at levels adequate to recover the full cost of providing the goods and services. The fees should therefore be set at a level aiming at the attainment of full-cost recovery.

4.13 The LD needs to, in collaboration with the Department of Health, review the justifications for not charging radiation workers or their employers for periodic examinations carried out after the workers' first employment.

Need to improve performance pledge

4.14 For occupational clinical service, the LD has set a performance pledge that clients at the two occupational health clinics would be attended to within 30 minutes of the appointment time.

4.15 For 2016, the LD reported on its website 100% achievement for meeting the performance pledge. Audit examination revealed that although the pledge was originally meant to provide clinical service to clients within 30 minutes of the appointment time, staff at the clinics had interpreted the pledge as referring to the time required to attend to the clients and register their arrival. Hence, the 100% achievement was only the achievement of approaching the clients to register their arrival within 30 minutes.

Audit recommendations

4.16 **Audit has *recommended* that the Commissioner for Labour should:**

- (a) **in collaboration with the Director of Health, take measures to reduce the no-show rate of radiation workers for medical examinations;**
- (b) **monitor the utilisation of time slots reserved for medical examinations for radiation workers to ensure that the clinical resources are optimally utilised as far as practicable;**
- (c) **in collaboration with the Director of Health, review the justifications for not charging radiation workers or their employers for periodic medical examinations carried out at the KTOHC after the workers' first employment; and**
- (d) **spell out clearly that the performance pledge is to provide clinical service to clients within 30 minutes of the appointment time.**

Response from the Government

4.17 The Commissioner for Labour agrees with the audit recommendations. He has said that the LD will consult the Director of Health on the implementation of those recommendations relevant to the Department of Health.

Workplace inspection

Need to monitor progress of workplace inspections

4.18 Audit noted that the LD did not monitor:

- (a) the number of outstanding inspections, i.e. the inspections already brought up for inspection but not yet carried out; and
- (b) the delay in carrying out inspections after they were brought up.

4.19 ***Long outstanding inspections.*** In 2016, the OSHB conducted 4,205 inspections on occupational health (see Table 15 in para. 4.3). Of the 4,205 inspections, 2,030 (48%) were conducted by the OHD for Hong Kong and Kowloon (OHD(H)). Audit selected 30 outstanding inspections of the OHD(H) as at 30 June 2017 and performed an ageing analysis to ascertain the time lapse since the inspections were brought up. Audit found that all the 30 inspections had been outstanding for more than six months (see Table 18). The outstanding periods ranged from 7 months to 4.25 years, averaging 2.17 years.

Table 18

**Analysis of time lapse of 30 outstanding inspections
(30 June 2017)**

Time lapse	Number of outstanding inspections
> 6 months to 1 year	6 (20%)
> 1 year to 2 years	7 (24%)
> 2 years to 3 years	10 (33%)
> 3 years to 4 years	6 (20%)
> 4 years to 5 years	1 (3%)
Total	30 (100%)

Source: Audit analysis of LD records

4.20 ***Long delay in carrying out inspections.*** Audit selected two inspections conducted in each month by the OHD(H) in the period from July 2016 to June 2017. For the 24 inspections selected, Audit compared the dates of inspections with the bring-up dates to identify those inspections with delays. Audit found that there were delays in 13 (54%) of the 24 inspections (see Table 19). The delay ranged from 4 days to 3 years, averaging 11 months.

Table 19

**Delay in carrying out inspections
(July 2016 to June 2017)**

Delay (Year)	Number of inspections	
No delay	11 (46%)	
≤ 1 year	8 (33%)	} 13 (54%)
> 1 year to 2 years	4 (17%)	
> 2 years to 3 years	1 (4%)	
Total	24 (100%)	

Source: Audit analysis of LD records

Remarks: The delay ranged from 4 days to 3 years.

Audit recommendations

4.21 **Audit has recommended that the Commissioner for Labour should:**

- (a) **closely monitor the progress of workplace inspections;**
- (b) **compile management information on the outstanding inspections, e.g. the number of and the ageing analysis of such inspections;**
- (c) **take measures to minimise the number of outstanding inspections in future; and**

- (d) ascertain the number of existing backlog inspections and take effective measures to clear the backlog as soon as practicable.

