

CHAPTER 2

Lands Department

<h4>Administration of short term tenancies</h4>
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**Audit Commission
Hong Kong
23 October 2006**

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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ADMINISTRATION OF SHORT TERM TENANCIES

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PART 1: INTRODUCTION

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

Background

1.2 The Hong Kong Special Administrative Region has a total land area of 110,372 hectares, of which 34,517 hectares (31% – Note 1) are managed by the Lands Department (Lands D), including unleased government land and land held under short term tenancies (STTs). The Administration's policy is that where there is vacant government land which has not been designated for a specific use or is not required for development in the near future, it will take the opportunity to make the land available through STTs for temporary use. The STT policy objectives include:

- (a) ensuring temporary beneficial use of the land which would help reduce the cost of preventing the land from unlawful occupation or environmental/health problems;
- (b) obtaining revenue from what would otherwise be idle land resources; and
- (c) establishing a system of temporary tenure which can be administered easily, fairly and cost effectively.

1.3 In 2005-06, the Lands D:

- (a) administered 4,019 STTs (as at 1 April 2005);
- (b) raised \$967 million rental income from the STTs; and
- (c) spent \$8 million in managing the unleased land (including the cost of fencing off the sites and providing security-guard services).

Note 1: *The remaining 75,855 hectares (69%) of land mainly comprise land for country parks, private developments and infrastructures.*

1.4 The Lands D grants STTs by:

- (a) **Open Tender.** Land that is likely to be of general commercial interest is let by open tender. Examples include STTs for stores, fee-paying public car parks, plant nurseries and golf driving ranges;
- (b) **Direct Grant.** STT may be granted directly where the land is of no general commercial interest and there is only one interested party. Examples of uses include works areas required for public projects or by utility companies, and sites for non-profit-making activities by charitable/non-profit-making organisations for which policy support by the relevant policy bureau has been given;
- (c) **Regularisation of unauthorised occupation of government land.** When unlawful occupation of government land without structures is detected by the Lands D, it may be regularised under certain circumstances by the issue of an STT to the occupier at market rent. The Lands D considers that this is a pragmatic way of resolving the unlawful occupation problem of government land and obviates the need for deploying considerable manpower in conducting frequent inspections to prevent its re-occupation; and
- (d) **Conversion from Government Land Licence/Permit.** Since the mid-1970s, it has been the Government policy to convert old land licences to STTs to effect better land control. The land licences were issued in the past to regularise squatters in the rural areas of the New Territories or for other specified purposes and are rarely issued nowadays.

1.5 The Lands Administration Office (LAO) of the Lands D is responsible for administering STTs. Under the LAO, there are 12 District Lands Offices (DLOs – Note 2) which are responsible for administering STTs within their districts. An organisation chart of the Lands D is at Appendix A. The Lands D has promulgated STT guidelines through the Lands Administration Office Instructions and Technical Circulars.

Note 2: *Formerly there were 14 DLOs. With effect from 1 April 2004, the DLO/Hong Kong West and the DLO/Hong Kong South have been merged into the DLO/Hong Kong West and South, and the DLO/Tsuen Wan and the DLO/Kwai Tsing have been merged into the DLO/Tsuen Wan and Kwai Tsing.*

Audit review

1.6 The Audit Commission (Audit) has conducted a review of the Lands D's administration of STTs with reference to its laid down objectives and procedures. The review focused on the following areas:

- (a) administration of rent arrears (PART 2);
- (b) monitoring of tenants' performance (PART 3); and
- (c) enforcement of tenancy conditions (PART 4).

Audit has found that there are areas where improvement can be made by the Lands D in administering STTs and has made a number of recommendations to address the issues.

Acknowledgement

1.7 Audit would like to acknowledge with gratitude the full cooperation of the staff of the Lands D during the course of the audit review.

PART 2: ADMINISTRATION OF RENT ARREARS

2.1 This PART examines the actions taken by the Lands D in respect of STT rent arrears.

Standing Accounting Instruction requirements

2.2 According to Standing Accounting Instruction (SAI) 800, Controlling Officers are required to regularly review their revenue generating procedures and activities to ensure that:

- (a) demand notes for the collection of revenue are issued promptly; and
- (b) if payments are not received within a reasonable time, appropriate and timely actions are taken, such as issuing reminders and taking legal action if necessary.

Annual return of arrears of revenue

2.3 As laid down in SAI 1020:

- (a) Controlling Officers are required to produce each year a statement of all debts and charges which were due to the Government but were not paid by 31 March (i.e. annual return of arrears of revenue);
- (b) the return should also show which of the debts and charges overdue by 31 March were still outstanding by 30 June;
- (c) the return should include:
 - (i) all demand notes issued under the General Demand Note System;
 - (ii) debts and charges covered by demand notes processed outside the General Demand Note System; and
 - (iii) debts and charges raised other than in the form of a demand note, e.g. by letters;

- (d) in determining whether a debt is due and payable, the following rules apply:
 - (i) if a demand note has been raised, the due date of the debt is the date specified in the demand note; and
 - (ii) in all other cases, a debt or charge is normally due as it arises even though it has not been formalised by way of a demand note;
- (e) all debts and charges should be included in the return unless they are cancelled or written off; and
- (f) accounts under dispute should be regarded as arrears but shown separately in the return.

The Lands D's annual return of arrears of revenue

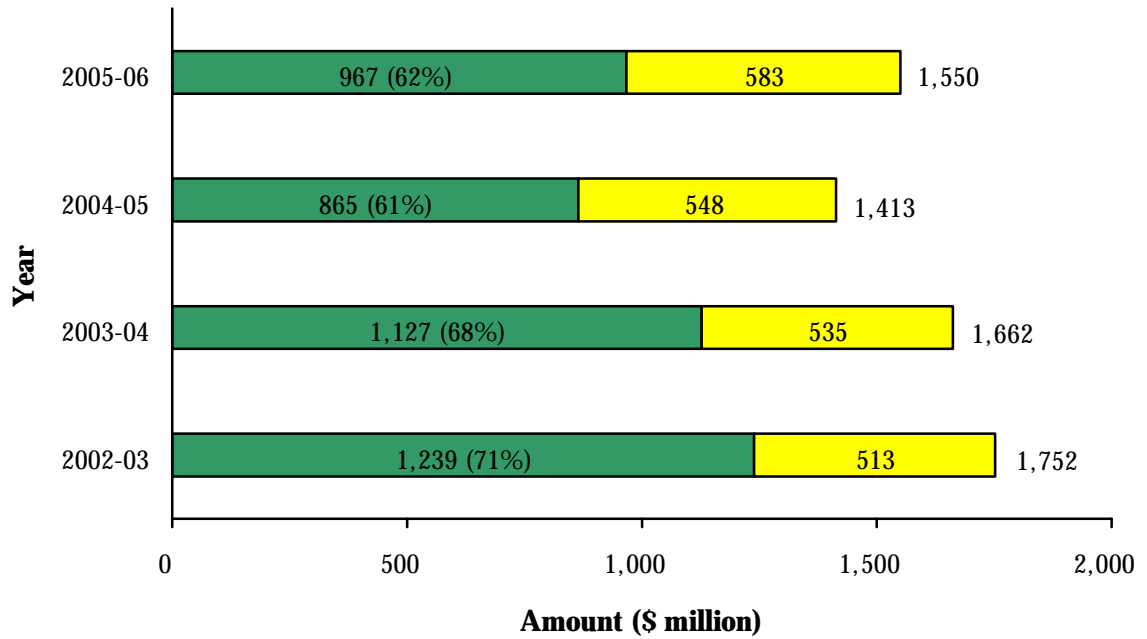
2.4 For the purpose of the annual return of arrears of revenue, Controlling Officers are required to report the arrears under individual Revenue Heads. Accordingly, the Lands D has reported the STT rent arrears (Note 3) under Revenue Head 7 (Properties and investments) of the General Revenue Account (GRA) (Note 4). In the past four years (2002-03 to 2005-06), STT rents made up about two-thirds of the Lands D's revenue under GRA Revenue Head 7 (see Figure 1).

Note 3: *In this report, unless otherwise specified, rent arrears refer to outstanding STT rents, the related interest and amounts due to the Government.*

Note 4: *The Lands D's Revenue Head 7 also includes the department's other revenue items, namely Government rents, land licence fees, rents from extensions of leases, rents from government properties and interest.*

Figure 1

**Lands D's revenue collected under Revenue Head 7
(2002-03 to 2005-06)**



Legend: STT rent
 Others (see also Note 4)

Source: *Lands D records*

Audit observations

Need to comply with SAI requirements

2.5 In an examination of the Lands D's annual returns of arrears of revenue for the past six years (1999-2000 to 2004-05), Audit noted that there were four significant STT rent arrears cases which had not been included in the returns in accordance with SAI 1020 (see Table 1).

Table 1

**Rent arrears not included in Lands D's annual returns
(1999-2000 to 2004-05)**

Case	Financial Year	Particulars	Estimated amount (\$ million)
1-1	1999-2000 to 2002-03	<p>In March 1999, an STT tenant abandoned the site before the expiry of the fixed term in October 1999. In January 2000, the Department of Justice (D of J) issued a letter to the tenant demanding payment of the rent arrears for March to October 1999.</p> <p>In August 2003, the Financial Services and the Treasury Bureau (FSTB) approved the writing-off of the rent arrears because the tenant (a limited company) had been wound up and it had no assets or funds for distribution to creditors.</p>	10 (for 1999-2000 to 2002-03)
1-2	2003-04 and 2004-05	<p>Between 2003 and 2005, an STT tenant (Company A, a limited company) did not pay rent for three STTs. In 2003, the tenant commenced legal proceedings against the Government (see para. 2.14(b)). The Lands D did not issue rent demand notes from 2003 to 2005 as legal proceedings were being taken against the tenant to recover the rent arrears.</p>	5 (for 2003-04) 26 (for 2004-05)

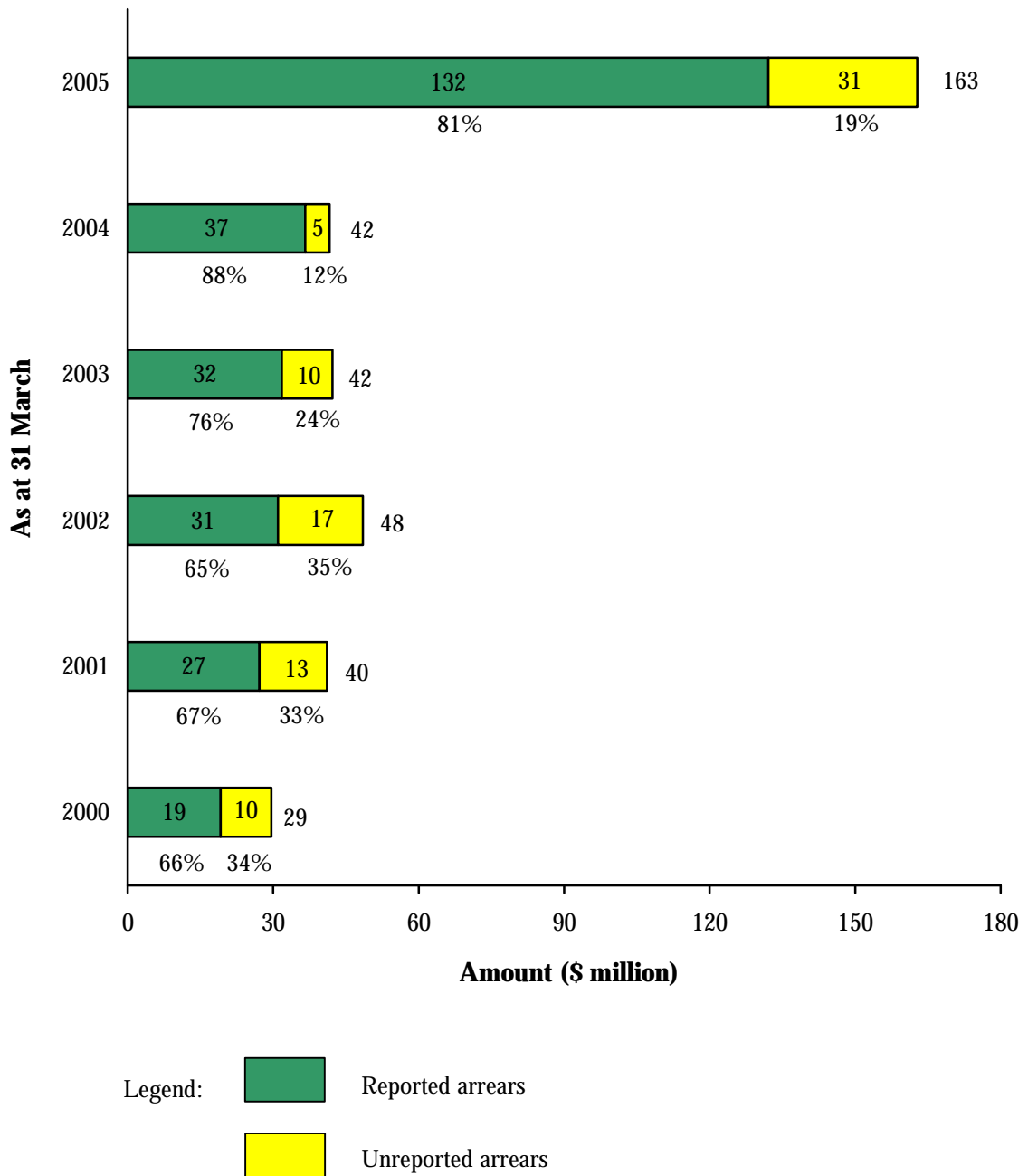
Case	Financial Year	Particulars	Estimated amount (\$ million)
1-3	2004-05	In 2004, an STT tenant (Company B, a limited company) did not pay rent for 40 STTs and commenced legal proceedings against the Government (see para. 2.14(a)). During the period, the Lands D issued demand notes for 36 STTs. However, the Lands D did not issue rent demand notes for the remaining four STTs because it was taking actions to terminate the tenancies and to repossess the sites.	5 (for 2004-05)
1-4	2000-01 and 2001-02	In 2000, an STT tenant commenced legal proceedings against the Lands D concerning its action to terminate two STTs. While the legal proceedings were in progress, the Lands D did not issue rent demand notes from 2000-01 to 2001-02. In mid-2002, the tenant fully paid the outstanding rent.	3 (for 2000-01) 7 (for 2001-02)

