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Panel on Housing

Meeting on 16 April 2010

**Updated background brief on
divestment of Housing Authority's retail and car-parking facilities
(Position as at 9 April 2010)**

Purpose

This paper sets out the divestment of retail and car-parking (RC) facilities of the Housing Authority (HA), and gives a brief account of the views and concerns expressed by the relevant Panels.

Background

2. Divestment of HA's RC facilities was first mooted in 2000, with the objective of enabling HA to focus its resources on its core function as the provider of public housing in Hong Kong. This objective was in line with the direction provided in the Report on the Review of the Institutional Framework for Public Housing published in June 2002, which recommended that HA should progressively divest its non-core assets, i.e. the commercial portfolio (RC facilities). The reasons for the divestment, according to the Administration, were two-fold. First, it would enable HA to focus its resources on its core functions as a provider of subsidized public housing. Second, with the cessation of production and sale of Home Ownership Scheme flats, HA lacked a recurrent source of income. Proceeds from the divestment would help to meet HA's funding requirements in the short term.

3. In July 2002, HA appointed a consultant to assess the feasibility of the divestment, recommend the divestment strategy, and formulate an implementation proposal. Based on the findings of the consultancy study, the Administration put forward a divestment proposal to the Chief Executive in Council for consideration on 15 July 2003. The Chief Executive in Council decided that HA's agreement should be sought to divest its RC facilities, and that the net proceeds from the divestment should entirely go to HA. On 24 July 2003, HA agreed in principle to divest its RC facilities and approved, inter alia, the establishment of the Supervisory Group on Divestment to monitor and steer the divestment project.

Details of the divestment

4. HA agreed to adopt the following broad strategy to take forward the divestment -

- (a) A Real Estate Investment Trust (REIT)¹ structure (The Link REIT) would be established to hold HA's RC facilities to be divested;
- (b) A new company to manage The Link REIT, The Link Management Limited (The Link), would be set up. This company would be beneficially owned by unit-holders of The Link REIT and held in trust by The Link REIT's trustees;
- (c) Initially, HA would assign the cash flow of the RC facilities to The Link and sign a sale and purchase agreement with it in respect of RC facilities. On this basis, The Link would make an initial public offering (IPO) on The Stock Exchange of Hong Kong;
- (d) At a later stage when preparation of relevant land leases were completed, HA would transfer the legal title of the RC facilities to The Link; and
- (e) The Link would pay to HA for the sale of the RC facilities by two installments: a major proportion of the sale amount would be paid immediately after the IPO and the balance would be paid upon the completion of transfer of legal titles.

5. HA also decided that other than a small proportion of the RC facilities which might be unsuitable for divestment because of their poor location, small scale, old age or obsolescent condition, all RC facilities would be divested in one go. The divestment project included 180 RC facilities.

Listing of The Link REIT

6. The Link was incorporated in February 2004 as a HA wholly owned subsidiary, which assumed in March 2005 the management functions for the 180 RC facilities to be divested.

7. On 8 December 2004, one day before the closing of the public offering period for The Link REIT, two public rental housing (PRH) tenants filed an application for judicial review of HA's statutory power to divest its asset. HA subsequently announced its decision to postpone the listing of The Link REIT on 20 December 2004.

¹ According to the Code on Real Estate Investment Trusts (REIT Code) issued by the Securities and Futures Commission, a REIT is a collective investment scheme constituted as a trust that invests primarily in real estate with the aim to provide returns to holders derived from the rental income of the real estate. Funds obtained by a REIT from the sale of units in the REIT are used in accordance with the constitutive documents to maintain, manage and acquire real estate within its portfolio.

8. On 20 July 2005, the Court of Final Appeal ruled that HA had the power to divest its RC facilities. HA then announced on 6 September 2005 the decision to re-launch the global offering of units in The Link REIT. On 14 November 2005, an Offering Circular for the re-launched IPO was issued. The Link REIT was subsequently listed on 25 November 2005. The total proceeds received by HA from the divestment amounted to \$34.1 billion.

Major concerns on the divestment project

9. The Panel on Housing (HG Panel) was first briefed on the divestment project on 3 November 2003, after HA had agreed in principle to divest its RC facilities. A series of meetings were held to receive progress up-date on the divestment project and discuss its possible impacts. Of particular concern to members was the impact of the divestment on commercial tenants and service providers of RC facilities. Deputations from the retail, catering, and medical sectors were invited to express their views. Members considered that The Link should maintain dialogue with the commercial tenants to see how their concerns could be addressed, and that the Administration should play an active role in the process.

