

CHAPTER 8

Home Affairs Department

<h3>Licensing of hotels and guesthouses</h3>

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

Report No. 47 of the Director of Audit contains 11 Chapters which are available on our website at <http://www.aud.gov.hk>.

Audit Commission
26th floor, Immigration Tower
7 Gloucester Road
Wan Chai
Hong Kong

Tel : (852) 2829 4210
Fax : (852) 2824 2087
E-mail : enquiry@aud.gov.hk

LICENSING OF HOTELS AND GUESTHOUSES

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PART 1: INTRODUCTION

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

The Hotel and Guesthouse Accommodation Ordinance

1.2 In 1988, the Government formed a task force to study fire and other hazards of guesthouses and similar accommodation such as hotels. Based on the recommendations of the task force, the Government decided to introduce a licensing system for establishments providing such accommodation.

1.3 In May 1991, the Hotel and Guesthouse Accommodation Ordinance (HAGAO — Cap. 349) was enacted to provide for a statutory licensing scheme for hotels and guesthouses (Note 1). The aims of the scheme are to:

- (a) enable the Government to keep a comprehensive register of guesthouses and similar accommodation and to impose necessary requirements and standards for their operation; and
- (b) ensure that such establishments comply with existing requirements in respect of fire safety, structural safety, health and hygiene.

The Office of the Licensing Authority

1.4 The HAGAO designates the Secretary for Home Affairs as the Hotel and Guesthouse Accommodation Authority (hereinafter referred to as the Licensing Authority). The Office of the Licensing Authority (OLA) of the Home Affairs Department (HAD) is responsible for operating the licensing scheme, including the implementation and enforcement of the HAGAO.

Note 1: *Under the HAGAO, hotels and guesthouses include holiday flats and holiday camps, but exclude premises in which all accommodation is exclusively provided on the basis of a minimum period of 28 continuous days for each letting.*

1.5 As at 30 June 2006, the OLA, headed by the Chief Officer (who is a Chief Building Surveyor), had an establishment of 67 staff members comprising mainly officers seconded from the Buildings Department and the Fire Services Department (FSD). In 2005-06, the estimated annual expenditure of the HAD on licensing work was \$34.3 million. The organisation chart of the OLA as at 30 June 2006 is at Appendix A.

1.6 As at 30 June 2006, there were 1,142 establishments licensed under the HAGAO, comprising 151 hotels, 817 guesthouses, 136 holiday flats and 38 holiday camps.

Director of Audit's Report No. 22

1.7 In 1994, the Audit Commission (Audit) carried out a review of the implementation of the licensing schemes of hotels, guesthouses and clubs. The results of the review were included in the Director of Audit's Report No. 22 of March 1994. In its Report of June 1994, the Public Accounts Committee (PAC), among other things:

- (a) expressed concern about the slow progress in the implementation of the licensing schemes and recommended that necessary monitoring work should be carried out on those hotels and guesthouses which held scheduled licences (see para. 3.7) to ensure that the progress of their scheduled fire safety improvement works was satisfactory; and
- (b) noted that the licensing schemes had been running at a deficit and recommended that the Secretary for Home Affairs should prepare an action plan so that the Government's financial objective of full-cost recovery of the licensing schemes could be achieved quickly.

1.8 The two issues raised by the PAC are dealt with in PART 3 (for scheduled licences), and PART 5 (for cost recovery).

Audit review

1.9 Audit has recently conducted a review to examine the economy, efficiency and effectiveness of the OLA in operating the licensing scheme for hotel and guesthouse accommodation. The review has focused on the following areas:

- (a) processing of licence applications (PART 2);
- (b) enforcement of licensing requirements (PART 3);
- (c) enforcement action against unlicensed establishments (PART 4);

- (d) cost recovery (PART 5);
- (e) promotion of licensed establishments (PART 6); and
- (f) performance management (PART 7).

1.10 Audit has found areas where improvement can be made and has made a number of recommendations to address the issues.

General response from the Administration

1.11 The **Director of Home Affairs**, also on behalf of the Secretary for Home Affairs, accepts that there is room for improvement in the OLA's licensing work, and generally agrees with all the audit recommendations. She has said that she appreciates the efforts Audit has made in conducting the review.

Acknowledgement

1.12 Audit would like to acknowledge with gratitude the full cooperation of the staff of the OLA during the course of the audit review.

PART 2: PROCESSING OF LICENCE APPLICATIONS

2.1 This PART examines the processing of licence applications by the Building Safety Unit (BSU), the Fire Safety Unit (FSU) and the Administration Unit of the OLA.

Processing of licence applications

2.2 The procedures for processing **new licence applications** are as follows:

- (a) an applicant submits a completed standard application form, together with the necessary documents (e.g. layout plans of the premises);
- (b) the BSU and the FSU carry out initial inspections of the premises to identify upgrading requirements in respect of building and fire safety;
- (c) the OLA issues a letter of upgrading requirements to the applicant to inform him of the improvement works to be completed by a certain date;
- (d) upon receipt of the applicant's report of completion of the required works, the BSU and the FSU conduct compliance inspections to ascertain whether all the upgrading requirements are met; and
- (e) on satisfactory confirmation of the compliance of all the requirements and after collecting the licence fee, the OLA issues a licence to the applicant.

2.3 For processing new licence applications, the OLA has laid down internal management targets (see Appendix B), including the following:

- (a) a letter of upgrading requirements should be issued within 35 working days of receipt of an application; and
- (b) a licence should be issued within seven working days of receipt of confirmation that all requirements have been met.

These internal management targets help control the time taken by the OLA in processing new licence applications. However, the total time taken for issuing a new licence mainly depends on the time taken by the applicant in completing all the improvement works in compliance with the licensing requirements.

- 2.4 The procedures for processing **licence renewal applications** are as follows:
- (a) the Administration Unit issues a letter to a licensee, four months before the expiry of the current licence, reminding him to submit an application for licence renewal;
 - (b) on receipt of the applicant's application for licence renewal, the BSU and the FSU conduct renewal inspections of the premises to ascertain whether they continue to meet licensing requirements;
 - (c) if irregularities are found, the OLA issues a warning letter to the licensee, requiring him to rectify them by a certain date and report back to the OLA for follow-up inspection; and
 - (d) if no irregularities are found, or if all irregularities are rectified, the OLA renews the licence after collecting the licence fee.

2.5 An OLA internal management target requires that a licence should be renewed before expiration, provided that the renewal application is received not less than three months before expiration and the required documents are submitted at least three weeks before expiration (see Appendix B). According to the OLA, the expected time taken to complete the processing of a licence renewal application is two to three months.

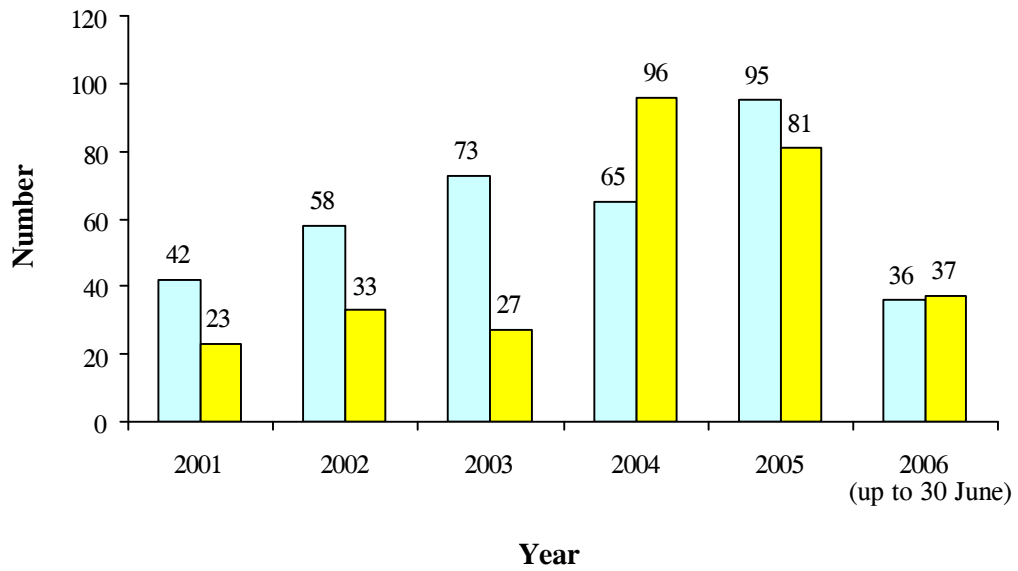
2.6 Since 21 December 2001, an applicant with good records (Note 2) can apply for a licence with a validity period of more than one year (up to seven years for a purpose-built hotel/guesthouse, and up to three years for other premises). The procedures for processing annual and multi-year licence applications are generally the same.

2.7 Figures 1 and 2 show, for the years 2001 to 2006 (up to 30 June 2006), the number of licence applications completed for new licence applications, and licence renewal applications, respectively.