Source: Audit analysis of Lands D records

2.6 In accordance with SAI 1020, a debt or charge is normally due as it arises even though it has not been formalised by way of a demand note (see para. 2.3(d)(ii)). **Therefore, Audit considers that the rent arrears due from the tenants in Cases 1-1 to 1-4 should have been included in the Lands D's annual returns of arrears of revenue for the respective financial years.**

2.7 Due to the non-inclusion of the four cases in the returns, Audit estimates that, for the six years 1999-2000 to 2004-05, the Lands D under-reported its rent arrears by 12% to 35% (see Figure 2).

Figure 2
Lands D's reporting of rent arrears
(1999-2000 to 2004-05)



Source: *Audit analysis of Lands D records*

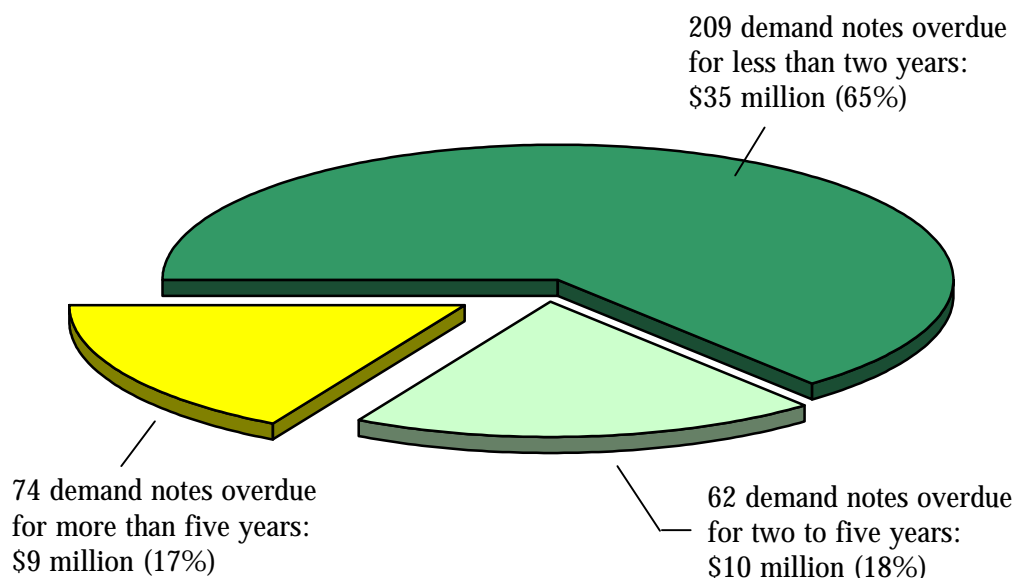
2.8 The objectives of SAI 1020 are to help enhance control and accountability of outstanding debts and charges due to the Government and improve monitoring of debt recovery. **Audit considers that there is room for improvement in the Lands D's compliance with SAI 1020.** The Lands D should conduct a review of the rent arrears cases prior to 2006 to ascertain if there were other omission cases which would affect the accuracy of the arrears return for the coming years.

Need to take prompt action on long outstanding STT rents

2.9 As at 31 March 2006, of the \$54 million STT rent arrears (as recorded by the General Demand Note System – see para. 2.3(c)(i)), \$9 million (17%) were overdue for more than five years (see Figure 3).

Figure 3

**STT rent arrears
(31 March 2006)**



Source: Audit analysis of Lands D's General Demand Notes

2.10 Audit test check of ten STT rent arrears cases revealed that there were indications that recovery actions for four long outstanding cases would not be fruitful. However, up to 30 June 2006, action to write off the rent in arrears had not been completed (see Table 2).

Table 2
Outstanding rent from four STT tenants
(30 June 2006)

Case	Unpaid-rent period	Particulars	Rent arrears (\$'000)
2-1	April to September 1999	In March 2004, having sought legal advice in 2003 that further recovery actions would not be fruitful, the District Lands Office/Shau Tin (DLO/ST) proposed to write off the rent arrears.	1,459
2-2	January to July 1998	In October 2003, the D of J advised that the tenant (a limited company) was wound up in May 2003 and it was not cost-effective for further recovery actions. In September 2005, the DLO/ST proposed to write off the rent arrears.	731
2-3	October 1995 to April 1996	Since 1997, the Lands D had been unable to find the whereabouts of the tenant. In June 2003, the District Lands Office/Sai Kung (DLO/SK) proposed to write off the rent arrears.	31
2-4	January 1991 to November 1992	In 1993, the Lands D's Legal Advisory and Conveyancing Office (LACO) advised that the tenant was a shell company with no company assets, and it might be fruitless to take recovery proceedings. In June 2003, the DLO/SK proposed to write off the rent arrears.	26

Source: Lands D records

2.11 **Audit considers that the Lands D should take timely action to write off long outstanding rent arrears if recovery actions would be futile.**

Audit recommendations

2.12 **Audit has recommended that the Director of Lands should:**

- (a) **comply with SAI 1020 when preparing annual returns of arrears of revenue by including in the returns debts or charges not formalised by demand notes (see para. 2.6);**
- (b) **conduct a review of the rent arrears in the 2005-06 return of arrears of revenue to ensure compliance with SAI 1020 (see para. 2.8); and**
- (c) **conduct a review of the long outstanding cases of rent arrears and take timely write-off action if the Lands D is satisfied that recovery actions would be futile (see paras. 2.10 and 2.11).**

Response from the Administration

2.13 The **Director of Lands** accepts the audit recommendations in paragraph 2.12. He has said that:

- (a) the Lands D is conducting a review with a view to optimising the existing departmental guidelines on the handling of rent arrears;
- (b) the Lands D will update its departmental accounting circulars and the Lands Administration Office Instructions to advise its staff to comply with SAI 1020;
- (c) the Lands D will conduct a review of the rent arrears in the 2005-06 return of arrears of revenue; and
- (d) the Lands D will take timely action to write off outstanding cases of rent arrears.

Measures to improve STT administration

Challenges in managing car-park STTs

2.14 As shown in Figure 2, the Lands D's rent arrears of \$163 million as at 31 March 2005 were \$121 million more than those of \$42 million as at 31 March 2004. The increase was mainly due to the following five rent arrears cases (all car-park STTs):

- (a) **Case 3-1.** In 2004, the tenant (Company B) did not pay rent for 40 car-park STTs and commenced legal proceedings against the Government. The company also did not return two STT sites after their tenancies had been terminated by the Lands D. In July 2005, the company proposed an overall settlement of all legal proceedings with the Government and offered to pay a lump sum. In August 2005, the Financial Secretary approved the Lands D's recommendation to write off the remaining arrears (\$18 million). In September 2005, the Lands D accepted the company's settlement offer and repossessed the two sites, 9 months and 15 months respectively after the termination of the tenancies;
- (b) **Case 3-2.** In 2003, the tenant (Company A) did not pay rent and commenced legal proceedings against the Government. The number of STTs with rent arrears increased from three in 2003 to five in 2004. The company did not return three of the five STT sites until 17 to 22 months after the termination of the tenancies. In 2006, the company was wound up on petition of the Government. Accordingly, the legal proceedings in this case were not pursued;
- (c) **Case 3-3.** In 2004, the tenant (Company C) did not pay rent for two car-park STTs and commenced legal proceedings against the Government. Up to mid-September 2006, the legal proceedings had been in progress;
- (d) **Case 3-4.** In 2004, the tenant (Company D) did not pay rent for one car-park STT and commenced legal proceedings against the Government. Up to mid-September 2006, the legal proceedings had been in progress; and
- (e) **Case 3-5.** In 2004, the tenant (Company E) did not pay rent for one car-park STT and commenced legal proceedings against the Government. In March 2006, Company E paid the rent arrears. The related legal proceedings were discontinued.

2.15 The five rent arrears cases in paragraph 2.14 revealed the following issues that the Lands D faced in managing car-park STTs:

- (a) once a tenant had commenced legal proceedings against the Government, the Lands D had difficulties in recovering the rent arrears. The tenant could continue occupying the sites without paying rent for a lengthy period (see para. 2.14(a) to (e)); and
- (b) the Lands D had difficulties in repossessing the sites even after termination of the tenancies because of the ongoing legal proceedings (see para. 2.14(a) and (b)).

Measures to deal with the issues

2.16 ***Performance review introduced in 2002.*** Since June 2002, the Lands D has introduced measures which would take into account tenants' past performance when considering the grant of new STTs to them (see details in PART 3). Regarding the tenants of the five rent arrears cases in paragraph 2.14, the Land Administration Meeting (LAM – Note 5) had reviewed their tenders for new STTs.

2.17 ***Rental deposit increased in 2004.*** In view of the increasing number of car-park STT tenants who defaulted on rent payments, in October 2004, LAM decided to increase the rental deposit for STT tenders for car parks or related uses (such as container storage, car display and car sale) from three-month to six-month rents.

2.18 ***Measures approved by LAM in 2005.*** In June 2005, LAM carried out a review of the car-park STTs under litigation initiated by the tenants. In June and November 2005, LAM decided to introduce the following new measures for car-park STTs:

- (a) ***Personal guarantee.*** LAM found that, as many STT tenants were limited companies with no substantial assets, enforcement actions against them were not effective. Therefore, LAM considered it appropriate to introduce a new measure that would require a personal guarantee from a shareholder or a director of the company concerned. LAM noted that this measure was in line with the usual commercial practice; and
- (b) ***Measures to minimise legal challenges.*** After a review of the tenants' claims, LAM agreed to introduce new measures to minimise the risk of legal challenges in future by:

Note 5: *LAM is chaired by the Deputy Director (General) of the Lands D, with other senior officers of the Lands D as members. Its main function is to consider specific issues affecting individual land transactions, including the administration of STTs.*

- (i) adding a new clause in the STT agreement stipulating that only the written contents of the tenancy agreement would form the STT;
- (ii) adding a new clause in the STT agreement permitting the Government to set off the rent arrears by the deposits held for all other STTs of the same tenant;
- (iii) requiring a special deposit to ensure the due performance of the tenancy conditions by a tenant where substantial upgrading works are required of the tenant;
- (iv) requiring STT tenderers to provide a statutory declaration of the ownership and directorship details of all related companies, including those registered overseas;
- (v) revising a tenancy clause which would require a tenant to bear the costs of all diversion of utilities;
- (vi) adding a new clause in the STT agreement to require a car-park STT tenant to commence and continue to operate the STT site as a car park; and
- (vii) reducing the fixed term of new car-park STTs to one year, though the STTs may be renewable. This arrangement would allow a tenant to opt out after one year.

2.19 ***Longer-term car-park leases proposed in 2006.*** In March 2006, LAM agreed to explore a proposal to grant longer-term car-park leases (say for seven years) and sell the car-park leases as assets. This would avoid rent collection problems during the lease period. As at June 2006, the Lands D was consulting the car-park operators on the proposal.