Attendance of representatives of The Link

10. At the HG Panel meeting held on 9 May 2006, representatives of The Link and the Administration were invited to discuss the provision and management of RC facilities in PRH after the divestment of the facilities by HA, and how to address the concerns about rent increases on commercial premises in The Link's shopping centres and markets. Members were disappointed that no representative of The Link attended the meeting. A motion to invite the Chairman and Chief Executive Officer of The Link (CEO/The Link) to attend a HG Panel meeting was carried. The motion also specified that where The Link refused to attend the meeting again, the Panel would consider exercising the power conferred under the Legislative Council (Powers and Privileges) Ordinance (Cap. 382) to order the attendance of the persons.

11. As The Link again declined the invitation of HG Panel to attend the meeting on 4 January 2007, members passed the following motion -

"That this Panel regrets that Mr Victor SO Hing-woh, Executive Director and Chief Executive Officer of The Link Management Limited (The Link), has refused to attend a meeting of the Legislative Council for discussion of issues relating to the Link's management of facilities divested by the Housing Authority, and proposes that Mr SO be invited again to attend a meeting of this Panel."

The situation had been improved since the appointment of the new CEO/The Link in 2008.

Impacts of the divestment project

12. Matters relating to the management of divested RC facilities, and protection

of interests of non-skilled workers engaged in services contracted out by The Link were discussed at the joint meeting of the HG Panel and the Panel on Manpower on 5 June 2006. Members called on The Link to continue with the concessionary rent arrangement for certain facilities, such as clinics, to meet the needs of PRH tenants; and allowing temporary use of venues by non-profit making bodies for holding community activities. Members also expressed grave concern about The Link's plan to reduce some 1 400 jobs, which might have adverse impact on non-skilled workers engaged by The Link's service contractors. They urged The Link to give priority to existing staff in the recruitment of customer service personnel.

13. When the divestment of RC facilities of HA was again discussed by the HG Panel on 4 January 2007, members reiterated their concerns about the high rental increases in respect of The Link's shopping centres and market stalls, and whether social welfare organizations could continue to benefit from concessionary rents. There was also question on the "one-stop medical zone" concept (the Concept) developed by The Link, which grouped existing separated clinics and laboratories in a one-stop facility. Members found the Concept undesirable as this would cause inconvenience to patients, particularly the elderly, who presently could use the service of nearby clinics without any need to travel. Some members were of the view that the Concept was an excuse for the Link to vacate premises at favourable locations to new tenants who could afford higher rents. They opined that the Administration should play an active role to ensure that these shopping centres and market stalls could continue to meet the needs of PRH tenants, and provide them with services and goods at affordable prices.

14. At the HG Panel meeting on 16 December 2008, the new CEO/The Link gave a presentation on The Link's rental strategies and approach, adding that The Link's interests were aligned with those of its tenants, communities, and investors. While The Link would continue to exercise strong corporate and social responsibilities, it was held 100% accountable to investors. Its rent approach aimed at keeping rents competitive and to the market.

15. Some members however pointed out that the decision to divest RC facilities was wrong from the start. The hefty increase in the rents of RC facilities after divestment had not only affected the livelihood of retailers, many of whom had been forced out of business, but also tenants of public housing estates. Despite the repeated calls for The Link to reduce rents, these had been declined on the ground that The Link was held accountable to its shareholders. The situation would be further aggravated if The Link sold the RC facilities. They stressed that the Administration could not be absolved from the management of RC facilities within HA's public housing estates even after the divestment. To resolve the problem, the Government should seriously consider buying back the shares of The Link, which was part of its duty under Article 105 of the Basic Law to protect the rights of individuals to acquisition of property.

16. In the light of an allegation that The Link had failed to effect payment for management fees of estate common areas (ECA), the HG Panel held a special meeting on 28 September 2009 to discuss the arrangement on management fees of common areas shared between HA and The Link, as well as the progress of transfer of the legal

titles of the divested RC facilities to The Link. Members noted that The Link had failed to effect payment of management fees of the majority of the housing estates for July and August 2009. In this connection, HA issued a letter through its legal representative to The Link on 9 September 2009 to recover the outstanding amount of around \$8 million. While acknowledging that The Link had paid off all the management fees in arrears in mid-September 2009, some members considered that interests should be charged on the management fees in arrears. To avoid similar recurrences, members welcomed the decision of The Link to make direct payment into the respective ECA management fund accounts.

