

# **EFFORTS OF THE RATING AND VALUATION DEPARTMENT IN SAFEGUARDING REVENUE ON RATES AND GOVERNMENT RENT**

## **Executive Summary**

1. The Rating and Valuation Department (RVD) is responsible for the assessment and collection of rates under the Rating Ordinance (Cap. 116) and government rent under the Government Rent (Assessment and Collection) Ordinance (Cap. 515). Currently, rates and government rent are respectively charged at 5% and 3% of the rateable value which is the estimated annual rental value of a property. For the assessment and collection of rates and government rent under the Ordinances, the RVD maintains records of all properties that have been assessed to rates and those liable for assessment to government rent in a Valuation List and a Government Rent Roll respectively, which are updated through General Revaluations (GRs), interim valuations and deletions. The RVD conducts GRs annually to bring the rateable values of all properties up to date to reflect changes in market rental values. It may also at any time make interim valuations of newly-built properties and properties which have undergone structural alterations, and make deletions to remove properties which have ceased to be liable for assessment to rates/government rent. As at 1 April 2015, the Valuation List contained 2.43 million assessments with a total rateable value of \$608.6 billion and the Government Rent Roll contained 1.89 million assessments with a total rateable value of \$354.1 billion. For 2014-15, the RVD collected rates of \$22.3 billion and government rent of \$9.3 billion. The Audit Commission (Audit) has recently conducted a review to examine the RVD's efforts in safeguarding revenue on rates and government rent.

### **General Revaluations**

2. The RVD collects rental information for GR purposes mainly by issuing some 307,700 requisition forms (Form R1As) each year to selected properties requiring owners/occupiers concerned to provide rental information. The RVD also obtains rental information from about 51,100 Form CR109s lodged by landlords of

## Executive Summary

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domestic properties under the Landlord and Tenant (Consolidation) Ordinance (Cap. 7) and some 47,700 copies of stamped tenancy agreements from the Inland Revenue Department each year. After analysis and adjustment in accordance with the law, the reported rental information is used to assess the rateable values of properties in the Valuation List based on computer-assisted mass appraisal techniques (paras. 2.3, 2.5 and 2.6).

3. ***Need to monitor the accuracy of rental information furnished in Form RIAs.*** After completion of each GR, the RVD conducts a rental verification exercise by selecting some 240 cases to ascertain the accuracy of information furnished in Form RIAs. For the GRs from 2010-11 to 2015-16, the average in-order rate was only 71%. Discrepancies were found in 28% of the sampled cases. For example, three property owners had provided inaccurate rental information for three to four years. The inaccurate rental information furnished in Form RIAs could undermine the accuracy of rateable values generated in the GRs and warrants management attention. Audit also notes that the RVD only selected ratepayers of multiple properties for rental verification purposes. To improve the monitoring of reported rental information, the RVD needs to consider using stratified sampling to divide ratepayers into multiple-property and single-property sub-groups for conducting the rental verification exercises (paras. 2.7, 2.8 and 2.10).

4. ***Need to step up follow-up actions on non-compliance with Form RIA submission requirements.*** Of some 307,700 Form RIAs issued for each annual GR from 2010-11 to 2015-16, about 56,400 (18%) ratepayers failed to complete and return the Form RIAs. While the RVD had taken prosecution actions on or issued warning letters for some of the non-returned cases, the number of ratepayers who had failed to file Form RIAs for three years consecutively increased by 22% from 6,100 in the 2010-11 GR to 7,417 in the 2015-16 GR (para. 2.9).

5. ***Need to improve the cost-effectiveness of obtaining rental information on subdivided properties for GR purposes.*** In 2012, the RVD introduced a new Form RIA requiring ratepayers to report (in addition to rental information) whether their properties had been subdivided or combined (i.e. structural alterations that might affect their rateable values). For the GR of 2013-14, the RVD issued

## Executive Summary

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3,189 Form R1As to all ratepayers in 116 buildings which were found by the Buildings Department (BD) to have 800 subdivided properties. However, of 2,244 Form R1As returned, only 44 reported rental and subdivided unit information, suggesting that ratepayers may not be forthcoming in disclosing information on their subdivided properties. The RVD had not conducted similar exercises in subsequent GRs as it was considered not cost-effective to issue Form R1As to all ratepayers in buildings with subdivided properties. In Audit's view, the RVD can improve the cost-effectiveness of obtaining rental information on subdivided properties for GR purposes by targeting those identified by the BD (paras. 2.12 to 2.15).

