

CHAPTER 8

**Department of Health
Education Bureau
Food and Environmental Hygiene Department
Leisure and Cultural Services Department**

Hiring of service contractors and professionals

**Audit Commission
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30 October 2014**

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. 63 of the Director of Audit contains 10 Chapters which are available on our website at <http://www.aud.gov.hk>

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HIRING OF SERVICE CONTRACTORS AND PROFESSIONALS

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HIRING OF SERVICE CONTRACTORS AND PROFESSIONALS

Executive Summary

1. Government bureaux and departments (B/Ds) hire service contractors and professionals regularly to perform services including cleansing, facilities management, security and diagnostic services. The Government's procurement policy is to obtain goods and services at the best value for money and award contracts for supplying goods and services through open, fair, competitive and transparent procedures. Controlling Officers, responsible for the management of services procured, should observe and uphold the culture of compliance with the requirements set out in the Stores and Procurement Regulations (SPRs) issued by the Financial Secretary/Secretary for Financial Services and the Treasury under section 11(1) of the Public Finance Ordinance (Cap. 2).

2. In the past decade, Government expenditure on hiring service contractors and professionals under Subhead 111 of the General Revenue Account had increased from \$2.62 billion in 2004-05 to \$7.18 billion in 2013-14. In view of the significant and increasing expenditure on the hiring of service contractors and professionals, the Audit Commission (Audit) has recently conducted a review of four B/Ds' processes and practices in the acquisition of such services. A number of contracts were selected from the four B/Ds, namely the Department of Health (DH), Education Bureau (EDB), Food and Environmental Hygiene Department (FEHD), and Leisure and Cultural Services Department (LCSD), for review.

Sourcing of service providers

3. *DH: Need to critically assess the tender price for the procurement of health screening service under single tenders.* According to SPR 325, limited (single or restricted) tender procedures shall only be used in circumstances when open competitive tendering would not be an effective means of obtaining the requisite stores or services. Since 2003, the DH has used single tenders to obtain

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health screening service for visitors at the Hong Kong International Airport from Contractor A. For the period from April 2012 to March 2016, there was a significant increase in the contract value (by 171% from \$30.6 million to \$82.9 million). The contract rate charged per man-hour for the screening services at the Airport was twice that charged for similar services obtained through open tenders at the boundary and the cruise terminal. Audit considers that the DH needs to critically assess all relevant factors during tender/contract negotiations with a view to obtaining the required services at the best value for money (paras. 2.4, 2.7, 2.9, 2.14 and 2.24).

4. ***EDB: Need to review the use of single tenders and explore the market of service providers for Student Assessment (SA) programme.*** Between December 2000 and January 2011, the EDB had entered into three consecutive single-tender contracts with Contractor B for the development of the Basic Competency Assessment (BCA) in Chinese Language, English Language and Mathematics. The current four-year contract was valued at \$319 million. The BCA comprises two programmes, namely the SA and the Territory-wide System Assessment (TSA). According to the EDB, the SA and TSA came as a package and, especially when the BCA was at an early development, engaging one single institution to implement the two programmes was considered more appropriate and effective in ensuring consistency. Besides, Contractor B is the only service provider who can provide the BCA service having regard to its knowledge about the local school curriculum and its ability to hold public examinations in school centres (paras. 2.25, 2.27, 2.28 and 2.38).

5. More recently, the EDB informed Audit that it had separately contracted out in 2012 certain tasks of the SA programme to another service provider as a pilot project to assess the feasibility of engaging other service providers in the development of SA items. Audit welcomes the EDB's initiative. Given that the SA programme mainly involves the development of competency assessment items and maintaining the SA system and database, Audit considers that the justification for the continued use of single tender for the SA programme (bundled with the TSA) may diminish with time and it is time to consider separating the SA programme for procurement by open competitive tenders (paras. 2.38 and 2.39).

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6. ***FEHD: Limited number of service providers for FEHD's cleansing contracts may increase concentration risks.*** As at June 2014, the FEHD had outsourced its street cleansing services in 19 districts under 25 two-year contracts at a total value of \$1,740 million. These contracts were awarded through open tenders to five contractors, one of which was awarded 10 contracts with a total value of \$653 million (38% of \$1,740 million). Whilst Audit noted that the situation had improved as at September 2014, Audit considers that the FEHD needs to continue monitoring the situation and take necessary measures, where appropriate, to enhance competition and reduce concentration risks in future tendering exercises (paras. 2.41, 2.42 and 2.44).

7. ***LCSD: Limited number of service providers for venue cleansing and supporting service contracts.*** As at March 2014, the LCSD had awarded through open tendering 41 contracts for the provision of cleansing and supporting services to its venues at a total value of \$1,913 million to eight contractors. Of these contracts, 32 contracts were awarded to two contractors with a total value of \$1,780 million (93% of \$1,913 million), with one having been awarded 20 contracts totalling \$1,236 million in value. Since a large majority of the LCSD's venue cleansing and supporting services are provided by two contractors, Audit considers that the LCSD needs to critically review its tendering strategy and consider the use of more contractors to reduce concentration risks (paras. 2.45, 2.46 and 2.48).

8. ***B/Ds: Procurement procedures not always adopted to enhance competition.*** According to the SPRs, B/Ds shall follow tender procedures when making purchases of services exceeding \$1.43 million. Audit examination of contracts selected from the four B/Ds found that while some contractors provided same/similar services with a total value exceeding \$1.43 million during the year, such services were not or could not be aggregated into a single contract to achieve better economy of scale and follow the tender procedures for procurement in accordance with the SPRs (paras. 2.49 and 2.50).

Specification of service requirements

9. Tender specifications define the requirements of the procuring departments and what the tenderers are expected to provide. According to the SPRs, tender specifications shall meet the basic Government procurement principles of transparency, openness and fairness. In setting tender specifications, B/Ds should also guard against over-restrictive requirements which might have the effect of protecting existing service providers in the market from potential competition, thus reducing or limiting choices and potentially affecting prices (paras. 3.2, 3.10 and 3.11).

10. ***FEHD: Need to reflect street washing service requirements accurately in tender specifications.*** Audit noted that there were significant discrepancies between the service locations specified in the FEHD's tender documents and those specified in the work plans proposed by the successful tenderers, which formed part of the contracts. Audit considers that for fair competition, the FEHD needs to critically review the locations for street washing as specified in the tender documents to ensure that they are complete and well justified to meet the actual needs, ensure that the tenders received comply with the service requirements as specified in the tender documents, and take measures to incorporate all required locations into the contracts awarded to the successful tenderers (paras. 3.6 and 3.8).

11. ***LCSD: Setting of mandatory requirements specified in its venue management contracts.*** As at 31 March 2014, the LCSD outsourced the management support services for 14 sports centres through open tenders. All the contracts were awarded to one contractor. Audit found that according to the tender document, the tenderer needs to meet certain mandatory requirements on its year of experience in management support services at recreational or sports facilities. Audit considers that the LCSD needs to critically review whether it is possible to revise the mandatory requirements with a view to encouraging competition, increasing choices and avoiding over-reliance on a single contractor (paras. 3.12, 3.14 and 3.19).

Monitoring service delivery

12. ***EDB: Monitoring of BCA contracts.*** Under the terms of the BCA contracts, no sub-contracting by Contractor B is allowed except with prior written approval of the EDB. Audit notes that Contractor B has sub-contracted part of the contracts without obtaining written approval of the EDB. Besides, the utilisation of the SA system was low. In the past three years from 2011 to 2013, under the third BCA contract, some 60% of primary schools and 80% of secondary schools had not logged into the system to create assessments for their students. The EDB needs to identify the reasons for the low utilisation and closely monitor the future utilisation of the SA programme (paras. 4.5, 4.6, 4.11 and 4.15).

13. ***FEHD: Requirements specified in its recyclables collection service contracts not effectively enforced.*** Since 2000, the FEHD has been outsourcing its recyclables collection service. The service contracts stipulated that the contractor shall not dispose of any recyclables in any landfill, refuse transfer stations or any other waste disposal facilities without prior consent of the FEHD. In May 2013, the media reported cases of improper disposal of collected recyclables by the contractor and similar cases were also found by the FEHD's surprise inspections in the same month. Under the terms of the new recyclables collection contract for the period from August 2014 to July 2016, the contractor is required to deliver plastic recyclables collected to "*recyclables recyclers*" (instead of "*recyclables collectors*") nominated by the contractors and approved by the FEHD. However, the requirement for the contractors to deliver non-plastic recyclables to "*recyclables collectors*" remained unchanged (paras. 4.16, 4.18 to 4.20).

14. ***FEHD: Monitoring of street washing services.*** Audit analysed the service locations specified in the daily work programmes approved by the FEHD for five districts and found that they varied significantly from those locations specified in the work plans which formed part of the contracts. Audit could not find documentation to ascertain that the Health Inspectors concerned had brought such variations from contracts to the attention of the Senior Health Inspectors (paras. 4.26 and 4.27).

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15. Audit review of the FEHD's inspection results revealed inadequacies in its monitoring of the contractors' services, such as conducting inspections on a fairly regular basis which might be anticipated by the street washing teams. Audit's on-site inspections in five districts to observe the actual operation of street washing by the FEHD's contractors in July and August 2014 also found irregularities. For example, in one district, Audit found, among others, that:

- (a) the street washing team had not carried out street washing at some of the scheduled service locations as specified in the daily work programmes;
- (b) the team spent much shorter than scheduled time in washing the service locations; and
- (c) the team returned to the water filling point for sign off much earlier than the scheduled time.

The FEHD needs to consider implementing a more effective mechanism for monitoring the contractors' delivery of services (paras. 4.31, 4.33 and 4.34).

Way forward

16. The audit review has identified room for improvements in a number of areas in the four B/D's hiring of service contractors and professionals. In particular, some of the procurements reported could have achieved better value for money through more determined and focused efforts to introduce competition among eligible tenderers and through closer monitoring of contractors' performance. Audit considers that B/Ds should be reminded to comply with the relevant Government regulations and guidelines on their hiring of service contractors and professionals from time to time (paras. 5.5 and 5.6).

Audit recommendations

17. **Audit recommendations are made in PART 5 of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that:**

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Sourcing of service providers

- (a) the Director of Health should critically assess all relevant factors during tender/contract negotiations with a view to obtaining the required services at the best value for money;
- (b) the Secretary for Education should consider whether other tendering options can be brought into the SA programme separately when opportunity arises so as to reap the benefits of competitive bidding;
- (c) the Director of Leisure and Cultural Services should critically review the LCSD's tendering strategy and consider the use of more contractors to reduce concentration risks;

Specification of service requirements

- (d) the Director of Food and Environmental Hygiene should critically review the service locations specified for street washing in the tender documents to ensure that such locations are justified and meet the actual needs;
- (e) the Director of Leisure and Cultural Services should critically review whether it is possible to revise the mandatory requirements for the provision of management support services at sports centres with a view to encouraging competition;

Monitoring service delivery

- (f) the Secretary for Education should identify the causes for the low utilisation of the SA programme and closely monitor the utilisation of the SA programme;
- (g) the Director of Food and Environmental Hygiene should consider implementing a more effective mechanism for monitoring the delivery of street washing services by the contractors;

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Way forward

- (h) **the Secretary for Financial Services and the Treasury should, in conjunction with the Director of Government Logistics, remind B/Ds to comply with the relevant Government regulations and guidelines on the hiring of service contractors and professionals; and**
- (i) **the Director of Government Logistics should take on board the audit observations mentioned in this audit review in the Government Logistics Department's reviews of B/Ds' compliance with the SPRs.**

Response from the Administration

18. The Administration generally agrees with the audit recommendations.

PART 1: INTRODUCTION

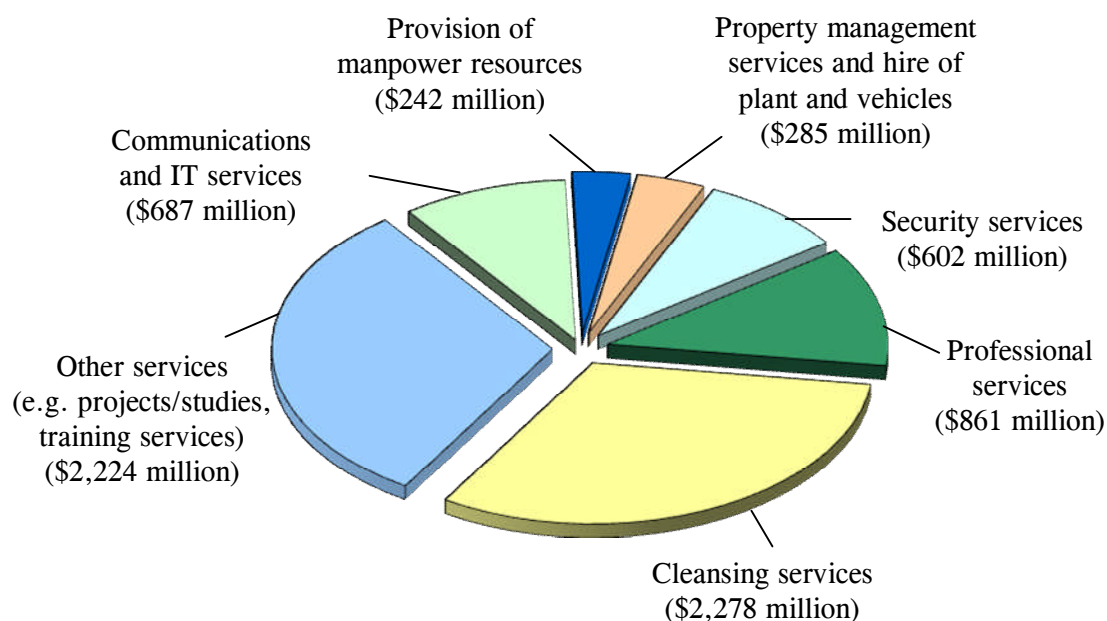
1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

Background

1.2 Government bureaux and departments (B/Ds) hire service contractors and professionals regularly to perform services including cleansing, facilities management, security and diagnostic services. In 2013-14, Government expenditure incurred by B/Ds on hiring services and professionals (Note 1) was \$7.18 billion comprising expenditure items as shown in Figure 1.

Figure 1

**Expenditure items on hiring service contractors and professionals
(in 2013-14)**



Source: Audit analysis of Treasury records

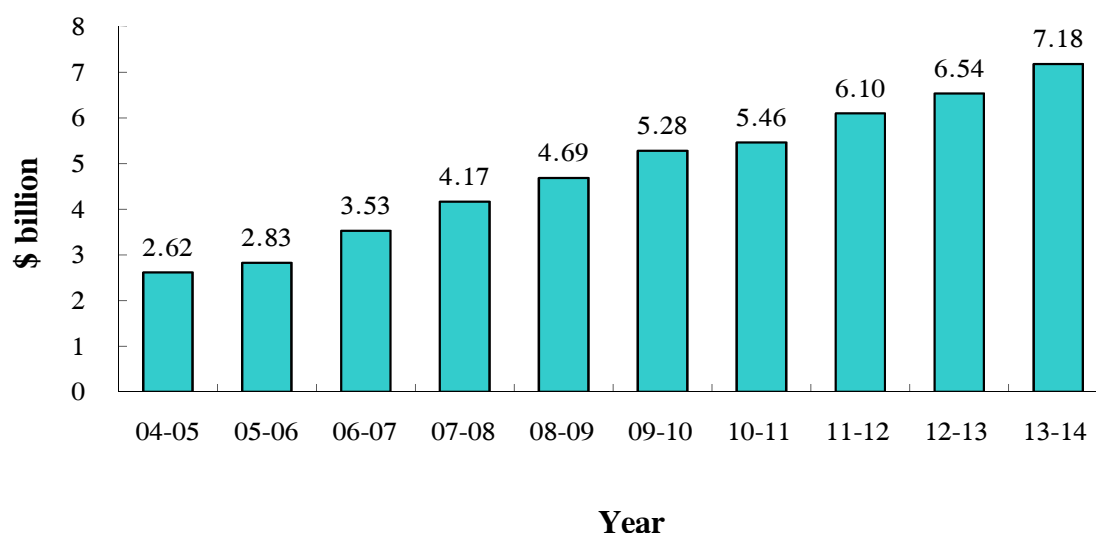
Note 1: *The expenses are charged to Subhead 111 Hire of services and professional fees under general departmental expenses of the General Revenue Account.*

Introduction

1.3 During the past decade, Government expenditure on hiring service contractors and professionals had increased from \$2.62 billion in 2004-05 to \$7.18 billion in 2013-14 (see Figure 2).

