

THE HONG KONG HOUSING AUTHORITY

Memorandum for the Housing Authority

Management Enhancement Programme : Next Steps For Corporate Reform

PURPOSE

To seek Members' endorsement of proposals aimed at a further streamlining of service provision generally, and of the broad direction for increasing private sector involvement (PSI) in the Housing Authority (HA)'s estate management and maintenance (EMM) services in particular.

BACKGROUND

2. In meeting the goals of the Government's public housing programme, the HA and the Department as its executive arm have responded actively to changing social needs and demands for greater cost efficiency. Under the Management Enhancement Programme (MEP) launched in 1997, a number of reform initiatives both large and small, spanning all aspects of the HA's work have already been implemented. Examples of major reforms include -

- (a) re-organisation along business lines (including merger of management and maintenance functions);
- (b) establishment of corporate and business planning process;
- (c) devolution and decentralisation of responsibilities and accountability; and
- (d) reduction of development & construction lead time.

3. As the process of corporate reform has progressed, the real cost of service provision has been brought into clearer focus. At the corporate level, as highlighted by the Department in discussion of the 1999/2000's budget in the HA Finance Committee meeting held on 7 January 1999, the cost of corporate overheads appears to be disproportionately high when compared with other large public sector organizations. Increasing public expectations regarding both the quality and cost-effectiveness of the HA's service provision demand that this phenomenon be examined as a matter of some urgency.

4. At the business level, the search for greater cost efficiency has raised the question whether the HA could get better value for money from greater PSI in the provision of services. This question has become particularly acute in the area of EMM services as a result of the successful implementation of the Tenants Purchase Scheme (TPS) and other home ownership initiatives. Under these schemes, many of the HA's customers who are now tenants will become owners, with the right to choose who manages their property. This change of client base has obvious implications for the Department's staff.

5. The remainder of this paper sets out how the Department proposes to proceed on these issues. The first briefer section puts forward a proposal aimed at further streamlining service provision generally. The second longer section examines the recent Consultant's report on greater PSI in the management and maintenance of the HA's estates and makes recommendations on the way forward.

CORPORATE LEVEL - CUTTING OVERHEADS

6. The first HA Corporate Plan was produced in 1998. In the course of preparing this plan and its successor, it has become clear that corporate overheads appear excessively high. Corroboration of this in respect of one of the four core businesses has been provided by the recent report on greater PSI. However the reasons for the high overheads and the reasons for variations between the four core businesses are not clear. It is therefore proposed that a study be undertaken on the following -

- (a) establishing accurate service costing information;
- (b) analysing the reasons for any disproportionately high overhead costs;
- (c) streamlining the Department's organizational structure at all levels, and more specifically, de-layering and de-centralisation of support and overhead functions; and
- (d) strengthening internal control and auditing.

An independent consultant will be commissioned immediately to examine the above aspects and to make recommendations for improvements within six months. Implementation of any proposed changes will commence by mid 2000.

BUSINESS LEVEL - PRIVATIZATION OF EMM FUNCTIONS

7. The HA already makes good use of private sector skills and efficiency by contracting out a wide range of service provision from construction through to the EMM functions. As part of the search for increased cost-effectiveness under the MEP, a Consultant, PricewaterhouseCoopers, was commissioned in 1998 to explore the opportunities for greater PSI in service delivery generally and EMM services in particular. The following paragraphs summarize the Consultant's recommendations with regard to EMM services, give an account of the reaction of interested parties to them, set out the Department's view and make recommendations on the way forward.

CONSULTANT'S RECOMMENDATIONS

8. The Consultant presented their report to the HA on 4 March 1999 vide Paper No. HA 18/99. The report was released to the staff and interested parties on the same day. The Consultant's major observations and recommendations are -

- (a) There are benefits, both in terms of cost and service quality, from greater PSI in the Department's services.
- (b) There is a particular urgency to review the way EMM services are provided because of increasing opportunities for home ownership brought about by the TPS and other initiatives. If the owners choose not to hire the Department's services, and if the HA does nothing now, the number of surplus staff may reach some 4,000 in ten years' time (or approximately 1,300 discounting natural wastage).
- (c) Of the five options studied for greater PSI (subsidiary company, joint venture, private company, management buy-out, a phased service transfer), the phased service transfer will best meet the HA's needs, but the option of management buy-out can also be considered if staff come forward with workable proposals.
- (d) Property services in the private sector have now evolved into a well-developed market. While the private sector would have difficulty absorbing the whole of the HA's portfolio at one go, a phased transfer involving absorption of the Department's staff as part of the contracting out process would overcome this.
- (e) Phasing out the transfer of all existing EMM services within a period of 5 to 7 years would be both more manageable and less risky.