### Interim valuations

6. The RVD makes use of information from other departments to identify properties that may require interim valuations, including occupation permits issued by the BD for new buildings, and alteration and addition works of buildings notified by the BD. The RVD also gathers information on altered properties by site inspections and Form R1As. According to the RVD, the fact that a property or structure is unauthorised does not affect its liability for assessment to rates. Likewise, the assessment to and/or the payment of rates for these unauthorised building works (UBWs) does not imply that they have legal status. In making interim valuations in accordance with the Rating Ordinance, the RVD cannot recover retrospectively the rates for more than 24 months (paras. 3.3, 3.5, 3.7 and 3.8).

### *Need to strengthen interim valuations of assessable UBWs*

7. *Notification arrangements of assessable UBWs.* In November 2000, the then Secretary for the Treasury endorsed the proposal of a Task Force set up under the then Planning and Lands Bureau not to collect rates from new or re-erected illegal rooftop structures on the basis that prompt action would be taken by the BD to clear such structures. In 2001-02, the BD agreed to notify the RVD of its planned enforcement actions against illegal rooftop structures on single-staircase buildings by copying to the RVD removal orders and compliance letters issued to owners/occupiers concerned. In 2004, the BD agreed to the RVD's request for copies of removal orders and compliance letters pertaining to other types of UBWs (such as subdivided units) which were assessable to rates (paras. 3.10 to 3.12).

## Executive Summary

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8. *Need to improve the instructions for RVD staff on following up removal notifications of un-assessed UBWs.* Subsequent to the agreed notification arrangements with the BD, the RVD issued departmental instructions in 2002 and 2005 (currently still in force) stipulating, among other things, that RVD staff should not take further actions on un-assessed illegal rooftop structures and UBWs respectively which were subjected to the BD's removal notifications. According to the RVD, under the established rating principles, a property which was transient in nature would not be assessed to rates and the issue of a removal order signified the determination of clearance of the targeted illegal structure soonest possible. The departmental instructions were premised on the requirement of the removal orders that illegal rooftop structures/UBWs should be removed within one to three months and thus their existence would be too transient to satisfy the rateability requirement. However, Audit found that there were deficiencies in the RVD's instructions on follow-up actions on removal notifications of assessable UBWs, as follows:

- (a) there was no documentary evidence to indicate that before issuing the 2005 departmental instruction, the RVD had ascertained from the BD whether UBWs issued with removal orders could be removed shortly; and
- (b) Audit analysis of 54,637 cases with removal orders for assessable types of UBWs issued by the BD from 2001 to 2015 revealed that 16,304 (30%) had not been complied with as at 31 December 2015. In particular, 10,192 cases had remained outstanding for two years or more after the issue of removal orders, indicating that the RVD's presumption that UBWs would be demolished soon after the issue of removal orders was not always valid (paras. 3.13 to 3.15).

9. *Need to extend the coverage of the notification arrangements of assessable UBWs.* Under the agreed notification arrangements, the BD had not provided the RVD with information on assessable types of actionable UBWs without removal orders issued. According to the BD's database, from 2001 to 2015, removal orders had not been issued for 59,032 cases found with assessable types of actionable UBWs. As shown in paragraph 8(b) above, actions to demolish UBWs with removal orders issued could take a long time, not to mention those without statutory removal orders issued. Given the 24-month time-bar in recovering rates, there is a risk of loss of rates revenue if the rateable values of properties with assessable UBWs are not reassessed in a timely manner. Based on the RVD's records, the rateable values of properties with assessable subdivided units could

## Executive Summary

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increase by 5% to 217% (averaging 58%) upon reassessments (paras. 3.17, 3.18 and 3.20).

10. *Need to improve the instructions for BD staff in copying removal notifications of assessable UBWs to the RVD.* For the 2004 agreed notification arrangements of UBWs, two instructions were issued, one for advertising signs and the other for UBWs in general. For advertising signs, BD staff concerned were required to copy removal orders and any consequential compliance letters to the RVD. For UBWs in general, BD staff concerned were required to copy compliance letters and letters of withdrawal of removal orders to the RVD. However, there was no laid-down requirement to copy removal orders to the RVD. Based on Audit's test check of 85 removal orders selected from the BD's database, only 7 (8%) were copied to the RVD and it appeared that the RVD was not informed of the existence of most of the removal orders (paras. 3.21 and 3.22).