Figure 2

**Expenditure on hiring service contractors and professionals
(2004-05 to 2013-14)**



Source: Audit analysis of Treasury records

1.4 B/Ds are required to comply with the laid-down policies and regulations in relation to hiring of service contractors and professionals. According to the Guide to Procurement issued by the Financial Services and the Treasury Bureau (FSTB):

- (a) the procurement policy of the Government is to obtain goods and services at the best value for money in support of its programmes and activities;
- (b) the Government is committed to providing equal opportunities for domestic and foreign suppliers and service providers, participating or competing in Government procurement;

- (c) contracts for supplying goods and services to the Government are awarded through open, fair, competitive and transparent procedures; and
- (d) procurement of goods and specified services covered by the Agreement on Government Procurement of the World Trade Organization (WTO GPA) is conducted in accordance with the provisions of the Agreement (Note 2).

1.5 According to the Stores and Procurement Regulations (SPRs) issued by the Financial Secretary/Secretary for Financial Services and the Treasury under section 11(1) of the Public Finance Ordinance (Cap. 2), Controlling Officers (COs) are responsible for the procurement of services within the financial limits set out in the SPRs, and the management of services procured. They shall observe and uphold the culture of compliance with the requirements set out in the SPRs, regularly remind all the staff concerned about their needs to always comply with the SPRs and closely monitor their compliance. The Government Logistics Department (GLD) regularly checks whether B/Ds comply with the SPRs in respect of procurement of stores, services and revenue contracts of value not exceeding the B/Ds' departmental limit (tender cases above the departmental limit are not included as they are well considered by the relevant tender boards — see para. 2.3) and management of stores, and makes recommendations for their improvement measures.

1.6 To assist B/Ds in the procurement of services, the Efficiency Unit of the Chief Secretary for Administration's Office issues best practice guides to proactively help them improve their expertise and disseminate the latest global best practices in outsourcing and contract management (Note 3).

Note 2: *The WTO GPA applies to procurement of specified services for contracts of a value not less than 130,000 Special Drawing Rights (the Hong Kong Dollar equivalent is HK\$1,541,000 for the calendar years of 2014 and 2015) which is an international currency unit set up by the International Monetary Fund. According to the 2012 Agreement, the specified services cover eight types of services, namely computer and related services, rental/leasing services without operators, courier, telecommunications and related services, environmental (e.g. sewage, refuse disposal, sanitation and similar services), financial, transport and other business services (e.g. building-cleaning and advertising services).*

Note 3: *In 2007 and 2008, the Efficiency Unit published "A General Guide to Outsourcing (Third edition)", "Competition and Contracting: Learning from Past Experience" and "A User Guide to Contract Management".*

Management and compliance risks identified in recent audit studies

1.7 Hiring of service contractors and professionals by B/Ds had attracted some public attention. From time to time, there were media reports and complaints on the hiring of service contractors and professionals, pointing to areas such as the placing of contracts with one or a few contractors, failure in service delivery, non-performance of services by contractors' staff, etc.

1.8 In the past years, the Audit Commission (Audit) had conducted a number of audit reviews that covered the use of service contractors by B/Ds, revealing cases of non-compliance and areas where improvement could be made. Some more recent examples are shown below:

- (a) five B/Ds did not conduct competitive tendering before obtaining the services from the Electrical and Mechanical Services Trading Fund (reported in Chapter 5 "Electrical and Mechanical Services Trading Fund" of the Director of Audit's Report No. 62 of April 2014);
- (b) some B/Ds made repeated purchases of less than \$1.43 million each by quotation or low value purchases of not exceeding \$50,000 by purchasing cards without consolidating them to purchase in bulk with a view to obtaining more competitive prices (reported in Chapter 8 "Procurement and supplies services provided by the Government Logistics Department" of the Director of Audit's Report No. 59 of October 2012); and
- (c) one department awarded four current cleansing services contracts of smaller scopes or shorter durations by quotations as compared with the old ones. Without such changes, tender procedures would have been required (reported in Chapter 4 "Procurement of goods and services for correctional institutions" of the Director of Audit's Report No. 58 of March 2012).

Audit review

1.9 In view of the significant and increasing expenditure on the hiring of service contractors and professionals, this audit study aims to review the processes and practices engaged by different B/Ds in the acquisition of such services and identify areas for improvement and attention. In this connection, a number of contracts were selected from four B/Ds, namely the Department of Health (DH), Education Bureau (EDB), Food and Environmental Hygiene Department (FEHD) and Leisure and Cultural Services Department (LCSD) for the review (Note 4). Focus is placed on the following areas:

- (a) sourcing of service providers (PART 2);
- (b) specification of service requirements (PART 3);
- (c) monitoring service delivery (PART 4); and
- (d) way forward (PART 5).

Audit has identified areas for improvement and attention, and has made a number of recommendations to address the issues.

Acknowledgement

1.10 Audit would like to acknowledge with gratitude the full cooperation of the staff of the DH, EDB, FEHD and LCSD during the course of the audit review.

Note 4: *In 2013-14, the four B/Ds spent \$3.46 billion (FEHD: \$1.63 billion, LCSD: \$1.15 billion, DH: \$0.36 billion and EDB: \$0.32 billion), i.e. 48% of the total expenditures of \$7.18 billion incurred under expenditure Subhead 111. These four B/Ds were among the top five B/Ds incurring such expenditure.*

PART 2: SOURCING OF SERVICE PROVIDERS

2.1 This PART examines the sourcing of service providers by the selected B/Ds through the use of different procurement procedures. The following issues are discussed:

- (a) the hiring of service contractors through limited tenders (paras. 2.2 to 2.39);
- (b) the concentration of service contracts in a limited number of contractors (paras. 2.40 to 2.48); and
- (c) the need to use proper procurement procedures in accordance with SPRs (paras. 2.49 and 2.50).

Hiring services through open tendering is a preferred option

2.2 According to the SPRs, competition is a reliable safeguard against bidders overcharging and holding Government to ransom. In order to achieve best value for money and maintain open and fair competition, the SPRs stipulate that Government procurement exceeding \$1.43 million (for goods and services — Note 5) in value should normally be done by open tenders where all interested suppliers/service providers are free to submit their tenders. Only under exceptional circumstances are B/Ds allowed to use limited (single or restricted) tenders in Government procurement.

2.3 Since July 2013, B/Ds have the delegated authority to establish their Departmental Tender Committees (DTCs — Note 6) to approve the award of contracts through tenders with value not exceeding \$5 million without going through the GLD

Note 5: *The term “services” in this context excludes services for construction and engineering works.*

Note 6: *The DTC, chaired by a directorate officer not lower than D2 rank who shall be at least one rank higher than the chairman of the B/D’s Tender Assessment Panel, comprises not less than three persons.*

Tender Board (Note 7). The GLD Tender Board is responsible for the award of contract through tenders with value greater than \$5 million but not exceeding \$15 million. For tenders with value exceeding \$15 million, the Central Tender Board (CTB — Note 8) is responsible for reviewing B/D's tender assessments and advising the Permanent Secretary for Financial Services and the Treasury (Treasury) on the acceptance of tenders and award of contracts, and gives advice to B/Ds for future guidance where appropriate.

Circumstances under which limited tendering can be used

2.4 Under limited tendering, tenders are invited from only one (i.e. single tendering) or a limited number of contractors/suppliers/service providers. According to SPR 325, limited tender procedures shall only be used in circumstances when open competitive tendering would not be an effective means of obtaining the requisite stores or services, for example where there is:

- (a) extreme urgency brought about by events unforeseeable by the procuring department; or
- (b) no reasonable alternative or substitute for reasons such that the stores or services can be supplied or provided only by a particular contractor/supplier/service provider.

2.5 Limited tender procedures shall only be initiated with the prior approval of the Permanent Secretary for Financial Services and the Treasury (Treasury), the Director of Government Logistics or her staff, as the case may be. The B/Ds shall

Note 7: *The GLD Tender Board, appointed by the Secretary for Financial Services and the Treasury under authority delegated by the Financial Secretary, is chaired by the Director of Government Logistics and comprises the Deputy Director of Government Logistics, Controller (Supplies Management) and Senior Treasury Accountant of the GLD.*

Note 8: *The CTB, appointed by the Financial Secretary, is chaired by the Permanent Secretary for Financial Services and the Treasury (Treasury) and comprises the Director of Government Logistics, Permanent Secretary for Development (Works) or representative, a legal advisor at a rank not lower than Deputy Principal Government Counsel and Deputy Secretary for Financial Services and the Treasury (Treasury).*

Sourcing of service providers

advise tenderers invited to submit their tenders in the same manner as open or selective tender procedures. Tenderers shall not be informed that tenders are being invited on a limited tendering basis.

Use of limited tenders by the four selected B/Ds

2.6 Audit reviewed the service contracts awarded by the four B/Ds through tenders and noted the position as shown in Table 1. It can be seen that as at March 2014, the DH had awarded three contracts through single tendering with contract values totalling \$113 million and the EDB had awarded one contract through single tendering with a contract value of \$327 million.

Table 1
Contracts awarded through tendering
(31 March 2014)

B/D	Through limited tendering		Through open tendering	
	No. of contracts	Contract value (\$ million)	No. of contracts	Contract value (\$ million)
DH	3	113 (single tender – Note)	27	173
EDB	1	327 (single tender)	18	122
LCSD	1	6	136	4,221
FEHD	—	—	140	3,884

Source: Audit analysis of GLD records

Note: The contract value included a \$83 million single-tender contract awarded by the DH in March 2014 for provision of screening services at the Hong Kong International Airport from April 2014 to March 2016 (i.e. Contract A3 mentioned in para. 2.7). The remaining contract value of \$30 million covered two single-tender contracts (i.e. Contracts A1 and A2 mentioned in para. 2.7) up to 31 March 2014.

Remarks: The contracts in force as at March 2014 may cover different contract periods.

In the light of the significant contract values involved in limited tendering, Audit examined all the four single-tender contracts, i.e. three in respect of the DH (Contracts A1 to A3 with contract value of \$113 million in total) and another for the EDB (Contract B3 with contract value of \$327 million).

Health screening services at the Hong Kong International Airport

Background

2.7 The contract value of \$113 million included a \$83 million single-tender contract awarded by the DH in March 2014 for the provision of screening services at the Hong Kong International Airport (HKIA) from April 2014 to March 2016 (i.e. Contract A3). The remaining contract value of \$30 million covered two single-tender contracts (i.e. Contracts A1 and A2) up to 31 March 2014. Since 2003, the DH has entered into single-tender contracts repeatedly with Contractor A (Note 9) to provide temperature screening service for visitors, and in recent years for inbound visitors only, at the HKIA (see Photographs 1 to 3). The two more recently completed contracts covered the period from April 2012 to March 2014 (Contract A1) and September 2013 to March 2014 (Contract A2 — Note 10). Since April 2014, the temperature and pregnant visitors screening services have been combined into a single contract (Contract A3). Appendix A shows a chronology of key events for the single-tender contracts awarded to Contractor A.

Note 9: *Contractor A is a private company established in 1997 as a subsidiary jointly owned by the Government (49% share) and a statutory body (51%) which is wholly owned by the Government. Contractor A is primarily set up for provision of aviation security related services, including aircraft security services, boarding gate security controls, access controls and guarding services to various facilities operators at the airport.*

Note 10: *In September 2013, owing to the increasing number of pregnant visitors, the DH entered into Contract A2 with Contractor A to provide a pregnant visitors screening service. The service included screening pregnant visitors, directing suspected pregnant visitors to the designated immigration counters for examination and travel document inspection.*

Photographs 1 to 3

Health Screening services at the HKIA

Photograph 1



Photograph 2



Photograph 3



Source: DH records

Significant increase in contract value and hourly charge rate

2.8 Audit noted that the hourly charge rate for the provision of Health Screening Assistants by Contractor A was quite stable from 2003 to 2009. However, the contract value and the hourly rate in the more recent contracts with Contractor A for the provision of health screening services had kept on increasing. Details are shown in Tables 2 and 3 respectively.

Table 2

**Contract value on provision of health screening services
(July 2003 to March 2016)**

Year	Service period	Service duration (a) (Month)	Contract value (b) (\$ million)	Monthly charge (c) = (b) ÷ (a) (\$ million)
2003	3 Jul 2003 to 2 Nov 2003 (Note 1)	4	—	—
	3 Nov 2003 to 2 Jul 2004	8	10.4	1.3
2004	3 Jul 2004 to 31 Mar 2005	9	9.6	1.1
2005	1 Apr 2005 to 30 Sept 2005	6	2.8	0.5
	1 Oct 2005 to 31 Mar 2006 (Note 1)	6	2.8	0.5
2006	1 Apr 2006 to 31 Mar 2007	12	5.5	0.5
2007	1 Apr 2007 to 31 Mar 2008	12	6.5	0.5
2008	1 Apr 2008 to 31 Mar 2009	12	7.6	0.6
2009	1 Apr 2009 to 31 Mar 2010	12	9.1	0.8
	26 May 2009 to 1 Nov 2009 (Note 2)	5.3	8.0	1.5
	2 Nov 2009 to 31 Mar 2010 (Note 2)	5	3.4	0.7
2010	1 Apr 2010 to 31 Mar 2012	24	22.7	0.9
2012	1 Apr 2012 to 31 Mar 2014 (Contract A1)	24	28.6	1.2
2013	16 Sep 2013 to 31 Mar 2014 (Contract A2)	6.5	2.0	0.3
2014	1 Apr 2014 to 31 Mar 2016 (Contract A3)	24	82.9	3.5

Source: DH records

Note 1: After the outbreak of the Severe Acute Respiratory Syndrome in 2003, the DH engaged Contractor A to provide temperature screening, health declaration form (suspended in December 2009) and health information leaflet distribution (suspended in June 2010) services at the HKIA. Owing to the unpredictable development of the Severe Acute Respiratory Syndrome, the DH arranged short-term contracts until 2005.

Note 2: Owing to the outbreak of Human Swine Influenza, the DH awarded two additional contracts, covering the period from 26 May 2009 to 31 March 2010, for provision of health declaration form collection service (with service suspended in December 2009).

Sourcing of service providers

Table 3
Single-tender contracts for provision of
health screening services by Contractor A at HKIA
(April 2012 to March 2016)

	Contract A1	Contract A2	Contract A3
Service	Temperature screening	Pregnant visitors screening	Temperature and pregnant visitors screening
Service period	1.4.2012 – 31.3.2014 (24 months)	16.9.2013 – 31.3.2014 (6.5 months)	1.4.2014 – 31.3.2016 (24 months)
Contract value	\$28.6 million	\$2.0 million	\$82.9 million
Contract value per month	\$1.2 million	\$0.3 million	\$3.5 million
Daily man-hours provision:			
(a) Assistant	618 hours	68 hours	833 hours (Note 1)
(b) Supervisor	24 hours	17 hours	42.5 hours
Contract cost per man-hour (Note 2)	\$61	\$119	\$130
Staff education level required for Assistant according to:			
(a) service specifications	Secondary 3	Secondary 5 (Note 3)	Secondary 3 (Note 3)
(b) contractor's recruitment criteria	Same as above	Same as above	Secondary 5

Source: Audit analysis of DH records

Note 1: The daily provision of Assistants (833 man-hours) includes 68 man-hours (8%) catered for pregnant visitors screening.

Note 2: The contract cost per man-hour was calculated by dividing the contract value per day of operation with the number of daily man-hours provided under each contract.

Note 3: In Contract A2, the DH set the education level required for Assistants at Secondary 5 having regard to the service requirement to communicate with foreign visitors. However, in Contract A3, the DH re-set the education level required in the service specifications to Secondary 3. On enquiry, the DH informed Audit that the re-setting to Secondary 3 in Contract A3 was based on its experience from the operation of Contract A2.