Note 2: *An applicant is considered to have good records if he has been managing a hotel/guesthouse for the preceding 12 months and no licence conditions have been breached during that period.*

Figure 1

**New licence applications completed
(2001 – 2006)**

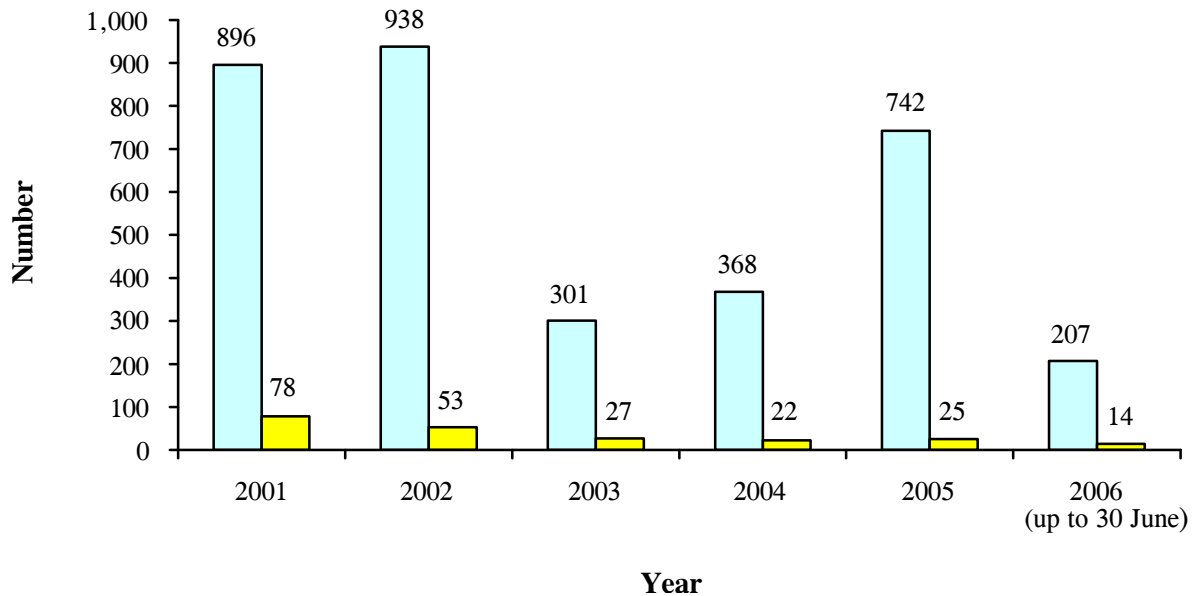


Legend: ■ New licences issued
■ Applications rejected/withdrawn

Source: *OLA records*

Figure 2

**Licence renewal applications completed
(2001 – 2006)**



Legend: ■ Renewed licences issued

■ Applications rejected/withdrawn

Source: OLA records and Audit analysis

Audit observations

Time span to complete processing licence applications

2.8 Table 1 shows the time span to complete processing (i.e. from the application date to the approval/rejection/withdrawal date) of licence applications in 2005-06.

Table 1
Time span to complete processing licence applications
(2005-06)

Time span (Number of days)	New licence applications (Number)	Licence renewal applications (Number)
0 to 60	40	231
61 to 90	7	191
91 to 120	4	149
121 to 180	26	56
181 to 360	76	23
361 to 540	29	1
541 to 720	3	—
721 to 930	1	—
Total	<u>186</u>	<u>651</u>

} 47 (25%)
 } 422 (65%)
 } 229 (35%)
 } 33 (18%)

Source: OLA records and Audit analysis

2.9 As shown in Table 1, in 2005-06, the processing of a considerable number of licence applications was completed within 90 days. However, some applications took a longer time. For example, 33 (18%) of the 186 new licence applications took more than 360 days. Of the 651 licence renewal applications, the complete processing of 229 (35%) took more than 90 days.

2.10 As it takes time for an applicant to complete all the improvement works to comply with the licensing requirements, the long time span to complete processing some of the applications (as shown in Table 1) should **not** entirely be attributed to the performance of the OLA. In September 2006, the HAD informed Audit that the OLA monitored its performance in processing licence applications mainly by reference to its internal management targets (see Appendix B). In this regard, the OLA is required to submit quarterly reports on the achievement of these internal management targets to the responsible Assistant Director of the HAD, and provide explanations for cases which have not met the targets.

2.11 According to the OLA, during the period 1 January 2005 to 30 June 2006, of the 178 new licence applications (excluding 59 applications which were withdrawn/rejected) in which the OLA had issued no objections in principle to the premises being used as a hotel/guesthouse, the target of having the OLA letter of upgrading requirements issued within 35 working days was met in 169 (95%) applications (Note 3). During the same period, for the 118 new licence applications of which all the requirements had been completed to the OLA's satisfaction, the target of having the licence issued within seven working days was met in all but one application.

Audit sample of licence applications examined

2.12 Audit selected a sample of 40 licence applications (hereinafter referred to as Sample A) to ascertain the reasons for the long time taken and whether there is room for improvement in processing licence applications. Sample A comprises:

- (a) 10 cases of new licence applications which had been outstanding for more than six months as at 31 March 2006;
- (b) 10 cases of new licence applications which took more than six months to complete processing in 2005-06;
- (c) 10 cases of licence renewal applications which had been outstanding for more than six months as at 31 March 2006; and
- (d) 10 cases of licence renewal applications which took more than two months to complete processing in 2005-06.

2.13 In the 20 new licence applications in Sample A (see para. 2.12(a) and (b) above), the OLA's internal management target of issuing the OLA letter of upgrading requirements within 35 working days was met in 18 cases. For the other two applications, the OLA informed Audit that both cases involved changes in use of the land, from non-domestic to domestic use. There were then discussions at the policy bureau level on how these cases should be handled. Hence, the OLA did not meet the said target in these two cases. Other audit findings on Sample A are reported in paragraphs 2.14 to 2.26.

Note 3: *Of the 9 (178 less 169) cases in which the target was not met, 5 cases involved delay in processing. Of the remaining 4 cases, 3 were related to premises located in the same building and the OLA suspected that the applications were split so as to avoid some additional safety requirements. The remaining case was also related to some existing licensed premises in the same building. Hence, the OLA had taken a longer time to review these 4 cases.*

2.14 Table 2 shows an analysis of the time span (Note 4) to complete the required improvement works in respect of 17 successful applications in Sample A.

Table 2
Time span to complete required improvement works
(30 June 2006)

Time span (Number of days)	Number of cases (Note)		
	Successful new licence applications	Successful licence renewal applications	Total
0 to 120	—	3	3
121 to 300	1	1	2
301 to 500	10	—	10
501 to 700	—	—	—
701 to 900	1	—	1
901 to 1,200	—	1	1
Total	12	5	17

Source: OLA records and Audit analysis

Note: This covers 17 successful applications in Sample A.

Completion of required improvement works

2.15 ***Need to ensure completion of improvement works.*** Audit noted that in four cases in Sample A, the OLA approved the licence renewal applications despite the fact that the required improvement works had not yet been completed. **The OLA needs to ensure that the required improvement works are completed before approving licence renewals.**

Note 4: *This refers to the time between the date of the OLA letter of upgrading requirements for new licence applications (see para. 2.2(c)) or the OLA warning letter for licence renewal applications (see para. 2.4(c)), and the work completion date.*

2.16 *Need to specify completion due date and monitor progress.* In five cases in Sample A, the completion due dates for the required improvement works were not specified in writing by the OLA. In another five cases, there were long periods (ranging from 6 to 15 months) during which no follow-up action was taken by the OLA. **Audit considers that the OLA needs to specify clearly the completion due date for improvement works, and to closely monitor the work progress.**

2.17 *Need to provide additional information about special requirements.* In 11 new licence applications in Sample A, the long time span to complete the improvement works was due to the unsatisfactory completion of work items. This required rectification by the applicants and re-inspections by the OLA. Of the 11 cases, 10 cases involved special requirements (e.g. removing solid walls or raised floor). **In Audit's view, to facilitate compliance, the OLA needs to consider ways of providing additional information to applicants about the requirements of improvement works, particularly special requirements.**

Review of long outstanding cases

2.18 Under the OLA's laid-down procedures, a Vetting Committee (chaired by the Chief Officer of the OLA) holds monthly meetings to review new licence applications which have not been finalised within 12 months from the date of application. In Sample A, Audit noted that one such new licence application had not been referred to the Vetting Committee. **The OLA needs to ensure that the said review requirement is complied with.**

2.19 Audit noted that 10 licence renewal applications in Sample A had been outstanding for more than 12 months. Of these 10 applications, two were eventually withdrawn by the applicants and one was rejected by the OLA. **In Audit's view, the OLA needs to consider introducing a review requirement, similar to that for new licence applications (see para. 2.18), for long outstanding licence renewal applications.**

Need to observe application deadline for licence renewal

2.20 Under section 9(1) of the HAGAO, applicants have to submit their renewal applications before the requisite deadline (i.e. not less than three months before the expiry date of the current licence). Under section 9(5) of the HAGAO, any licence in respect of which an application is made under section 9(1) shall remain in effect until the determination by the Licensing Authority of such application.

2.21 According to the OLA's laid-down procedures, the first reminder should be sent four months before the licence expiry date to remind licensees of the deadline for submitting renewal applications. However, Audit notes that in the reminder letters, nothing is mentioned of the consequence if a renewal application is not submitted on time. In 14 cases in Sample A, the OLA processed the renewal applications despite late submissions (i.e. the applicant not meeting the requisite deadline).

2.22 In response to the Director of Home Affairs' request for advice on a licence renewal application from a guesthouse, which was made on 27 August 2004, only four days before the expiration date of the licence on 31 August 2004, in March 2006 the Department of Justice (D of J) advised that:

- (a) section 9(1) of the HAGAO provided that an application for renewal of a licence was to be made **not less than three months before** the expiration of the licence;
- (b) as the application for renewal had not been submitted before the requisite deadline under section 9(1), the licence did not remain in effect under section 9(5) (see para. 2.20);
- (c) the Licensing Authority treated the application for renewal as having been made in accordance with section 9(1), and the licence having remained in effect since 1 September 2004. In doing so, the Licensing Authority acted outside his powers; and
- (d) the guesthouse had been operating without a licence since 1 September 2004 (Note 5).

2.23 **In Audit's view, the OLA needs to take action to ensure that applicants submit their licence renewal applications before the requisite deadline. In the light of the D of J's advice, the OLA needs to seek further legal advice as to whether:**

- (a) **the Licensing Authority is empowered to approve applications for licence renewal which are not submitted before the requisite deadline; and**
- (b) **the licences in respect of such renewal applications remain in effect until the determination by the Licensing Authority of such applications.**

Note 5: *In September 2006, the OLA was seeking further legal advice from the D of J. The licence of this guesthouse had not been renewed.*

2.24 Audit noted that, of the 634 licence renewal applications approved in 2005-06, 349 (55%) were submitted **after** the requisite deadline. **Audit considers that the OLA needs to, in the light of further legal advice, address issues arising from the validity of renewing such licences.**

Compliance with licensing requirements

2.25 Audit noted that, in 15 licence renewal applications in Sample A, the applicants did not comply with the OLA licensing requirements during the licence period. They took a long time to comply with the licensing requirements (e.g. restoring common escape routes to their original condition). Up to 30 June 2006, only 6 applicants succeeded in renewing their licences. The renewed licences were issued, on average, more than 6 months after the licence expiry date.