### *Need to step up efforts in identifying un-assessed advertising signs for interim valuations*

11. The Rating Ordinance provides that all advertising signs can be considered for assessment to rates either as separate properties or additional values to be included in the properties on which they are erected. As at April 2015, there were 9,368 separately assessed advertising signs with a total rateable value of \$1.8 billion. In December 2015, Audit conducted a survey of large-sized advertising signs affixed externally to buildings in selected streets of six districts and found that 41 (41%) of the 100 selected advertising signs had not been assessed to rates (paras. 3.26, 3.30 and 3.31).

### *Need to enhance the monitoring of timeliness of interim valuations*

12. From April 2014 to September 2015, the RVD completed 30,693 new interim valuations. However, Audit found that 46 interim valuations involving rates of mainly village houses were not completed within the 24-month time-bar, resulting in a loss of revenue. For 32 of the 46 interim valuations, the relevant documents required for initiating interim valuations were received by the RVD, on average, 104 months after their effective dates of interim valuations. There is a need to take

## Executive Summary

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measures to prevent recurrence of similar problems. The RVD also needs to enhance the monitoring of timeliness of interim valuations and regularly provide the Financial Services and the Treasury Bureau with information on all revenue loss cases (paras. 3.35, 3.36 and 3.39).

### **Rates exemption for rural properties**

13. The Rating Ordinance provides two forms of rates exemptions for specific types of rural properties. One is exemption from assessment to rates for New Territories village houses within designated village areas (DVAs), and for agricultural land and buildings. The other is exemption from payment of rates for certain village houses outside DVAs and occupied by indigenous villagers. The exemptions are granted on the condition that the owners/occupiers comply with prescribed criteria (paras. 1.8, 4.2, 4.10 and 4.20).

14. *Need to put in place compliance checking of rates-exempted village houses within DVAs.* As at 31 December 2015, there were 105 DVAs covering some 16,460 houses in 140 villages. The Rating Ordinance provides that any rates-exempted village houses within DVAs shall comply with the prescribed size, height and type criteria (such as not more than three storeys). Audit notes that the RVD has not put in place compliance checking of village houses in DVAs to ensure that they meet the prescribed criteria. Audit's site inspections of two DVAs revealed that 58 village houses therein had four or five storeys. Audit examination of the RVD's government rent records of 228 houses in 12 selected villages within nine DVAs also revealed that 18 houses had been assessed as 4-storey or 5-storey buildings for government rent purposes. While these village houses did not comply with the prescribed 3-storey criterion, the RVD had not taken actions to cancel their exemptions from assessment to rates (paras. 4.3 to 4.6 and 4.9).

15. *Need to enhance the compliance checking of rates-exempted village houses outside DVAs.* The Director of Home Affairs is delegated with the authority to grant exemption from payment of rates to certain village houses outside DVAs, which are occupied by indigenous villagers. As at December 2015, some 19,000 eligible villagers involving 25,000 units in village houses situated in nine districts had been granted such rates exemption. The existing policy is that the exempted village houses shall comply with the same prescribed criteria as those for village houses within DVAs, and should not contain any UBWs. To monitor their

## Executive Summary

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compliance with the rates exemption eligibility criteria, the Home Affairs Department (HAD) has sought the assistance of eight relevant District Lands Offices (DLOs) of the Lands Department (LandsD) to identify village houses containing UBWs by conducting document checks against their UBWs records and field inspections. Audit has found that:

- (a) some of the document checks and field inspections were not conducted in a timely manner. For example, of the 270 field inspections requested by the HAD from June 2014 to June 2015, 22 (8%) were still outstanding as at December 2015; and
- (b) there is a need to consider stepping up the field inspections as the inspection results suggest a high incidence of ineligible cases. For example, a sample check of the inspection results revealed that in 120 inspections, 48 (40%) rates-exempted houses were found having UBWs (paras. 4.10 to 4.12, 4.14, 4.18 and 4.19).