2.9 As shown in Table 3, the monthly charge for temperature screening and pregnant visitors screening in Contract A3 had increased from \$1.5 million (\$1.2 million in Contract A1 and \$0.3 million in Contract A2) to \$3.5 million in Contract A3, or an increase of 130% even though the daily man-hours provision only increased by 20%. In Contract A3, the hourly charge rate for Assistants was 2.2 times the rate used in Contract A1 for temperature screening. Hence, the contract value had increased from \$30.6 million (\$28.6 million in Contract A1 and \$2 million in Contract A2) to \$82.9 million in Contract A3.

Tender negotiation with Contractor A

2.10 **Contract A2.** As outlined at Appendix A, the DH received a tender from Contractor A in relation to the tender for Contract A2. During the review of the tender offer, the DH noted a significant increase in the charge rates for the Assistants engaged for pregnant visitors screening and requested Contractor A to provide information on the proposed charge basis. In August 2013, Contractor A replied that:

- (a) it was not appropriate for them to give a detailed breakdown of their operating costs;
- (b) there were also indirect staff costs and operating overheads. The former related to officers at Security Inspector rank and above who were responsible for the supervision and management of the Security Officers, as well as the support and training of staff, whilst the latter covered costs incurred in the provision of uniform and equipment, accommodation, transport, etc.;
- (c) the prices quoted in Contract A2 had accurately reflected their total costs (comprising direct and indirect staff costs and operating overheads) plus a 5% mark-up to take account of the additional administrative work arising from the higher and more stringent staff criteria and requirement specified in the tender; and
- (d) in view of their good and long-standing partnership with the DH, Contractor A agreed to waive the 5% mark-up.

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As a result of the tender negotiation, the contract value of Contract A2 was reduced from \$2.1 million to \$2 million. Audit found no records which indicated that the DH had further negotiated with Contractor A since the receipt of the above information. In the event, Contract A2 (for pregnant visitors screening) was entered with Contractor A at a value of \$2 million. The hourly charge rate for Assistants in Contract A2 was 1.9 times the rate used in Contract A1 for temperature screening.

2.11 **Contract A3.** Following the receipt of Contractor A's offer in February 2014, the DH requested Contractor A to provide justifications for the charge rates proposed for Contract A3. In late February and early March 2014, Contractor A replied that:

- (a) the charge rates were worked out on a cost-recovery basis;
- (b) the charge rate under Contract A1 was significantly below cost recovery and a comparison between the offered rate for the next two years with those under Contract A1 was unrealistic;
- (c) Contractor A was primarily set up for the provision of aviation security related service, and all recruitment criteria and policies were decided on such basis. Contractor A's recruitment requirement for Assistants had been adjusted from Secondary 3 to Secondary 5 level;
- (d) it had experienced substantial increases in overhead such as double-digit increases in medical insurance, uniform and accoutrement expenditures; and
- (e) the new requirement in Contract A3 for the provision of additional manpower for meal break reliefs had increased their staff cost by 14%.

2.12 According to the tender report submitted by the DH to the CTB in March 2014, the DH considered prices quoted by Contractor A for Contract A3 were fair and reasonable given Contractor A's explanations in paragraph 2.11.

Significantly higher salary rates in comparison with other control points

2.13 Audit noted that in 2013, the DH had similarly contracted out the health screening services at two other boundary control points, namely the Shenzhen Bay Port and Man Kam To (Contract A4 — Note 11), and the Kai Tak Cruise Terminal (Contract A5). In comparison, the scope and nature of temperature screening services under Contracts A3, A4 and A5 are generally similar (see Table 4), although they operate in different environments. In response to Audit's enquiry, in September 2014, the DH responded that the difference in hourly rates charged by the contractors under Contracts A3, A4 and A5 may be due to different cost factors, such as provision of office space and accessibility of work locations, adopted in these contracts. Whilst these might have accounted for the differences to a certain extent, Audit noted that Contracts A4 and A5 were let through open tendering whereas Contracts A1 to A3 were let by single tenders. With Contract A3 which involved a contract value of \$82.9 million, the DH had not obtained cost breakdown from Contractor A to support the latter's calculation of the hourly charging rates.

2.14 With Contracts A4 and A5 which were let through open tendering, the DH received five and nine conforming offers respectively. Audit compared the hourly rates charged by Contractor A in Contract A3 with that charged by the two other contractors in Contracts A4 and A5, and noted that the hourly rates charged in Contract A3 roughly doubled the rates charged for similar services at the boundary and the cruise terminal (see Table 4).

Note 11: *Prior to the use of outsourcing, the DH engaged non-civil service contract staff to provide health screening services in all boundary control points. In consideration of the scale and structure of different boundary control points, in August 2013, the DH decided to carry out the first batch of outsourcing arrangements in Shenzhen Bay Port and Man Kam To Boundary Control Points.*

Table 4

**Comparison of contracts for
provision of health screening services at various control points**

	Contract A3	Contract A4	Contract A5
Control point	Airport	Boundary	Cruise terminal
Service	Temperature and pregnant visitors screening	Temperature and pregnant visitors screening	Temperature screening
Type of tender	Single tender	Open tender	Open tender
Number of conforming offers received	One	Five	Nine
Service period	1.4.2014 – 31.3.2016 (24 months)	1.12.2013 – 30.11.2015 (24 months)	1.6.2013 – 31.5.2015 (24 months)
Contract value	\$82.9 million	\$51.1 million	\$2.7 million
Daily man-hours provision:			
(a) Assistant	833 hours	1,019.5 hours	127.5 hours
(b) Supervisor	42.5 hours	53 hours	8.5 hours
Contract cost per man-hour	\$130	\$65	\$55
Staff education level required for Assistant according to:			
(a) service specifications	Secondary 3	Secondary 3	Secondary 3
(b) contractor's recruitment criteria	Secondary 5	Secondary 3	Secondary 3

Source: Audit analysis of DH records

Risk of paying a higher price for the health screening services

2.15 According to the service specifications of Contract A3, the DH has required the Assistants providing health screening services at the HKIA to have attained at least Secondary 3 education level, which is the same education level

requirement for all Assistants working at boundary control points and the cruise terminal (see Table 4). However, Contractor A informed the DH that their recruitment requirement for such Assistants was Secondary 5 level (see para. 2.11(c)) and with Contract A3 being a single tender, the DH had no alternatives but accepted the use of Assistants with an education level of Secondary 5 level which was higher than the requirement standard set out in the service specifications and higher than that in Contracts A4 and A5. The DH estimated that the increase in service charge owing to Contractor A's higher entry requirement was around \$30.4 million for the 24-month contract period.

2.16 In response to Audit's enquiry, in October 2014, the Security Bureau (SB) informed Audit that:

- (a) the business of Contractor A was conducted with the principal objective of maintaining security at the airport in the public interest and not of generating profits for distribution to the shareholders. In this regard, their charges did not aim to generate profits, but only to recover the total costs incurred for service provision and operating the company; and
- (b) according to Contractor A, the substantial increase in the charging rate of Contract A3 as compared to Contracts A1 and A2 was mainly due to the following:
 - (i) the hourly service rate in Contract A1 was substantially below cost recovery level because a detailed cost analysis was not performed given the time constraint. Revisions in charges in subsequent contracts were therefore necessary to fully recover the costs;
 - (ii) the expansion of service scope in temperature screening (as entailed by a substantial increase in the number of passengers at the airport) and contract terms in Contract A3 had led to a substantial increase in the number of staff requested by the DH from Contractor A; and
 - (iii) between the contracts, Contractor A had introduced catch-up pay to reduce the high turnover rate of staff, and implemented annual salary adjustment. Qualifications and requirements of their staff had also been upgraded, which resulted in higher staff costs.

Need to review the use of single tenders to obtain health screening service

2.17 As early as September 2003, in giving its approval for the DH to use single tendering, the FSTB stated that, if security consideration was not overriding:

- (a) there was a case for the DH to seriously explore the feasibility of inviting open tenders for the health screening service, which did not seem to be highly skilled;
- (b) single tendering was a tide-over measure; and
- (c) urgency would be the only reason to justify single tendering.

2.18 In connection with the security issue, the DH had also sought advice from the SB. In September 2003, the SB advised the DH that:

- (a) the employment of Contractor A for health screening at the HKIA was highly preferred from the security point of view; and
- (b) the use of other outside agencies would create vulnerability in the security system at the airport and inevitably Contractor A's involvement would be necessary to reduce the risk.

In response to the DH's enquiry, in September 2013, the SB advised the DH that it was preferable to continue engaging Contractor A in providing the services in order to provide better assurance to aviation security of Hong Kong as a whole.

2.19 In February 2014, when approving the invitation of a single tender from Contractor A for Contract A3, the FSTB indicated that the approval was subject to the condition that Contractor A was the only suitable agency in the market for the provision of the required services on aviation security grounds.

2.20 In March 2014, when considering the DH's tender report for Contract A3, the CTB noted that the health screening services required in the contract were not the core business of Contractor A, and questioned whether single

tender should continue to be adopted for this contract in future. The CTB suggested that the DH should explore the possibility of letting out the contract by open tender in future with a view to enhancing competition.

2.21 Before proceeding with awarding Contract A3 which is a mission-critical and high-value contract, Audit however noted no documentary evidence showing that the DH had conducted market research to ascertain the number of potential bidders and their security risk profiles for the provision of the required services in line with SPR 350 (Note 12). In contrast, Audit noted that in the two open tender exercises for Contracts A4 and A5 (see Table 4 in para. 2.14), the DH had obtained five and nine conforming offers respectively. This indicates the availability of potential bidders in the market.

2.22 In response to Audit's enquiry on the justification for continuing with the single-tender procurement for Contracts A1 to A3, in October 2014, the SB informed Audit that:

- (a) the Hong Kong Special Administrative Region, through the membership of the People's Republic of China in the International Civil Aviation Organisation, was obliged to maintaining the high aviation security standards in compliance with aviation security standards and recommended practices established by the Organisation;
- (b) in view of the security risks associated with the international aviation industry, and in view of the serious potential consequences associated with these security risks, the HKIA needed to maintain security standards which were generally higher than other land or sea control points; and
- (c) since 2003, the SB had been maintaining the policy that the provision of such services by Contractor A was highly preferable in view of the importance of safeguarding the overall security at the airport. The use of

Note 12: *According to SPR 350(e), for mission-critical or high-value contracts, departments may consider conducting a market research or non-binding express of interest exercise to better understand the goods or services likely to be available in the market, technological trends, number of potential bidders, etc. Such information is useful to ensure proper design of the mandatory and desirable features in order to obtain responsive and competitive tenders.*

other outside agencies might increase the risks in the security system. Relevant B/Ds would continue to adopt measures that were necessary and appropriate in maintaining such high security standards at the airport.

2.23 Audit notes the SB's explanations, but also observes that apart from Contractor A which provides aviation security controls such as access control to restricted areas and baggage screening, various other companies from the private sector also provide different services (e.g. aircraft cabin cleansing, passenger escort and courier services) in airport restricted areas.

2.24 Given the significant increase in contract value for the airport health screening services (particularly with the high contract cost per man-hour at the HKIA as compared with similar contracts at other boundary control points and the Kai Tak Cruise Terminal, as shown in Table 4 in para. 2.14), Audit considers that the DH needs to critically assess all relevant factors, including the justification for accepting the provision of Assistants at Secondary 5 education level at a higher cost as compared with Secondary 3 level at other control points, during its future tender/contract negotiations with Contractor A. In the long term, it should determine an appropriate procurement strategy, balancing the need to obtain cost-effective services on one hand and the risk of aviation security on the other hand.

Language and Mathematics Basic Competency Assessment

Background

2.25 Between December 2000 and January 2011, the EDB had entered into three consecutive single-tender contracts (Contracts B1 to B3) with Contractor B for the development of the Basic Competency Assessment (BCA) in key learning areas of the three subjects, namely Chinese Language, English Language and Mathematics. The BCA was one of the proposals put forward by the Education Commission in its Report on Reform Proposals for the Education System in Hong Kong published in September 2000 to enhance the effectiveness of the assessment mechanisms in facilitating learning and teaching and accepted by the Chief Executive in the 2000 Policy Address.

2.26 Through the BCA, the concept of basic competency, which represents the essential part of the curriculum, was introduced to schools and the public as the minimally acceptable level of knowledge and skills from which a student should acquire in order to progress to the next Key Stage without extra learning support. The three Key Stages are at Primary 1 to 3 (KS1), Primary 4 to 6 (KS2) and Secondary 1 to 3 (KS3) levels.

2.27 The BCA comprises two programmes, namely the Student Assessment (SA) and Territory-wide System Assessment (TSA) programmes, as shown below:

SA programme

1. It is a voluntary on-line assessment programme accessed by schools at any time during the school year to diagnose individual students' basic competency in the three subjects (Chinese Language, English Language and Mathematics) at levels from KS1 to KS3, while giving timely support and guidance to students to attain basic standards. As a quality assessment tool for web-based learning and teaching support, the SA system allows teachers to use the assessment items on the web-based central assessment item bank to create assessments to address students' needs and monitor their learning progress.
2. The main objective of the SA is to provide one of the various assessment tools to be used in the classroom or at home that could provide feedback for teachers to evaluate the progress of students so that early intervention or improvement in teaching could be made. It provides instant feedback to students and teachers through computerized marking and instant reports on students' performance after they complete the on-line assessment.

TSA programme

3. It is a mandatory, large-scale, territory-wide and secure assessment programme centrally administered and conducted in paper and pen mode in schools in Hong Kong for students at Primary 3, Primary 6 and Secondary 3 levels. It aims to gauge the performance of students on the three subjects (Chinese Language, English Language and Mathematics) at the end of the three Key Stages against a defined standard of basic competency. The TSAs for Primary 3, Primary 6 and Secondary 3 are conducted annually covering oral assessments for Chinese Language and English Language on a sampling basis and written assessments on the three subjects.

(to be continued)

Sourcing of service providers

(Cont'd)

4. Reports on the territory-wide overall performance of schools and individual school reports with aggregated information on students' performance of the three subjects at basic competency are provided annually for the reference of schools to improve learning and teaching and for the Government to review support strategies and curricula. Together with other school-based assessment data, the TSA and SA would thus help promote the culture of Assessment for Learning (i.e. using the assessment to collect evidence of student learning as an integral part of the learning and teaching cycle for providing timely information for students to enhance their learning and enable teachers to review and improve their teaching) in schools.

2.28 A summary of the three BCA contracts covering the period from December 2000 to December 2014 are shown in Table 5.

Table 5

**Single-tender contracts for the development of the BCA
(December 2000 to December 2014)**

Contract	Contract period	Duration (Year)	Contract value (\$ million)		
			SA	TSA	Total
B1	December 2000 to December 2006	6.0	104	117	221
B2	May 2007 to December 2010	3.5	77	176	253
B3	January 2011 to December 2014	4.0	99	220	319
	Total	13.5	280	513	793

Source: EDB records

Justification for single tenders to acquire BCA services

2.29 According to the SPRs, single tendering could only be used when only one contractor could provide the required services. In seeking approval from the FSTB to select Contractor B through single tendering, the EDB has provided the following reasons:

- (a) Contractor B is the most experienced and respected local institution in the development of large-scale examinations and assessments;
- (b) it is the only institution in Hong Kong that has the required experience as well as technical and subject expertise in developing and administering large-scale territory-wide examinations and assessments;
- (c) the school sector requires certainty and stability in the administration of the assessment programmes;
- (d) besides technical know-how, it is imperative that the institution which administers the BCA should have a deep knowledge of the local education system and be able to inspire the school sector with confidence;
- (e) the services to be provided under the new contract should be highly compatible with those provided under the previous contracts to ensure continuity and avoid abortive work. No other local institutions can undertake this project in a seamless manner; and
- (f) overseas testing institutions are not suitable alternatives since they are unfamiliar with the local educational context.

2.30 When considering Contract B1, the FSTB had requested the EDB to provide further clarification about the nature and scope of the project as well as the single tendering approach. The FSTB had also expressed reservations about the single tendering approach regarding Contracts B2 and B3. In February 2007, when seeking approval from the FSTB for the use of single tender for Contract B2, the EDB undertook to conduct a review to examine the tendering arrangements near the end of Contract B2. In May 2010, the EDB informed the FSTB that it had conducted the review and considered it most appropriate and effective to continue with single tendering. However, the EDB informed Audit in July 2014 that no

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separate review report had been prepared, but the review results were all incorporated into the relevant documents for reporting to and seeking approval from the FSTB in respect of Contract B3.