2.26 **In Audit's view, the OLA needs to ascertain whether licensees are complying with the licensing requirements during the licence period. The OLA may need to conduct more inspections during the licence period (see also para. 3.2).**

Audit recommendations

2.27 **Audit has recommended that the Director of Home Affairs should:**

Completion of required improvement works

- (a) **remind OLA staff to ensure that the required improvement works are completed before approving licence renewals;**
- (b) **specify in writing to applicants the due date for the completion of required improvement works;**
- (c) **take measures (e.g. regular site visits) to closely monitor the progress of improvement works;**
- (d) **consider ways of providing additional information to applicants about the requirements of improvement works to facilitate compliance (e.g. setting out the requirements in a checklist, providing detailed specifications on special requirements, and arranging on-site briefings by OLA staff);**

Review of long outstanding cases

- (e) ensure that the requirement of referring all long outstanding new licence applications to the Vetting Committee for review is complied with;
- (f) consider including long outstanding licence renewal applications in the review by the Vetting Committee;

Need to observe application deadline for licence renewal

- (g) take action to ensure that applicants submit their licence renewal applications before the requisite deadline under section 9(1) of the HAGAO;
- (h) seek further legal advice as to whether:
 - the Licensing Authority has the power to approve applications for licence renewal which are not submitted before the requisite deadline; and
 - the licences in respect of such renewal applications remain in effect until the determination by the Licensing Authority of such applications;
- (i) in the light of further legal advice:
 - take necessary action to address issues arising from the validity of renewing the licences granted in respect of renewal applications not submitted before the requisite deadline; and
 - inform licensees of the consequence of not submitting renewal applications before the requisite deadline; and

Compliance with licensing requirements

- (j) take necessary measures to ascertain whether licensees are complying with the licensing requirements during the licence period. These may include, for example, conducting more inspections during the licence period.

Response from the Administration

2.28 The **Director of Home Affairs** generally agrees with the audit recommendations. She accepts that there is room for improvement in the HAD's licensing work and she will make improvement taking into account Audit's recommendations. She has said that the HAD has implemented the following improvement measures with immediate effect:

- (a) since March 2004, the OLA has stated in all letters of requirements issued to new licence applicants that they should complete the required works within four months. It would be, however, unrealistic to expect a five-star hotel to complete all works within the four-month period. The OLA will therefore revise its letters of requirements so that hotels will be required to complete all required works within one year, while other premises (e.g. guesthouses and holiday flats) will be required to complete all required works within four months. The OLA will visit all premises (both hotels and non-hotels) in four months' time after the date of the letter of requirements to monitor work progress. For premises which are required to complete the works within four months, the OLA will consider granting an extension of time to the applicant after the four-month period only if the upgrading works are in good progress. If the works are not in good progress, the OLA will consider rejecting the application. The same applies to hotels which are required to complete the works within a year. An extension of time will be granted only if the OLA is satisfied with the progress of works;
- (b) in order to closely monitor outstanding cases, the OLA will ensure that all new licence applications not finalised within 12 months from the date of application are submitted to the Vetting Committee chaired by the Chief Officer of the OLA, for review. A report of the Vetting Committee has, since November 2005, been submitted to the responsible Assistant Director of the HAD on a monthly basis. To further step up the HAD's monitoring role, all cases that do not meet the requirement of completing the works within the stipulated time-frame will be submitted to the responsible Assistant Director for discussion at monthly meetings with the OLA. Similarly, cases not meeting the internal management targets will also be submitted to the responsible Assistant Director for discussion at monthly meetings with the OLA;
- (c) in order to facilitate compliance by the applicants, apart from explaining the requirements to applicants on site, a follow-up letter setting out the requirements will be issued to the applicants after every inspection. The OLA staff have been reminded to strictly adopt a consistent approach in terms of technical requirements for all applications. Moreover, the telephone number of the OLA case officer is included in the correspondence and applicants may contact the subject officer direct for clarification;

- (d) to further improve its planning and monitoring process, the OLA is working on a computer system to track the progress of all new licence applications and renewal applications. The system will be modelled on the Enforcement Management Information System (EMIS) already implemented in the Enforcement Unit of the OLA;
- (e) under section 9(1) of the HAGAO, applicants have to submit their renewal applications not less than three months before the expiry date of the current licence. The OLA is seeking legal advice as to whether the OLA has the power to approve applications for licence renewal which are not submitted before the requisite deadline and whether the licences in respect of such renewal applications remain in effect until the determination by the OLA of such applications. In order to remind applicants to submit their licence renewal applications in a timely manner, the HAD will, in consultation with the D of J, revise the approval letter when the licence is first issued and the reminder sent to licensees four months before the licence expiry date, to include the consequence of not submitting licence renewal applications according to section 9(1) of the HAGAO;
- (f) in order to improve the monitoring of licensees' continuous compliance with the licensing requirements during the licence period (see para. 2.26), the FSU of the OLA will, apart from conducting at least one inspection each year to ensure compliance with all fire safety licensing requirements and obtaining updated safety and maintenance certificates (see para. 3.2), carry out further inspections and take follow-up action should irregularities persist; and
- (g) for a licence renewal application where irregularities have been found during the renewal inspections, after the licensee has rectified all the irregularities to the OLA's satisfaction and has the licence renewed, the OLA (both the BSU and the FSU) will step up the monitoring work by conducting compliance inspections of the premises during the licence period.

PART 3: ENFORCEMENT OF LICENSING REQUIREMENTS

3.1 This PART examines the efforts made by the OLA to enforce the licensing requirements for hotel and guesthouse accommodation.

Inspection of licensed establishments

3.2 Annually, the FSU conducts inspections of all licensed premises to ensure that the required fire services installations are properly maintained. The BSU also conducts each year renewal inspections of the premises holding annual licences, and compliance inspections of about 20% of the premises holding multi-year licences.

3.3 For all licences with a licence period exceeding three years (e.g. hotels holding four-year to seven-year licences), the licensee is required to appoint an Authorised Person to submit an annual certificate to the OLA to confirm that there is no substantial alteration to the premises, that the licensee has not contravened any licence conditions, and that the premises are in safe condition.

Audit observations

3.4 To ascertain whether there is room for improvement in the OLA's enforcement procedures, particularly in relation to establishments with multi-year licences, Audit selected nine cases (Note 6) for examination. Audit found that:

- (a) in five of the nine selected cases, although they had been scheduled for BSU inspections, no records of BSU inspections could be found in the case files; and
- (b) of the remaining four cases with records of BSU inspections:
 - (i) in three cases, the inspections were not reported in accordance with the standard inspection checklist which requires the reporting of all aspects of building and fire safety; and
 - (ii) in one case, the inspection was not conducted within the OLA's planned inspection schedule.

Note 6: *The audit sample comprises: (a) three cases randomly selected from establishments with two-year or three-year licences scheduled for inspection; and (b) all of the six establishments with seven-year licences scheduled for inspection.*

Audit recommendations

- 3.5 **Audit has recommended that the Director of Home Affairs should:**
- (a) **put in place monitoring procedures to improve control over the inspection of establishments with multi-year licences; and**
 - (b) **ensure that OLA staff carry out and report the results of inspections for establishments with multi-year licences in accordance with the standard inspection checklist and the planned inspection schedule.**

Response from the Administration

3.6 The **Director of Home Affairs** generally agrees with the audit recommendations. She has said that, although no BSU inspections were conducted for the five selected cases mentioned in paragraph 3.4(a), the FSU of the OLA had conducted annual inspections of all these premises.

Hotels and holiday camps holding scheduled licences

Hotels holding scheduled licences

3.7 As from 1 September 1993, hotels were required to obtain licences under the HAGAO. For those hotels which were not able to meet the full licensing requirements, they had been issued, since September 1993, with licences to which a schedule of works was attached. The schedule specified the building and fire safety improvement works which the hotel operator had to complete within a specified period. These licences are referred to as **scheduled licences** and hotels holding such licences as **scheduled hotels**.

Arrangements for completion of improvement works

3.8 Initially, the Secretary for Home Affairs set the target completion date of improvement works for scheduled hotels at the year 2000. In June 1998, after consultation with the hotel operators, the Secretary for Home Affairs agreed to revise the target completion date to August 2002.

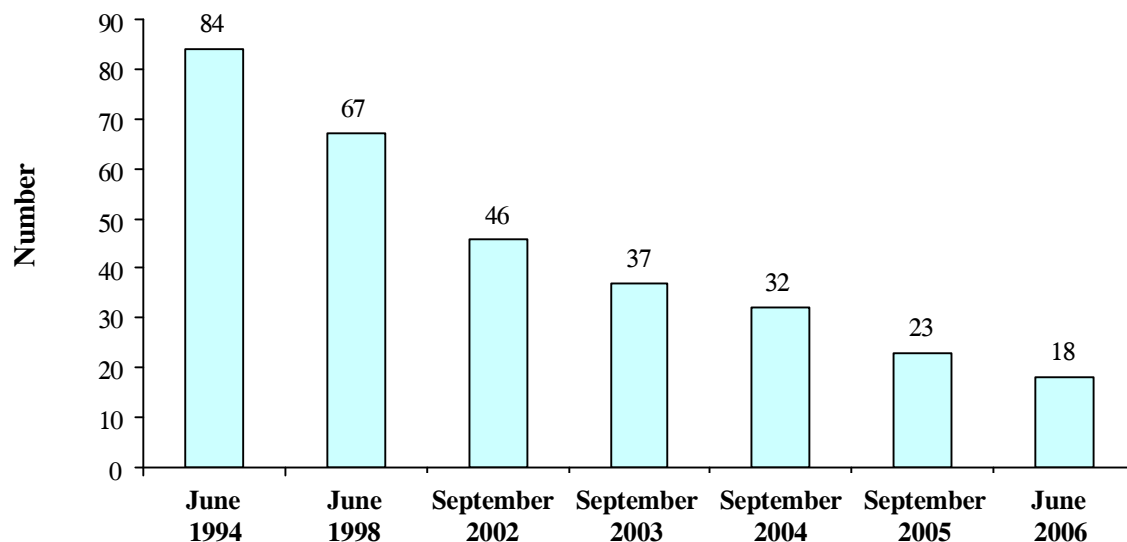
3.9 In August 2002, the Director of Home Affairs advised the Secretary for Home Affairs that 46 scheduled hotels had not completed the improvement works. According to the Director of Home Affairs, the major outstanding work item of these hotels was to meet the fire safety requirements in respect of ventilation systems. In the same month, after further consultation with the hotel operators, the Secretary for Home Affairs approved that the scheduled licences of the 46 hotels be renewed for another year (i.e. to expire in September 2003).