Response from the Government

4.22 The Commissioner for Labour agrees with the audit recommendations. He has said that:

- (a) inspections on occupational health adopt a risk-based approach. The relevant Technical Note of the LD stipulates that workplaces identified as high-risk or moderate-risk should be brought up for inspection within prescribed timeframes;
- (b) under the bring-up mechanism, low-risk cases do not need to be brought up and do not have a prescribed inspection deadline; and
- (c) while noting that all cases of outstanding/delayed inspections identified (except for one) are low-risk cases, the LD agrees that proper use of the bring-up system should be monitored in accordance with the risk-based inspection approach so as to address the backlog situation.

Performance reporting

Need to improve reporting of performance indicators in COR

4.23 For occupational health services, the LD reports the number of “investigations/surveys/examinations/assessments/clinical consultations” in the COR as its performance indicator. For 2016, the LD reported in the COR that it had achieved 22,629 “investigations/surveys/examinations/assessments/clinical consultations” (see Table 1 in para. 1.7). Audit noted that the number comprised:

- (a) 2,983 investigations;
- (b) 7,018 surveys;
- (c) 1,471 medical examinations;

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- (d) 713 assessments; and
- (e) 10,444 clinical consultations at the two occupational health clinics.

4.24 Audit found that the information reported in the COR needed improvement. Under the LD's method of calculating the number of surveys:

- (a) for each survey conducted by more than one officer, the LD counted as if there was one survey for each officer; and
- (b) for each survey which lasted for more than one half-day period, the LD counted as if there was one survey for each half-day period.

Audit recommendations

4.25 **Audit has *recommended* that the Commissioner for Labour should:**

- (a) **with a view to enhancing transparency, consider reporting separately in the COR the number of investigations, surveys, examinations, assessments and clinical consultations; and**
- (b) **review the appropriateness of the existing method of calculating and presenting the number of surveys reported in the COR.**

Response from the Government

4.26 The Commissioner for Labour agrees with the audit recommendations. He has said that owing to the varied complexity of different surveys, the LD reports the number of surveys in such a manner to accurately reflect the manpower deployed to conduct surveys. For instance, for sizeable workplaces such as hospitals, a particular kind of survey may have to be conducted more than once in different locations of the workplace, hence more than one survey will be counted as a result. The LD will provide information on how the surveys are calculated in the COR.

Appendix A
(para. 1.5 refers)

List of occupational diseases
(31 July 2017)

Caused by physical agents	
1	Inflammation, ulceration or malignant disease of the skin or subcutaneous tissues or of the bones, or blood dyscrasia, or cataract, due to electro-magnetic radiations (other than radiant heat), or to ionising particles
2	Heat cataract
3	Dysbarism, including decompression sickness, barotrauma and osteonecrosis
4	Cramp of the hand or forearm due to repetitive movements
5	Subcutaneous cellulitis of the hand (Beat hand)
6	Bursitis or subcutaneous cellulitis arising at or about the knee due to severe or prolonged external friction or pressure at or about the knee (Beat knee)
7	Bursitis or subcutaneous cellulitis arising at or about the elbow due to severe or prolonged external friction or pressure at or about the elbow (Beat elbow)
8	Traumatic inflammation of the tendons of the hand or forearm (including elbow), or of the associated tendon sheaths
9	Carpal tunnel syndrome
Caused by biological agents	
10	Anthrax
11	Glanders
12	Infection by leptospira
13	Pulmonary disease due to the inhalation of the dust of mouldy hay or other mouldy vegetable produce, and characterised by symptoms and signs attributable to a reaction in the peripheral part of the bronchopulmonary system, and giving rise to a defect in gas exchange (Farmer's lung)
14	Infection by organisms of the genus brucella
15	Tuberculosis
16	Parenterally contracted viral hepatitis
17	Infection by streptococcus suis
18	Avian chlamydiosis
19	Legionnaires' disease
20	Severe acute respiratory syndrome
21	Avian influenza A