Tender negotiations with Contractor B

2.31 Although competitive tendering was not conducted, Audit noted that for Contracts B2 and B3, the EDB had negotiated the contract price with Contractor B. The audit findings are set out in paragraphs 2.32 to 2.37.

2.32 **Contract B1.** In December 2000, the EDB informed the FSTB that comparison of prices with similar contracts could not be made since it was the first time that the EDB invited a single tender to develop the BCA. Despite this, the EDB estimated the cost for the BCA service to be about \$217 million by making reference to the costs incurred in other EDB's projects (Note 13). As the tender price for Contract B1 was \$185 million, the EDB considered the tender price reasonable. Therefore, no tender negotiation was conducted for Contract B1.

2.33 **Contract B2.** The tender price received from Contractor B for Contract B2 was \$291 million. In view of the substantial increase of \$106 million as compared with Contract B1, in May 2007, the CTB requested the EDB to conduct tender negotiation with Contractor B.

2.34 In response to Audit's enquiry, in September 2014, the EDB informed Audit that:

- (a) under Contract B2, Contractor B had to fulfill the substantial increase in the required services as set out in the tender invitation document;

Note 13: *These included the Hong Kong Attainment Test, Secondary School Places Allocation System and Academic Aptitude Test.*

- (b) the IT infrastructure supporting the BCA (Note 14) would be redeveloped;
- (c) the SA question bank would be expanded from 8,000 to 20,000 items to meet the aspiration of the school sectors; and
- (d) since the TSA was fully rolled out, the provision of assessment literacy training for teachers at primary and secondary levels would be required.

2.35 Taking into account the above, in May 2007, the EDB informed the CTB that according to Contractor B, there was no room for downward adjustment unless the EDB reduced the scope of the services required. The EDB considered that the contract price was reasonable. In the same month, the Permanent Secretary for Financial Services and the Treasury (Treasury), on the recommendation of the CTB, approved the award of Contract B2 to Contractor B at a value of \$291 million.

2.36 **Contract B3.** In view of another significant increase of tender price (\$347.5 million) over the contract value of Contract B2 (\$291 million), the EDB advised that it had conducted rounds of tender negotiation with Contractor B in August 2010. In the negotiation, the EDB considered that the tender price was on the high side, with almost 20% increase in cost but reduced service requirements in the SA programme (i.e. no system redevelopment, reduced output of SA items, no requirement for introducing computerised adaptive tests and Assessment Literacy Training for teachers) when compared with Contract B2.

2.37 In October 2010, the EDB informed the FSTB that according to Contractor B, the increase was mainly due to increase in:

Note 14: *This covered both the SA and TSA for which the system would be redeveloped as a multi-tier system with: (a) web servers to handle Internet connections with teachers and students; (b) application servers comprising a number of customised programs for creating (including item selection and presentation, scheduling of assessment) and processing assessment (i.e. marking, result reporting and data analysis); and (c) database servers to provide a centralised item bank of the three subjects and storage for assessment results and students data.*

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- (a) the revised overheads charging rate (from 10% to 20% of direct cost) as a result of Contractor B's corporate policy change;
- (b) administration cost due to an inclusion of commercial office rental for the full contract period; and
- (c) staff cost caused by an adjustment in cost structure of SA item setting.

Following negotiations with Contractor B, in September 2010, Contractor B offered a special discount and reduced some of the costs, while producing more SA items. The tender price was reduced from \$347.5 million to \$327.4 million. According to the tender report submitted to the CTB in October 2010, the EDB considered that the tender price was fair and reasonable.

Need to review the continued use of single tender for SA programme

2.38 As mentioned in paragraph 2.29(a) and (b), the EDB considers that Contractor B is the only service provider which can provide the BCA service having regard to its knowledge about the local school curriculum and its ability to hold public examinations in school centres. However, the increasing cost of the three BCA contracts (see Table 5 in para. 2.28) is a cause for concern. In September 2014, the EDB informed Audit that:

- (a) the launch of the BCA in 2000 was to introduce a rather new concept of basic competency to the education sector through the implementation of the SA and TSA and to change the culture of assessment;
- (b) given that the SA and TSA came in a package under the BCA especially when the BCA was at an early development stage, engaging one single institution to implement both assessment programmes was considered more appropriate and effective in ensuring consistency in defining the basic competencies for different Key Stages, and hence in the quality of assessment items;
- (c) the IT infrastructure for the BCA project was redeveloped under Contract B2 in 2007 to enhance the user-friendliness of the systems;

- (d) after ten years of development, the EDB however considered that:
 - (i) the basic competencies in the three subjects had already been well defined;
 - (ii) the school sector had also become well familiar with the concept of basic competency and had gradually experienced a change in the culture of assessment; and
 - (iii) it was an opportune time to explore whether other local or overseas institutions would have the capability to develop quality SA items with a larger variety while Contractor B would continue to assume a coordinating role in running the IT system;
- (e) in 2012, the EDB separately contracted out the development of KS3 (Secondary 3) English Listening and Speaking task to another service provider as a pilot project to assess the feasibility of engaging other service providers in the development of SA items; and
- (f) the EDB was planning to upgrade the SA to another on-line assessment bank. Development of new SA items would no longer be required while only minimal support to maintain the SA system in this transitional period would be required under the next BCA contract. In case the upgraded assessment bank would need to be managed by a service provider, open tender would be considered.

2.39 Audit welcomes the EDB's initiative in paragraph 2.38(e) and (f). Given that the SA programme mainly involves the development of competency assessment items and maintaining the SA system and database, Audit considers that with the passage of time, the justification for the continued use of single tender for the SA programme (bundled with the TSA) may diminish and it is time to consider separating the SA programme for procurement by open competitive tenders.

Limited number of service providers for major contracts

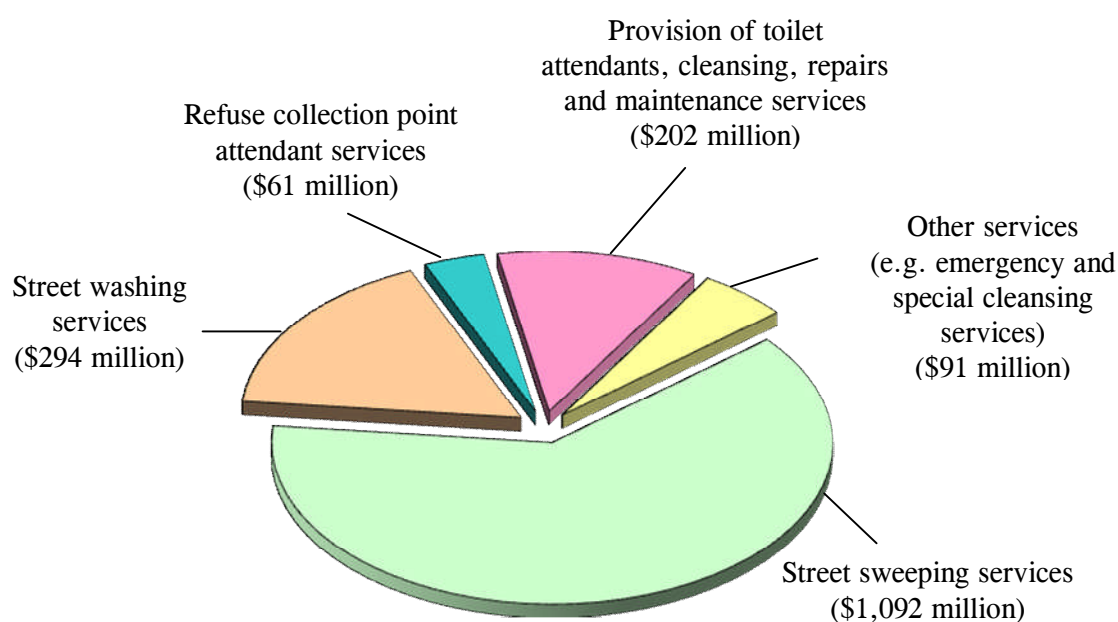
2.40 To enable B/Ds to establish a good tender framework, the Efficiency Unit has issued “A General Guide to Outsourcing” to promulgate the best practice principles to be followed throughout the tender process. According to the Guide, the tender process should not create obstacles to competition against the potential tenderers. B/Ds need to guard against over-reliance on a few dominant contractors as their under-performance or non-performance could lead to significant service disruptions. The SPRs warn B/Ds to avoid over-reliance on a single contractor and to enhance open and fair competition.

Provision of cleansing services by FEHD service providers

2.41 Audit noted that most of the FEHD’s cleansing services had been outsourced. As at June 2014, the FEHD had outsourced its street cleansing services in 19 districts under 25 two-year contracts at a total value of \$1,740 million, comprising different categories of services as shown in Figure 3.

Figure 3

Services specified in the street cleansing contracts



Source: FEHD records

2.42 While the street cleansing services were open to tender bids from service providers, a comparison of the two recent tender exercises indicated that the average number of tenderers per contract decreased from 4.1 to 3.6. The 25 existing contracts were awarded to five contractors, one of which was awarded 10 contracts with a total value of \$653 million (38% of \$1,740 million). Details are shown in Table 6.

Table 6
FEHD's street cleansing contracts
(June 2014)

Contractor	No. of contracts	Contract value (\$ million)
C1	10 (40%)	653 (38%)
C2	5	416
C3	5	310
C4	4	280
C5	1	81
Total	25	1,740

Source: Audit analysis of FEHD records

2.43 Audit noted that the CTB, in assessing the tenders, had expressed concerns about the risks of placing contracts in the hands of a few contractors and advised the FEHD on ways to enhance competition. For example, in considering the two contracts (\$106 million) for District A, the CTB noted the award of the contracts to Contractor C1 and recommended that the FEHD should consider restricting the number of contracts to be awarded to each tenderer for risk management purpose.

2.44 In response to Audit's enquiry, in September 2014, the FEHD informed Audit that the following measures had been taken to enhance competition and reduce the risk of over-reliance:

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- (a) splitting large contracts into smaller ones;
- (b) staggering tender exercises so that contracts could be let out in phases;
- (c) promoting tender exercises by means of wider publicity and tender briefing;
- (d) relaxing unnecessary mandatory/tender requirements;
- (e) avoiding assessment criteria and/or reducing the weighting of assessment criteria which were inherently in favour of the existing contractor; and
- (f) restricting the number of contracts to be awarded to the same tenderer if the tender involved more than one contract and were not subject to the WTO GPA.

The average number of tenders received per contract had been quite stable over the past years and there was no indication of a downward trend. The situation had kept on improving, with the number of the FEHD contracts held by Contractor C1 decreasing. As at September 2014, while the total number and value of contracts awarded remained at 25 and \$1,740 million respectively, Contractor C1 was awarded seven contracts (\$426 million), Contractor C2 six contracts (\$491 million) and Contractor C4 six contracts (\$432 million). The FEHD should continue monitoring the situation and take necessary measures to enhance competition, when appropriate, for the street cleansing services.

Provision of cleansing and supporting services in LCSD venues

2.45 As at March 2014, the LCSD had awarded 41 contracts for the provision of cleansing and supporting services to its venues at a total value of \$1,913 million to eight contractors. Audit noted that 78% (32 contracts) of these contracts were awarded to two contractors with a total value of \$1,780 million (93% of \$1,913 million). Details are shown in Table 7.

Table 7

**Provision of cleansing and supporting services in LCSD's venues
(March 2014)**

Contractor	No. of contracts	Contract value (\$ million)
D1	20	1,236
D2	12	544
D3	4	64
D4	1	55
D5	1	6
D6	1	4
D7	1	2
D8	1	2
Total	41	1,913

Source: Audit analysis of LCSD records

2.46 As shown in Table 7, 20 cleansing and supporting service contracts totalling \$1,236 million in value were awarded to one contractor (Contractor D1). In Audit's view, the concentration of cleansing and supporting service contracts for LCSD venues in two contractors requires close monitoring. Audit notes that in considering the award of two contracts (totalling \$328 million) to Contractor D1 in March 2013, the CTB noted that the contractor had a lion share of such service contracts and considered that the LCSD should, subject to the legal advice on the applicability of the WTO GPA on tenders of this kind, map out a tendering strategy with a view to avoiding over-reliance on a few service providers for the services. The CTB also requested the LCSD to revert to it with the review result before the tender exercise for the next batch of leisure venues was conducted.

Sourcing of service providers

2.47 In response to Audit's enquiry, in September and October 2014, the LCSD informed Audit that:

- (a) tendering exercises must be conducted in accordance with the law. As advised by the FSTB, B/Ds must take heed of the Department of Justice's advice on the possible risk of challenge against the restriction on the maximum number of contracts to be undertaken by the same contractor if such a restriction was not set on the basis of the assessment of the contractors' capability of undertaking the contracts concerned. After consulting the Department of Justice in April 2013, the LCSD had been following this policy and practice;
- (b) in May 2013, after obtaining the legal advice from the Department of Justice, the LCSD informed the FSTB that it would continue to adopt its practice (i.e. without a restriction on the number of contracts to be undertaken by the same contractor) pending the formulation and promulgation of new Government-wide policies and directives in this respect;
- (c) in restricting the number of awards to individual contractor(s), the LCSD would likely have to pay more in terms of the contract price and incur increased efforts in contract management in view of the larger number of contractors of various sizes; and
- (d) from risk management perspective, the LCSD had prepared a departmental contingency plan to tackle the problems of unforeseen cessation or disruption of services by contractors due to their failure in fulfilling the contractual obligations.

2.48 Since a large majority of the LCSD's cleansing and supporting services to its venues are contracted out to two contractors (see Table 7), Audit considers that the LCSD needs to critically review its tendering strategy, and where appropriate and feasible, consider the use of more contractors, thereby reducing the management risk of relying on several contractors to deliver the services.

Procurement procedures not always adopted to enhance competition

2.49 For purchases of services not exceeding \$1.43 million in value, B/Ds are allowed to invite quotations (Note 15). According to the SPRs:

- (a) services of similar nature are, in normal practice, consolidated in a single purchase or contract;
- (b) B/Ds should ensure that they do not evade the limits by dividing procurement requirements into instalments or by reducing the usual duration of contracts;
- (c) in making the procurement, B/Ds should consolidate requirements of services of similar nature as far as possible to achieve better economy of scale; and
- (d) B/Ds shall follow tender procedures when making purchases of stores and services exceeding \$1.43 million.

2.50 ***Repeated purchases exceeding \$1.43 million.*** From the contracts selected from the four B/Ds under review (see para. 1.9), Audit found that while some contractors provided same/similar services with a total value exceeding \$1.43 million, such services were not or could not be aggregated into a single contract to achieve better economy of scale and follow the tender procedures for procurement in accordance with the SPRs as illustrated in Cases 1 and 2.

Note 15: *According to the SPRs, the number of invitations for quotation required for procuring services with a value:*

- (a) *not exceeding \$50,000 is more than one quotation; and*
- (b) *exceeding \$50,000 but not exceeding \$1.43 million is not less than five written quotations.*

Case 1

1. Since 2001, the DH has adopted quotation procedures in procuring radiology services for different health clinics. According to the contract terms, the contractor shall provide designated radiologists who are registered Specialists in Radiology of the Medical Council of Hong Kong for the provision of precise professional diagnosis and reporting services on X-ray films/images or special X-ray examinations (with direct interaction with patients). The current six contracts were awarded to Contractor E (with three radiologists). Individual values of these six contracts were all below the quotation limit of \$1.43 million (see para. 2.49) with details shown below:

Contract (Note)	Period	Diagnosis and reporting service	Service location	Duration (Month)
E1	Dec 2012 – Jun 2014	X-ray film	Clinic A	18
E2	Dec 2012 – Jun 2014	Special X-ray examination	Clinic A	18
E3	Jan 2013 – Jul 2014	X-ray film/image	Clinic A	18
E4	Jun 2013 – Jun 2015	X-ray image	Clinic B	24
E5	Jan 2014 – Jan 2016	X-ray image	Clinic A/C	24
E6	Aug 2013 – Jul 2014	X-ray film (including courier service)	Contractor's office	12

Note: Contracts E1 to E3 and E6 were renewed and awarded to Contractor E in June 2014.