Audit observations

Need to expedite actions to implement approved measures

2.20 To give effect to the new measures approved by LAM in 2005 (see para. 2.18), the Lands D has to amend the STT agreement and tender notice. Up to mid-September 2006, the Lands D had implemented the measures in paragraph 2.18(b)(v) to (vii), but had not implemented the remaining measures in paragraph 2.18(a) and paragraph 2.18(b)(i) to (iv). **Audit considers that there is a need for the Lands D to expedite**

implementation of these measures with a view to reducing the likelihood of legal challenges.

Audit recommendation

2.21 **Audit has recommended that the Director of Lands should expedite implementation of the outstanding measures for improving the administration of STTs (see para. 2.20).**

Response from the Administration

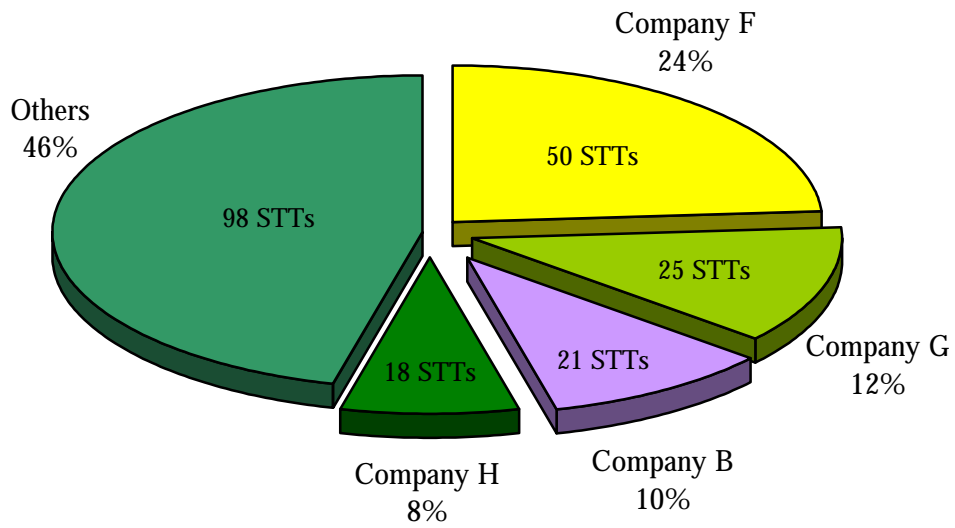
2.22 The **Director of Lands** accepts the audit recommendation in paragraph 2.21. He has said that the Lands D is taking action to incorporate appropriate clauses into the STT agreement with a view to strengthening tenancy enforcement. This includes the Government's right to set off rent arrears owed by a tenant against his rental deposits held for other STTs (see para. 2.18(b)(ii)).

Provision of car parks by STTs

2.23 Car-park STTs supply a large number of parking spaces for different types of vehicles. The provision of parking spaces by STTs is particularly important for overnight parking of goods vehicles. According to the Environment, Transport and Works Bureau (ETWB), in September 2004, the 12,300 parking spaces for goods vehicles provided by STTs made up 20% of the territory-wide supply of 62,400 related parking spaces (Note 6). In November 2005, the Lands D considered that there was a need to monitor the car-park STT holdings by individual tenants. In March 2006, the Lands D conducted an analysis of the 212 car-park STTs by tenant (see Figure 4).

Note 6: *This is based on the October 2005 "Report on Parking Demand and Supply and Progress of Improvement Measures" for the Legislative Council Panel on Transport.*

Figure 4
Analysis of 212 car-park STTs by tenant
(March 2006)



Source: Lands D records

Remarks: For Companies B and F, the car-park STTs of their related companies are included as their STTs.

2.24 As illustrated in Figure 4, there were four major car-park STT tenants, each holding 18 to 50 car-park STTs. Each year, they paid substantial STT rents (see Table 3).

Table 3
Annual rent from four major car-park STT tenants
(March 2006)

Tenant	Number of car-park STTs held	Estimated annual rent (Note) (\$ million)
Company F	50	139
Company G	25	72
Company B	21	53
Company H	18	40
Total	114	304

Source: Lands D records

Note: This is based on 12-month rent payable for the car-park STTs held by the respective tenants in March 2006.

Audit observations

Need for financial vetting of major car-park STT tenants

2.25 The financial capability of the four STT tenants to successfully carry out their car-park operations warrants the Lands D's attention because:

- (a) given the scale of their operation, there could be a significant disruption to the supply of parking spaces if they discontinue their business; and
- (b) a large amount of government revenue is at stake if they do not pay the STT rents.

2.26 **Financial vetting.** At present, the Lands D does not check whether the tenderers holding a large number of STTs have adequate financial resources to successfully carry out the car-park operations. In this connection, Audit notes that other government departments have adopted financial vetting of tenderers, as follows:

- (a) **Housing Department.** The Housing Department (HD) requires its tenderers to provide a statement on the amount of capital to be invested for the proposed uses of the sites let to them. The HD also requires tenderers to give evidence of their financial ability to commit the capital investment and to discharge the obligations of the tenancy agreements. The financial capability of the tenderers is one of the considerations in awarding tenancies by the HD;
- (b) **Leisure and Cultural Services Department.** The Leisure and Cultural Services Department (LCSD) carries out financial vetting of tenderers if the contract value exceeds \$2.5 million. If the tenderers do not meet the financial requirements, the LCSD usually requires them to pay a higher deposit; and
- (c) **Works departments.** The ETWB requires its approved contractors for public works to maintain a certain minimum level of employed and working capitals in order to qualify for tendering for public works. In general, a contractor has to meet a progressively higher capital requirement for tendering for works of a larger contract value. He has to make up any shortfall in the capital requirement by either:
 - (i) increasing his company's share capital, partners' funds or proprietor's funds, which are to be paid up in cash; or
 - (ii) arranging a bank loan that is not repayable within 12 months.

In accordance with the ETWB's administrative rules, the works departments must satisfy themselves that the tenderers are financially capable of successfully carrying out all the government contracts they hold before awarding them new contracts.

2.27 Audit notes that, notwithstanding that the Lands D has implemented a number of improvement measures concerning car-park STTs, none of these measures is related to vetting the financial capability of car-park STT tenants. **Given the scale of their operation and the substantial amount of government revenue involved, Audit considers that there is merit to consider introducing procedures to vet the financial position of these tenants.**

Need for additional control over settlement arrangement

2.28 In the course of the legal proceedings for the five rent arrears cases in paragraph 2.14, the tenants concerned had proposed settlement of the cases. After due consideration, the Lands D accepted the tenants' proposals for Cases 3-1 and 3-5, but rejected the proposals for the other three cases. As a settlement may involve accepting a sum smaller than the amount of unpaid rent, there is a need for proper control over the handling of the tenants' settlement offers. **In this regard, Audit considers that there is room for improvement, as follows:**

- (a) ***Senior management's involvement.*** The Lands D had not issued internal guidelines on the level of authority that the DLOs should seek before accepting a tenant's settlement proposal or making a counter-offer. Audit noted that there were different practices:

Case	LAM's involvement	Lands D Deputy Director's involvement
3-1 and 3-2	No	Yes
3-3	Yes	Yes
3-4	No	No
3-5	Yes	Yes

To strengthen internal control, Audit considers that there is a need to define the circumstances under which the DLOs should seek approval from a higher authority before accepting a tenant's proposal or making a counter-offer; and

- (b) ***Prior consultation with the FSTB.*** According to Financial Circular No. 6/2000, the waiving of a claim by the Government is a loss and the responsible Controlling Officer needs to comply with the laid down write-off procedures. The authority to write off a loss in excess of \$500,000 is vested with the Secretary for Financial Services and the Treasury. Accordingly, before the Lands D accepts a settlement offer or making a counter-offer that would involve waiving of a claim of over \$500,000, the FSTB needs to be consulted. Audit noted that for Case 3-1, the Lands D had consulted the FSTB before accepting the tenant's settlement offer that would involve waiving of a claim of over \$500,000. As for Cases 3-2 and 3-3, the Lands D had made counter-offers that each involved waiving of a claim of over \$500,000. The Lands D had consulted the FSTB before making the counter-offer for Case 3-2, but not for Case 3-3.

Audit recommendations

- 2.29 **Audit has recommended that the Director of Lands should:**
- (a) **consider introducing procedures for vetting the financial position of major car-park STT tenants before awarding them new car-park STTs (see para. 2.27);**
 - (b) **prescribe the circumstances under which the DLOs should seek the approval of a Lands D Deputy Director or LAM before making a counter-offer to a tenant's settlement proposal (see para. 2.28(a)); and**
 - (c) **ensure that the Secretary for Financial Services and the Treasury is consulted before making a counter-offer to a tenant's settlement proposal involving write-off or waiver of revenue of over \$500,000 (see para. 2.28(b)).**

Response from the Administration

2.30 The **Director of Lands** accepts the audit recommendations in paragraph 2.29. He has said that the Lands D:

- (a) will draw up guidelines and revise the Lands Administration Office Instructions for implementing the recommendations; and
- (b) for a specific tenancy, may carry out financial vetting of the prospective tenant prior to granting an STT to him to ensure that he is financially capable of operating the permitted facilities under the tenancy.

2.31 The **Secretary for Financial Services and the Treasury** supports the audit recommendation in paragraph 2.29(a). He has said that while the tendering procedures set out in the Stores and Procurement Regulations need not be applied to STTs (see para. 3.2), the Lands D may consider making reference to these Regulations on financial vetting before awarding an STT to ensure that a tenderer is financially capable of fulfilling the STT requirements.

PART 3: MONITORING OF TENANTS' PERFORMANCE

3.1 This PART examines the Lands D's system of monitoring of tenants' performance.

STT tender system

3.2 The Lands D adopts a simple tender system for letting STT sites. Under this system, the Lands D does not have to follow the full tender procedures in the Stores and Procurement Regulations (Note 7). The Lands D has been given delegated authority to award an STT without making a submission to the Central Tender Board, as follows:

- (a) in 1977, the then Secretary for the Environment delegated to the Director of Lands the authority to accept the highest tender. In other cases, the Director needed to submit his recommendations to the Central Tender Board. The Director had in turn delegated the authority to accept the highest tender to the District Lands Officers; and
- (b) in 1980, the Secretary for the Environment extended the Director of Lands' authority to:
 - (i) reject all tenders received in a tender exercise; and
 - (ii) accept the second highest tender in the event that there was a technical error or an unacceptable declared use of the site in the highest tender.

In cases in which the highest tenders were not accepted for other reasons, the Director needed to make recommendations to the Central Tender Board. The Director had delegated the authority in (i) and (ii) to the Deputy Director of Lands (General), who acted on the recommendations of LAM.

Development of a performance review system

Measures introduced in 2002

3.3 In early June 2002, the Lands D consulted the then Secretary for the Treasury when processing STT tenders from two tenants with unsatisfactory past performance. The

Note 7: *For example, the Lands D does not have to publish invitations for STT tenders by Gazette Notices.*

Secretary advised that, while the Lands D could not ban any tenderers from tendering, it could reject tenders on the grounds of unsatisfactory past performance without making a submission to the Central Tender Board. The Lands D accepted the advice and implemented the following measures for monitoring STT tenants with unsatisfactory performance:

- (a) **Six-monthly performance review.** For STT tenants with records of tenancy breaches, LAM would consider whether new STTs would be awarded to them on a case-by-case basis. LAM would apply this assessment procedure to tenders from companies with substantially the same directors or shareholders as these tenants. In mid-June 2002, LAM identified some tenants with tenancy breaches (hereinafter referred to as the **identified tenants**) and decided that their performance should be reviewed in six months' time to determine whether the assessment procedure should continue to be applied. In doing so, the Technical Information Unit (TIU) of the LAO was responsible for:
 - (i) updating LAM on the performance of the identified tenants based on returns from the DLOs; and
 - (ii) disseminating the results of LAM's review of the identified tenants' performance to the DLOs;
- (b) **Company search.** The Lands D would conduct company searches to find out the directors and shareholders of the identified tenants. The TIU would provide such information to the DLOs for reference when checking the directors and shareholders of the tenderers; and
- (c) **Submission of shareholding information by tenderers.** If tenderers were limited companies, the Lands D would require them to submit documents giving details of their directors and shareholders. LACO would revise the tender notice to give effect to this new measure.