Appendix A
(Cont'd)
(para. 1.5 refers)

Caused by chemical agents	
22	Poisoning by lead or a compound of lead
23	Poisoning by manganese or a compound of manganese
24	Poisoning by phosphorus or an inorganic compound of phosphorus or the anti-cholinesterase or pseudo anti-cholinesterase action of organic phosphorus compounds
25	Poisoning by arsenic or a compound of arsenic
26	Poisoning by mercury or a compound of mercury
27	Poisoning by carbon bisulphide
28	Poisoning by benzene or a homologue of benzene
29	Poisoning by a nitro- or amino- or chloro-derivative of benzene or of a homologue of benzene, or poisoning by nitro-chlorobenzene
30	Poisoning by dinitrophenol or a homologue or by substituted dinitrophenols or by the salts of such substances
31	Poisoning by halogen derivatives of hydrocarbons of the aliphatic series
32	Poisoning by diethylene dioxide (dioxan)
33	Poisoning by chlorinated naphthalene
34	Poisoning by oxides of nitrogen
35	Poisoning by beryllium or a compound of beryllium
36	Poisoning by cadmium
37	Dystrophy of the cornea (including ulceration of the corneal surface) of the eye
38	Primary epitheliomatous cancer of the skin
39	Chrome ulceration including perforation of nasal septum
40	Primary neoplasm of the epithelial lining of the urinary tract (renal pelvis, ureter, bladder and urethra), including papilloma, carcinoma-in-situ and invasive carcinoma
41	Peripheral poly-neuropathy
42	Localised new growth of the skin, papillomatous or keratotic
43	Occupational vitiligo

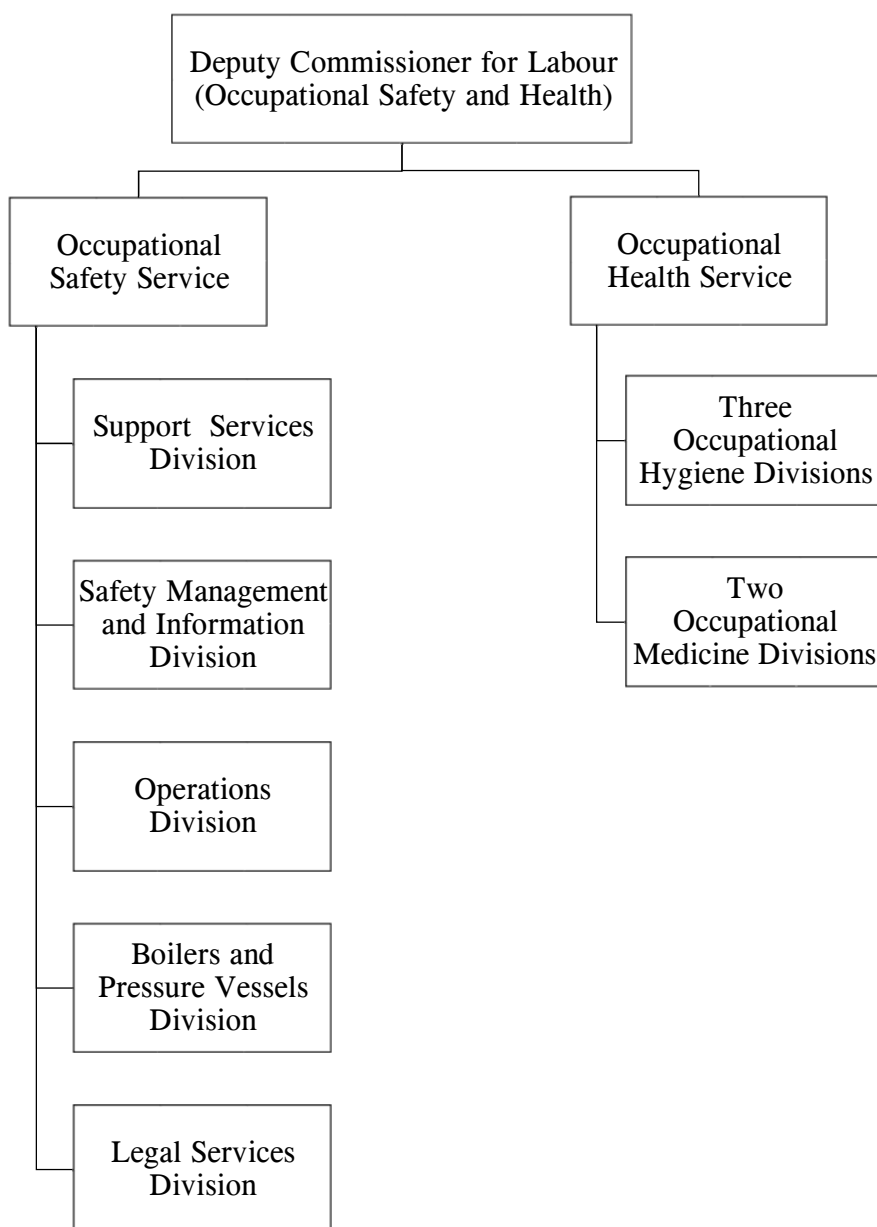
Appendix A
(Cont'd)
(para. 1.5 refers)