16. *Need to obtain information from the LandsD on unauthorised change of use of agricultural land and buildings for identifying ineligible rates-exempted cases.* In 2015, the RVD and the LandsD agreed that the DLOs would notify the RVD of the re-entry/vesting cases, cancellation of re-entry/vesting cases and cases of unauthorised structures on agricultural land demolished. However, the notification arrangement does not cover unauthorised structure cases for which the LandsD has issued warning letters. Audit review of three such cases of unauthorised structures on agricultural land revealed that the structures were mainly used for storage purposes, indicating that the use of the agricultural land concerned had changed. However, two of the three cases were still exempted from assessment to rates (para. 4.21).

### Collection of rates and government rent

17. As at 30 September 2015, the total amount of outstanding rates and government rent was \$172 million, representing 0.5% of the annual amount demanded of about \$33 billion. An ageing analysis of the outstanding rates and government rent shows that \$54 million (31%) had been outstanding for two years or more (para. 5.5).

## Executive Summary

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18. *Need to consider taking re-entry or vesting action for long outstanding arrears cases with charging orders registered.* In a sample check of nine arrears cases, Audit found that in one case, the defaulter had owed rates and government rent since 2007 for 16 properties against which the RVD obtained charging orders to protect the Government's legal interest in May 2010. In December 2015, after more than five years of unsuccessful attempts to demand payment, the RVD referred the 16 properties to the LandsD to consider taking re-entry or vesting action, at which time the amount in default had increased to \$1 million (para. 5.6).

19. *Need to expedite actions to deal with bona vacantia cases.* The Companies Ordinance (Cap. 622) provides that, where a company is dissolved, the property vested in the company immediately before its dissolution is vested in the Government as bona vacantia. As at 30 September 2015, there were 14 bona vacantia cases of outstanding rates and/or government rent amounting to \$1.3 million. The relevant properties were vested in the Government from 1997 to 2010. For 10 cases, the RVD took 7.5 years or more to refer them to the LandsD for taking possession of the defaulting companies' properties (para. 5.7).

### Audit recommendations

20. **Audit recommendations are made in the respective sections of this Audit Report. Only the key ones are highlighted in this Executive Summary. Audit has *recommended* that the Commissioner of Rating and Valuation should:**

#### *GRs*

- (a) **take measures to improve the accuracy of rental information furnished in Form R1As for GRs and closely monitor the situation (para. 2.16(a));**
- (b) **step up follow-up actions on repeated cases of non-compliance with Form R1A submission requirements, such as taking prosecution actions in warranted cases and issuing advisory letters in non-prosecuted cases (para. 2.16(c));**
- (c) **seek the assistance of the BD to improve the cost-effectiveness of obtaining rental information on subdivided properties for GR purposes (para. 2.16(e));**



## Executive Summary

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### *Interim valuations*

- (d) review the 2005 departmental instruction with a view to strengthening the procedures for using UBWs information obtained from the BD for rating assessment purposes (para. 3.40(a));
- (e) seek the assistance of the BD in extending the scope of the notification arrangements of assessable UBWs to cover those without removal orders issued (para. 3.40(b));
- (f) step up efforts in identifying un-assessed advertising signs for interim valuations (para. 3.40(d));
- (g) for the 32 cases of late interim valuations, take measures to prevent recurrence of similar problems (para. 3.40(f));

### *Rates exemption for rural properties*

- (h) put in place compliance checking of rates exemption eligibility of the village houses in DVAs (para. 4.22(a));
- (i) review the government rent records of the village houses within DVAs to see if there are ineligible cases of rates exemption and take prompt actions to revoke their rates exemption (para. 4.22(c));
- (j) seek the assistance of the LandsD in providing information on unauthorised change of use of agricultural land and buildings identified in the course of its enforcement work for taking timely actions on ineligible rates-exempted cases (para. 4.22(e)); and

### *Collection of rates and government rent*

- (k) remind staff concerned to refer long outstanding arrears cases with charging orders registered to the LandsD for consideration of taking re-entry or vesting actions in a timely manner and take prompt actions on bona vacantia cases (para. 5.8).

## Executive Summary

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21. Audit has *recommended* that the Director of Buildings should share with the RVD all UBWs information required for rating assessment purposes (para. 3.41).

22. Audit has *recommended* that the Director of Home Affairs should consider stepping up the field inspections of rates-exempted village houses (para. 4.23(b)).

23. Audit has *recommended* that the Director of Lands should remind the eight DLOs to complete the document checks and field inspections of rates-exempted village houses requested by the HAD in a timely manner (para. 4.24(a)(i)).

### Response from the Government

24. The Government generally agrees with the audit recommendations.