3.10 To facilitate the early completion of outstanding works, the OLA liaised with each scheduled hotel to agree on a works programme to be completed by a specified date. Each scheduled hotel had to strictly adhere to the works programme. To monitor works progress, the OLA required the hotel operators to submit bi-monthly works programmes and quarterly progress reports. This requirement was specified in the scheduled licences for compliance.

3.11 With the completion of the required improvement works, the number of scheduled hotels decreased from 84 in June 1994 to 18 in June 2006. Details are shown in Figure 3.

Figure 3

Hotels holding scheduled licences



Source: OLA records

Holiday camps holding scheduled licences

3.12 In addition, as at June 2006, two holiday camps were holding scheduled licences. They have been required to complete building and fire safety improvement works within the target completion dates specified in the licences.

Audit observations

3.13 As at June 2006, there were still 18 hotels and 2 holiday camps holding scheduled licences. To ascertain whether there is room for improving the process, Audit selected the OLA records of five scheduled hotels and two holiday camps (hereinafter referred to as Hotels A to E, and Holiday Camps X and Y, respectively) for examination. The audit findings are reported in paragraphs 3.14 to 3.19.

Need to specify realistic completion dates for improvement works

3.14 According to the OLA, the complexity of improvement works and the time required for their completion varied among those establishments holding scheduled licences. The OLA would, therefore, liaise with each scheduled licensee to agree on a works programme for completion by a certain date. However, Audit noted that, in all the hotels and holiday camps examined, the target completion date of works specified in the scheduled licence was not the expected completion date as shown in the agreed works programme. The OLA's practice was to dovetail the target completion date of the works with the licence expiry date. If the required works were not completed by the licence expiry date, the target completion date of works would be set at the next licence expiry date and the scheduled licence would still be renewed for another year.

3.15 **In Audit's view, the OLA needs to assess, in consultation with the scheduled licensees, the time-frame required for the completion of the required improvement works to ensure that the target completion dates, as specified in the scheduled licences, are realistic.**

Need to closely monitor progress of outstanding works

3.16 As mentioned in paragraph 3.10, scheduled hotels were required to submit to the OLA bi-monthly works programmes and quarterly progress reports. Since September 2003, the OLA has submitted quarterly progress reports on all scheduled hotels to the HAD senior management for discussion at regular monthly meetings.

3.17 Audit however noted that the scheduled hotels submitted their works programmes and progress reports at irregular intervals (and often with substantial delay) and in different formats showing varying work details. **Audit considers that the OLA needs to ensure that the scheduled licensees submit works programmes and progress reports in accordance with the agreed time interval (para. 3.16) and in a standard format.**

Follow-up action on delays

3.18 Audit noted that the main line of action taken by the OLA to expedite the completion of the required improvement works was by means of issuing warning letters. Table 3 shows an analysis of the warning letters issued during the period September 2002 to June 2006.

Table 3
Warning letters issued to seven scheduled licensees
(September 2002 – June 2006)

Scheduled licensee (Note)	Warning letters issued (Number)
Hotel A	1
Hotel B	2
Hotel C	1
Hotel D	4
Hotel E	1
Holiday Camp X	3
Holiday Camp Y	—

Source: OLA records

Note: This refers to the seven establishments selected for audit examination (see para. 3.13).

3.19 **In Audit's view, in addition to the issue of warning letters, the OLA needs to take more proactive and vigorous measures, including enforcement measures provided under the HAGAO (e.g. prosecution action), to ensure that scheduled licensees complete the improvement works as early as possible.**

Latest development

3.20 According to the works programmes as at June 2006, of the 18 scheduled hotels, 16 were expected to finish their scheduled works and obtain full licences by the end of 2006. The remaining two scheduled hotels would finish their works by mid-2007. With regard to the two holiday camps holding scheduled licences, the outstanding works were scheduled to be completed by the end of 2006.

Audit recommendations

3.21 To ensure that the remaining 20 establishments holding scheduled licences can meet the full licensing requirements as early as possible, Audit has *recommended* that the Director of Home Affairs should:

Need to specify realistic completion dates for improvement works

- (a) in consultation with the scheduled licensees, review the target completion dates of the required improvement works as specified in the scheduled licences to ensure that they are realistic;

Need to closely monitor progress of outstanding works

- (b) take measures to closely monitor the progress of outstanding works. These include requiring the scheduled licensees to submit works programmes and progress reports in accordance with the agreed time interval and in a standard format; and

Follow-up action on delays

- (c) take more proactive remedial measures in a timely manner if problems are identified. These include:
 - (i) holding discussions with the scheduled licensees to resolve any difficulties in meeting the licensing requirements; and
 - (ii) in addition to warning letters, considering using other enforcement measures provided under the HAGAO (e.g. prosecution action).

Response from the Administration

3.22 The Director of Home Affairs generally agrees with the audit recommendations. She has said that:

- (a) of the 18 hotels still holding scheduled licences, four have already passed the ventilation inspection and could be deleted from the list of scheduled hotels once all documentation procedures are cleared. As regards the two holiday camps holding scheduled licences, the improvement works of one have been completed and can be deleted from the list once all documentation procedures are cleared whereas the improvement works of the other would be completed by end 2006;

- (b) the HAD noted that in the past, there were some delays for scheduled hotels in carrying out the improvement works. In order to make the operators of these hotels expedite action in completing the required improvement works, during the period between January 2004 and June 2006, the OLA had conducted a total of 220 visits and issued a total of 21 warnings to the 14 remaining scheduled hotels (excluding the four that can be deleted in the near future as mentioned in (a) above);
- (c) to facilitate the monitoring work, the OLA requires all scheduled hotels to submit quarterly progress reports on the works programmes (see para. 3.10). The OLA will ensure that the submission of progress reports is made in strict accordance with the agreed timing and in the required format;
- (d) the OLA will continue to hold regular discussions with scheduled licensees to resolve any difficulties in complying with the licensing requirements and to ensure that the completion dates of the required improvement works are realistic. The OLA had already sent out in early September 2006 invitation letters to the scheduled hotels inviting them to a liaison meeting. This will establish a platform for all concerned to exchange their views and identify feasible solutions to problems encountered;
- (e) in order to assist the scheduled licensees to complete their scheduled works and obtain a full licence as soon as possible, agreement has been made between the OLA and the Ventilation Division of the FSD to implement a series of new measures with immediate effect. These include establishing a “case officer” system in the Ventilation Division of the FSD whereby a case officer will be responsible for inspection of all scheduled hotels;
- (f) in the past, scheduled licensees were required to report to the Ventilation Division of the FSD direct for inspection upon completion of the ventilating system upgrading works. In order to improve communication and monitoring, with immediate effect, the FSU of the OLA will be the single point of contact. Scheduled licensees will be asked to send all correspondence to the OLA for processing; and
- (g) in addition to the issue of warning letters to the scheduled hotels, the OLA will consider taking more proactive measures provided under the HAGAO.

PART 4: ENFORCEMENT ACTION AGAINST UNLICENSED ESTABLISHMENTS

4.1 This PART examines the enforcement action taken by the OLA against unlicensed hotel and guesthouse establishments (hereinafter referred to as unlicensed establishments).

Identification of suspected unlicensed establishments

4.2 The Enforcement Unit of the OLA is responsible for taking enforcement action against unlicensed establishments. The Enforcement Unit obtains information about suspected unlicensed establishments from the following sources:

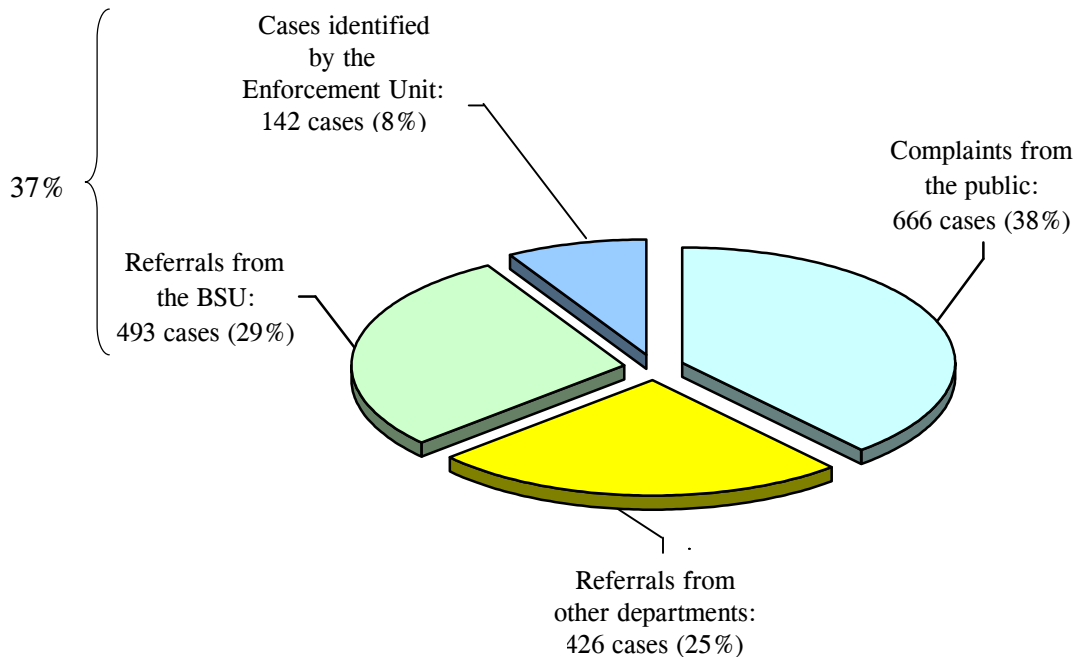
- (a) ***Complaints from the public.*** These include verbal complaints (e.g. telephone or in person) and written complaints (e.g. e-mails or letters);
- (b) ***Referrals from other government departments.*** These include referrals from the Buildings Department and the FSD of suspected cases which they come across during their inspections;
- (c) ***Referrals from the BSU.*** The BSU refers suspected cases to the Enforcement Unit if: (i) a licence application has been rejected or withdrawn; (ii) a licence has not been renewed; and (iii) a licensed establishment has ceased operation; and
- (d) ***Cases identified by the Enforcement Unit.*** These include cases identified by field surveillance and from a search of newspaper advertisements, and cases of past prosecutions against unlicensed establishments.