Caused by miscellaneous agents	
44	Inflammation or ulceration of the skin produced by dust, liquid or vapour (including the condition known as chloracne but excluding chrome ulceration)
45	Inflammation or ulceration of the mucous membrane of the upper respiratory passages or mouth produced by dust, liquid or vapour
46	Carcinoma of the nasal cavity or associated air sinuses (nasal carcinoma)
47	Byssinosis
48	Occupational asthma
Caused by inhalation of silica or asbestos	
49	Silicosis
50	Asbestosis
51	Mesothelioma
Other	
52	Occupational deafness

Source: LD records

Remarks: Items 1 to 48, items 49 to 51 and item 52 are occupational diseases prescribed under the ECO, the Pneumoconiosis and Mesothelioma (Compensation) Ordinance and the Occupational Deafness (Compensation) Ordinance respectively.

**LD's OSHB:
Organisation chart (extract)
(31 March 2017)**



Source: LD records

**List of 23 trades identified by LD as hazardous trades
(31 July 2017)**

Item	Trade
1	Agriculture and livestock production and agriculture services
2	Beverage manufacturing
3	Catering
4	Container handling services, car parks, toll bridge, road or vehicular tunnel operation
5	Food manufacturing
6	Godowns
7	Hong Kong Government Departments (limited to those trades in individual government workplaces bearing risk levels comparable to other hazardous trades of the list)
8	Hotels
9	Laundries
10	Manufacture of electrical machinery, apparatus, appliances and supplies
11	Manufacture of non-metallic mineral products
12	Manufacture of plastic products
13	Manufacture of wearing apparel
14	Metal products
15	Printing
16	Property management and guard services
17	Repair services
18	Sanitary and similar services
19	Ship building and ship repairing
20	Supermarkets and convenience stores, department stores and fuel related stores
21	Textiles
22	Waste recycling industry
23	Welfare institutions

Source: LD records

Acronyms and abbreviations

Audit	Audit Commission
BEC	Building and engineering construction
COR	Controlling Officer's Report
DoJ	Department of Justice
DSO	Divisional Occupational Safety Officer
ECO	Employees' Compensation Ordinance
FIUO	Factories and Industrial Undertakings Ordinance
FIU (SM)	Factories and Industrial Undertakings (Safety Management)
FIU (SOSS)	Factories and Industrial Undertakings (Safety Officers and Safety Supervisors)
ISG	Integrated Services Group
KTOHC	Kwun Tong Occupational Health Clinic
LD	Labour Department
LegCo	Legislative Council
MIP	Mega Infrastructure Project
MPR	Monthly Progress Report
MST	Mandatory safety training
OHD	Occupational Hygiene Division
OHD(H)	Occupational Hygiene Division for Hong Kong and Kowloon
OSHB	Occupational Safety and Health Branch
OSHO	Occupational Safety and Health Ordinance
RSA	Registered Safety Auditor
RSO	Registered Safety Officer
TCP	Training course provider