2. ***Inviting quotations from same list of radiologists.*** In the renewal exercises for each of the six contracts since 2008, quotations had been invited from the same list of some 20 radiologists. There are no documented records indicating why the DH only used the same list of radiologists for inviting quotations. Audit considers that the DH needs to update the quotation invitation lists more regularly.

3. In September 2014, the DH informed Audit that: (a) the DH made telephone calls to potential contractors from different channels (e.g. website of the Hong Kong Medical Council, Yellow Pages) to compile the invitation list, which was last updated in 2008; and (b) for more regular updates and telephone calls, the DH considered that it needed to balance the costs and benefits, and be mindful of possible complaints from the radiologists for repeated enquiries from the DH.

Case 1 (Cont'd)

4. ***Varying duration of Contract E3.*** For the renewal of Contract E3 which was due to expire in January 2011 (the first renewal), the DH found that the quotation received exceeded the quotation limit of \$1.43 million (see para. 2.49) and could not accept it. Having reviewed the operational requirement, the DH decided to shorten the service period from 18 to 12 months. Instead of inviting quotation again, the DH requested the contractor to confirm if he would provide the service for the revised period at the same rate, terms and conditions as he previously quoted. Following his confirmation, the contract value was lowered to below \$1.43 million for the revised 12-month period (till January 2012).

5. For the second renewal of Contract E3 for 12 months (January 2012 to January 2013), the DH accepted the lowest quotation received which was below the quotation limit of \$1.43 million. However, for the third renewal of Contract E3, the DH renewed at the value below \$1.43 million for a longer period of 18 months (January 2013 to July 2014) without documenting the reasons for extending the contract duration.

6. In September 2014, the DH informed Audit that:

- (a) for the first renewal of Contract E3, quotations were invited from the list of 19 radiologists. However, only one offer was received which quoted a rate 1.7 times of the rate of the expiring contract. Price negotiation was attempted but failed. Having considered that the price increase might be due to short-term fluctuation at that time, the DH decided to shorten the contract duration from 18 to 12 months;
- (b) for the second renewal of Contract E3, the rate quoted by the contractor dropped by 33% and the 12-month contract was awarded. For the third renewal, the 18-month contract was awarded as the rate quoted by the contractor only increased by 7%; and
- (c) the procurement strategy/process was designed after considering various factors, such as location of the clinics, avoidance of over-reliance on a single contractor, smaller value contracts could attract radiologists for more competitive pricing, and different service nature of the six contracts.

7. ***Need for review of procurement strategy.*** While individual values of Contracts E1 to E6 did not exceed the quotation limit of \$1.43 million, the aggregate value was 4.3 times of the limit. In Audit's view, the DH needs to review its procurement procedures with a view to enhancing competition and meeting the requirements of the SPRs.

Source: DH records

Case 2

1. Since 2006, the LCSD has procured special security management services quarterly to tackle noise nuisance problem at Park A. Through invitation for quotations, the contracts were awarded to a contractor who provided staff with past experience in disciplined services. The staff were required to work six hours a day in maintaining order at the park such as restricting the use of heavy duty sound equipment, and erection of sun umbrellas by the singing groups. In 2012-13 and 2013-14, the LCSD spent a total of \$5.4 million in hiring the services through repeated short-term contracts on a quarterly basis.

2. *Need to obtain competitive services through open tendering.* Audit noted that the LCSD had, since July 2013, planned to obtain the services at Park A through longer-term open tender contracts. However, up to September 2014, quarterly service contracts awarded through quotations were still in use. Audit considers that the LCSD needs to expedite action to obtain competitive services through open tendering as soon as practicable for Park A.

3. In response to Audit's enquiry, in October 2014, the LCSD informed Audit that the LCSD:

- (a) had been working closely with the District Council concerned and the district community with a view to identifying new innovative means to tackle noise nuisances. Hence, it was necessary for the LCSD to launch a number of measures as a pilot scheme and then evaluate the effectiveness of these measures before considering whether some measures should be implemented on a longer term basis; and
- (b) had decided to engage special security guards with working experience in disciplinary force with a view to stepping up the enforcement to control and contain singing activities at Park A. As these singing activities were very dynamic and reasonably localised, and the cost-effectiveness of the special security services had yet to be proven, the LCSD had to adopt a prudent approach by engaging such services on a short-term basis by invitation of quotations. After establishing that engagement of special security guards should continue, a long-term contract was being arranged to source the requisite services for Park A.

Source: LCSD records

PART 3: SPECIFICATION OF SERVICE REQUIREMENTS

3.1 This PART examines the specification of service requirements set by the selected B/Ds. The following issues are examined:

- (a) need to set out clearly service requirements in tender specifications (paras. 3.2 to 3.3);
- (b) need to reflect the FEHD's street washing service requirements accurately in tender specifications (paras. 3.4 to 3.9); and
- (c) setting of mandatory requirements specified in the LCSD's venue management contracts (paras. 3.10 to 3.19).

Need to set out clearly service requirements in tender specifications

3.2 Tender specifications define the requirements of the procuring departments and what the tenderers are expected to provide. According to the SPRs, tender specifications shall meet the basic Government procurement principles of transparency, openness and fairness. Specifications should contain sufficient information for the tenderers to determine the nature, scope and estimated quantity or value of goods or services required, their characteristics, standards to be met, performance under specified conditions and other relevant information in order to obtain conforming and competitive bids.

3.3 To assess how clear and accurate the service requirements are specified in the tender documents, Audit selected the FEHD's street washing service for review.

Need to reflect FEHD's street washing service requirements accurately in tender specifications

3.4 As highlighted in paragraph 2.41, the FEHD outsourced most of its street cleansing services to contractors. Under the street cleansing contracts, contractors are required to provide the street washing services by washing teams each comprising one supervisor-cum-driver and three cleansing staff. As at June 2014, the contract value of street washing services amounted to \$294 million (or 17%) of the total contract value of \$1,740 million for street cleansing contracts.

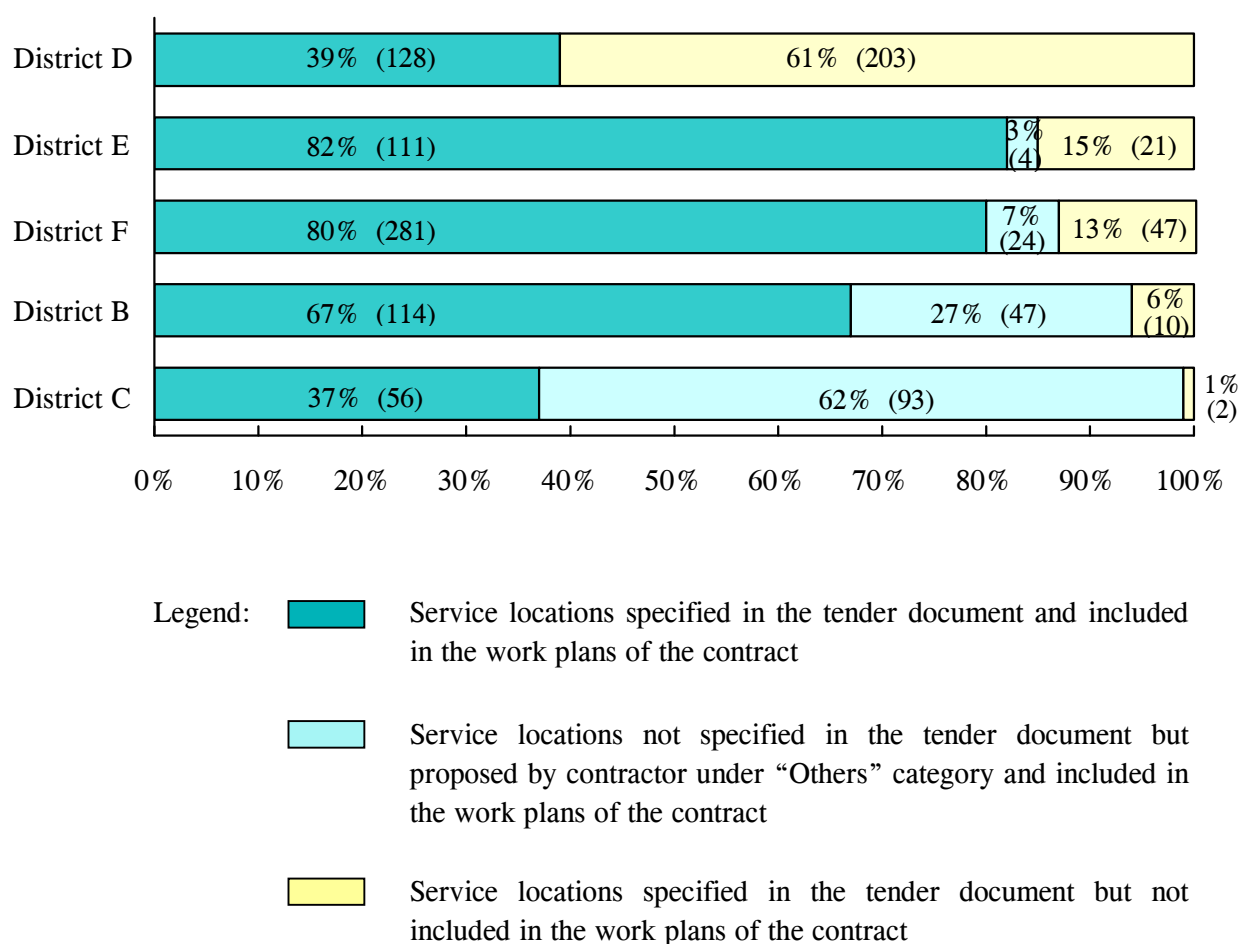
3.5 The requirements of street washing services, including service locations and frequency of service required for individual locations, are specified in the tender documents of the FEHD. Tenderers are required to propose detailed work plans with street washing schedules (Note 16) for the service requirements specified in the tender documents. Tenderers are also required to propose the number and posts of staff, number of street washing vehicles and their working hours for the work shifts specified in the tender documents and other proposed work shifts. Tender prices are based on the monthly rate derived from the hourly charge rate for the proposed resources (i.e. staff and vehicles) and the hours of services required/to be provided for the whole contract period. Tenders have to go through a competitive bidding which accords 70% weighting to price proposal and 30% to technical proposal. For the successful tenderer, the work plans become part of the contract with the Government.

3.6 Audit selected tender documents on the street washing services of five districts (Districts B to F) to compare the work plans of the contracts in force as at March 2014. The contract value of street washing services for these five districts was \$64 million. The contractors were required to provide 23 street washing teams with 92 staff (i.e. 69 cleansing workmen and 23 supervisor-cum-drivers) at a monthly rate of \$2.7 million. Audit noted that there were significant discrepancies, as shown in Figure 4, between the service locations specified in the tender documents and those provided in the work plans as proposed by the tenderers (see para. 3.5), which formed part of the contracts.

Note 16: *The street washing schedules provided by the tenderers in their work plans showed the routes of the service locations, times of arrival and departure for each location, water-filling times and meal break (if any).*

Figure 4

Discrepancies in service locations between the tender documents and the contractors' work plans (which formed part of the contracts)



Source: Audit analysis of FEHD records

Remarks: Figure in the bracket is the number of service locations.

3.7 For example, 61% of the service locations in District D specified in the tender documents for street washing were not included in the contractor's work plan of the contract. According to the specifications of service requirements, lanes and steps of streets are required to be washed by the washing teams. Despite these discrepancies in service locations between the tender documents and the contractor's work plan, the contract was awarded at a contract value of \$73 million to Contractor C2 who was the sole tenderer in the tendering exercise and had obtained a passing

Specification of service requirements

mark (Note 17) for the quality of its work plan. Audit noted that the same applied to the previous contract for District D, which was similarly awarded to Contractor C2, in which the majority of the locations as specified in the tender documents were not included in Contractor C2's work plan.

3.8 For fair competition, it is important when evaluating the street washing tenders to ensure that the service requirements as specified in the tender documents have been complied with before contracts are awarded to the service contractors. Audit considers that the FEHD needs to critically review the locations for street washing as specified in the tender documents to ensure that they are complete and well justified to meet the actual needs, and take measures to incorporate all required locations into the contracts awarded to the successful tenderers.

3.9 In response to Audit's enquiry, in September 2014, the FEHD informed Audit that it would:

- (a) remind all districts to critically review the locations specified for street washing in the tender documents to ensure that such locations were justified and met the actual needs;
- (b) set out these locations clearly in the tender documents and pay special attention to the relevant proposals in the work plans submitted by the bidders during the vetting of tenders and awarding of contracts; and
- (c) take measures to ensure that such locations were clearly set out in the contract awarded to the successful bidder.

Note 17: *Under the FEHD's marking scheme for tender assessment, Contractor C2 obtained 7.5 marks (maximum 30 and passing mark 7.5) for the quality of the work plan.*

Setting of mandatory requirements specified in LCSD's venue management contracts

3.10 According to the SPRs, mandatory features are those features that are so fundamental or essential to the acceptability of the tender that non-compliance with any of them will render the tender non-conforming. Desirable features are not standards or specifications that must be met but normally take the form of assessment criteria in the marking scheme and more technical scores will be given if the tenderer can provide more desirable features with performance better than the specified level. The SPRs require that in setting the tender specifications, B/Ds should guard against over-restrictive requirements.

3.11 Requirements more restrictive than necessary limit the ability of service providers in the market to compete with an incumbent. These might also have the effect of protecting existing service providers in the market from potential competition, thus reducing or limiting choices and potentially affecting prices. Audit selected the tender documents of the LCSD's management support services for sports centres, which specify at least three years of relevant experience in such services at recreational or sports facilities as mandatory requirements (see para. 3.14 below), for review.

Outsourcing the management support services of sports centres

3.12 As at 31 March 2014, the LCSD had 95 sports centres. The LCSD outsourced the management support services of 14 sports centres (including operating the computerised booking system, maintaining the sports equipment, providing cleansing and horticulture services) to one contractor (Contractor H) at a total value of \$130 million through four tender exercises.

3.13 Audit reviewed a tender exercise for outsourcing management support services of four sports centres. In April 2013, in addition to the nine sports centres already managed by Contractor H (as one was managed by another contractor at that time), the contracts for these four sports centres were awarded to Contractor H at a total value of \$44 million for a 36-month period from May 2013 to April 2016.

Specification of service requirements

3.14 According to the mandatory requirements specified in the tender documents, the tenderer must have:

- (a) at least three years of cumulative experience in the provision of management services at recreational or sports facilities within the past ten years prior to 1 March 2013; and
- (b) either:
 - (i) completed a contract with an annual contract value of not less than \$1.3 million in the provision of management services at recreational or sports facilities and the last one year of that contract must fall within the past three years prior to 1 March 2013; or
 - (ii) been performing as at 1 March 2013 a contract with the contract commencement date not less than one year prior to 1 March 2013 and with an annual contract value of not less than \$1.3 million in the provision of management services at recreational or sports facilities.

3.15 In response to the tender invitation, the LCSD received offers from six to seven tenderers for individual sports centres. However, only three to four tenderers met the mandatory requirements and were further evaluated in the technical and price proposal assessment.

3.16 In considering the tenders in April 2013, the CTB noted that:

- (a) there was a tenderer with rich experience in the provision of management services for heritage, educational and ecological facilities. The tenderer was not considered further by the LCSD as it failed to meet the mandatory requirement that the facilities should be recreational or sports related. The CTB suggested that the LCSD should review whether the experience required needed to be directly related to recreational or sports facilities with a view to enhancing competition in future tender exercises; and

- (b) Contractor H had a lion share of the contracts for the provision of management support services to the sports centres outsourced by the LCSD. The CTB considered that the competition in tenders of this kind was obviously not healthy and recommended that the LCSD should, from a risk management angle, map out a tendering strategy with a view to avoiding over-reliance on a few service providers for the services.

3.17 In December 2013, in recommending the approval for the award of contracts for three other sports centres for a 36-month period from February 2014 to January 2017 to Contractor H, the CTB reiterated its concern after noting the LCSD's view against restricting on the number of contracts awarded to the same contractor in future tender exercises. The CTB considered that the LCSD should critically consider how tender competition for these services, which were not covered by the WTO GPA, could be enhanced as it was not desirable to over-rely on a single contractor.