4.3 If a case merits further action, a case file is opened and a Building Surveyor of the Enforcement Unit will be in charge of the case and take necessary enforcement action.

Audit observations

4.4 Figure 4 shows an audit analysis of suspected cases of unlicensed establishments by source of referral, for the period January 2001 to June 2006. It shows that suspected cases identified by the OLA (i.e. Enforcement Unit and BSU) accounted for 37% of the total number of suspected cases identified.

Figure 4
Sources of referral of 1,727 suspected cases of unlicensed establishments
(January 2001 – June 2006)



Source: OLA records and Audit analysis

4.5 With the increasing demand for guesthouses by Mainland visitors after the introduction of the Individual Visit Scheme (Note 7) in July 2003, the OLA has made efforts to promote licensed guesthouses, and has taken more enforcement action against unlicensed guesthouses (e.g. by warning letters and prosecution — see Table 4 in para. 4.10). Audit considers it necessary for the OLA to continue stepping up the Enforcement Unit’s efforts in the following areas with a view to identifying suspected unlicensed establishments for enforcement action:

Note 7: *The Individual Visit Scheme allows travellers from the Mainland to visit Hong Kong on an individual basis. As at May 2006, the Individual Visit Scheme covered 220 million Mainland residents in 44 cities.*

- (a) *Need to adopt a more proactive approach.* **Audit considers that the Enforcement Unit needs to put in place a proactive system to identify unlicensed establishments for enforcement action.** In planning the tasks to be carried out, the system should take into account seasonal factors (such as long holidays) and location (such as proximity to tourist attractions);
- (b) *Need to conduct more field surveillance operations.* Field surveillance is an effective way to identify unlicensed establishments, especially for districts with a large number of establishments. The OLA informed Audit that, from time to time, the Enforcement Unit had carried out field surveillance operations. For example, in March and April 2006, the Enforcement Unit conducted two field surveillance operations in Mong Kok in which six suspected unlicensed establishments were identified. **Audit considers that the Enforcement Unit needs to consider increasing the frequency and the coverage of such field surveillance operations;** and
- (c) *Need to expand the scope of media search.* At present, the Enforcement Unit searches for suspected unlicensed establishments mainly by reference to guesthouse advertisements published in one local Chinese newspaper. **Audit considers that there is a need for the Enforcement Unit to expand the scope of media search.** Nowadays, information on hotels and guesthouses is available on the Internet, including details of tourist accommodation in Hong Kong. For example, in August 2006 Audit downloaded from a website information about 283 guesthouses located in the Yau Tsim Mong District. Among these guesthouses, 34 (12%) could not be found in the database of licensed establishments of the OLA. **Audit considers that the Enforcement Unit needs to make full use of the Internet to locate suspected unlicensed establishments.**

Audit recommendations

- 4.6 **Audit has recommended that the Director of Home Affairs should:**
- (a) **put in place a proactive system in the Enforcement Unit for identification of unlicensed establishments;**
 - (b) **increase the frequency and coverage of the Enforcement Unit's field surveillance operations; and**
 - (c) **expand the scope (including making full use of the Internet) of media search for hotels and guesthouses to help identify suspected unlicensed establishments in the territory.**

Response from the Administration

4.7 The **Director of Home Affairs** generally agrees with the audit recommendations, including increasing the frequency and the coverage of field surveillance operations. She has said that:

- (a) the Enforcement Unit of the OLA has initiated many enforcement actions in recent years. These include large-scale operations against unlicensed guesthouses conducted in association with the Hong Kong Police Force in various districts, planned surveys against some black spots and field surveillance operations looking for new target premises. During each operation, tens to hundreds of target premises were raided;
- (b) the Enforcement Unit has taken into account the seasonal factor in working out the details of its inspections of holiday flats. Saturday night patrols are more frequent in summer holidays and large-scale operations are always held ahead of major holidays, such as the “Golden Weeks”;
- (c) to facilitate the reporting of suspected unlicensed establishments, a proforma has been devised to facilitate the general public to report unlicensed premises. Report forms have been issued to all District Councils inviting District Councillors to report to the OLA if they are aware of any suspected unlicensed premises; and
- (d) at present, an officer of the OLA has been tasked to search for advertisements on guesthouses from newspapers on a daily basis. He has been assigned to conduct regular Internet search for suspected unlicensed premises with immediate effect.

Enforcement action against suspected unlicensed establishments

4.8 To help monitor the progress of enforcement action against suspected unlicensed establishments, the OLA has drawn up in 2003 the “Procedural Guidelines on Conducting Policing Inspection and Particulars for Prosecution Inspection for Suspected Unlicensed Operations”. Upon the opening of a case file on a suspected unlicensed establishment, the following enforcement action is taken:

- (a) ***Preliminary inspections.*** A team comprising normally two Licensing Inspectors conducts one or more preliminary inspections (also called policing inspections) at the premises concerned to ascertain whether there is evidence, prima facie, that an unlicensed establishment is in operation. If there is such evidence and the operator has not been warned before, the Enforcement Unit issues a warning letter to the operator requiring him to cease operation and to apply for a licence if he still wants to carry on business. If the operator has been warned before, the Enforcement Unit will not issue a warning letter but will proceed to conduct in-depth inspections;

- (b) ***In-depth inspections.*** If an unlicensed establishment is still in operation after being warned, a team comprising normally three Licensing Inspectors conducts in-depth inspections (also called particulars for prosecution inspections) to collect evidence for prosecution; and
- (c) ***Prosecution action.*** The Enforcement Unit prepares an investigation report and sends it to the D of J. Upon receiving D of J's advice that the evidence collected is sufficient, the Enforcement Unit instigates prosecution under the HAGAO by applying for a summons.

4.9 The Enforcement Unit operates a computer system, the EMIS, for managing and processing suspected cases of unlicensed establishments. For each case, the system records information about the unlicensed establishment (e.g. its name and address), the enforcement action taken, and the up-to-date status of the case (i.e. preliminary inspection, in-depth inspection or prosecution).

Workload of the Enforcement Unit

4.10 Table 4 shows the workload of the Enforcement Unit during the years 2001 to 2006 (up to 30 June 2006).

Table 4
Action taken by the Enforcement Unit
(2001 – 2006)

Year	New cases of suspected unlicensed establishments (Number)	Preliminary and in-depth inspections (Number)	Warning letters (Number)	Prosecution cases (Number)
2001	118	227	47	—
2002	194	454	60	—
2003	501	753	61	2
2004	324	1,509	85	24
2005	383	1,102	100	14
2006 (up to 30 June)	207	807	60	16
Total	1,727	4,852	413	56

Source: OLA records

Audit observations

Time span to complete action on suspected unlicensed establishments

4.11 Table 5 shows that, on average, it took 268 days to complete action (Note 8) in respect of suspected unlicensed establishments in the years 2001 to 2006 (up to 30 June). Table 6 shows that in 343 cases (19% of 1,842), the time span was more than 500 days.

Table 5
Average time span to complete action
in respect of suspected unlicensed establishments
(2001 – 2006)

Year	Average time span (Number of days)
2001	391
2002	389
2003	497
2004	253
2005	261
2006 (up to 30 June)	171
Overall	268

Source: OLA records and Audit analysis

Note 8: *The time span to complete action on a case is counted from the date of receiving the case to the date of closing it when enforcement action (see para. 4.8) ceased.*

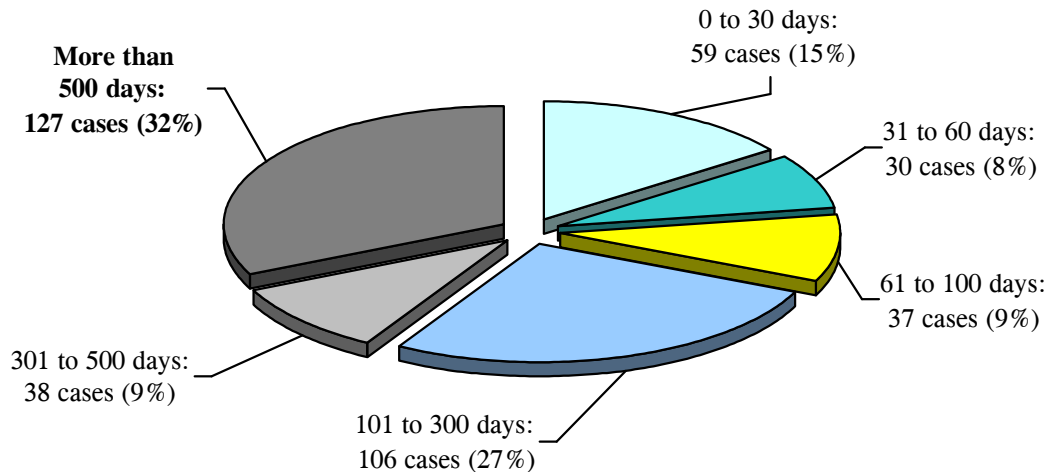
Table 6
Time span to complete action
in respect of suspected unlicensed establishments
(2001 – 2006)

Time span (Number of days)	Number of cases (Note)	Percentage
0 to 30	738	40%
31 to 60	5	1%
61 to 100	112	6%
101 to 300	415	22%
301 to 500	229	12%
More than 500	343	19%
Total	1,842	100%

Source: OLA records and Audit analysis

Note: This covers cases of suspected unlicensed establishments with action completed in the years 2001 to 2006 (up to 30 June).

