

Report No. 56 of the Director of Audit — Chapter 7

HONG KONG HOUSING AUTHORITY: MANAGEMENT OF COMMERCIAL PROPERTIES

Summary

1. The Hong Kong Housing Authority (HA) is a statutory body established under the Housing Ordinance (Cap. 283), with the Housing Department (HD) acting as its executive arm. In November 2005, the HA divested 180 retail and carpark (RC) facilities to a Real Estate Investment Trust (REIT) which was listed on the Stock Exchange of Hong Kong. Following the divestment, the HA has continued to manage the non-divested commercial properties and those provided under new public housing developments.

2. As at December 2010, the commercial and non-domestic properties under the HA's management comprised 168,600 square metres of retail areas and 27,000 carparking spaces, as well as factory, welfare and other miscellaneous premises. In 2009-10, HA commercial operations generated an operating surplus of \$461 million. The HA's Commercial Properties Committee (CPC) advises the HA on policies concerning its commercial, industrial and other non-domestic facilities, and optimising the financial return on its investment. The Audit Commission (Audit) has recently conducted a review of the management of HA commercial properties.

Management of retail premises

3. *Day-to-day management of retail premises.* Audit visited 12 HA major retail facilities between October 2010 and January 2011 and found that: (a) some storerooms had been altered by tenants for other uses without the HD's approval; (b) suspected gambling activities appeared prevalent in some retail facilities; (c) some let-out retail premises were not open for business (i.e. non-trading) during normal business hours; and (d) there were areas where improvements could be made in the implementation of the HA marking scheme. *Audit has recommended that the Director of Housing should: (a) request HD staff and contractors to step up their daily patrol work and unit-to-unit inspections to prevent unauthorised use and alteration of retail premises (including storerooms); (b) step up measures to combat suspected gambling activities in HA retail facilities; (c) ascertain the reasons for the prevalence of non-trading in some retail facilities and take actions to address them; and (d) remind HD staff and contractors to strictly follow the established procedures in enforcing the HA marking scheme.*

4. *Letting of retail premises.* Although many HA retail premises have remained vacant for a long time, the HD did not take adequate measures to ensure that these premises were widely publicised and put up for open tender as frequently as practicable. For a

vacant premises which did not attract any bidder in an open tender, the HD would normally take about two calendar months to re-tender the same premises. Also, HD staff may not have full market information when re-designating the trade appropriate for the premises in the re-tendering exercise. *Audit has recommended that the Director of Housing should: (a) ensure that all vacant retail premises available for letting are widely publicised; and (b) in re-letting vacant retail premises, further encourage prospective tenants to make trade suggestions.*

5. ***Implementation of improvement measures.*** In recent years, the HA has implemented a number of improvement measures for its retail premises, such as earmarking four retail facilities for early consideration of major improvement works and conducting “re-ordering” exercises in a number of markets. In setting the priority for major improvement works, the HD mainly took into account the commercial potential of the retail facilities concerned. Audit also noted that although the HD had taken improvement measures in some markets, their vacancy rates remained high. *Audit has recommended that the Director of Housing should: (a) duly take into account the vacancy rates of retail facilities when selecting them for major improvement works to enhance their commercial potential; and (b) take early actions to address the long-standing vacancy problem in some HA markets.*

6. ***Monitoring of operating expenditure.*** To ensure that retail facilities are operated cost-effectively, the HD has set major operating expenditure benchmarks for compliance by its estate housing managers. In 2009-10, many retail facilities had their operating expenditure exceeding the HD benchmarks. Some estate housing managers had not fully reported the non-compliance to the senior management, nor had they proposed adequate follow-up action for improving the situation. *Audit has recommended that the Director of Housing should improve the current monitoring mechanism to ensure that effective follow-up actions are taken on all cases of non-compliance.*

Management of car parks

7. ***Planning the provision of parking facilities.*** Prior to 2009, parking facilities for public housing developments were built according to old planning standards stipulated in the Hong Kong Planning Standards and Guidelines (HKPSG). According to HD records, for many aged estates, the provision of public housing carpark facilities had turned out to be greater than the actual demand, leading to high vacancy rates in many HA car parks. Since 2009, substantial revisions to the parking standards have been made to the HKPSG. *Audit has recommended that the Director of Housing should, in consultation with the Transport Department, continue to regularly review the parking planning standards, having regard to the changing supply and demand conditions.*

8. ***Measures to improve the utilisation of parking spaces.*** In recent years, the HD has taken various measures to improve the utilisation of parking spaces, including conversion of surplus carpark facilities into other beneficial uses and letting of parking spaces to non-residents. In 2010, the HD conducted strength-weakness-opportunity-threat (SWOT) analysis of 38 car parks (with occupancy rate below 70% and with more than 20 parking spaces) and categorised them into different groups for follow-up actions. *Given that many of the 38 car parks had a consistently low occupancy rate for many years, Audit*

has recommended that the Director of Housing should expedite efforts to implement the recommendations arising from the SWOT analysis.