Measures introduced between 2003 and 2005

3.4 Between 2003 and 2005, the Lands D introduced the following additional measures:

- (a) **Regular performance reporting for car-park STT tenants.** In May 2003, LAM considered that, as there were many problems and complaints relating to car-park STT tenants, a reporting mechanism should be introduced to monitor regularly the performance of such tenants. This mechanism would identify tenants with serious breaches of tenancy conditions for reference in awarding future tenancies;

- (b) **Three-monthly performance review.** In September 2003, LAM considered that the six-monthly performance review of the identified tenants (see para. 3.3(a)) might not be frequent enough to assess their performance. After deliberations, LAM decided that the TIU should conduct the performance review once every three months;

- (c) **Measures to improve transparency.** To state the Government's position clearly and to improve transparency, in September 2003, LAM decided that the Lands D would inform:
 - (i) all existing STT tenants that their performance would be a factor when considering their future tenders;

 - (ii) the tenderers of the reason if their tenders were rejected due to unsatisfactory past performance; and

 - (iii) all tenderers in the tender documents that their past and current performance would be taken into account in deciding the award of STTs;

- (d) **Change of company ownership.** In June 2004, to prevent an identified tenant from obtaining a new STT through gaining control of a tenant company, LAM decided that any change in the ownership or directorship of a tenant required the prior written approval of the DLO concerned. Failure by the tenant to obtain such an approval would constitute a breach of the STT condition, leading to termination of the tenancy; and

- (e) **Monitoring of car-park STT holding.** Tenants of car-park STTs provide to the public a large number of parking spaces for different types of vehicles. In November 2005, the Lands D considered that there was a need to monitor tenants' holding of car-park STTs to prevent market domination and minimise service disruption in the event that regulating action had to be taken against them. For this purpose, the Lands D introduced the following measures:
 - (i) the DLOs would keep a register of the tenants' holding of car-park STTs in their districts. The TIU would consolidate and report the information to LAM regularly; and

 - (ii) the DLOs would report to LAM if there was a concern that a tenant had a large proportion of car-park STTs in their districts.

Audit observations

Need for timely dissemination of LAM decision

3.5 Since June 2002, the Lands D has implemented an important regulating measure for monitoring the performance of identified tenants (and their related parties), i.e. LAM's assessment of the award of new STTs to them. Effective implementation of this measure requires timely dissemination of LAM decisions on the identified tenants (and their related parties). Otherwise, the DLOs responsible for assessing tenders would not be able to implement LAM directions.

3.6 **Audit found three cases where the DLOs were not informed in time of the latest LAM decisions concerning the identified tenants.** In the event, two DLOs granted three STTs to two identified tenants and a related party without referring the tenders to LAM for review. The three cases are summarised in paragraphs 3.7 to 3.12.

Case 4-1

3.7 **LAM decision.** At the time of introducing the performance review system in June 2002, LAM decided that a company (Company F) with unsatisfactory past performance in some STTs should be put under review. In November 2002, in view of an improvement in Company F's performance, LAM decided that the company's tenders needed not be subject to its review. However, due to subsequent changes in the company's performance, on 3 September 2003, LAM decided that the company's tenders should again be subject to its review.

3.8 **Award of STT.** In early September 2003, the District Lands Office/Tsuen Wan and Kwai Tsing (DLO/TW&KT) assessed tenders for a new STT in the New Territories. Company F submitted the highest tender. However, the DLO was not informed (until 22 September 2003) of the latest LAM decision of putting the company back on the review list. In mid-September 2003, the DLO awarded the STT to Company F without submitting its tender to LAM for review.

Case 4-2

3.9 On 3 September 2003, LAM decided that tenders from Company A should be subject to its review. In early September 2003, the DLO/TW&KT assessed tenders for another STT in the New Territories. Company A submitted the highest tender. However, the DLO was not informed (until 22 September 2003) of the latest LAM decision of putting the company on the review list. In mid-September 2003, the DLO awarded the STT to Company A without submitting its tender to LAM for review.

Case 4-3

3.10 **LAM decisions.** In December 2003, in assessing two STT tenders in Kowloon (hereinafter referred to as Areas 1 and 2), the District Lands Office/Kowloon East (DLO/KE) carried out company searches to ascertain if the tenderers were related to the identified tenants. In the event, the DLO found that:

- (a) among the tenderers bidding for the STT in Kowloon Area 1, a tenderer (Company I) was related to Company F which was on LAM review list (see para. 3.7). Accordingly, the DLO sought LAM advice on whether Company I's tender should be rejected. On 10 December 2003, LAM decided to reject Company I's tender. **However, other DLOs were only informed of the relationship between Companies F and I on 15 April 2004;** and
- (b) **among the tenderers bidding for the STT in Kowloon Area 2, a tenderer (Company J) was related to Company F through two intermediate companies, Companies I and K,** as follows:
 - (i) Company I had shareholding in Company J. LAM had rejected Company I's tender because of its relationship with Company F (see para. 3.10(a)); and
 - (ii) Companies J and F had shareholding in Company K. Company K also had unsatisfactory performance in one of the STTs managed by the DLO/KE (see para. 4.8(a)).

Accordingly, the DLO sought LAM advice on whether Company J's tender should be rejected. On 16 December 2003, LAM decided to reject Company J's tender. **However, other DLOs were only informed of the relationship between Companies F and J on 15 April 2004.**

3.11 **Award of STT.** In December 2003, the District Lands Office/Hong Kong West and South (DLO/HKW&S) assessed a sole tender submitted by Company J for an STT on Hong Kong Island. **However, the DLO/HKW&S had not been informed (until 15 April 2004) of the relationship between Companies J and F (see para. 3.10(b)).** Unlike the DLO/KE which had dealt with the two intermediate Companies I and K before, the DLO/HKW&S was unaware of the relationship between Companies J and F. In the event, in early January 2004, the DLO/HKW&S awarded the STT to Company J without submitting its tender to LAM for review.

3.12 In all three cases, the performance of the tenants was subsequently found to be unsatisfactory. As a result, the Lands D had to monitor these tenants' performance on a regular basis in accordance with the laid down procedures (see para. 3.4(a)).

Other cases

3.13 Apart from the three cases mentioned above, Audit also noted that there were three other cases in which some important LAM decisions were disseminated to the DLOs after a time lapse of 35 to 78 days (see Table 4).

Table 4

**Dissemination of LAM decisions to DLOs
(July 2004 to June 2006)**

Date of LAM decision	Date of dissemination of decision	Time elapsed (days)	LAM decision
3.6.2004	14.7.2004	41	To put a former identified tenant (whose performance deteriorated again) back on LAM review list
21.9.2005	8.12.2005	78	To put two identified tenants on LAM review list
10.5.2006	14.6.2006	35	To put two identified tenants on LAM review list

Source: Lands D records

3.14 **Audit considers that there is a need to ensure the timely dissemination of LAM decisions to the DLOs.** In this connection, Audit noted that LAM decisions were communicated to the DLOs by circulation of memoranda. Audit considers that the Lands D should consider using electronic mails to speed up the dissemination of LAM decisions.

Need to conduct timely performance reviews

3.15 In September 2003, LAM decided to adopt a three-month review cycle for the identified tenants (see para. 3.4(b)). Since then, the Lands D had conducted nine performance reviews. As summarised in Table 5, there were delays of 28 to 85 days in conducting four of these reviews.

Table 5
Delay in conducting three-monthly performance reviews
(March 2004 to May 2006)

Date of review	Date of preceding review	Delay (days)
(a)	(b)	(c) = (a) minus (b) minus 3 months
31.3.2004	3.12.2003	28
22.12.2004	18.8.2004	34
15.6.2005	22.12.2004	85
10.5.2006	23.11.2005	76

Source: Lands D records

Audit considers that the Lands D needs to conduct performance reviews in accordance with the LAM decision (see para. 3.4(b)).

Need to improve the reporting mechanism for car-park STT tenants

3.16 In May 2003, the Lands D introduced a mechanism for reporting on the performance of car-park STT tenants regularly (see para. 3.4(a)). Audit's review of the implementation of this mechanism shows that there was room for improvement, as follows:

- (a) ***Timeliness of performance report.*** The following three reports submitted to LAM did not mention the most up-to-date performance of the car-park STT tenants:

- (i) the report of May 2006 only showed the tenants' performance up to March 2006 (i.e. a two-month time lapse);
 - (ii) the report of June 2005 only showed the tenants' performance up to February 2005 (i.e. a four-month time lapse); and
 - (iii) the report of December 2003 only showed the tenants' performance up to October 2003 (i.e. a two-month time lapse);
- (b) **Reporting frequency.** There is no guideline on the frequency of reporting to LAM. The TIU usually submitted the performance reports of car-park STT tenants to LAM together with the three-monthly reviews of the identified tenants. However, for the three-monthly reviews in June 2004 and September 2005, no performance reports were submitted; and
- (c) **Reporting practices.** The TIU relied on returns provided by the DLOs for compiling the performance reports. There is no guideline on what aspects of the tenants' unsatisfactory performance that should be included in the returns. Two DLOs adopted different reporting practices, as follows:
- (i) from March 2004 to February 2005, the DLO/TW&KT's reports covered a tenant who had rent arrears for two STTs and did not return the sites immediately after termination of the tenancies. The tenant returned one site in April, and another one in September 2005. Since October 2005, the DLO had ceased to report on the two STTs although the rent arrears remained unsettled; and
 - (ii) commencing October 2003, the District Lands Office/North's reports covered a tenant who had rent arrears for two STTs and did not return the sites immediately after termination of the tenancies. While the tenant returned the two sites in November 2004, the DLO continued to report on the two STTs because the rent arrears remained unsettled.

Audit recommendations

3.17 **Audit has recommended that the Director of Lands should:**

- (a) **disseminate LAM decisions to the DLOs on a timely basis (paras. 3.6 and 3.14);**
- (b) **adopt more efficient methods to disseminate LAM decisions to the DLOs, e.g. by electronic mail (see para. 3.14);**

- (c) **require the TIU staff to comply with the three-monthly review requirement stipulated by LAM (para. 3.15); and**
- (d) **improve the mechanism for submitting reports on car-park STT tenants to LAM by:**
 - (i) **requiring the TIU staff to show the up-to-date performance of the tenants in the reports (para. 3.16(a));**
 - (ii) **requiring the TIU staff to submit reports on a regular basis (para. 3.16(b)); and**
 - (iii) **setting out the nature of the tenants' unsatisfactory performance necessitating the DLOs' reports (para. 3.16(c)).**

Response from the Administration

3.18 The **Director of Lands** accepts the audit recommendations in paragraph 3.17. He has said that:

- (a) since January 2006, LAM decisions have been disseminated to DLOs immediately after ratification;
- (b) as regards the audit recommendation in paragraph 3.17(b), relevant DLO staff are now able to see all LAM decisions on STTs through Lands D's intranet;
- (c) as regards the three-monthly performance review requirement (see para. 3.17(c)), the frequency of periodic reporting to LAM may be changed depending on the situation; and
- (d) the reporting format will be standardised (see para. 3.17(d)(iii)).

3.19 The **Secretary for Financial Services and the Treasury** supports the audit recommendations in paragraph 3.17 to strengthen the measures for monitoring STT tenants with unsatisfactory performance. He has said that this is in line with the spirit of the Stores and Procurement Regulations that departments shall devise an effective monitoring mechanism to ensure that a contractor performs to standard and complies with the terms of a contract.

PART 4: ENFORCEMENT OF TENANCY CONDITIONS

4.1 This PART examines the Lands D's enforcement of tenancy conditions of STTs.

STT conditions

4.2 The TIU and LACO have jointly developed a standard STT agreement. It may be modified to suit individual circumstances. The salient tenancy conditions include:

- (a) **Tenant's obligation.** A tenant shall pay the rent, use the STT site for the specified purpose and maintain it in good conditions;
- (b) **Tenancy duration.** The duration of an STT varies, depending on the plan for permanent development of the site. Generally, it is for a fixed term of one to three years for STTs granted by tender. If the site is not required for development at the end of the fixed term, the Lands D may renew the STT by means of a periodic tenancy (i.e. either quarterly or yearly). The rent for the periodic tenancy is subject to review;
- (c) **Payment terms.** The rent is usually payable quarterly in advance. The Lands D charges interest on overdue rents at a specified rate. A deposit, which may vary between three to six months' rents, is held to secure compliance with the conditions of the tenancy agreement. Since October 2004, the Lands D has increased the deposit for car-park STTs from three to six months' rents (see para. 2.17); and
- (d) **Termination of tenancy.** There are two ways to terminate a tenancy, namely:
 - (i) **Normal termination.** If an STT site is required for development at the end of the fixed term, the Lands D may terminate the STT by serving a Notice-to-quit either three months in advance or according to the period prescribed in the STT; and
 - (ii) **Early termination.** The Lands D may terminate a tenancy before the end of the fixed term in the event of a breach of the tenancy conditions by the tenant. The Lands D may issue an Eviction Notice to effect the forfeiture at any time and without any payment of compensation.

4.3 ***The role of District Lands Conferences.*** The Lands D has set up District Lands Conferences (DLCs – Note 8) to consider, among other things, STT conditions. When a site is available for letting, the DLO concerned first draws up an STT proposal and a draft tenancy agreement for the DLC members' consideration. The DLO takes into account the members' advice regarding the use of the site and any special conditions required before finalising the STT for the DLC's approval.