4.12 Figure 5 shows an ageing analysis of 397 cases of suspected unlicensed establishments (unlicensed guesthouses and holiday flats) under action as at 30 June 2006. **They had been under action, on average, for 366 days, with 127 cases (32%) under action for more than 500 days.**

Figure 5**Ageing analysis of 397 cases of suspected unlicensed establishments under action
(30 June 2006)**

Source: OLA records and Audit analysis

Audit sample of suspected unlicensed establishments examined

4.13 Audit reviewed a selected sample of 40 cases of suspected unlicensed establishments (hereinafter referred to as Sample B) to ascertain whether there is room for improvement in taking enforcement action. Sample B comprised:

- (a) 20 cases randomly selected from cases under action as at 31 March 2006;
- (b) 10 cases randomly selected from cases completed in 2005-06; and
- (c) 10 cases randomly selected from the prosecution action cases of 2003-04 to 2005-06.

The audit findings are reported in paragraphs 4.14 to 4.29.

Delay in commencing enforcement action

4.14 Enforcement action on suspected unlicensed establishments is preceded by preliminary inspections. The time interval between the date of receiving a referral case, and the date of the first preliminary inspection by the Enforcement Unit for the cases in

Sample B is shown in Table 7. **Audit noted that in three cases, the elapsed time was more than 100 days.**

Table 7

Time elapsed before conducting the first preliminary inspection

Time elapsed (Number of days)	Number of cases (Note)
0 to 10	21
11 to 20	5
21 to 40	3
41 to 100	1
101 to 700	3
Total	33

Source: OLA records and Audit analysis

Note: This covers 33 cases referred to the Enforcement Unit in Sample B, excluding 7 cases identified by the Enforcement Unit itself.

4.15 There were 13 complaint cases (see para. 4.2(a)) in Sample B. For complaint cases, according to the OLA’s own requirements, the first preliminary inspection has to be conducted within nine working days of receiving the complaint. This requirement had been met for all the 13 complaint cases.

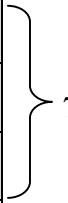
4.16 For cases referred to the Enforcement Unit by the BSU and other departments (see para. 4.2(b) and (c)), according to the OLA’s own requirements, the first preliminary inspection has to be conducted within 30 working days. Audit noted that for cases referred by the BSU in Sample B, there were 3 cases in which the Enforcement Unit conducted the first preliminary inspection more than 100 days after receiving the case. In one of these cases, the Enforcement Unit conducted the first preliminary inspection 647 days after receiving the case.

Long time span to complete preliminary inspections

4.17 Table 8 shows an analysis of the time span to complete the preliminary inspections for the cases in Sample B.

Table 8
Time span to complete preliminary inspections

Time span (Number of days)	Number of cases (Note)
0 to 100	24
101 to 200	4
201 to 300	2
301 to 400	1
401 to 1,400	4
Total	35



Source: OLA records and Audit analysis

Note: This covers 35 cases in Sample B for which preliminary inspections had been completed as at 30 June 2006.

4.18 As shown in Table 8, there were seven cases which took more than 200 days for completing preliminary inspections. For these seven cases, more than one preliminary inspection was required, and the inspections were generally not conducted in a timely manner. For example, in one case, there was a long time lag of 225 days between the third and the fourth inspections. In another case, a warning letter was issued 153 days after the third preliminary inspection.

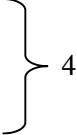
Long time span to complete in-depth inspections

4.19 Table 9 shows an analysis of the time span to complete the in-depth inspections for the cases in Sample B.

Table 9

Time span for the Enforcement Unit to complete in-depth inspections

Time span (Number of days)	Number of cases (Note)
0 to 100	4
101 to 200	4
201 to 300	1
301 to 400	3
401 to 900	1
Total	13



Source: OLA records and Audit analysis

Note: This covers 13 cases in Sample B for which in-depth inspections had been completed as at 30 June 2006.

4.20 As shown in Table 9, in four cases, the Enforcement Unit took more than 300 days to complete the in-depth inspections. These in-depth inspections were generally not conducted in a timely manner.

Need to closely monitor the progress of enforcement action

4.21 In view of the long time span to complete the action on suspected unlicensed establishments (see paras. 4.11 to 4.20), Audit considers that the OLA needs to closely monitor the progress of enforcement action in each case.

Need to maintain accurate and up-to-date enforcement records

4.22 Audit noted that the case status and the last action date of cases were not properly recorded in the EMIS. Of the 20 cases still under action in Sample B (see para. 4.13(a)), the case status and the last action date of 10 cases were not updated in a timely matter. **The OLA needs to maintain accurate and up-to-date records in its computer system.**

Need to provide management information on a regular basis

4.23 The EMIS provides useful information for planning, directing and monitoring enforcement action against suspected unlicensed establishments. Such information includes, for example, the number of cases under action, the results of enforcement action taken, and analyses of outstanding cases by age and by case status. However, Audit notes that such information is not provided to the management of the OLA on a regular basis. **The OLA needs to make better use of the EMIS to provide relevant information to the senior management.**

Need to conduct inspections at appropriate times

4.24 According to a standing instruction of the OLA, inspections of suspected unlicensed establishments should initially be conducted during normal office hours. If initial inspections are not successful, further inspections should be conducted at a time of the day which coincides with the mode of operation of the establishment's business (e.g. for unlicensed guesthouses, inspections should be conducted at night).

4.25 In practice, for unlicensed holiday flats, inspections are mainly conducted on Saturdays. However, for unlicensed guesthouses, Audit noted seven cases (22% of the 32 cases of unlicensed guesthouses in Sample B) in which further inspections were not conducted at night as required by the said OLA standing instruction. **Audit considers that the OLA needs to ensure that inspections are conducted at times when there is business operation inside the suspected unlicensed establishments.**

Need to devise guidelines for invoking sections 19(1) and 20(1)

4.26 Section 19(1) of the HAGAO provides that the Secretary for Home Affairs may, in respect of any hotel or any guesthouse, give such directions in writing to ensure that:

- (a) the safety of guests in the hotel or the guesthouse is promoted in a proper manner;
- (b) adequate apparatus and equipment required as safeguards against fire or other hazard are provided in the hotel or the guesthouse; and
- (c) the provisions of the HAGAO are complied with.

4.27 Section 20(1) of the HAGAO further provides that the District Court shall make an order in writing directing that a hotel or a guesthouse shall close and shall cease to be used as a hotel or a guesthouse, where it is proved to the satisfaction of the District Court on the information submitted by the Secretary for Home Affairs that:

- (a) there is any danger or risk of danger to guests in the hotel or the guesthouse; or
- (b) the requirements of a direction given under section 19(1) of the HAGAO have not been complied with.

4.28 In response to Audit's enquiry, in June 2006, the OLA advised that, in its enforcement action against unlicensed establishments:

- (a) the OLA had not invoked section 19(1) or section 20(1) of the HAGAO before; and
- (b) the OLA would consider invoking section 20(1) only when the premises of an unlicensed establishment posed imminent danger.

4.29 In Audit's view, the Secretary for Home Affairs' directions under section 19(1) and the closure order under section 20(1) of the HAGAO are effective means of enforcement against unlicensed establishments. The OLA needs to make use of these provisions, especially in handling the recalcitrant cases. **The OLA needs to consider drawing up guidelines, in consultation with the D of J, to set out the circumstances under which the OLA would invoke sections 19(1) and 20(1) of the HAGAO. To enhance the deterrent effect, the OLA also needs to consider mentioning in the standard warning letter the powers of the Secretary under the above provisions.**

Audit recommendations

4.30 **Audit has recommended that the Director of Home Affairs should:**

Need to closely monitor the progress of enforcement action

- (a) **closely monitor the action of the Enforcement Unit with a view to ensuring that there is no undue delay;**

Need to maintain accurate and up-to-date enforcement records

- (b) ensure that the EMIS is updated in a timely manner to monitor the progress of enforcement action taken against unlicensed establishments;

Need to provide management information on a regular basis

- (c) make use of the EMIS to provide relevant information to the senior management of the OLA (e.g. regular reporting of the status of outstanding cases and results of enforcement action);

Need to conduct inspections at appropriate times

- (d) ensure that inspections are conducted at times when there is business operation inside suspected unlicensed establishments;

Need to devise guidelines for invoking sections 19(1) and 20(1)

- (e) consider drawing up guidelines, in consultation with the D of J, that set out the circumstances under which the OLA would invoke sections 19(1) and 20(1) of the HAGAO; and
- (f) to enhance the deterrent effect, consider mentioning in the standard warning letter the powers of the Secretary for Home Affairs under sections 19(1) and 20(1) of the HAGAO.

Response from the Administration

4.31 The **Director of Home Affairs** generally agrees with the audit recommendations. She accepts that there is room for improvement in the OLA's enforcement work and the HAD will take the audit recommendations into account. She has said that:

- (a) the time taken to complete action against a suspected unlicensed establishment very often depends on the time taken to go through due process of law, which is beyond the control of the OLA. It depends on a number of factors. For some cases, the file could be closed relatively quickly, e.g. cases involving unlicensed establishments which immediately ceased operation upon receipt of warning letters issued by the OLA. Cases involving establishments that were subsequently found out to be let on a monthly rental basis (and hence outside the control of the HAGAO) could also be closed immediately. However, there are

many cases which require a few preliminary inspections (e.g. the premises may be inaccessible during the first few inspections), a few decoy operations, detailed discussions with the D of J, etc. The fixing of a trial hearing date is also beyond the OLA's control and may take a few months;

- (b) in recent years, the Enforcement Unit has made great efforts to complete action on suspected unlicensed establishments. Some of the improvements in the Enforcement Unit's performance in its enforcement work against suspected unlicensed establishments are shown at Appendix C;
- (c) at present, cases which fail to meet the OLA's own management targets for a preliminary inspection are submitted to the responsible Assistant Director on a quarterly basis. To step up the HAD's efforts in monitoring enforcement action, the frequency of submission will be changed to monthly;
- (d) the EMIS has been a great tool to assist the Enforcement Unit in monitoring the progress of all enforcement cases. As the EMIS was only introduced in early 2006, there might be some delays in updating the information. The HAD staff have been advised to update the relevant computer records normally within five working days of their respective action. The case summary available from the EMIS will be circulated to the management of the OLA for monitoring purposes on a monthly basis; and
- (e) the OLA will, in consultation with the D of J, draw up guidelines to set out the circumstances under which the OLA should invoke sections 19(1) and 20(1) of the HAGAO, and include the direction and closure order provisions in the standard warning letters issued to operators of suspected unlicensed establishments.