3.18 In response to Audit's enquiry, in September and October 2014, the LCSD informed Audit that:

- (a) the current mandatory requirements as mentioned in paragraph 3.14 were not excessive because the management support service contracts for the sports centres were complicated contracts involving heavy financial and human resources from the contractors, as well as requiring the contractors to possess the expertise of recreational and sports management (Note 18), to provide a holistic scope of services inclusive of all management duties (Note 19) in addition to security, cleansing and horticulture duties. The

Note 18: *This refers to the expertise of both hardware (facilities management, maintenance and operation) and software (supervision of recreation and sports coaches and instructors, checking of their qualifications as sports coaches and instructors, organisation and delivery of recreation and sports training programmes and activities to boost up utilisation of the sports centres and to increase revenue).*

Note 19: *The contractor has to deal with all operational matters (including handling of general emergencies as well as accidents of sports injuries) and public enquiries (including investigation and making replies to public complaints) without the presence or immediate guidance of any LCSD staff.*

Specification of service requirements

contractor had to be fully conversant with the management of recreational or sports facilities to ensure high performance to provide good services to the public and to upkeep the department's image;

- (b) in the past tendering exercises, there had been more than one qualified contractors (normally three to four), illustrating that the mandatory requirements had not pre-empted any other bidders. It was a special occurrence in the last round of tendering in 2013-14 that all of the 14 contracts were awarded to one contractor;
- (c) the LCSD had assessed from a risk management angle the scenario that only one contractor was awarded with all the contracts for the sports centres. It had devised a comprehensive contingency plan for districts to deal with the default of contractors in case of failure which was already in place for years and the services could be resumed within a reasonably short period of time. Of the 95 sports centres, only 14 (15%), which are geographically dispersed, were outsourced. The overall risk on the impact of service suspension upon the default of a contractor was minimal; and
- (d) the LCSD would review the mandatory requirements, including the relevant experience, and if appropriate consider whether there was room for relaxing the requirements so that the pool of qualified contractors could be expanded to enhance competition.

3.19 Audit notes the views of the CTB and the LCSD (see paras. 3.16 to 3.18). With the current situation that all the contracts for providing management support services to the 14 sports centres are awarded to only one contractor, Audit considers that there is a need for the LCSD to critically review whether it is possible to revise its mandatory requirements with a view to encouraging competition, increasing choices and avoiding over-reliance on a single contractor.

PART 4: MONITORING SERVICE DELIVERY

4.1 This PART examines the monitoring of service delivery by the selected B/Ds. The following audit issues are examined:

- (a) requirements for monitoring contractor's performance (paras. 4.2 to 4.3);
- (b) monitoring of the BCA contracts by the EDB (paras. 4.4 to 4.15);
- (c) requirements specified in the FEHD's recyclables collection service contracts not effectively enforced (paras. 4.16 to 4.21); and
- (d) monitoring of the FEHD's street washing services (paras. 4.22 to 4.35).

Requirements for monitoring contractor's performance

4.2 COs are responsible for the management of the services procured. According to SPR 535, B/Ds shall devise an effective monitoring mechanism to ensure that a contractor performs to standard and complies with the terms of a contract. B/Ds shall evaluate the performance of their contractors and keep the performance records.

4.3 To assess the effectiveness of performance management procedures in practice, service contracts from the four B/Ds were selected for review. Audit identified areas for improvement in the EDB's monitoring of the BCA contracts and FEHD's monitoring of its recyclables collection services and street washing services.

Monitoring of BCA contracts by EDB

4.4 As mentioned in paragraph 2.25, the EDB entered into three contracts (Contracts B1 to B3) with Contractor B through single tendering to develop the BCA in Chinese Language, English Language and Mathematics since December 2000.

Sub-contracting by Contractor B

4.5 Under the contract terms, no sub-contracting by Contractor B is allowed except with prior written approval of the EDB. The EDB may determine the terms and conditions of the sub-contract and require the sub-contractor to enter into a direct undertaking in favour of the EDB on such terms as it considers appropriate.

4.6 Audit notes that Contractor B has sub-contracted part of the three contracts (Contracts B1 to B3) to different sub-contractors. In the tender proposal of Contract B1 and the subsequent correspondence between Contractor B and the EDB, Contractor B had mentioned that it intended to sub-contract the development of the application software for both the SA and TSA programmes to a service bureau through tendering. However, Audit could not find any document which indicated the EDB's formal approval of the sub-contracting. In response to Audit's enquiry, in August and September 2014, the EDB informed Audit that:

- (a) there were records showing that the EDB was in the picture of the sub-contract under Contract B1 to develop the SA system when the BCA was first launched in 2000;
- (b) Contractor B had not sought the EDB's prior approval for the sub-contracts;
- (c) Contractor B informed the EDB that following the arrangement under Contract B1, web-services related to the IT system were contracted out;
- (d) in fact, it had only come to the EDB's attention recently that contracting out the conversion of web-items to a third party had been an established practice for Contractor B since the BCA Project was first launched in 2000;
- (e) the EDB considered that the conversion of web-items only constituted a small part of the whole SA item development process; and
- (f) the EDB had reminded Contractor B of the contractual requirements and requested Contractor B to provide it with information on all major sub-contracts under Contract B3.

4.7 For one of the sub-contracts, Audit notes that the unit rate charged by the sub-contractor for developing the web-based features in the SA is only about 25% of the rate charged on the EDB by Contractor B, although such information may not be directly comparable as Contractor B might have incurred other costs to ensure the work quality of the sub-contractor. Nevertheless, such information may be useful for the EDB for tender evaluation or negotiation when assessing the reasonableness of the single-tender price proposed by Contractor B.

4.8 To protect the interest of the Government, Audit considers that the EDB should ensure that Contractor B duly complies with the contract terms on sub-contracting, and obtains its prior written approval before entering into sub-contracts with other parties.

Committed services not achieved for Contract B2

4.9 Audit noted that by the end of Contract B1 (December 2006), the web-based SA system had been developed and could house 54,000 SA items. As at December 2006, about 8,000 SA items were developed by Contractor B for use by schools to conduct the assessment for students. Under Contract B2, Contractor B could only develop 9,000 new SA items compared to the 20,000 items required. Moreover, at the end of Contract B2 (December 2010), half of the 8,000 SA items developed under Contract B1 could not be satisfactorily transferred to the SA system because of the IT system enhancement made under Contract B2. As a result, an amount agreed between the EDB and Contractor B was deducted from the contract for the under-performance of Contractor B under Contract B2.

4.10 Under Contract B3, the EDB had requested Contractor B to categorise the contract sum into fixed and variable costs so that payment could be readily calculated and deducted in case of under-performance. The EDB also requested Contractor B to submit quarterly reports for closer monitoring of the delivery of service.

Low utilisation of SA programme

4.11 According to the EDB's records, as at the completion of Contract B1 (December 2006), 65% of primary schools and 80% of secondary schools had created accounts to access the SA system to assist learning and teaching. For Contract B2 (from May 2007 to December 2010), the EDB informed Audit in

Monitoring service delivery

September 2014 that it did not maintain records on the utilisation rate of the SA system since the system was redeveloped and launched in July 2009. Starting from 2011, instead of using the number of schools creating accounts to measure system utilisation, system utilisation has been measured by using the number of schools creating assessments for their students. In the past three years from 2011 to 2013 under Contract B3, the EDB records indicated the following percentages of schools which had logged into the SA system to create assessments for students:

Year	Primary schools	Secondary schools
2011	31%	13%
2012	37%	17%
2013	40%	20%

In other words, in 2013, 60% of the primary schools and 80% of the secondary schools had not logged into the SA system to create assessments for students.

4.12 In the Annual Progress Report on Contract B3 for 2013, Contractor B reported, among other things, that there were 20% of secondary schools logged into the SA system to create assessments for students as compared to 40% of primary schools. The low number of primary and secondary school users suggested that more promotion of the SA programme was required. In October 2014, the EDB informed Audit that the SA was only an alternative assessment tool to be used by schools on a voluntary basis. Since it covered basic competencies which represented only part of the curriculum, schools were not encouraged to rely on the SA as the only assessment tool but to use it according to the progress of different levels, classes or students. Not every student in Primary 1 to Secondary 3 would use the assessment tool.

4.13 ***Promotion of SA programme.*** According to the Annual Progress Reports on Contract B3, Contractor B had held seminars/workshops to encourage schools to use the SA more frequently as a tool for enhancing teaching and learning. In the past three years from 2011 to 2013, Contractor B:

- (a) held about 100 seminars/workshops for about 4,400 people (including heads of primary and secondary schools, primary and secondary school teachers, university academics and students, and members of general public); and

- (b) launched a school-based pilot scheme on using the SA system involving three primary schools in 2012 and nine schools (six primary and three secondary) in 2013 with the aim of assisting teachers to use the SA data in diagnosing the strengths and weaknesses of individual students and help schools facilitate the development of school-based assessment through the use of the SA programme.

4.14 Despite the efforts for promoting the SA programme, the utilisation of the SA system was still low and there is still room for improvement. In response to Audit's enquiry, in September 2014, the EDB informed Audit that:

- (a) it had tasked Contractor B to conduct a survey with schools in June 2014 to better understand the usage of the SA among teachers to ascertain the underlying reasons for the low utilisation of the SA system and to seek suggestions for improvement; and
- (b) positive feedback was received from teachers who appreciated the value of the SA and agreed that the class reports and student reports had helped them identify the strengths and weaknesses of their students. It was also noted that a number of schools had been using the SA in a continuous manner.

4.15 In view of the significant financial resources involved in the SA programme (some \$280 million for Contracts B1 to B3 — see Table 5 in para. 2.28) and in order to reap its benefits, Audit considers that the EDB needs to identify the reasons for the low utilisation and closely monitor the future utilisation of the SA programme.

Requirements specified in FEHD's recyclables collection service contracts not effectively enforced

4.16 Following the publication of the Waste Reduction Framework Plan (Note 20) by the Government, the Three-Colour Waste Separation Bin Scheme was introduced in 1998 to provide three-colour bins at public places to recover waste

Note 20: *The plan aims to change community attitudes and approaches to waste. It points out the need to transfer emphasis from collecting and transporting waste to landfills for disposal to waste prevention and reuse of waste materials.*

paper, metal and plastic materials. Since 2000, the FEHD has been providing the recyclables collection service through the use of outsourcing. Under the Policy Framework for the Management of Municipal Solid Waste (2005-2014) published in 2005, the Government aims to tackle the waste problem by reducing the amount of municipal solid waste, increasing the recovery rate of such waste and reducing its disposal in landfills.

4.17 In July 2012, three recyclables collection service contracts for the period from August 2012 to July 2014 were awarded through open tendering to one contractor (Contractor G) at a total value of \$12.7 million. According to the contract terms, Contractor G was required to operate ten recyclable collection vehicles to collect the recyclables at over 3,000 collection points in Hong Kong and deliver the collected recyclables to the “recyclables collector” approved by the FEHD. From August 2012 to June 2014, Contractor G delivered about 1,360 tonnes of recyclables (comprising 330 tonnes of plastics, 1,000 tonnes of paper and 30 tonnes of metal) to the recyclables collector.

4.18 Contractor G was required to submit daily records showing the weight of each type of recyclables collected for the FEHD’s inspection. The contract stipulated that Contractor G shall not dispose of any recyclables in any landfill, refuse transfer stations or any other waste disposal facilities without prior consent of the FEHD. Contractor G shall make available to the FEHD documentary evidence of recyclables exported or sold locally.

Improper disposal of recyclables by Contractor G

4.19 In May 2013, the media reported cases where the staff of Contractor G improperly disposed of collected recyclables in refuse collection points. Since then, the FEHD has implemented a surveillance programme to ensure the proper separation, handling and disposal of the collected recyclables by Contractor G. The FEHD deploys the Intelligence Unit (IU — Note 21) to conduct surprise inspections

Note 21: *The IU, headed by a Chief Health Inspector, performs multifarious functions ranging from intelligence collection to law enforcement, acts on complaints to conduct ad hoc inspections to check the contractors’ performance, and provides support service to district staff in handling complex issues that require surveillance.*

along the routes of the recyclable collection vehicles. During two surprise inspections in May 2013, Contractor G was found to have disposed of collected plastic recyclables directly into refuse collection bins. In accordance with the contract terms, the FEHD served two notices of blatant default (Note 22) on Contractor G for the improper disposal of recyclables.

Revised specifications in the renewed contracts

4.20 Following consultation with the Environmental Protection Department (EPD), the FEHD revised the terms of the new recyclables collection contracts for the period from August 2014 to July 2016. The new terms require the contractors to deliver the plastic recyclables collected to “*recyclables recyclers*” (instead of “recyclables collectors”) nominated by the contractors and approved by the FEHD (Note 23). However, the requirement for the contractors to deliver non-plastic recyclables to “recyclables collectors” remained unchanged. In Audit’s view, the FEHD needs to, in consultation with the EPD, consider making similar revisions for non-plastic recyclables in future tenders.

4.21 In response to Audit’s enquiry, in September 2014, the FEHD informed Audit that:

- (a) it would consult the EPD on the need and the practicality of incorporating similar requirements for other types of non-plastic recyclables, e.g. metal and paper; and

Note 22: *The FEHD is entitled to serve notices of blatant default on the contractor if the contractor, his employees or sub-contractors commit serious defaults in the course of providing the required services. For each notice of blatant default, the contractor is charged \$3,931. The number of such notices will affect the performance score of the contractor in future tendering exercises.*

Note 23: *According to the FEHD, contractors are required to nominate not more than two plastic recyclers and their independent capability in handling plastic recyclables will be confirmed by the EPD through site inspections. The FEHD will take into account the results of the EPD’s site inspections before approving the nominated recyclables recyclers.*

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- (b) the key considerations included whether the collection contractor would face difficulties in properly disposing of these wastes of higher commercial value and whether there were established recyclers who would carry out the recycling processes for these wastes in Hong Kong.

Monitoring of FEHD's street washing services

4.22 As mentioned in paragraph 3.4, the contract value of the FEHD's street washing services amounted to \$294 million as at June 2014. Contractors are required to render the services by providing street washing vehicles with washing teams each comprising one supervisor-cum-driver and three cleansing staff according to the working hours for their work shifts as specified in the contracts. The FEHD pays the contractors at a monthly rate of \$12 million as calculated and specified in the contracts.

4.23 According to the contract terms, the FEHD will review the management plan, work plan, quality assurance plan and contingency plan of the contractors. Where it finds that the existing plans are inadequate, the contractors shall, upon request by the FEHD, submit revised plans with such modifications required (without involving additional payment from the FEHD) to ensure adequate provision of the services to the FEHD's satisfaction.

Daily work programmes and FEHD's inspections

4.24 According to the FEHD's "Operational Manual for Management of Public Cleansing Contracts" and "Operation Manual for Cleansing Services", contractors should provide daily work programmes which specify the time and service locations for street washing services to meet the work schedules (see Note 16 in para. 3.5) and service level requirements in such frequency, order, at such times and such locations as laid down in the contracts. Health Inspectors should require the contractors to review and revise the work schedules from time to time to ensure adequate provision of the services or to suit the actual needs. The contractor should not vary or amend such schedules which are currently in force without the prior approval from the Senior Health Inspectors concerned.

4.25 To ensure that the contractors are providing satisfactory services according to the approved work schedules and the contract terms, Senior Foremen, Health Inspectors and Senior Health Inspectors would conduct random inspections in accordance with departmental guidelines. The Senior Foremen, who are in charge of individual areas where street washing services are provided, are required to record the results of their inspections in the daily work programmes, and the Health Inspectors would sign off the programmes accordingly. During the inspection, if irregularities are found and rectification is not made within the specified response time, the Senior Foremen will recommend Health Inspectors to issue warning letters or Default Notices (Note 24) on the contractors.

Variations between service locations specified in work plans of the contracts and daily work programmes

4.26 Audit analysis of the daily work programmes as approved by the FEHD for the five selected districts (see para. 3.6) for the month of March 2014 indicates that there were significant variations between the service locations specified in the work plans which formed part of the contracts and the locations specified in the daily work programmes. Details are shown in Table 8.