9. ***Conversion of surplus carpark facilities into other uses.*** Since 2006, the HD has converted some underutilised parking facilities into other uses. As at January 2011, four projects were completed and successfully leased out. One of these projects related to leasing part of a car park to an organisation. Although this project was a commercial letting according to HD records, the rent charged to the organisation was on a par with the concessionary rent normally applicable for welfare lettings. This was contrary to the HD's established practice of charging market rate for commercial lettings. *Audit has recommended that, in exploring major conversion of commercial premises in future, the Director of Housing should ensure that the rent for the converted premises is assessed, duly taking into account the conversion costs and the proposed use of the premises.*

Management of factory estates

10. Having regard to its core mission of providing subsidised rental housing, the HA decided in 1989 to progressively absolve itself from the ownership and management of factory estates in the long term. Since then, a number of factory estates had been cleared. As at January 2011, the HA still managed seven factory estates. Of these, the Chai Wan Factory Estate (CWFE) was built in 1959 using old design standards without lift service. The remaining six, completed in or after 1979, were built to comparatively modern standards.

11. ***Clearance of old factory estates.*** In November 2000, the HA reviewed the position of the old factory estates (those built in the late 1950s to mid-1970s). Given the obsolete design and increasing maintenance costs, the HA noted that the estates were approaching the point where clearance needed to be considered. Up to January 2011, the HA had cleared all old factory estates, except the CWFE. The CWFE had been running at a deficit of about \$2 million each year and was in poor building conditions. Audit raised concern about a lack of a definite clearance plan for the CWFE. In the event, the CPC approved in March 2011 a clearance plan for the CWFE.

12. ***Long-term development of newer factory estates.*** Since 1989, it has been the HA's policy to absolve itself from the ownership and management of factory estates (see para. 10). However, up to January 2011 (after more than 21 years), the HD had not formulated a long-term strategy to implement the policy. *Audit has recommended that the Director of Housing should review the position of the six newer factory estates and develop a strategy for their long-term development.*

13. ***Subletting of factory premises.*** Under the provisions of factory tenancy agreement, a tenant should not sublet factory premises without HD written permission. To help detect subletting or unauthorised use of factory premises, the HD has laid down procedures to be followed by its staff. These procedures include conducting thorough inspection of each factory unit on a 18-month cycle covering the checking of any change of factory name and trade, and whether the factory is operated by the tenant or by an

unauthorised person. Audit visited two factory estates and examined their inspection records. Audit found that HD procedures had not been properly followed.

14. Audit also found that many factory units bore names or carried out trades which were different from those shown in HD records. Audit selected some factory units for conducting business registration search. The results indicated that, for some of these units, the tenants were not the business owners. Instead, businesses were operated by third parties. *Audit has recommended that the Director of Housing should follow up on the suspected subletting cases identified by Audit and step up efforts to combat the problem of subletting.*

Performance measurement and reporting

15. The HA has set various key performance indicators (KPIs) and targets for the management of commercial properties. The KPIs include vacancy rate for retail premises, rent arrears, and operating expenditure as a percentage of income. Audit found that: (a) the HD had not properly calculated the vacancy rates of retail premises for reporting to the CPC; (b) the HD did not systematically collect feedback on the residents' satisfaction level on various aspects of performance in the management of commercial properties; and (c) apart from retail premises, there were no KPIs/targets to measure the vacancy position of other types of properties. *Audit has recommended that the Director of Housing should: (a) review and revise the basis for calculating the vacancy rate of retail premises; (b) devise a mechanism to gauge, and report to the CPC, the residents' satisfaction level concerning management of commercial properties; and (c) consider setting specific KPIs and targets for different types of commercial properties.*

The way forward

16. The divestment of 180 RC facilities in 2005 (see para. 1) was the first exercise of its kind implemented by the HA. In 2006, the Administration reported that the HA would look for opportunities to further divest the remaining RC facilities and those to be built in the future. In December 2009, the Secretary for Transport and Housing said that the HA still had no plan to further divest its properties. There have been various issues arising from the 2005 divestment exercise, including the transfer of legal titles of divested properties from the HA to the REIT. *Audit has recommended that the Director of Housing, in consultation with the Secretary for Transport and Housing and the Secretary for Financial Services and the Treasury, should: (a) conduct a post-implementation review of the 2005 divestment exercise to evaluate its effectiveness and to identify if there are lessons to be learnt; and (b) based on the outcome of the review, map out the way forward for the management of HA commercial properties.*

Response from the Administration

17. The Director of Housing agrees with the audit recommendations.

April 2011