PART 5: COST RECOVERY

5.1 This PART examines the recovery of cost incurred by the OLA for the issue of new licences, renewed licences, and transferred licences.

Fees payable upon issue of licences

5.2 In accordance with the Hotel and Guesthouse Accommodation (Fees) Regulations (Cap. 349B), the fee currently payable upon issue of a licence ranges from \$3,970 to \$118,800 for new licence, and \$2,590 to \$61,250 for renewed licence. The fee payable for transferring a licence is \$140 (see para. 5.15). In 2005-06, the revenue collected by the OLA under the HAGAO was \$8.6 million.

5.3 According to Financial Circular No. 10/99 dated 28 September 1999, fees charged by the Government should in general be set at levels adequate to recover the full cost of providing the goods or services. In determining the level of fee increase, the guidelines of the Financial Services and the Treasury Bureau (FSTB) issued in April 2000 have to be followed (Note 9).

Determination of licence fees

Fee structure

5.4 When the HAGAO was enacted in 1991, the Hotel and Guesthouse Accommodation (Fees) Regulations only provided one scale of fees for the issue of annual licences. In 1998, the HAGAO was amended to provide for the issue of licences with a validity period of up to seven years. At present, the fee structure provides different scales of fees, with a total of 182 fee items, for the issue of annual and multi-year licences.

Note 9: *The FSTB guidelines are to achieve full-cost recovery within:*

- (a) *seven years for those fees with existing cost recovery rate of less than 40%, through a 20% increase;*
- (b) *three to seven years for those fees with existing cost recovery rate of between 40% and 70%, through a 15% increase; and*
- (c) *one to three years for those fees with existing cost recovery rate of over 70%, through a 10% or lower increase.*

Costing approach

5.5 In the costing exercise in connection with the review of licence fees in 2001 (see para. 5.7), the costing approach was discussed among the Director of Home Affairs, the Director of Accounting Services, the Secretary for Home Affairs and the Secretary for Financial Services and the Treasury. In December 1999, the parties agreed to adopt the “processing time approach” (Note 10) in calculating the full cost incurred in processing an application for a new/renewed licence under the HAGAO.

Review of licence fees

5.6 Since 1998, the OLA carried out a review of licence fees in 2001 and another review in 2005. Details of the two reviews are given in paragraphs 5.7 to 5.11.

Review of fees in 2001

5.7 In 2000, the OLA conducted a detailed costing exercise, using the processing time approach. The exercise showed that, at 2000-01 price level, the then prevailing fees recovered 34% to 56% of the full cost of issuing new licences, and 66% to 100% of that of renewal of licences.

5.8 In order to achieve full-cost recovery (see para. 5.3), in May 2001, the Secretary for Home Affairs decided that:

- (a) for establishments with more than 100 rooms, the fees would be set at a full-cost recovery basis at 2000-01 price level; and
- (b) for establishments with 100 rooms or less, the fees for issue of new, and renewed licences should aim to recover the full cost within one to five years, and one to three years, respectively.

Note 10: *Under this approach, the following elements are included in the cost calculation:*

- (a) **Staff cost.** *The time taken by each rank of staff on all steps for processing an application is assessed and converted into staff cost;*
- (b) **Housekeeping cost.** *This is the staff cost indirectly involved in HAGAO licensing; and*
- (c) **Other costs.** *These include accommodation cost, departmental expenses, central administration overheads and departmental administration overheads.*

5.9 The new set of fees came into effect in December 2001. It recovered, at 2000-01 price level, 45% to 100% of the full cost of issuing new licences, and 76% to 100% of that of renewal of licences. Since then, the Government had frozen most fees and charges in view of the economic downturn. Consequently, licence fees under the HAGAO had not been revised until 2005.

Review of fees in 2005

5.10 In line with the government decision to resume the revision of fees and charges in 2004 (Note 11), the OLA conducted another costing exercise, using the processing time approach. It was found that the then prevailing fees recovered, at 2004-05 price level, 45% to 99% of the full cost of issuing new licences, and 83% to 108% of that of renewal of licences.

5.11 In October 2005, the Secretary for Home Affairs decided that the fees would be revised as follows:

- (a) for hotels and guesthouses with over 100 rooms, an increase in fees of not more than 1% for issue of new and renewed licences;
- (b) for hotels and guesthouses with 100 rooms or less, an increase in fees from 10% to 15% for issue of new licences;
- (c) for hotels and guesthouses with 6 to 100 rooms, an increase in fees of 10% or less for renewal of licences; and
- (d) for hotels and guesthouses with one to five rooms, an adjustment in fees for renewal of licences, ranging from a reduction of 7% to an increase of 1%.

The revised licensed fees under the HAGAO came into effect in January 2006.

Note 11: *The Financial Secretary, in his 2004-05 Budget Speech, stated that the Government would first review the fees that did not directly affect people's livelihood or general business activities.*

Audit observations

Full-cost recovery objective not yet achieved

5.12 Up to June 2006, the objective of full-cost recovery had not yet been achieved. For example, for establishments with 4 to 100 rooms, the fees of 1-year and 2-year new licences recovered, at 2004-05 price level, 52% to 70% of the full cost of issuing licences. **Audit considers that the OLA needs to ensure that the licence fees are periodically revised to achieve full-cost recovery in accordance with the FSTB guidelines.**

Rejected/withdrawn applications

5.13 Each year, a large number of applications for new licences or renewed licences were rejected/withdrawn (see Figures 1 and 2 in para. 2.7). The Administration Unit, the BSU and the FSU had carried out substantial work in processing these applications. However, the cost of such work was excluded from the OLA's costing exercises in 2000 and 2004. **In Audit's view, the OLA needs to ascertain whether this cost should be recovered.**

Applications for transfer of licence

5.14 Under section 12 of the HAGAO, a licensee may apply to transfer his licence to another person. The transferred licence will last until its original expiry date.

5.15 A fee of \$140 is collected by the OLA for a transfer in accordance with the Schedule of the Fees for Official Signatures and Miscellaneous Services Notice (Cap. 2M). In 2005-06, 38 applications for transfer of licence were approved and \$5,320 was collected.

5.16 In response to Audit's enquiry, in July 2006, the OLA advised that:

- (a) in processing an application for transfer of licence under the HAGAO, the Administration Unit would vet the application for any irregularities. The case file would then be passed to the BSU to ascertain whether the transferee had maintained good records if the licence concerned was a multi-year licence (see para. 2.6). The BSU and the FSU would also comment on any specific conditions/outstanding upgrading requirements that the transferee had to comply with; and
- (b) upon approval of the transfer application, the Administration Unit would issue a letter to the applicant to return the original licence for endorsement of the amendment.

5.17 In view of the work carried out by the OLA for processing transfers of licence, the existing fee of \$140 might not have recovered the full cost. **Audit considers that the OLA needs to re-assess the fee level for transferring a licence.**

Audit recommendations

5.18 **Audit has recommended that the Director of Home Affairs should:**

- (a) **ensure that the licence fees under the HAGAO are periodically revised to achieve full-cost recovery in accordance with the FSTB guidelines;**
- (b) **ascertain whether the cost of processing rejected/withdrawn applications should be recovered; and**
- (c) **re-assess the fee level on transfer of licence having regard to the costs of processing an application for transfer.**

Response from the Administration

5.19 The **Director of Home Affairs** generally agrees with the audit recommendations. She has said that:

- (a) the licence fees under the HAGAO are being reviewed and the fee proposals are being prepared in accordance with the FSTB guidelines to achieve full-cost recovery; and
- (b) the OLA will review whether the cost of rejected/withdrawn applications for new licences or licence renewals should be recovered. The OLA will also consider the feasibility of revising the fee to be charged for transfer of licence. The implementation of both recommendations will require legislative amendment to the HAGAO.

PART 6: PROMOTION OF LICENSED ESTABLISHMENTS

6.1 This PART examines the OLA's efforts in promoting establishments licensed under the HAGAO.

Benefits of promoting licensed establishments

6.2 Promotion of licensed establishments would benefit both tourists and licensees as more tourists would patronise licensed accommodation. This provides additional incentive for operators of establishments to apply for licences under the HAGAO.

6.3 The OLA has various measures to promote licensed establishments. These include:

- (a) logos for identifying licensed establishments; and
- (b) promotion through the Internet.

Logos of licensed establishments

6.4 There are logos for identifying guesthouses for tourists, guesthouses for local people and holiday flats. The logos are issued to operators when their applications for new licence or licence renewal are successful. The OLA asks the operators to display the logos in a prominent position at the licensed premises. There are no logos for identifying other licensed establishments (e.g. hotels and holiday camps).

Audit observations

6.5 In response to Audit's enquiry, in July 2006, the OLA advised that it did not have information about the number of licensed establishments displaying the logos. It also had not conducted a review of the effectiveness of displaying the logos in promoting patronage of the licensed establishments. Audit considers that the OLA needs to assess the effectiveness of asking the licensed establishments to display the logos. The OLA also needs to consider whether logos should be issued to other licensed establishments such as holiday camps.

6.6 To help users identify the licensed establishments, the OLA may need to consider including in the standard licence conditions guidelines on how the logo should be displayed.

6.7 Audit also noted that when a licence was cancelled or not renewed, there was no requirement that the logo should be returned to the OLA. The OLA had no information regarding unlicensed establishments displaying expired/fake logos. In Audit's view, the OLA needs to address the risk of expired/fake logos being displayed. There is a need to consider requiring the logos to be returned to the OLA upon licence cancellation or non-renewal.

Audit recommendations

6.8 **Audit has recommended that the Director of Home Affairs should consider:**

- (a) **assessing the effectiveness of the identification logos of licensed establishments;**
- (b) **the feasibility of issuing logos for identifying licensed establishments such as holiday camps;**
- (c) **including in the standard licence conditions for licensed establishments guidelines on the proper display of logos at their premises;**
- (d) **assessing the risk of expired/fake logos being displayed by unlicensed establishments; and**
- (e) **requiring the logos to be returned to the OLA when the licences are cancelled or lapsed.**

Response from the Administration

6.9 The **Director of Home Affairs** welcomes the audit recommendations on the promotion of licensed establishments by making use of the guesthouse logos.