Site inspections

4.4 The Lands Administration Office Instructions state that:

- (a) "ideally" each STT site should be inspected once a year; and
- (b) more frequent inspections are desirable and should be arranged as staff and other work priorities permit.

4.5 The DLOs carry out an inspection upon:

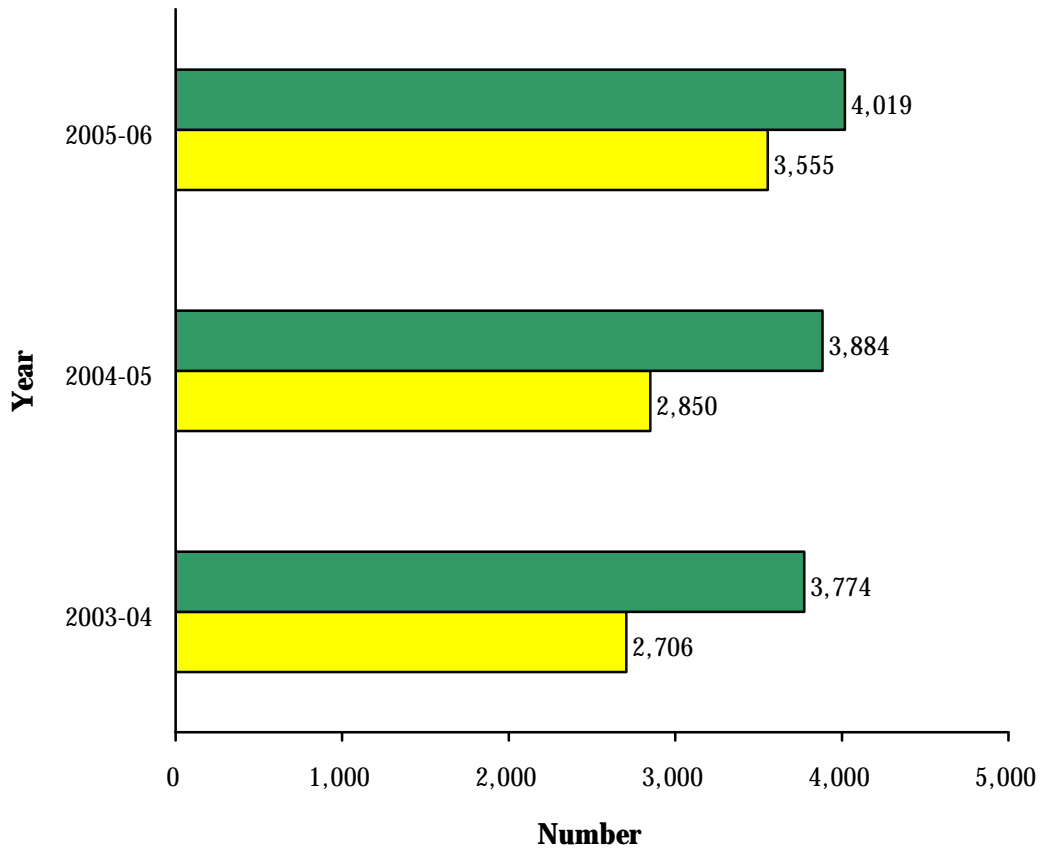
- (a) the rent review of an STT (which is normally due every three to five years); or
- (b) receipt of a complaint in respect of an STT.

Owing to the need to respect the tenant's privacy and right of peaceful occupation of the land, the DLO staff do not normally conduct inspections inside premises erected on STT sites, except where the Lands D has detected persistent breaches or received complaints. Figure 5 shows the number of STTs administered and the number of DLO site inspections in the past three years (2003-04 to 2005-06).

Note 8: *The DLCs are chaired by the relevant Regional Assistant Directors of the Lands D, depending on the issues involved. Members of the DLCs include representatives from the District Offices of the Home Affairs Department, Buildings Department, Fire Services Department, Planning Department, Transport Department and the relevant works departments.*

Figure 5

**Number of STTs and site inspections
(2003-04 to 2005-06)**



Legend: Number of STTs (Note)
 Number of site inspections carried out by DLOs

Source: *Lands D records*

Note: *The number of STTs is based on the position as at 1 April of that financial year.*

Enforcing tenancy conditions

4.6 Upon detecting a tenancy breach, depending on the severity and urgency of the breach, the responsible DLO would take the following actions:

- (a) notifying the tenant verbally on site of the detected breach, if appropriate, or in writing asking him to rectify the breach;
- (b) sending a warning letter to the tenant if the breach is not rectified within a reasonable period of time;
- (c) issuing a notice of intended re-entry if the warning is ignored;
- (d) delivering a Notice-to-quit to the tenant by fax or by mail. The same notice would be posted on site;
- (e) taking action to recover possession of the site; and
- (f) arranging for the demolition of structures on site, as appropriate.

Audit examination

4.7 Audit selected four STT cases for reviewing the DLOs' enforcement actions against the pertinent tenants, namely:

- (a) Cases 5-1 to 5-3 which are related to the unauthorised use of STT sites for car-park purposes (see paras. 4.8 to 4.15); and
- (b) Case 5-4 which is related to the unauthorised use of an STT site for residential purposes (see paras. 4.18 to 4.30).

Unauthorised use of sites for car-park purposes

4.8 To compare the enforcement actions taken by different DLOs in handling unauthorised use of sites as fee-paying car parks, Audit reviewed the following three STT cases:

- (a) **Case 5-1.** In June 2000, the DLO/KE let out by tender a site in Kowloon to Company K for a fixed term of two years. The specific usage of the site was for an amusement park and other compatible uses. Since July 2000, there had been

complaints that the company breached the tenancy conditions, including the unauthorised use of the site as a fee-paying car park (see Appendix B for details);

- (b) **Case 5-2.** In January 2001, the DLO/HKW&S let out by tender a site on Hong Kong Island to Company F for a fixed term of five years. The tenancy conditions required the company to construct and start operating a petrol-filling station by January 2003. Since May 2001, there had been complaints that the company breached the tenancy conditions, including the unauthorised use of the site as a fee-paying car park (see Appendix C for details); and
- (c) **Case 5-3.** In February 2002, the District Lands Office/Kowloon West (DLO/KW) let out by tender a site in Kowloon to Company A for a fixed term of two years. The site was for use as a plant nursery and a flower stall. In January 2003, there were complaints that the company had breached the tenancy conditions by using the site as a fee-paying car park (see Appendix D for details).

Audit observations

Need for guidelines to ensure more effective and consistent enforcement actions

4.9 Audit noted that the Lands D had not promulgated guidelines on enforcement actions against tenants in breach of tenancy conditions. A comparison of the enforcement actions taken by the DLOs concerned in the three cases in Table 6 revealed inconsistencies. The DLOs concerned took 19 months in Case 5-1, and 35 months in Case 5-2 to issue notices to terminate the STTs. These were much longer than the one month taken by the DLO in Case 5-3, notwithstanding that:

- (a) all three cases involved the unauthorised use of the sites as fee-paying car parks; and
- (b) Cases 5-1 and 5-2 involved breaches of other STT conditions.

Table 6
Enforcement actions taken in three cases
(July 2000 to April 2004)

	Case 5-1	Case 5-2	Case 5-3
Term of STT	Let in June 2000 for a fixed term of 2 years	Let in January 2001 for a fixed term of 5 years	Let in February 2002 for a fixed term of 2 years
Breach of tenancy condition: unauthorised use of site as fee-paying car park	Yes	Yes	Yes
Other breaches	Unlicensed food business and unauthorised building structures	The requirement to construct and operate a petrol-filling station was not complied with	Not applicable
Early tenancy termination action	No, Notice-to-quit was only issued in February 2002 for normal termination of the STT at the end of fixed term	Yes, Eviction Notice was issued in April 2004	Yes, Eviction Notice was issued in February 2003
Number of warning letters issued before taking tenancy termination action	28	9	3
Time from first discovery of the breach to taking tenancy termination action	19 months (from July 2000 to February 2002)	35 months (from May 2001 to April 2004)	One month (from January to February 2003)

Source: *Lands D records*

4.10 **Audit considers that there is a need for the Lands D to issue guidelines on the enforcement actions against tenants in breach of STT conditions.** Audit also considers that the Lands D needs to monitor the DLOs' enforcement practices to ensure that prompt and effective actions are taken against tenants in breach of tenancy conditions, particularly those relating to the unauthorised use of STT sites as fee-paying car parks. The reasons are as follows:

- (a) the specified uses of STT sites are determined by the DLC after careful consideration of the community needs. Unauthorised use of the sites for other purposes may not be in the public interest;
- (b) the STT rent that could otherwise be obtained for fee-paying car parks may be higher than that for the specified non-car-park uses, as exemplified in Cases 5-1 to 5-3 (see Table 7). Unauthorised use of STT sites as fee-paying car parks is undesirable from the revenue point of view; and
- (c) it is unfair to other car-park operators who pay full market rents for operating fee-paying car parks. The Lands D received some complaints from other car-park operators regarding Cases 5-1 and 5-2.

Table 7

Car-park and non-car-park STT rents

Case	Actual annual rent for non-car-park use (Note) (\$/m²)	Market annual rent for car-park use (\$/m²)	Basis of market rent
5-1	14	391	The rent of a neighbouring car-park STT site.
5-2	106	407	The rent obtained from re-letting the site for car-park use in September 2005.
5-3	53	600	The damages claimed against Company A for using the STT site as a car park.

Source: *Audit analysis of Lands D records*

Note: *For comparison purposes, the annual rent is divided by the area of the STT site in square metres (m²).*

Need for more flexible site inspection arrangements

4.11 Upon receiving a complaint, the DLO concerned usually carried out investigations by site inspections. During the inspections, if there was evidence on breaches of STT conditions, the DLO would take appropriate enforcement actions. Audit examination of Cases 5-1 and 5-2 revealed that, in Case 5-1, the site inspections were more effective than those in Case 5-2 in obtaining useful evidence, as follows:

- (a) **Case 5-1.** In early August 2000, the DLO/KE received complaints that the STT tenant had operated a fee-paying car park as there was overnight car parking when the amusement park was not in operation. In August 2000, the DLO/KE staff carried out four site inspections, of which three were carried out either at 7 a.m., or from 7 p.m. to 8 p.m., focusing on the alleged overnight car-park operation. The inspections revealed that the cars parked on site could not have belonged to the amusement park patrons. These site inspections were effective in obtaining evidence that the tenant had operated a fee-paying car park; and
- (b) **Case 5-2.** From May 2001 to May 2003, the DLO/HKW&S received four complaints that the STT tenant had operated a fee-paying car park. One of the complaints pointed out that the unauthorised car-park operation took place especially during evenings and public holidays. From May 2001 to June 2003, the DLO/HKW&S staff carried out ten site inspections. However, all these inspections were carried out on weekdays and during normal office hours. In the event, the inspections revealed no unauthorised car-park operation. On a Saturday afternoon in July 2003, the DLO staff carried out a site inspection and found that the STT site was used as a fee-paying car park.

4.12 Audit noted that the Lands D had issued guidelines on handling enquires and complaints from the public. However, these guidelines did not require the DLOs to carry out inspections outside office hours. As illustrated in paragraph 4.11, different DLOs adopt different approaches to carrying out site inspections outside office hours. **To enhance the effectiveness of site inspections, Audit considers that the Lands D should issue guidelines to DLOs on this issue.**

Need for proper control over release of rental deposit

4.13 **Case 5-2.** In March 2003, LACO advised the DLO/HKW&S that if the Government suffered a loss of rental income upon forfeiture of an STT (Note 9), it could make a claim for damages against the tenant. The tenancy agreement also provided that in case of the tenant's default in performance or observance of any of the tenancy conditions, the Government was entitled to deduct the amount of loss and damages from the rental deposit.

4.14 For Case 5-2, the DLO terminated the tenancy in May 2004. While the tenant had paid in advance the quarterly rent up to the end of June 2004, the Government suffered a loss of rental income from July 2004 up to the date of re-letting the site in September 2005. According to the Lands D's internal guidelines, before a refund of deposit was made, the DLO concerned should check to ensure that all the outstanding debts due from the tenant had been deducted. However, in July 2004, the Lands D refunded the deposit in full to the tenant without deducting from it the loss of rental income.

4.15 In May 2006, in response to Audit observations in paragraphs 4.13 and 4.14, the Lands D said that:

- (a) the DLO/HKW&S should have awaited the re-letting result and considered offsetting any losses against the deposit before making the refund;
- (b) however, the DLO was under pressure to terminate the STT and make the site available for re-letting. As the rent received from the re-letting was higher than that under the original STT, the Government's financial position had not been totally compromised; and
- (c) in the light of Audit's comments, the DLO would consult LACO to ascertain if the Government could claim any damages from the tenant.