It should be noted that the essential differences between the phased service transfer and the existing outsourcing arrangement for EMM services of Home Ownership Schemes and new public rental housing estates are the grouping of estates into batches for service transfer and the condition that the successful bidders will take on staff who choose to join the private sector.

REACTION TO THE CONSULTANT'S REPORT

Staff & The Alliance of the Department's Staff Unions

9. Following the release of the Consultant's report, the Department has widely consulted the views of staff. A questionnaire was dispatched together with the executive summary of the Consultant's report to each and every staff of the Department. A fax hotline was set up and two open forums were arranged for staff. There were focus group discussions and goodwill visits, and meetings were arranged with staff representatives of the consultative committees. The Alliance of the Department's Staff Union has also presented their views to the HA Members and has counter-proposed a Sixth Option attached at **Annex A**.

10. Altogether about 3,900 questionnaires were received through the fax hotline, representing some 27% of the Department's establishment. A detail analysis of the response is given at **Annex B**, which shows that majority resist the Consultant's report, viewing it as a threat to their civil servants' status. Against this general resistance, there is however a spectrum of opinions shown, with some staff at one end expressing interest on the details of the release package, and some at the other indicating that they will stay put.

11. The Alliance's Sixth Option emphasizes staff's self-strengthening and a fair competition with the private sector over a two-year trial period. According to the Alliance's presentation to the HA Members, their stance is as follows -

- (a) they accept that reform is necessary;
- (b) they have no intention to become an obstacle in reform; and
- (c) they do not object to competition introduced by contracting out the EMM services, but they do request a chance to prove their cost-effectiveness under a streamlined management model with delegation of authority to the estate level.

The General Public & Tenants/Owners of the HA's Housing Stock

12. An independent consultant was commissioned to conduct surveys on the general public including the tenants/owners of the HA's housing stocks, basically on their expectation on the service standard, and their views on greater PSI in the HA's EMM services.

13. The opinions collected show increasing expectation to upgrade the EMM services, and are generally in support of greater PSI. Majority agree to the Consultant's observation that the PMAs would incur lower running costs and deploy their staff more flexibly than the Department. A summary of the quantitative and qualitative studies is attached at **Annex C** and a brief overview of the statistics is as follows -

	PRH	HOS/PSPS	Private	Overall
Support PSI	42%	65%	57%	52%
Against PSI	24%	8%	10%	14%
No comment	34%	27%	33%	34%

Property Management Agencies (PMAs)

14. A briefing session on the Consultant's report was held for the PMAs on the HA's Approved Lists, and meetings were arranged to solicit constructive views from individual PMAs. Their feedback is summarized at **Annex D**.

15. The PMAs are enthusiastic about greater PSI in the EMM services. They favour the phased service transfer approach recommended by the Consultant as they will be able to take up the EMM services in a progressive manner. The PMAs have also indicated that they have the capability to be engaged in a wider scope of services. They are prepared to take on the Department's staff although the differences in culture and employment terms would have to be ironed out, and they support the Consultant's view that staff should have a "clean break" with the Department allowing the PMAs to operate in a fully commercial way. The PMAs recognize that customer satisfaction and quality assurance are the key aspects in successfully pursuing greater PSI.

LegCo Members, Political Parties & Interested Groups

16. The Department has explained the rationale for exploring greater PSI in the HA's services to LegCo members of the Panel on Housing and the Panel on Public Service. The Department has met with leading political parties and interested groups to solicit views on the Consultant's observations.

17. The majority of the views consider increasing PSI as the trend to respond to changing social needs. There is a unanimous call for ensuring the service standard alongside cost-effectiveness consideration. While the effect on staff is a major concern, the common view is that decision on the HA's broad direction must be taken in terms of the public interest.

MAIN CONCERNS

18. From the feedback received, the benefits of introducing competition through greater PSI are well recognized, but not without reservation that the HA's commitment on EMM services may change, plus a number of concerns which can be summarized into the following major areas -

- (a) staff's job security, career prospect, the bridging-over arrangements, and the release package which will have to be fair and attractive to staff on the one hand and accountable to the public on the other;
- (b) the differentials in operating costs between the Department and the private sector should be addressed in parallel with the consideration of greater PSI;
- (c) performance monitoring on the EMM services to ensure no deterioration in the standard, or rather to seek an enhancement of the level of performance; and
- (d) the optimum time frame for the implementation of the phased service transfer notwithstanding the Consultant's recommendation of 5 to 7 years.