17. On the progress of transfer of legal titles, the HG Panel noted that the legal titles of 40 divested properties had yet to be assigned to The Link REIT. Some members enquired whether the delay in the transfer of legal titles would have cost implications on the part of the Government. Other members were concerned that The Link REIT might sell some of the less profitable divested properties if it was allowed to sell the properties upon legal transfer of titles. Given that the RC facilities were divested to The Link REIT at a very low price and without going through a public tender, The Link was obliged to ensure provision of adequate services to estate residents. To this end, there might be a need for the Administration to audit the accounts of The Link REIT.

18. Noting that The Link would be spending a lot in refurbishing the divested RC facilities, some members enquired if The Link had consulted retailers/estate residents before introducing any changes to upgrading the RC facilities. They pointed out that unlike rents before the divestment which were inclusive of all costs, retailers under the management of The Link had to pay maintenance fees and electricity charges separately. Retailers would have no choice but to transfer the additional costs, including the increase in rents after refurbishment, to consumers. Other members held the view that The Link was trying to increase its profit through rent increase and staff reduction so that its senior management could enjoy high salaries and bonuses.

19. On management and maintenance of the divested RC facilities, some members noted that the management staff of The Link were required under IPO circular to hold valid estate agent licences in order to manage the estates. However, none of the senior management staff of The Link were licensed estate agents. Other members expressed concern that The Link had leased out about 8 000 car park spaces to non-residents without applying for exemptions nor paying waiver fees in accordance with the terms of the Government lease. The Link had also failed to install and upgrade fire safety installations in the RC facilities in line with fire safety regulations. Many recreational facilities managed by The Link had become dilapidated due to improper maintenance. The Administration and The Link's responses to members' concerns are hyperlinked below for ease of reference.

Latest development

20. The Administration and The Link have been invited to brief members on the latest progress of provision and management of divested RC facilities in public housing estates at the HG Panel meeting on 16 April 2010.

Relevant papers

Information paper provided by the Administration for the Housing Panel meeting on 21 June 2005

<http://www.legco.gov.hk/yr04-05/english/panels/hg/papers/hg0621cb1-1787-5-e.pdf>

Information paper provided by the Administration for the Housing Panel meeting on 20 October 2005

<http://www.legco.gov.hk/yr05-06/english/panels/hg/papers/hg1020cb1-62-3-e.pdf>

Information paper provided by the Administration for the Housing Panel meeting on 9 May 2006

<http://www.legco.gov.hk/yr05-06/english/panels/hg/papers/hg0509cb1-1396-6-e.pdf>

Minutes of the Housing Panel meeting on 9 May 2006

<http://www.legco.gov.hk/yr05-06/english/panels/hg/minutes/hg060509.pdf>

Information paper provided by the Administration for the Housing Panel and Manpower Panel joint meeting on 5 June 2006

<http://www.legco.gov.hk/yr05-06/english/panels/hg/papers/hgmp0605cb1-1632-1-e.pdf>

Minutes of the Housing Panel and Manpower Panel joint meeting on 5 June 2006

<http://www.legco.gov.hk/yr05-06/english/panels/hg/minutes/hgmp0605.pdf>

Minutes of the Housing Panel meeting on 4 January 2007

<http://www.legco.gov.hk/yr06-07/english/panels/hg/minutes/hg070104.pdf>

Information paper provided by the Administration for the Housing Panel meeting on 16 December 2008

<http://www.legco.gov.hk/yr08-09/english/panels/hg/papers/hg1216cb1-378-7-e.pdf>

Minutes of the Housing Panel meeting on 16 December 2008

<http://www.legco.gov.hk/yr08-09/english/panels/hg/minutes/hg20081216.pdf>

Information paper provided by The Link for the Housing Panel special meeting on 28 September 2009

<http://www.legco.gov.hk/yr08-09/english/panels/hg/papers/hg0928cb1-2661-1-e.pdf>

Information paper provided by the Administration for the Housing Panel special meeting on 28 September 2009

<http://www.legco.gov.hk/yr08-09/english/panels/hg/papers/hg0928cb1-2661-2-e.pdf>

Minutes of the Housing Panel special meeting on 28 September 2009

<http://www.legco.gov.hk/yr08-09/english/panels/hg/minutes/hg20090928.pdf>

Supplementary information paper provided by The Link for the Housing Panel special meeting on 28 September 2009

<http://www.legco.gov.hk/yr08-09/english/panels/hg/papers/hg0928cb1-317-1-e.pdf>

Supplementary information paper provided by the Administration for the Housing Panel special meeting on 28 September 2009

<http://www.legco.gov.hk/yr08-09/english/panels/hg/papers/hg0928cb1-339-1-e.pdf>

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