Note 9: *The loss of rental income shall cover the period from the date of forfeiture to the original expiry date of the STT or the date of re-letting of the site, whichever is the earlier.*

Audit recommendations

- 4.16 **Audit has recommended that the Director of Lands should:**
- (a) **issue guidelines to DLOs stipulating the types and timing of enforcement actions DLOs should take against tenants in breach of tenancy conditions (see para. 4.10);**
 - (b) **closely monitor the DLOs' performance to ensure that they take prompt and effective enforcement actions (see para. 4.10);**
 - (c) **issue guidelines requiring DLO staff to conduct site inspections outside office hours, if warranted (see para. 4.12);**
 - (d) **remind DLO staff to deduct outstanding debts due to the Government before making a refund of rental deposit to a tenant (see para. 4.14); and**
 - (e) **take action to recover the loss of rental income from the tenant of Case 5-2 if the Government is entitled to do so (see para. 4.15(c)).**

Response from the Administration

4.17 The **Director of Lands** accepts the audit recommendations in paragraph 4.16. He has said that the Lands D:

- (a) will review the existing departmental guidelines on monitoring tenants' performance in complying with the tenancy conditions and on enforcement actions taken by the Lands D staff;
- (b) will draw up guidelines to implement the audit recommendation in paragraph 4.16(a) although the guidelines cannot cover all possible breaches;
- (c) will review the Lands Administration Office Instructions regarding the audit recommendation in paragraph 4.16(c); and
- (d) is taking action to implement the audit recommendation in paragraph 4.16(e).

Unauthorised use of site for residential purposes

Case 5-4

4.18 In 1976, the then New Territories Administration (NTA – Note 10) granted a short term tenancy (STT 1) to a company (Company L) for a site in Sha Tin for the purpose of facilitating the construction of power lines nearby. Subsequently, the site was let to other tenants mainly for storage purposes through three STTs, as follows:

- (a) in 1979, the NTA granted STT 2 to a company (Company M);
- (b) in 1994, the Lands D granted STT 3 to a tenant (Tenant A); and
- (c) in 2000, the Lands D granted STT 4 to Tenant A.

In August 2006, STT 4 was terminated at Tenant A's request. A summary of the four STTs and a chronology of the key events are at Appendices E and F respectively.

Audit observations

Need to take effective enforcement action

4.19 Since the Lands D took over the administration of STTs in April 1982, it had carried out 33 inspections (including re-visits) of the Sha Tin STT site (see Table 8).

Note 10: *Before the establishment of the Lands D in April 1982, the NTA (which was reorganised to become the City and New Territories Administration (CNTA) in 1981) was responsible for land administration matters in the New Territories.*

Table 8
Lands D's inspections of the Sha Tin STT site
(April 1982 to August 2006)

STT	Year	Date	Finding	Action taken	
STT 2	1983	17 November	No irregularities found	Not applicable	
	1984	9 August	Breach of tenancy condition – using the site for residential purposes	Verbal warning given	
		18 September	The tenancy breach was rectified	Not applicable	
		4 October and 19 December	Site used for storage	Not applicable	
	1985	25 October	No irregularities found	Not applicable	
	1989	14 April	Breach of tenancy condition – using the site for residential purposes	No record (Note 1)	
		12 September	Site reverted to storage use	Not applicable	
	1990	17 September	Breach of tenancy condition – using the site for residential purposes	Warning letter issued	
		21 November	No irregularities found	Not applicable	
	1991	29 May	No irregularities found	Not applicable	
		8 July	Site used for storage	Not applicable	
	1992	20 October	Breach of tenancy condition – using the site for residential purposes	Nil	
	STT 3	1994	23 June	Unauthorised occupation of government land for car-port use (Note 2)	Warning letter issued
			20 July	Unauthorised occupation of government land for car-port use	Requested the HD to clear the car-port structure (Note 3)
1995		25 October	Unauthorised occupation of government land for car-port use	Nil	
1996		16 September	Unauthorised occupation of government land for car-port use	Nil	
		25 November	Breach of tenancy condition – using the site for residential purposes	Verbal warning given	
1997		21 May	Site used for storage	Not applicable	

STT	Year	Date	Finding	Action taken
STT 3	1999	8 November	Unauthorised occupation of government land for car-port use	Nil
		14 December	Breach of tenancy condition (residential use) and unauthorised occupation of government land for car-port use	Warning letter issued
	2000	17 January and 29 February	Rectification works inadequate – domestic structures not yet demolished	Warning letter issued
STT 4	2000	2 and 8 March	Rectification works completed – domestic structures demolished	Not applicable
		7 August and 27 September	No irregularities found	Not applicable
		17 October	Site used for storage	Not applicable
	2002	22 April	(Note 4)	(Note 4)
		22 October	Breach of tenancy condition – using the site for residential purposes	Warning letter issued
		4 December	Site used for storage	Not applicable
	2005	28 September	No irregularities found	Not applicable
	2006	1 August	No irregularities found	Not applicable

Source: Lands D records

Note 1: There was no record showing that action had been taken. In September 2006, the Lands D informed Audit that: (a) following the inspection in April 1989, Tenant A did turn up in July 1989 to explain that the premises had been used for storage purposes; and (b) hence follow-up action should have been taken though there was no file record on such action.

Note 2: Under the Land (Miscellaneous Provisions) Ordinance (Cap. 28), the Government can take enforcement action against unauthorised occupation of government land. Before April 2006, the HD was responsible for controlling squatters on unleased government land. Since April 2006, the Lands D has taken over the squatter control function.

Note 3: The Lands D sent memoranda to the HD in September and October 1994, and February 1995 on the issue. In June 1995, Tenant A sent a letter to the HD, informing it that he was negotiating with the DLO/ST on matters relating to the tenancy.

Note 4: The inspection was carried out in response to Tenant A's complaint of break-ins. After the inspection, the DLO/ST accepted Tenant A's request for allowing a watchperson to stay on site for improving security.

4.20 **Of the 33 site inspections carried out between 1983 and 2006, the Lands D found that:**

- (a) **during 7 inspections** (in respect of STT 2 – on 9 August 1984, 14 April 1989, 17 September 1990 and 20 October 1992; in respect of STT 3 – on 25 November 1996 and 14 December 1999, and in respect of STT 4 – on 22 October 2002), **the tenant had breached the tenancy conditions by using the site for residential purposes;** and
- (b) **during 6 inspections** (in respect of STT 3 – on 23 June 1994, 20 July 1994, 25 October 1995, 16 September 1996, 8 November 1999 and 14 December 1999), **the tenant had occupied the adjoining government land without approval.**

4.21 Audit examination of the enforcement action taken by the Lands D (as shown in Table 8 in para. 4.19) revealed that there was room for improvement in the following areas:

- (a) **the Lands D did not issue a warning to the tenant upon finding during an inspection on 20 October 1992 that he had used the site for residential purposes;**
- (b) **upon finding unauthorised occupation of the adjoining government land for car-port use on 20 July 1994, the Lands D requested the HD to clear the car-port structure. However, the Lands D did not make similar requests with the HD regarding the three similar findings on 25 October 1995, 16 September 1996 and 8 November 1999.** Audit notes that, with effect from April 2006 (see Note 2 to Table 8 in para. 4.19), the Lands D would take enforcement action itself to clear occupied sites (as it has taken over the control of squatters on unleased government land);
- (c) **the Lands D did not promptly carry out a follow-up inspection after finding that the tenant had breached the tenancy conditions or had occupied government land without approval, as follows:**
 - (i) for the breach (using the site for residential purposes) noted on 14 April 1989, the Lands D only carried out a follow-up inspection **five months later** on 12 September 1989, in which it was found that the breach had been rectified;
 - (ii) for the finding on unauthorised occupation of adjoining government land for car-port use on 23 June 1994, the Lands D first carried out a follow-up inspection on 20 July 1994 and noted that the occupation had not been rectified. The Lands D carried out a second inspection

15 months later on 25 October 1995, finding that the unauthorised occupation still persisted; and

- (iii) for the breach (using the site for residential purposes) noted on 25 November 1996, the Lands D only carried out a follow-up inspection **six months later** on 21 May 1997, in which it was found that the breach had been rectified;
- (d) **Audit examination of the Lands D's inspection records revealed that, during inspections on 9 August 1984, 17 September 1990 and 14 December 1999, the Lands D had found building structures (such as a loft, a kitchen and bathrooms) within the STT premises which might require approvals from the Buildings Department (Note 11) under the Buildings Ordinance (Cap. 123). As far as Audit could ascertain, the Lands D had not sought advice from the Buildings Department regarding the propriety of the structures; and**
- (e) for the breach (using the site for residential purposes) noted on 14 December 1999, the Lands D specifically required the tenant to demolish some domestic fixtures (such as bathtubs, a wall cabinet and water heaters). **However, the Lands D did not make the specific requirements for the same breach detected on other occasions.**

Room for improvement in checking tenant's status

4.22 In November 1989, the Lands D carried out a check of the up-to-date status of Company M with the then Registrar General's Department. It found that there was no record of Company M registering with the then Companies Registry. In March 1990, in response to the Lands D's enquiry, the Registrar General's Department advised that:

- (a) Company M was not a limited company incorporated under the Companies Ordinance (Cap. 32); and
- (b) for the particulars of an unlimited company, the Lands D could check with the Business Registration Office.

Note 11: *Before the establishment of the Buildings Department in 1993, the Building Development Department (1982 to 1986) and the Buildings Ordinance Office of the Buildings and Lands Department (1986 to 1993) were responsible for enforcing the Buildings Ordinance.*

4.23 In December 1992, the Lands D carried out a check of Company M because it had learned that another company (Company N) had taken over its business. The Lands D found that Company M had ceased business in 1989. Audit noted that the Lands D only checked with the Business Registration Office 33 months after the Registrar General's Department's advice in March 1990. Audit considers that there was room for improvement in the Lands D's checking of the tenant's status.

Need to clarify the Lands Administration Office Instructions

4.24 Since 1988, the Lands Administration Office Instructions have stated that:

- (a) for an STT granted directly, the concerned District Lands Officer has delegated authority to approve an STT modification in respect of a change of tenants; and
- (b) a contentious STT modification case should be submitted to the DLC for making a recommendation.

4.25 In February 1993, Company N and Tenant A applied to the Lands D for a transfer of the tenancy to Tenant A, saying that Tenant A had been the actual user of the STT site. In June 1993, the District Lands Officer/Shu Tin approved the tenancy transfer by terminating STT 2 and granting STT 3 to Tenant A for storage of non-dangerous goods. In giving the approval, the DLO/ST indicated that:

- (a) STT 2 would normally be terminated as the site was being used for residential purposes in breach of the tenancy conditions;
- (b) neither the Government Property Agency (GPA) nor the then Agriculture and Fisheries Department wished to use the site. Due to its isolated location, leaving it vacant would result in management problems and a loss of rental income;
- (c) other than the observed breach, there had been no complaint about the use of the STT site over the previous ten years; and
- (d) the termination of STT 2, as an alternative to the tenancy transfer, would not be in the Government's interest.

4.26 Apparently, the DLO/ST did not consider the granting of STT 3 as a contentious case which, according to the Lands Administration Office Instructions (see para. 4.24(b)), should have been submitted to the DLC. **Audit considers that there is a need to clarify the circumstances under which an STT case should be regarded as contentious, requiring a submission to the DLC.**

Need to strengthen STT administration

4.27 **When granting STT 3 to Tenant A in January 1994, the Lands D had not implemented additional measures to ensure that the tenant would not use the site for residential purposes.** The Lands D only carried out routine inspections, of which 20 in total were carried out during the tenancy of STT 3 and STT 4 (from January 1994 to August 2006). During three of the inspections (on 25 November 1996, 14 December 1999 and 22 October 2002), the Lands D found that the site had repeatedly been used for residential purposes in breach of the tenancy conditions (see Table 8 in para. 4.19). For these breaches, the Lands D only issued verbal or written warnings. In view of the recurring nature of these breaches, Audit considers that the Lands D should have taken more stringent enforcement actions, such as terminating the tenancy.

4.28 Audit examination revealed that the Lands D's copy of the STT 3 agreement (effective 1 January 1994) only bore the tenant's signature, but without the signature of the landlord (i.e. the Government's representative). In December 1999, in response to DLO/ST's enquiry, LACO advised that:

- (a) although the Government's representative did not sign on the STT 3 agreement, the tenancy was validated by the conduct of both parties, i.e. the rent payment by the tenant and its acceptance by the Government; and
- (b) the Government was entitled to issue a Notice-to-quit in case of the tenant's breach of the tenancy conditions.

Audit considers that there was room for improvement in this area.