Note 24: *The FEHD is entitled to serve the following three types of Default Notices on the contractor if the contractor, his employees or sub-contractor commit such defaults in the course of providing the required services:*

- (a) *notices of blatant default for serious defaults in performance (e.g. leaving work post early without replacement and without the FEHD's consent). For each notice, the contractor is charged \$3,931;*
- (b) *notices of default in performance (e.g. failing to meet the required standards or any terms and conditions of the contracts and after warning without rectification). In any month, the contractor is charged at \$2,055 for each of the first 10 notices, \$2,523 for each of the 11th to 20th notices and \$4,058 for each of the 21st and beyond; and*
- (c) *notices of behavioural default for misbehaved manner of the contractor's employees while performing services (e.g. sleeping, idling, frequent idle chatting, smoking). For each notice, the contractor is charged \$749.*

Table 8

**Service locations specified in contracts for
street washing services and in the daily work programmes
(March 2014)**

District	Service locations		Variations on service locations	
	Specified in contract	Specified in contract and included in daily work programmes	Specified in contract but <u>not</u> included in daily work programme	<u>Not</u> specified in contract but included in daily work programme
	(a) (No.)	(b) (No.)	(c) = (a)-(b) (No.)	(d) (No.)
B	161	122	39	31
C	149	102	47	37
D	128	97	31	58
E	115	86	29	18
F	305	159	146	22

Source: Audit analysis of FEHD records

4.27 It is understood that service locations specified in the daily work programmes were agreed by the FEHD staff (usually the Senior Foremen who are also responsible directly for the random inspections) based on their assessment of the actual situation (i.e. the actual needs for street washing services in their districts), and flexibility is always needed. However, Audit could not find documentation on whether the Health Inspectors of the districts concerned had checked the daily work programmes to ensure that they really met the actual needs and that variations from the work plans of the contracts had been brought to the attention of their supervisors, i.e. the Senior Health Inspectors of the districts.

4.28 In response to Audit's enquiry, in September 2014, the FEHD informed Audit that:

- (a) the "names" of the street washing locations (and therefore the subsequent counting of number of these locations) specified by contractor in a contract might not necessarily be the same as those used/described in the daily work programmes in districts. For example, for District E, of the 29 locations specified in the work plans of the contract but not included in the daily work programmes (see Table 8), 19 locations which were described in other names had been provided with street washing services, whereas the remaining 10 locations were covered under the "high pressure hot water cleansing programmes". For District F, of those 146 locations specified in the work plans of the contract but not included in daily work programmes (see Table 8), 143 locations had been provided with street washing services;
- (b) the FEHD would review and follow up on the documentation required regarding checking of daily work programmes by district cleansing staff to ensure that the programmes met the actual needs and that any variations from contracts were brought to the attention of the appropriate officers of the districts;
- (c) the FEHD would review and revise the guidelines for approval of the daily work programmes for street washing services submitted by the contractors to ensure that any variations from contracts should be fully justified, approved by the appropriate level of officers and properly recorded; and
- (d) for ad hoc cases, the FEHD would consider requiring the Health Inspector (Contract Management) concerned to give prior verbal agreement for revision of daily work programmes which should be properly recorded.

FEHD's monitoring work

4.29 In September 2014, the FEHD informed Audit that:

- (a) the aim of its management of the service contracts was to assess the overall performance of the contractors through random checking by the contract management staff;
- (b) Senior Foremen were not required to supervise individual workmen of the contractors directly. They should focus on:
 - (i) carrying out field inspections on contractors' services to check the supervising ability and overall performance of the contractors;
 - (ii) conducting random checking on the record of services submitted by the contractors; and
 - (iii) maintaining effective communication with contractors' supervisors;
- (c) apart from these, the Quality Assurance (QA) Section would also conduct regular audit inspections to monitor the performance of front-line supervisors and the service delivery of contractors. The IU (see Note 21 in para. 4.19) would, acting on complaints, conduct ad hoc inspections to check the contractors' performance; and
- (d) Senior Foremen used portable electronic device (i.e. Personal Digital Assistants) to record inspection results, including satisfaction on contractors' work and notes for follow-up actions to be taken (e.g. issue of advisory letters, notices of default) as far as possible on the spot and upload the information to the Contract Management System for vetting by Health Inspectors or above.

4.30 Audit noted that during February to April 2014, the FEHD issued a total of four Default Notices (two notices of default in performance and two notices of behavioural default) in relation to the provision of street washing services in these five districts (Note 25). These included one case in District D for not providing services at the location and time specified in the daily work programme. However, the irregularities were not recorded in the daily work programme.

4.31 Audit's review of the daily work programmes of the five selected districts for February to April 2014 revealed that:

- (a) no site inspection was recorded in the daily work programmes of District B, and the Senior Foremen and Health Inspectors of this district did not sign off the daily work programmes;
- (b) the FEHD's inspection results did not indicate any irregularities found from the street washing services;
- (c) the inspections were conducted on a fairly regular basis which might be anticipated by the street washing teams. About 80% of the inspections were conducted in the first four hours of the day shifts (9 to 11 working hours per shift). For District C, about 90% of the inspections were conducted at two service locations (at around 20:30 to 22:30) of the night shifts. For District D, no inspection was conducted within the last two hours before the end of the night shifts at 23:00 in March 2014; and
- (d) the daily work programmes of two districts (Districts D and F) were not signed off on each day of the inspections by Health Inspectors. In District D, the inspection records were only stamped with the chops of the Health Inspectors in the following month.

Audit considers that the FEHD needs to improve its record keeping of all inspection records and summarise its inspection results so as to provide management with necessary information for regular review and assessment of the contractors' performance.

Note 25: *During July 2013 to April 2014, the FEHD issued a total of 16 Default Notices (6 notices of default in performance and 10 notices of behavioural default) in relation to the provision of street washing services in these five districts. For one case in District C, the irregularity for not providing the correct type of washing vehicle was recorded in the daily work programme.*

Monitoring service delivery

4.32 Audit notes that the electronic devices referred to in paragraph 4.29(d) do not record inspections conducted by Senior Foremen at individual service locations of the street washing routes. In September 2014, the FEHD informed Audit that it would review and revise the guidelines requiring the district staff to properly keep all inspection records.

Audit on-site inspections

4.33 The audit findings on the FEHD's inspection results revealed inadequacies in its monitoring of the contractors' services. In July and August 2014, Audit also conducted independent on-site inspections on the night shifts of five selected routes (with one route selected from each of the five districts) to observe the actual operation of street washing by the FEHD's contractors (Note 26). Audit noted that the contractors had provided the required resources (i.e. a street washing vehicle with a washing team of one driver and three cleansing staff) to perform the street washing work. However, Audit observed some irregularities (the audit inspection results for District B are summarised in Case 3 for illustration). By and large, similar observations were noted in the contractors' street washing services for the other four selected routes Audit inspected.

Note 26: *Street washing teams, comprising a supervisor-cum-driver and three cleansing staff, are required to provide street washing services according to the sequence of the service locations specified in the daily work programme at the specified time period. Street washing services are provided unless there is announcement of black rainstorm warning signal or hoisting of tropical cyclone signal number 8 or higher. During Audit's on-site inspections, no such signals were announced.*

Case 3

1. On 1 August 2014, Audit carried out an on-site inspection on the night shift of a selected street washing route in District B. The on-site inspection did not cover service locations not scheduled in the daily work programme of the selected route. Therefore, it was not known if the team had carried out street washing at any other unscheduled service locations.

2. According to the daily work programme, the contractor's team was expected to carry out street washing services at seven service locations during that night shift. Audit observed that the contractor's team had not carried out street washing at six of the seven service locations specified in the daily work programme. Among others, Audit noted that the team did not carry out any street washing work at one service location according to the time specified, apparently because of the heavy traffic conditions in the area at that moment.

3. For the only one scheduled service location which had been washed, the team washed only part of the areas of the location, taking only 27 minutes against the scheduled 50 minutes in washing.

4. The team returned to the water filling point for signing off about 1.5 hours earlier than the scheduled time (23:00), with some staff of the team leaving the water filling point at 21:37, and all the other staff left at 22:30.

5. The actual time recorded for street washing at the specified service locations in the daily work report subsequently submitted by the contractor deviated significantly from the time Audit observed. According to the daily work report submitted, all the seven service locations were reported to have been washed according to schedule except for one location which was not washed due to receipt of a special order to enhance washing at two locations (including one specified, and another not specified, in the programme). Audit however noted that at the time recorded in the daily work report for washing at these two locations, the street washing vehicle had in fact returned to the water filling point.

6. In September 2014, the FEHD informed Audit that it generally did not require contractors to submit daily work reports after completion of their daily work. Through clarification with the contractor by the FEHD on Audit's inspection results, Audit was given to understand that the street washing service for the route inspected on the date of audit inspection was seriously affected by the actual street conditions, such as busy traffic and special order for changing service location.

Source: FEHD records and Audit's inspections

Monitoring service delivery

4.34 Audit considers that the FEHD needs to:

- (a) consider implementing a more effective mechanism for monitoring the delivery of services by its contractors, including a surprise element in conducting inspections; and
- (b) critically review the services provided by contractors and consider revising the street washing routes by taking into factors such as:
 - (i) the practicability for the street washing teams to wash the service locations at the specified time schedule; and
 - (ii) whether there is a genuine requirement for the street washing services at the locations specified in the routes.

4.35 In response to Audit's enquiry, in September 2014, the FEHD informed Audit that it would:

- (a) remind all districts to step up checking (including surprise checks at night time) on the performance and services provided by their contractors;
- (b) review and revise the guidelines to implement effective mechanism in monitoring the contractors' performance, in particular at odd hours; and
- (c) remind the district staff to critically review the services provided by contractors and consider revising the street washing routes in future contracts by taking into account factors as mentioned in paragraph 4.34(b).

PART 5: WAY FORWARD

5.1 This PART explores good practices in other countries and examines the challenges ahead, and makes audit recommendations on the way forward. The following issues are covered:

- (a) the increasing emphasis placed on obtaining more cost-effective services by other countries (paras. 5.2 to 5.4);
- (b) the need for the FSTB and GLD to remind B/Ds to observe relevant Government regulations and guidelines (paras. 5.5 and 5.6); and
- (c) audit recommendations and response from the Administration (paras. 5.7 to 5.30).

Increasing emphasis placed on obtaining more cost-effective services by other countries

5.2 Audit has conducted research and noted that increasing attention is placed by other countries in enhancing competition and adopting good practice to obtain more cost-effective services from contractors and service providers. Management approach and good practices adopted by the U.K. and the U.S.A. are shown in the following paragraphs.

5.3 Based on a U.K. National Audit Office Memorandum for Parliament (November 2013), government contracting out can significantly reduce costs and help to improve public services. To achieve these benefits, the following three issues deserve greater attention:

- (a) There is a need for scrutiny over whether public service contracts are sufficiently competitive and whether the emergence of a few major contractors is in the public interest.
- (b) Understanding contractors' profits is important to ensure that their interests are aligned properly with that of the taxpayer.
- (c) Ensure that contractors are delivering services to the standards expected.

In particular, the government needs to ensure that the large contractors have the right culture and control environment to manage their operations. This requires transparency over contractors' performance and the use of contractual entitlement to information, audit and inspection. This should be backed up by the threat of financial penalties and being barred from future competitions if repeated and serious defaults are found.

5.4 Similarly, a U.S. Government Accountability Office Testimony (July 2013) found that most of the agencies it reviewed did not fully leverage their aggregate buying power. The greater use of a strategic sourcing approach is key to achieving successful services acquisition outcomes. Good practices under this approach include:

- (a) ***Maintaining spend visibility.*** Fragmented information on spending does not allow management to spot inefficiencies or opportunities for consolidating purchases. The starting point for strategic sourcing efforts is to have good data on spending through the development of compatible systems for tracking information on the government's contracting actions.
- (b) ***Enhancing competition by increasing the number of suppliers.*** It is important to share information on spending and increase market knowledge about suppliers to gain awareness of the procurement environment. This awareness positions management to make more informed contracting decisions.

(to be continued)

(Cont'd)

- (c) *Improving the specification of requirements.* Management closely examines services requirements in order to prevent unnecessary spending on services which are not absolutely needed.
- (d) *Centralising procurement.* Without a centralised procurement process, management ran the risk that different parts of the organisation could be buying the same item or service, thereby missing an opportunity to share knowledge to reduce costs. Centralising procurement does not necessarily refer to centralising procurement activity, but to centralising procurement knowledge.
- (e) *Developing category-specific strategies.* The most effective sourcing strategies, based on internal analyses of business requirements and information on spending and external analyses of market research, are used for each category of service.

Need for FSTB and GLD to remind B/Ds to observe relevant Government regulations and guidelines

5.5 The audit review has identified room for improvements in a number of areas in the Government's hiring of service contractors and professionals as illustrated from the cases selected for review. In particular, Audit has found that some of the procurements reported could have achieved better value for money through more determined and focused efforts to introduce competition among eligible tenderers and through closer monitoring of contractors' performance.

Way forward

Service	Audit observations	Relevant regulations and guidelines
Health screening service at the airport	<ul style="list-style-type: none"> Need to assess all relevant factors during tender/contract negotiations (paras. 2.13 and 2.15) 	SPRs 370 and 385
Development of the BCA	<ul style="list-style-type: none"> Need to review the use of single tender for the SA programme (para. 2.39) Sub-contracting by the contractor without prior written approval (para. 4.6) Low utilisation of the SA programme (para. 4.15) 	SPRs 325(a), 535 and Financial Circular No. 4/2013
FEHD street cleansing services	<ul style="list-style-type: none"> Services provided by few major contractors (paras. 2.44 and 2.48) 	SPR 350(e) and Appendix III(F) of SPRs
Cleansing and support services in LCSD venues		
Radiology services for different health clinics	<ul style="list-style-type: none"> Adopting quotation procedures for services of a similar nature with aggregate value exceeding \$1.43 million (Cases 1 and 2 of para. 2.50) 	SPR 205
Special security management services in LCSD parks		
FEHD street washing services	<ul style="list-style-type: none"> Service requirements not accurately reflected in tender specifications (para. 3.8) Variations between service locations specified in work plans of the contracts and daily work programmes not properly documented (para. 4.27) Need to implement a more effective mechanism for monitoring the service delivery by the contractors (para. 4.34) 	SPRs 350(e), 535 and Appendix III(F) of SPRs
Management support services in sports centres	<ul style="list-style-type: none"> Need to review the setting of mandatory requirements to enhance competition (para. 3.19) 	SPR 126(a)(i) and Financial Circular No. 2/2014

5.6 To uphold a culture of compliance for procurement, Audit considers that the Secretary for Financial Services and the Treasury, in conjunction with the Director of Government Logistics, needs to remind B/Ds to comply with the relevant Government regulations and guidelines from time to time.

Audit recommendations and response from the Administration

PART 2: Sourcing of service providers

5.7 Audit has *recommended* that the Director of Health should:

Health screening services at the HKIA

- (a) **critically assess all relevant factors (e.g. the justification for accepting the provision of Assistants at Secondary 5 education level as compared with Secondary 3 level at other control points) during the DH's tender/contract negotiations with Contractor A, and determine an appropriate long-term procurement strategy, balancing the need to obtain cost-effective services on one hand and the risk of aviation security on the other hand (see para. 2.24);**

Appropriate procurement procedures not always adopted to enhance competition

- (b) **review the DH's procurement procedures for radiology services with a view to enhancing competition and meeting the requirements of the SPRs (see para. 7 of Case 1); and**
- (c) **update the quotation invitation lists for radiology services more regularly with a view to enhancing competition (see para. 2 of Case 1).**

Way forward

5.8 The Director of Health agrees with the audit recommendations.

5.9 The Secretary for Food and Health agrees with the audit recommendations. He has said that he will follow up the audit recommendations with the DH.