Promotion through the Internet

6.10 The OLA provides information about licensed establishments at its website on the Internet. Such information includes the name, address, number of rooms, telephone number, fax number and e-mail address of licensed establishments. The website also

provides hotel and guesthouse search functions by name, by district and by number of rooms.

Audit observations

6.11 Audit notes that the websites of both the Hong Kong Tourism Board and the Tourism Commission are linked to the OLA website. In Audit's view, accessibility to the OLA website can be enhanced if other travel/tourist websites are also linked to it (e.g. the websites of overseas tourism bodies). The OLA website has recorded the number of visits made to the website. However, the OLA has not made use of this information to regularly assess the website's popularity.

Audit recommendations

6.12 **Audit has *recommended* that the Director of Home Affairs should consider:**

- (a) **regularly assessing the popularity of the OLA website; and**
- (b) **ways of enhancing accessibility to the OLA website.**

Response from the Administration

6.13 The **Director of Home Affairs** welcomes the audit recommendations on the promotion of licensed establishments by making use of the OLA website.

PART 7: PERFORMANCE MANAGEMENT

7.1 This PART examines the efforts made by the OLA in performance management.

Performance targets and indicators

7.2 The FSTB has devised guidelines on the reporting of performance information in the Controlling Officer's Reports (CORs). According to FSTB Circular Memorandum No. 14/2005 dated 10 October 2005, for individual programmes, Controlling Officers should focus more on targets when developing their performance measures and ensure that all targets and indicators are clearly stated. Targets should preferably measure outcomes instead of output or input.

Audit observations

Development of performance measures

7.3 According to the 2006-07 Estimates, the OLA's licensing work under the HAGAO falls within "Programme (4) Licensing" in the COR of the HAD. The following two performance indicators, which measure workload, were provided in the COR:

- (a) ***Hotels and guesthouses licensed.*** An estimate figure for 2006, together with the actual figures for 2004 and 2005, were provided on the number of hotels and guesthouses licensed; and
- (b) ***Inspections made.*** An estimate figure for 2006, together with the actual figures for 2004 and 2005, were provided on the number of inspections made. However, there was no indication about the nature of the inspections, and whether the inspections were conducted under the HAGAO, or other ordinances administered by the OLA.

7.4 To enhance performance reporting, the OLA needs to develop more meaningful performance measures. These include, for example, the number of enforcement actions taken (which may be further divided into inspections conducted, warning letters issued and prosecutions instigated) in respect of licensed and unlicensed establishments.

7.5 In accordance with the FSTB guidelines, the OLA needs to consider setting performance targets on its licensing and enforcement activities. As targets should preferably measure outcomes, the OLA also needs to develop performance targets that measure the effectiveness of its licensing programme.

Audit recommendations

7.6 **Audit has recommended that the Director of Home Affairs should:**

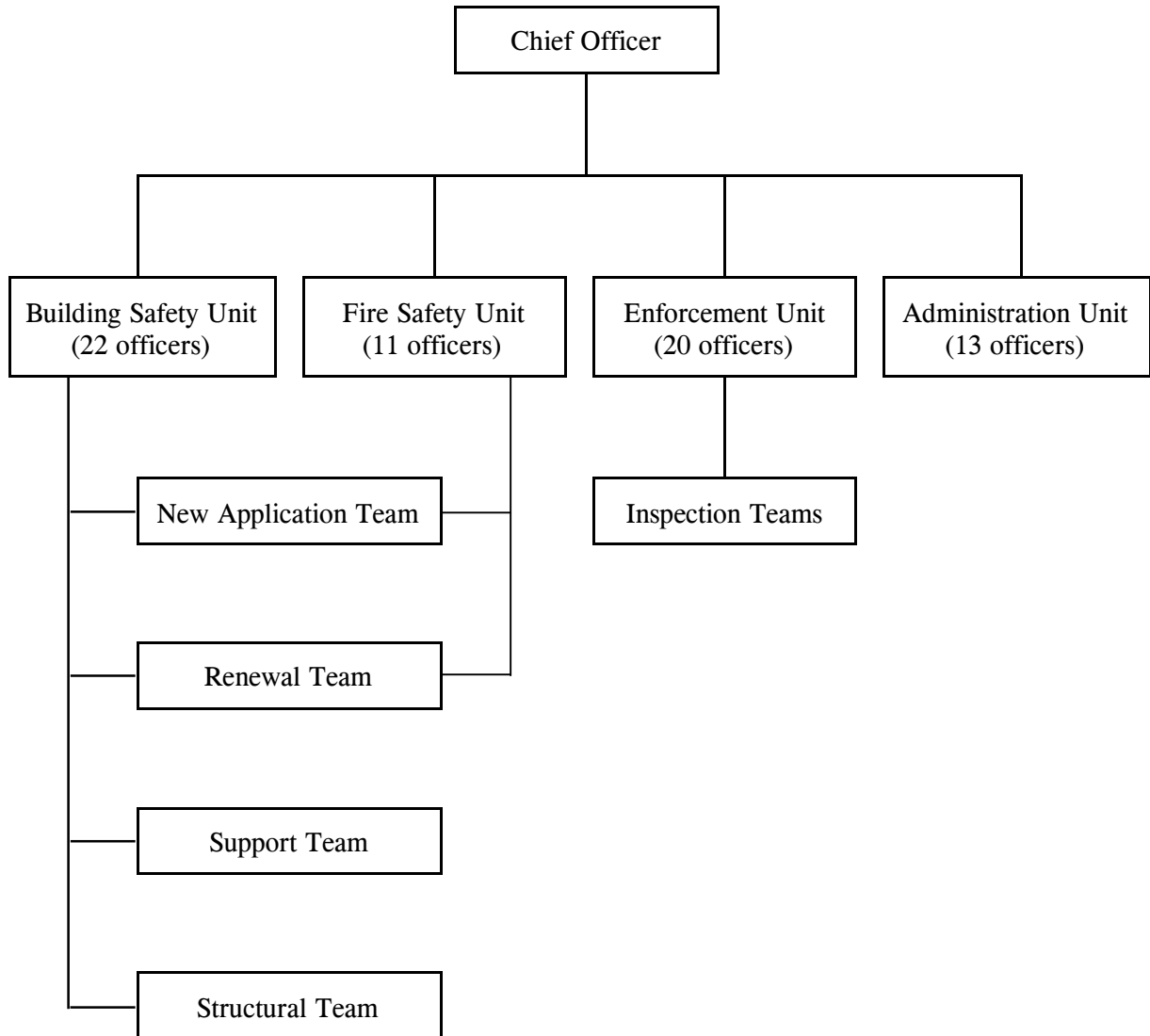
- (a) **develop more meaningful performance measures including, for example, the number of enforcement actions taken in respect of licensed and unlicensed establishments; and**
- (b) **consider setting performance targets on the various licensing and enforcement activities of the OLA carried out under the HAGAO, including targets that measure the effectiveness of the licensing programme.**

Response from the Administration

7.7 The **Director of Home Affairs** welcomes the audit recommendations on developing more meaningful performance measures and setting performance targets on the various licensing and enforcement activities of the OLA carried out under the HAGAO.

7.8 The **Secretary for Financial Services and the Treasury** agrees with the audit observations and recommendations. He has said that the FSTB will continue to urge bureaux/departments, including the HAD, to adhere to the FSTB guidelines in preparing the CORs.

Organisation chart of the Office of the Licensing Authority
(30 June 2006)



Source: OLA records

**Internal management targets of the Office of the Licensing Authority
(30 June 2006)**

Processing of licence applications

1. On receipt of an application for a new licence in respect of a purpose-built hotel/guesthouse, a “no objection in principle” letter should be issued **within 12 working days**.
2. On receipt of an application in respect of premises other than a purpose-built hotel/guesthouse, a letter of upgrading requirements should be issued **within 35 working days**.
3. On receipt of a renewal application not less than three months before expiration, and provided that the required documents are submitted at least three weeks before expiration, OLA should renew the licence **before expiration**.
4. On receipt of a report of completion of the required upgrading works from the applicant, arrangements for compliance inspection should be made **within seven working days**. The inspections should be conducted **within eight working days** if the premises are available for inspection.
5. On confirmation of compliance of all requirements, a licence should be issued **within seven working days**.

Source: OLA records

**Improvements in the Enforcement Unit's performance
in its enforcement work against suspected unlicensed establishments**

- (a) Comparing with previous years, the average time span between the date of receiving a case in respect of a suspected unlicensed establishment and the date of completing action has been on the decrease, as shown below:

	1,842 cases completed between January 2001 and June 2006	1,073 cases completed between August 2005 and August 2006
Time span to complete action on suspected unlicensed establishments	Average: 268 days (as shown in para. 4.11)	Average: 152 days

- (b) The Enforcement Unit has made great efforts to clear long outstanding backlog, as reflected by the increased number of cases completed in recent years, as follows:

Year	Number of cases completed
2001	14
2002	140
2003	191
2004	431
2005	586
2006 (up to 30 June 2006)	512

- (c) To improve its enforcement work, the OLA has, since early 2004, engaged Licensing Inspectors to carry out enforcement work. This staff restructuring in the Enforcement Unit has significantly improved the efficiency and effectiveness of its work. Based on a total of 1,055 cases received during the period 15 August 2005 to 15 August 2006, the average time between the case receipt date and the first inspection date was 13.5 days.
- (d) As a result of the OLA's enhanced enforcement work, there has been a sharp increase in the number of prosecutions. As shown in Table 4 of paragraph 4.10, there was a significant improvement in the enforcement work in recent years in terms of the numbers of warning letters issued and prosecution cases.

Source: *HAD memorandum to Audit*

Acronyms and abbreviations

Audit	Audit Commission
BSU	Building Safety Unit
COR	Controlling Officer's Report
D of J	Department of Justice
EMIS	Enforcement Management Information System
FSD	Fire Services Department
FSTB	Financial Services and the Treasury Bureau
FSU	Fire Safety Unit
HAD	Home Affairs Department
HAGAO	Hotel and Guesthouse Accommodation Ordinance
OLA	Office of the Licensing Authority
PAC	Public Accounts Committee