Lands D's follow-up action

4.29 In August 2006, the Lands D sought legal advice on the action that the Government could take in respect of the breaches of tenancy conditions. In this connection, Audit considers that the Lands D should, based on the legal advice obtained, consider taking appropriate action in respect of the findings mentioned in Table 8 in paragraph 4.19.

4.30 In the light of the audit findings in this case, Audit considers that there is a need for the Lands D to check on other STTs to see if there are similar breaches of tenancy conditions.

Audit recommendations

- 4.31 **Audit has recommended that the Director of Lands should:**
- (a) **take effective enforcement action against an STT tenant in breach of tenancy conditions by:**
 - (i) **issuing a warning letter to the tenant upon finding a breach (see para. 4.21(a));**
 - (ii) **carrying out a timely follow-up inspection to ascertain whether the breach has been rectified (see para. 4.21(c));**
 - (iii) **if suspected unauthorised building structures are found on an STT site, requesting the Buildings Department to carry out an investigation and take necessary action (see para. 4.21(d)); and**
 - (iv) **requiring the tenant to remove fixtures not compatible with the designated use of the STT site (see para. 4.21(e));**
 - (b) **take effective enforcement action against unauthorised occupation of government land, such as clearing the occupied site (see para. 4.21(b));**
 - (c) **require Lands D staff to check the business registration and company particulars of a tenant (who is holding an STT in the name of a firm) in a timely and thorough manner (see para. 4.23);**
 - (d) **clarify the circumstances under which an STT case should be regarded as contentious, requiring a submission to the DLC (see para. 4.26);**
 - (e) **for an STT tenant who has a past record of tenancy breaches, implement additional measures to deter him from committing similar breaches (see para. 4.27);**
 - (f) **for recurring tenancy breaches, consider taking more stringent enforcement action (such as terminating the tenancy) against the tenant (see para. 4.27);**
 - (g) **remind Lands D staff that all STT agreements must be signed by the Government's representative (see para. 4.28);**
 - (h) **based on legal advice, consider taking appropriate action against the tenant in Case 5-4 (see para. 4.29); and**

- (i) **conduct a check of other STTs with a view to finding out unauthorised use of the sites and take appropriate action as soon as possible (see para. 4.30).**

Response from the Administration

4.32 The **Director of Lands** accepts the audit recommendations in paragraph 4.31. He has said that:

- (a) the Lands D will review the Lands Administration Office Instructions with a view to incorporating guidelines for implementing the audit recommendations in paragraph 4.31(a)(i) and (ii), and 4.31(c), (d) and (g);
- (b) regarding the audit recommendation in paragraph 4.31(a)(iii), the Lands D will seek the Buildings Department's comments if suspected unauthorised building structures are found on an STT site;
- (c) regarding the audit recommendation in paragraph 4.31(a)(iv), the Lands D will draw up guidelines for its staff to investigate doubtful fixtures for further action (as physical and visual inspections may not be sufficient to establish the legality of fixtures);
- (d) regarding the audit recommendation in paragraph 4.31(b), the Lands D may regularise some cases of unauthorised occupation of government land by issuing STTs at market rental to the occupiers in accordance with the established policy (see para. 1.4(c));
- (e) regarding the audit recommendation in paragraph 4.31(g), at a meeting held in August 2006, he reminded all the Lands D's directorate grade officers that all STT agreements must be promptly signed by a Government representative;
- (f) regarding the audit recommendation in paragraph 4.31(h), the Lands D is seeking legal advice concerning the breaches of the tenancy condition by using the site for residential purposes, and will seek legal advice concerning the unauthorised occupation of the adjoining government land;
- (g) regarding the audit recommendation in paragraph 4.31(i), the Lands D will conduct inspections of all STTs for any unauthorised use of the sites in four months' time; and
- (h) the Lands D will continue to review the procedures for tenancy enforcement. It is considering taking the following improvement measures to further enhance the effectiveness in administering the STT system:

- (i) formulating a set of guidelines for enforcement action, such that warning letters and notices of termination are issued within a specific time limit;
- (ii) outsourcing part of the patrol and tenancy enforcement work with a view to conducting an inspection of every STT at least once a year;
- (iii) for recurring breaches, giving the tenant a shorter period to rectify the breaches;
- (iv) demanding higher deposits from tenants who are found to have repeatedly committed minor breaches; and
- (v) introducing a system of self-certification of compliance by private professionals for specific tenancies involving large areas or with mixed uses.

4.33 The **Secretary for Financial Services and the Treasury** has said that:

- (a) the Housing, Planning and Lands Bureau (HPLB) and the Lands D's measures to improve the monitoring and enforcement of tenancy conditions as well as the Lands D's checking of other STTs may have additional financial implications;
- (b) the bureaux/departments concerned will have to absorb the resource requirements from within their existing resources as far as possible; and
- (c) they will have to seek additional resources, if necessary, according to the established resource allocation procedure.

Notice-to-quit

4.34 When a DLO decides not to renew an STT, it has to serve a Notice-to-quit on the tenant. The effect of serving a Notice-to-quit is to terminate the tenancy upon its expiry and to demand possession of the site. The Lands D may take action under the Land (Miscellaneous Provisions) Ordinance to repossess the site if the tenant does not return it as required.

4.35 Since 2003, the Lands D has laid down the following guidelines on the proper serving of a Notice-to-quit in the Lands Administration Office Instructions:

“If the tenancy is terminable by one month’s notice expiring “at any time”, the one month Notice-to-quit can be given at any time and it will expire at midnight of the corresponding date of the following month. For example, if it is served on 10 October 2003, then its expiry date should fall on midnight of 10 November 2003 running over to 11 November 2003 The period of Notice-to-quit starts to run after the day on which the Notice-to-quit is served. It must be ensured that the Notice-to-quit should reach the intended recipient before its start date”.

Audit observations

Need to remind staff of the proper handling of Notice-to-quit

4.36 Notwithstanding the guidelines on the proper serving of a Notice-to-quit, Audit noted that there were two cases where the tenants took legal action to challenge the validity of the Notices-to-quit. These two cases (Cases 5-3 and 5-5 – see paras. 4.37 to 4.40) illustrated the need to remind DLO staff of the proper handling of Notices-to-quit to minimise the risk of legal challenges.

Case 5-3 – notice period of Notice-to-quit

4.37 As mentioned in Table 6 in paragraph 4.9, in February 2003, the Lands D issued an Eviction Notice to terminate the tenancy of Case 5-3. However, in 2003, Company A commenced legal proceedings regarding the Eviction Notice (see Appendix D). In February 2004, LACO advised the DLO to issue a Notice-to-quit as an alternative way to repossess the site. On 26 April 2004, the DLO issued a Notice-to-quit demanding the company to return the site on 26 July 2004. However, in July 2004, the company took legal action to challenge the validity of the Notice-to-quit on the grounds that the DLO had not given at least three months’ notice as required under the tenancy agreement. Apparently, the company claimed that the notice period was one day less than the required period.

4.38 In July 2004, LACO advised the DLO/KW not to take action to repossess the site as the Notice-to-quit was under legal challenge. As the company was subsequently wound up, the legal proceedings were not pursued. The validity of the Notice-to-quit was not determined by the court. Nevertheless, the DLO’s action to repossess the site was delayed by the legal challenge. **Audit considers that there is a need to remind DLO staff to exercise due care in determining the notice period of a Notice-to-quit.** In particular, they should be reminded to take note of LACO’s advice in 2003, as follows:

- (a) in computing the time for serving a Notice-to-quit, the day on which the Notice-to-quit was served should be disregarded as part of the notice period. For example, to fulfil a one-month notice requirement, a Notice-to-quit dated 19 May 2003 would expire on midnight of 19 June 2003; and
- (b) the tenant would be entitled to stay in possession of the site up to midnight of the expiry date on 19 June 2003.

Case 5-5 – demand note issued after serving Notice-to-quit

4.39 In February 2004, the District Lands Office/Tai Po (DLO/TP) issued a Notice-to-quit to terminate an STT in early June 2004 so that the site could be re-let (Note 12). In May 2004, the DLO/TP awarded a new STT to the highest tenderer pending a handover of the site from the outgoing tenant in June 2004. However, in May 2004, the DLO issued a rent demand note to the tenant for the period July to September 2004. In early June 2004, the tenant paid the demand note and refused to return the site. In mid-June 2004, the DLO refunded the paid rent to the tenant and requested him to vacate the site. In late June 2004, the tenant's legal representative claimed that the Government's issue of the rent demand note and acceptance of payment invalidated the Notice-to-quit. **Audit considers that, for an STT site, DLO staff should have checked to ensure that the rental period stated in a demand note should not cover any period after the expiry date of a related Notice-to-quit which had been issued.**

4.40 In view of the uncertainty over the Government's legal position, LACO advised the DLO/TP not to take action to repossess the site. While the tenant eventually discontinued his legal action, he only returned the site to the DLO in late August 2004. Because of the uncertainty in repossessing the site, the DLO did not ask the successful tenderer of the re-letting exercise to execute the new tenancy agreement until 26 August 2004. In the event, the tenderer decided not to take up the new tenancy.

Need to clarify the basis of calculating mesne profits

4.41 The Government may make a claim for damages (mesne profits) when a tenant remained in possession of an STT site after the expiry of the tenancy against the Government's will. Audit noted that, while the Lands D had issued guidelines on handling mesne profits, these guidelines did not state the basis of calculating such profits.

Note 12: *According to the Lands D's policy, if an STT site would not be required for development for another three years after the fixed term, the site should be re-tendered.*

4.42 For Case 5-5 (see paras. 4.39 and 4.40), in September 2005, LAM decided that the mesne profits to be claimed from the tenant should be based on the rent obtainable from the successful tenderer (which was higher than the rent paid by the tenant). However, in November 2005, LAM was informed that in September 2004, the DLO/TP made a demand for mesne profits from the tenant based on the rent paid. The tenant had indicated acceptance of the amount of mesne profits demanded. In the circumstances, LAM agreed that for this particular case, mesne profits would not be based on the rent obtainable from the tenderer. **Audit considers that there is a need to clarify the basis of calculating mesne profits so as to ensure that the DLOs act in a consistent manner.**

Audit recommendations

4.43 **Audit has recommended that the Director of Lands should:**

- (a) **remind DLO staff handling Notices-to-quit that they should:**
 - (i) **comply with LACO's advice in computing the required notice period of a Notice-to-quit (see para. 4.38); and**
 - (ii) **check that, before issuing an STT rent demand note, the rental period stated in the demand note should not cover any period after the expiry date of a related Notice-to-quit which has been issued (see para. 4.39); and**
- (b) **issue guidelines to DLOs to clarify the basis of calculating mesne profits (see para. 4.42).**

Response from the Administration

4.44 The **Director of Lands** accepts the audit recommendations in paragraph 4.43(a)(i) and (b). As regards the audit recommendation in paragraph 4.43(a)(ii), he has said that the Lands Administration Office Instructions have expressly mentioned that a demand note should be issued together with the Notice-to-quit to collect the rent up to the expiry date of the Notice-to-quit.

Sharing of management information

4.45 Apart from the Lands D, the HD, the GPA and the LCSD also let out properties and sites under their management on a short-term basis. For example, the HD sometimes lets out vacant housing sites for exhibition purposes. The LCSD and the GPA sometimes let out car-park facilities within sports compounds and within government premises respectively.

4.46 In mid-2005, the HPLB enquired with the Lands D whether its tenant (Company A) was related to an HD tenant (Company O), which operated an unauthorised car park at an HD site on Hong Kong Island. In July 2005, the DLO/KW conducted a company search and found that Company A did not have common shareholders and directors with Company O. Accordingly, in August 2005, the Lands D informed the HPLB that the relationship between the two companies could not be established.

Audit observations

Need to share tenants' information

4.47 While the Lands D found no relationship between its tenant (Company A) and HD's tenant (Company O), Audit examination revealed that Company O was related to two Lands D tenants with unsatisfactory performance records (i.e. tenants of Case 4-1 – see para. 3.7, and Case 5-1 – see para. 4.8(a)) through some common directors.

4.48 Audit noted that there were no arrangements for sharing information on tenancy breaches among the Lands D and other relevant government departments. Audit considers that improvement could be made on this issue. By sharing information on tenancy breaches among government departments:

- (a) the departments could take into consideration the tenants' unsatisfactory past performance in other government tenancies in assessing their tenders; and
- (b) STT tenants may be prompted to perform well in all tenancies granted by different government departments.

4.49 Audit noted that in the GPA's tender notice, there was a provision regarding the disclosure of the tenderers' information to other government departments, as follows:

“The information collected by means of the Form of Tender will be used and may be disclosed to other government departments for the purpose of processing this tender”.

In August 2006, the GPA informed Audit that the above provision was only applicable for processing the related tender, and the provision did not allow the GPA to disclose the tenderer’s information to other government departments for other purposes.