5.10 **Audit has *recommended* that the Secretary for Education should, given the changes in circumstances and technology advancement, critically review the continued use of Contractor B under the single tender approach for implementing the SA programme and consider whether other tendering options can be brought into the SA programme separately when opportunity arises (such as major system enhancement and introduction of new technology) so as to reap the benefits of competitive bidding (see para. 2.39).**

5.11 The Secretary for Education generally agrees with the audit recommendation. He has said that:

- (a) engaging one single institution to implement both the SA and TSA under the BCA was considered necessary in ensuring consistency in defining and assessing the basic competencies of different subjects, especially when the BCA was at an early stage of development; and
- (b) given that the concept of basic competencies has become very well-known in the school sector in recent years, the EDB plans to upgrade the SA system to a new online assessment bank. The EDB shall consider the optimal approach to procuring the services taking into account the desirability of quality assurance, more items and more diversity in item types as well as the implications of various tender options for the future sustainability, consistency and operation of the online system.

5.12 **Audit has *recommended* that the Director of Food and Environmental Hygiene should continue monitoring the situation and take necessary measures (e.g. reducing the contract size where appropriate) to enhance competition in future tendering exercises for the FEHD's street cleansing services (see paras. 2.43 and 2.44).**

5.13 The Director of Food and Environmental Hygiene agrees with the audit recommendation. She has said that the FEHD will continue taking effective measures to enhance competition in future tendering exercises for its street cleansing services, such as:

- (a) *Splitting large contracts into smaller ones.* This has already been implemented for the large contracts in five Districts and will be extended to other districts as appropriate;
- (b) *Promoting tender exercises and giving adequate guidance to tenderers;*
- (c) *Assessing whether existing “essential” or “mandatory” tender requirements should continue to be so specified.* Since 16 April 2014, the FEHD has, in line with Financial Circular No. 2/2014, stopped specifying the use of separate sealed envelopes for technical and price proposals as an “essential requirement”; and
- (d) *Reviewing and amending assessment criteria and/or marking schemes which may be inherently in favour of the existing contractor.* The FEHD has since September 2013 reviewed and fine-tuned assessment criteria such as record of past performance and record of compliance in the past 36 months with the wage level, daily maximum working hours, signed written employment contracts or standard employment contracts, wage payment by autopay for the purpose of enhancing the fairness of the tender exercise.

5.14 **Audit has recommended that the Director of Leisure and Cultural Services should:**

Limited number of tenderers for some major contracts

- (a) **critically review the LCSD’s tendering strategy, and where appropriate and feasible, consider the use of more contractors, thereby reducing the management risk of relying on several contractors to deliver the services (see para. 2.48); and**

Way forward

Appropriate procurement procedures not adopted to enhance competition

- (b) **expedite action to obtain competitive services through open tendering as soon as practicable for the special security management services at Park A (see para. 2 of Case 2).**

5.15 The Director of Leisure and Cultural Services generally accepts the audit observations and recommendations. She has said that:

Limited number of tenderers for some major contracts

- (a) the LCSD has followed, and will continue to follow, the SPRs and the practices of the GLD in conducting procurement activities having regard to guiding principles such as fairness, openness, cost-effectiveness, value for money and prudent risk management whilst being mindful of the advantages of promoting competition. The LCSD would follow up on the audit recommendations as appropriate and practicable; and

Appropriate procurement procedures not adopted to enhance competition

- (b) for Park A, having evaluated the effectiveness of measures introduced on a pilot basis and established the long-term need to engage special security guards who should possess working experience in disciplinary force to tackle noise nuisances arising from singing activities, the LCSD is sourcing a long-term contract through open tendering to acquire the requisite services.

PART 3: Specification of service requirements

5.16 **Audit has recommended that the Director of Food and Environmental Hygiene should:**

- (a) **critically review the service locations specified for street washing in the tender documents to ensure that such locations are justified and meet the actual needs (see para. 3.8); and**

- (b) **take measures to ensure that such service locations are fully incorporated into the tender documents and contracts awarded to the successful bidders (see para. 3.8).**

5.17 The Director of Food and Environmental Hygiene generally agrees with the audit recommendations. She has said that the FEHD will:

- (a) remind District Offices to critically review the locations specified for street washing in the tender documents to ensure that such locations are justified and meet the actual needs;
- (b) set out these locations clearly in the tender documents and pay special attention to the relevant proposals in the work plans submitted by the bidders during the vetting of tenders and awarding of contracts; and
- (c) take measures to ensure that such locations are clearly set out in the contract awarded to the successful bidders.

5.18 **Audit has recommended that the Director of Leisure and Cultural Services should critically review whether it is possible to revise the mandatory requirements for the provision of management support services at sports centres with a view to encouraging competition, increasing choices and avoiding over-reliance on a single contractor (see para. 3.19).**

5.19 The Director of Leisure and Cultural Services generally accepts the audit observations and recommendation. She has said that the LCSD will review the mandatory requirements, including the relevant experience and, if appropriate, consider whether there is room for relaxing so that the pool of qualified contractors can be expanded to enhance competition.

PART 4: Monitoring service delivery

5.20 **Audit has recommended that the Secretary for Education should:**

- (a) **ensure that Contractor B duly complies with the contract terms on sub-contracting (see para. 4.8);**

Way forward

- (b) ensure that Contractor B obtains the EDB's prior approval before entering into sub-contracts with other parties and obtain all previous sub-contracts for assessing the reasonableness of the cost elements built into the tender prices in future tendering exercises (see paras. 4.7 and 4.8); and
- (c) in view of the significant financial resources involved and to reap the benefits of the SA programme, identify the causes for the low utilisation and closely monitor the utilisation of the SA programme (see para. 4.15).

5.21 The Secretary for Education generally agrees with the audit recommendations. He has said that:

- (a) the EDB shall ensure that the contract terms on sub-contracting would be duly complied with. The EDB has already obtained information on previous sub-contracts from the contractor and shall make reference to the sub-contract prices in assessing similar tenders in future; and
- (b) a survey on the views of the teacher users of the SA was conducted in July 2014. The EDB shall continue to explore possible means to enhance and closely monitor the utilisation of the SA.

5.22 **Audit has *recommended* that the Director of Food and Environmental Hygiene should, in consultation with the EPD, consider revising the specifications of the service requirements and relevant contract terms for non-plastic recyclables in future tenders (see para. 4.20).**

5.23 The Director of Food and Environmental Hygiene agrees with the audit recommendation. She has said that:

- (a) the recyclables collection service contract administered by the FEHD for collection of waste paper, metal and plastic materials is primarily a collection contract. Waste plastics are of generally low commercial value, and many plastic bottles collected from collection bins at street level are contaminated, rendering them not suitable for commercial recycling. To address the claim of the previous recyclables collection contractor that it

had difficulties in finding suitable local recyclers to receive the plastic recyclables it collected, the FEHD had revised the terms of the new contracts in consultation with the EPD, requiring the contractors to deliver plastic recyclables to “nominated recyclers” approved by the FEHD in consultation with the EPD. The contractor is required to nominate not more than two plastic recyclers and their capability in handling plastic recyclables will be confirmed by the EPD through site inspection. The FEHD will take into account the results of the EPD’s site inspection before approving the nominated recyclables recyclers; and

- (b) the FEHD will consult the EPD on the need and practicality of incorporating similar requirements for other types of non-plastic recyclables in future tenders, taking into account whether there are well-established recyclers who are indeed carrying out the recycling processes for waste paper and metal in Hong Kong.

5.24 The Director of Environmental Protection has said that the EPD will offer technical assistance to the FEHD as requested.

5.25 **Regarding the FEHD’s monitoring of the contractor’s street washing services, Audit has *recommended* that the Director of Food and Environmental Hygiene should:**

- (a) **review and revise the guidelines for approval of the daily work programmes for street washing services submitted by the contractors to ensure that any variations (e.g. service locations) from contracts should be fully justified, approved by appropriate level of officers and properly recorded (see para. 4.27);**
- (b) **ensure the proper keeping of all inspection records so as to provide management with necessary information for regular review and assessment of the contractors’ performance (see para. 4.31);**
- (c) **consider implementing a more effective mechanism for monitoring the delivery of services by the contractors (e.g. conduct more inspections and build in surprise element in conducting inspections — see para. 4.34(a)); and**

Way forward

- (d) **critically review the services provided by contractors and consider revising the street washing routes by taking into account factors such as the practicability for the street washing teams to wash the service locations at the specified time schedule and the need for providing such services in some locations (see para. 4.34(b)).**

5.26 The Director of Food and Environmental Hygiene agrees with the audit recommendations. She has said that the FEHD will:

- (a) review and revise the guidelines for approval of the daily work programmes for street washing services submitted by the contractors to ensure that any variations from the contracts should be fully justified, approved by the appropriate level of officers and properly recorded. For ad hoc cases, the FEHD will consider authorising the Health Inspector (Contract Management) of the District Office concerned to give prior oral agreement for revision of daily work programmes which should be properly recorded;
- (b) review and revise the guidelines requiring the staff of its District Offices to properly keep all inspection records;
- (c) critically review and revise the guidelines for the purpose of implementing a more effective mechanism for monitoring the contractors' performance, by including, in particular, an element of surprise in the inspection, and take appropriate actions against any default on the part of the contractors in accordance with the contract provisions; and
- (d) remind its District Offices to critically review the services provided by contractors and consider revising the street washing routes by taking into account factors such as the practicability for the street washing teams to wash the service locations at the specified time schedule and the need for providing such services in some locations.

PART 5: Way forward

5.27 **Audit has *recommended* that the Secretary for Financial Services and the Treasury should, in conjunction with the Director of Government Logistics, remind B/Ds to comply with the relevant Government regulations and guidelines (see para. 5.6).**

5.28 The Secretary for Financial Services and the Treasury agrees with the audit recommendation. He has said that Government procurement is governed by the SPRs, supplemented by the Financial Circulars, Financial Services and the Treasury Bureau Circular Memoranda and relevant guidelines. Observance of these regulations and guidelines is an on-going requirement for all COs and public officers. The requirements are all accessible at the Central Cyber Government Office portal. The GLD organises annual SPR training courses for staff of all B/Ds and B/Ds are reminded of the Government procurement policies and regulations. The CTB and GLD Tender Boards also remind B/Ds on a need basis of the importance of, inter alia, enhancing competition and monitoring service delivery when need be.

5.29 **Audit has *recommended* that the Director of Government Logistics should:**

- (a) take on board the audit observations mentioned in this audit review in the GLD's reviews of B/Ds' compliance with the SPRs (see para. 5.5); and**
- (b) regularly remind B/Ds and provide support for them to properly follow the SPRs in the hiring of service contractors and professionals (see para. 5.6).**

5.30 The Director of Government Logistics has said that the GLD will take note of the audit observations made in this audit review and remind B/Ds in the annual SPR training courses for staff of all B/Ds to properly follow the SPRs when handling their procurement of goods and services. She has also said that:

Way forward

- (a) according to SPR 125, it is the responsibility of the COs to observe and uphold a culture of compliance with the SPRs. They are required to regularly remind the staff concerned about their need to always comply with the SPRs and closely monitor their compliance;
- (b) to assist the COs in fulfilling their self-monitoring duties as mentioned in (a) above, as a new monitoring measure, the GLD is now preparing a self-assessment checklist on compliance with the SPRs to facilitate the COs in reviewing regularly their supplies and procurement activities. After consulting various major departments and taking into account their workload involved, the GLD will suggest that the COs should conduct such self-assessment at least once every two years. The GLD will take on board the various audit observations made in this audit review and include them in the checklist for the CO's review and necessary follow-up actions;
- (c) at present, the GLD conducts supplies surveys and stock verifications (the surveys) on store units at least once every three years as prescribed in SPR 1005(a). Prior to 2014-15, these surveys covered management of stores and procurement of stores and services not exceeding the value of \$1.43 million arranged under the B/Ds' direct purchase authority. The GLD has expanded the scope of the surveys since 2014-15 to cover tender cases not exceeding the value of \$5 million (as cases above this limit are well considered by the relevant tender boards) arranged by B/Ds under the streamlined procurement procedures as promulgated under Financial Circular No. 4/2013 on "Streamlining Procurement Procedures". The GLD will take into consideration findings of the COs' review as mentioned in (b) above in conducting these surveys to cover B/Ds' tender cases not exceeding the value of \$5 million in future; and
- (d) the GLD has designated dedicated staff to provide helpdesk service to advise B/Ds on any enquiries they may have relating to procurement matters. Guidelines on Government procurement matters are also posted on the Central Cyber Government Office portal to provide easy reference for B/Ds.

**Key events for awarding repeated
single-tender contracts to Contractor A
(July 2003 to March 2014)**

Date	Event
3 July 2003	The first contract for temperature screening service was awarded to Contractor A through single tendering.
5 September 2003	The FSTB advised the DH that: <ul style="list-style-type: none"> • “Security” consideration, if overriding, would be a strong justification to support single tendering; and • otherwise, the FSTB would only agree that single tendering was a tide-over measure. Urgency would be the only reason to justify single tendering.
16 September 2003	The Security Bureau (SB) advised the DH that: <ul style="list-style-type: none"> • the employment of Contractor A for the health screening at the international airport was highly preferred from the security point of view; and • the use of other outside agencies would create vulnerability in the security system at the airport and inevitably Contractor A’s involvement would be necessary to reduce the risk.
3 July 2003 to 31 March 2014	Contracts for temperature screening service were awarded to Contractor A through single tendering. Contract A1 was the most recently completed one.
Events relating to Contract A2	
18 June 2013	The DH sought the FSTB’s approval to invite a single tender from Contractor A for provision of pregnant visitors screening service.
9 July 2013	The FSTB gave approval for the DH to invite a single tender from Contractor A for 12 months at an estimated cost of \$3.29 million.
9 July & 1 August 2013	The DH issued tender invitations (two rounds) to Contractor A. The service period was revised to 6.5 months.
21 August 2013	The DH received an offer from Contractor A at \$2.1 million and commenced tender evaluation and price negotiation.
26 August 2013	Contractor A revised its offer to \$2.0 million.
30 August 2013	The DH’s DTC approved the award of Contract A2 to Contractor A at \$2.0 million for 6.5 months.

Date	Event
Events relating to Contract A3	
19 September 2013	Upon the DH's enquiry, the SB informed the DH that it was preferable to continue engaging Contractor A in providing the services in order to provide better assurance to aviation security of Hong Kong as a whole.
17 October 2013	<p>The DH sought the FSTB's approval to invite a single tender from Contractor A. The DH stated that:</p> <ul style="list-style-type: none"> • the SB had given support vide the memo dated 16 September 2003 for Contractor A to provide health screening service at the international airport on aviation security ground (see above); • the DH considered it not appropriate to obtain such services by open tender; and • the pre-tender estimate of the contract value was \$72 million.
6 February 2014	The FSTB gave approval for the DH to invite a single tender from Contractor A subject to the condition that Contractor A was the only suitable agency in the market for the provision of the required services on aviation security reason. The DH, in the light of the FSTB's observations when processing the application, revised the pre-tender estimate of the contract value from \$72 million to \$61.2 million.
6 February 2014	The DH issued tender invitation to Contractor A.
21 February 2014	The DH received an offer from Contractor A at \$82.9 million and commenced tender evaluation and price negotiation.
4 March 2014	The DH submitted tender report to the CTB for consideration.
18 March 2014	<p>The CTB suggested the DH to:</p> <ul style="list-style-type: none"> • explore the feasibility to adopt open tender in future with a view to enhancing competition; and • seek further advice from the Department of Justice on the terms and conditions of Contract A3. <p>Clarifications on the contract terms were received from the Department of Justice on the same date.</p>
26 March 2014	On the advice of the CTB, the Permanent Secretary for Financial Services and the Treasury (Treasury) approved the award of Contract A3 to Contractor A at \$82.9 million.

Source: DH records

Acronyms and abbreviations

Audit	Audit Commission
BCA	Basic Competency Assessment
B/Ds	Bureaux/departments
CO	Controlling Officer
CTB	Central Tender Board
DH	Department of Health
DTC	Departmental Tender Committee
EDB	Education Bureau
EPD	Environmental Protection Department
FEHD	Food and Environmental Hygiene Department
FSTB	Financial Services and the Treasury Bureau
GLD	Government Logistics Department
HKIA	Hong Kong International Airport
IU	Intelligence Unit
LCSD	Leisure and Cultural Services Department
QA	Quality Assurance
SA	Student Assessment
SB	Security Bureau
SPRs	Stores and Procurement Regulations
TSA	Territory-wide System Assessment
WTO GPA	Agreement on Government Procurement of the World Trade Organization