4.50 In the Lands D’s tender notice, the tenderers were informed that their performance as Government’s tenants would be considered in the award of tenders, as follows:

“The Government will consider the past or current performance of the tenderers as tenants of the Government both in examining any tender submitted and in deciding whether to award the tender”.

4.51 In June 2006, in response to Audit enquiry regarding the sharing of information in the Lands D’s case, the Office of the Privacy Commissioner for Personal Data advised that, under the Personal Data (Privacy) Ordinance (Cap. 486):

- (a) personal data shall only be used for the purpose for which they were to be used at the time of collection of the data or a directly related purpose, unless the prescribed consent of the data subject is obtained; and
- (b) a data user shall, on or before collecting the personal data, inform data subjects from whom personal data are to be collected of the purpose for which the data are to be used and the possible transferees of the data.

4.52 **Audit considers that there is a need for the Lands D to liaise with relevant government departments with a view to devising suitable arrangements for sharing of tenants’ information.** In this regard, the Lands D should take into account the Office of the Privacy Commissioner for Personal Data’s views in paragraph 4.51 and seek legal advice on the issue if necessary.

Audit recommendations

4.53 **Audit has recommended that the Director of Lands should:**

- (a) **liaise with relevant government departments to devise suitable arrangements for sharing tenants' information; and**
- (b) **seek legal advice on the way forward to share tenants' information among relevant government departments (see para. 4.52).**

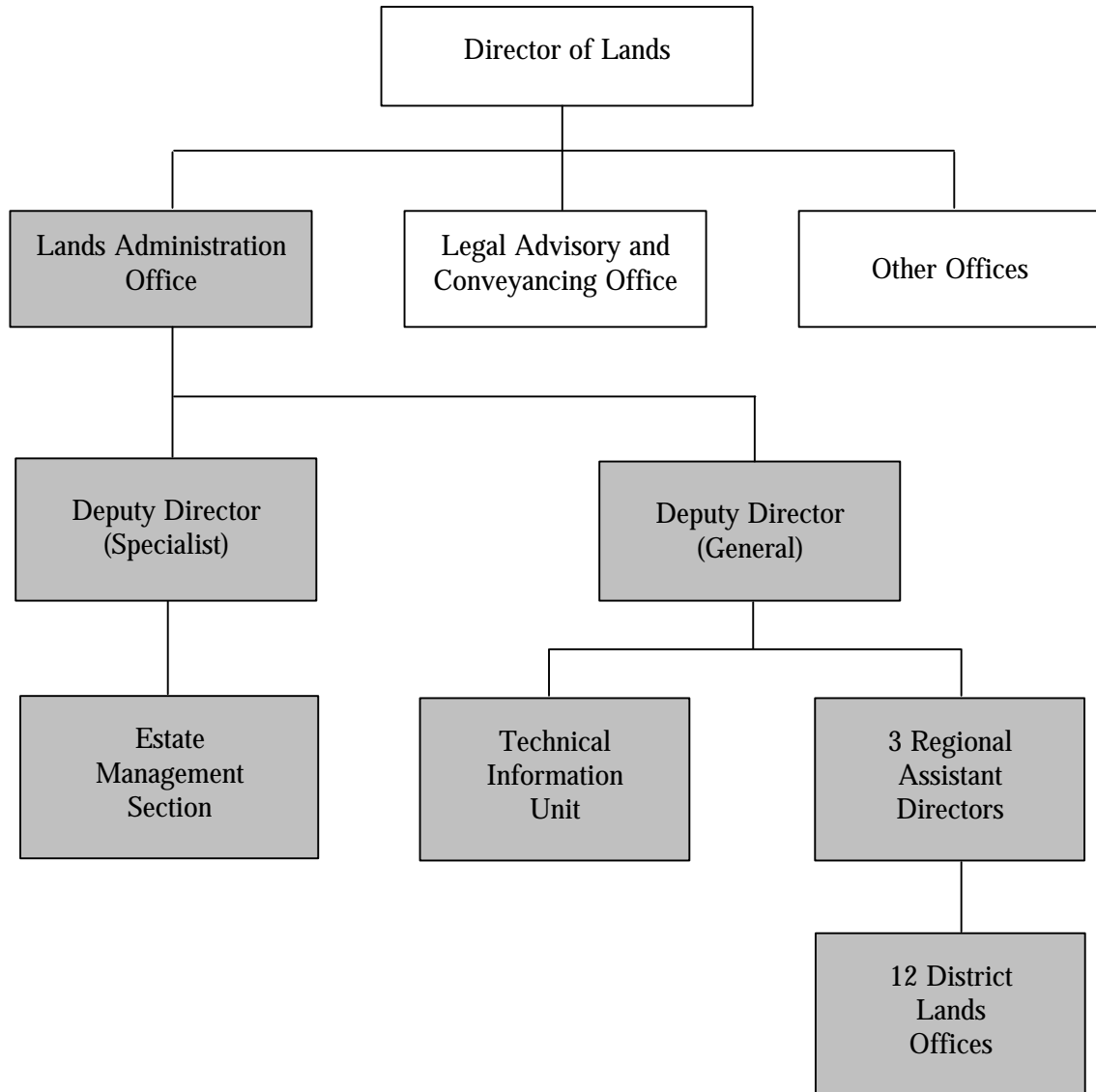
Response from the Administration

4.54 The **Director of Lands** accepts the audit recommendations in paragraph 4.53.

4.55 The **Government Property Administrator** welcomes the audit recommendations in paragraph 4.53 and undertakes to work closely with the Lands D on the issue.

4.56 The **Director of Leisure and Cultural Services** has said that, subject to legal advice and policy directives on the sharing of tenants' information among government departments, the LCSD would offer assistance to the Lands D to devise suitable arrangements.

Organisation chart of the Lands Department



Legend:  Offices responsible for managing STTs

Source: *Lands D records*

Chronology of key events of Case 5-1

January 2000	The DLC approved the letting of a site in Kowloon as a tethered balloon amusement ground and other compatible uses such as exhibition or bazaar.
June 2000	The DLO/KE let out by tender the site to Company K for a fixed term of two years.
July 2000	The Lands D received a complaint concerning the unauthorised use of the STT site as a fee-paying car park.
February 2002	The DLO issued a Notice-to-quit requiring the company to return the site to the Government in early June 2002. By this time, the DLO had received a total of 34 complaints, carried out 23 site inspections and issued 28 warning letters.
2002	The company commenced legal proceedings against the Government. In response, the Government made a counterclaim against the company.
2005	The court ruled in favour of the Government and ordered the company to return the site to the Government and pay damages.
July 2005	The Lands D repossessed the site.
2006	A winding-up order was made against the company. Up to mid-September 2006, the winding-up proceedings had been in progress.

Chronology of key events of Case 5-2

September 2000	The DLC approved the re-tendering of a site on Hong Kong Island for use as a petrol-filling station.
January 2001	The DLO/HKW&S let out by tender the site to Company F for constructing a petrol-filling station for operation by January 2003.
May 2001	The Lands D received a complaint concerning the unauthorised use of the STT site as a fee-paying car park.
February 2002	The DLO rejected the company's application for an extension of time to construct the petrol-filling station.
January 2003	The DLO found that no construction works for the station had taken place.
February and March 2003	LACO advised the DLO that: <ul style="list-style-type: none">(a) the warning letter issued by the DLO in January 2003 could be taken as the last warning;(b) forfeiture of the STT could take immediate effect; and(c) the Lands D was entitled to re-let the site for other purposes and to claim damages from the company if the Government suffered a loss of rental income.
June and September 2003	The company applied for extending the time to commence operating the petrol-filling station to February 2004. In view of the local residents' request for the STT site to be used as a petrol-filling station, the DLO withheld its forfeiture action and asked the company to expedite action to construct the station.
February 2004	The DLO found no construction works at the STT site.
March 2004	LAM approved the DLO's recommendation to forfeit the tenancy and re-tender the site.
April 2004	The DLO issued an Eviction Notice to the company. By this time, the DLO had received a total of 11 complaints, carried out 14 site inspections and issued nine warning letters.
May 2004	The DLO repossessed the site.
September 2005	The DLO re-let the site.

Chronology of key events of Case 5-3

August 2001	The DLC approved the use of a site in Kowloon for plant nursery.
February 2002	The DLO/KW let out by tender the site to Company A for a fixed term of two years.
January 2003	The Lands D received a complaint concerning the unauthorised use of the STT site as a fee-paying car park.
February 2003	The DLO issued an Eviction Notice to the company. By this time, the DLO had issued three warning letters to this company.
2003	The company commenced legal proceedings. In response, the Government made a counterclaim against the company.
February 2004	LACO advised the DLO that serving a Notice-to-quit to terminate the tenancy was an alternative to repossess the site.
April 2004	The DLO issued a Notice-to-quit to terminate the STT on the grounds that the fixed term of the STT had expired in February 2004.
2004	The company commenced legal proceedings regarding the Notice-to-quit.
September 2005	The company offered to return the site to the Government.
October 2005	The Lands D repossessed the site.
2006	The company was wound up. Accordingly, the legal proceedings in this case were not pursued.

Summary of STTs of Case 5-4

STT (Note)	Period	Tenant	Area (m²)	Designated use
STT 1	December 1976 to November 1979	Company L	1,858	Storage and helipad Permitted structure: not exceeding 25% of the tenancy area nor exceeding 6.1 metres in height
STT 2	December 1979 to December 1993	Company M	1,480 (December 1979 to mid-October 1983) 740 (mid-October 1983 to December 1993)	Storage of non-dangerous goods and helipad Permitted structure: not exceeding 25% of the tenancy area nor exceeding 6.1 metres in height
STT 3	January 1994 to February 2000	Tenant A	740	Storage of non-dangerous goods Permitted structure: not exceeding 25% of the tenancy area nor exceeding 6.1 metres in height
STT 4	March 2000 to August 2006	Tenant A	1,070	Storage of non-dangerous goods and kennel Permitted structure: storage (155 m ² × 7 m) porch (90 m ² × 4 m) water tank (1 m ²)

Source: *Lands D records*

Note: *The four STTs were let on the same basis, i.e. for a fixed term of one year and thereafter on a three-monthly basis until it was terminated by either party by giving a three-month notice.*

Chronology of key events of Case 5-4

October 1976	The Sha Tin DLC of the NTA approved the granting of STT 1 to Company L.
December 1979	At the request of Company L, the District Officer/Shu Tin of the NTA terminated STT 1 with Company L and granted STT 2 to Company M.
April 1982	The Lands D took over the administration of STTs from the CNTA.
November 1983	Company M submitted to the Lands D a Power of Attorney dated 28 October 1982 authorising Tenant A to deal with all aspects of STT 2.
December 1983	The DLO/ST approved Company M's application for a reduction in the site area from 1,480 m ² to 740 m ² with effect from mid-October 1983.
February 1993	Tenant A and Company N (which had taken over the business of Company M) applied for a transfer of the tenancy to Tenant A for recreational use, saying that Tenant A had been the user of the STT site for more than ten years.
January 1994	After seeking advice from the GPA and the Agriculture and Fisheries Department that the site was not required for government use, the Lands D terminated STT 2 with Company M and granted STT 3 to Tenant A for storage use.
February 2000	The Lands D informed Tenant A that his request for allowing residential accommodation at the site would not be considered.
March 2000	At the request of Tenant A, the Lands D terminated STT 3 and granted STT 4 to Tenant A. The permissible uses included storage of non-dangerous goods and a kennel.
August 2006	At the request of Tenant A, the Lands D terminated STT 4 and repossessed the site.

Acronyms and abbreviations

Audit	Audit Commission
CNTA	City and New Territories Administration
D of J	Department of Justice
DLC	District Lands Conference
DLO	District Lands Office
DLO/HKW&S	District Lands Office/Hong Kong West and South
DLO/KE	District Lands Office/Kowloon East
DLO/KW	District Lands Office/Kowloon West
DLO/SK	District Lands Office/Sai Kung
DLO/ST	District Lands Office/Shah Tin
DLO/TP	District Lands Office/Tai Po
DLO/TW&KT	District Lands Office/Tsuen Wan and Kwai Tsing
ETWB	Environment, Transport and Works Bureau
FSTB	Financial Services and the Treasury Bureau
GPA	Government Property Agency
GRA	General Revenue Account
HD	Housing Department
HPLB	Housing, Planning and Lands Bureau
LACO	Legal Advisory and Conveyancing Office
LAM	Land Administration Meeting
Lands D	Lands Department
LAO	Lands Administration Office
LCSD	Leisure and Cultural Services Department
m ²	square metres
NTA	New Territories Administration
SAI	Standing Accounting Instruction
STT	Short term tenancy
TIU	Technical Information Unit