DEPARTMENT'S ASSESSMENT AND VIEWS

19. The Department notes that the HA's existing and on-going policy of involving the private sector in the provision of a wide range of the HA's services is supported by the Consultant, and that the Consultant also supports the HA's views that further privatisation and corporate reform are necessary to secure improvements in departmental efficiency.

20. The Department has examined the Consultant's report in the light of the feedback received. The Department acknowledges the concern raised, but is convinced that these do not outweigh the benefits to be gained from an enhanced and accelerated process of privatization. Beyond this the Department also feels that, faced with the inevitability of redundancies if nothing is done sooner, it would be irresponsible not to provide an outlet for staff willing to transfer to the private sector.

21. In deliberating on the broad direction forward, it has thus been guided by the following four general considerations -

- (a) there should be no change to the HA's commitment to providing public housing and related services to those in need;
- (b) the service standard of the HA's properties should be assured;
- (c) the right of customers to choose should be respected; and
- (d) staff should be treated fairly and reasonably, and in anticipation of customers choosing private sector management, every avenue should be explored to facilitate the transfer of staff who wish to join the private sector.

The Alliance's Proposal - The Sixth Option

22. Against this backdrop, the Department has considered the proposal put forward by the Alliance, the Sixth Option, with some care. While it does not doubt the sincerity of staff in putting forward the proposal, the Department has grave reservations as to whether it would be practicable. The cost difference between services provided by the Department and those provided by PMAs is simply too great. Nevertheless, as not all the HA's estates can be privatised at the same time, staff will have ample opportunity to demonstrate whether or not they can in fact compete effectively with

streamlined manning scales and procedures in the residual properties. The Department will be happy to work with staff in this endeavour.

23. In this context, the Department feels bound to point out that the substantial differentials in operating costs, both at the estate direct cost level and in terms of management overheads, do not in any way reflect on the capability of individual staff members, most of whom have served the Department loyally and diligently for many years. Rather the gap in cost effectiveness flows from important structural differences between the private and the public sectors, including salary packages, staffing structures, and civil service rules and procedures which inevitably constrain the Department from operating in a fully commercial way.

24. While the Alliance's Sixth Option in part echoes the Department's corporate reform in streamlining the organization structures and work processes, it under-estimates the effect of these constraints on both costs and service flexibility. For example it does not fully address the fact that -

- (a) the private sector has an edge over in-house EMM services as the PMAs have greater flexibility, not only in salary structure and employment terms, but also in scope of services;
- (b) a major part of in-house overhead costs identified by the Consultant relate to non-estate based direct staff costs which are part and parcel of the property management services (**Annex E**).
- (c) typically supervisory manning scales are leaner in the private sector, and with delegation of authority such that greater responsibility is shouldered at estate level.

Nevertheless, as suggested earlier staff will have the opportunity to test their ability to compete once the first of the new model privatisation contracts are let and a clear basis of cost comparison is readily available.

Staff Concerns

25. The concerns expressed by staff are understandable as the future to them seems uncertain. However, the views of the community clearly indicate the need for the HA to increase its cost-effectiveness and standard of services. At the same time the impact of TPS has made the consideration of greater PSI both necessary and urgent. It is clear that the Department cannot afford to do nothing, otherwise staff will face the inevitable consequence of redundancy as and when the owners choose not to hire the Department's service.

26. The Department fully understands staff's anxiety over their job security and recognises the need to develop bridging-over arrangements. It will therefore seek to -

- (a) facilitate transfer of staff to the PMAs, by means of tender conditions specifying the number and categories of staff to be absorbed on contracting out the EMM services of existing public rental housing (PRH) stock as well as new PRH estates, so as to increase job opportunities for staff;
- (β) leave it open to staff who feel confident that they have the ability to compete with the private sector to put forward proposals for the management of an estate or groups of estates on a practical commercial basis;
- (c) work out with other relevant bureaux and departments a time limited but flexible arrangement and the best possible release package for staff who opt either to join the private sector, form their own company, or retire; and
- (d) implement a comprehensive manpower planning strategy including freezing recruitment, training staff for enhanced competencies, re-deployment, etc.

Monitoring of Service Standard

27. As the EMM services are increasingly contracted out, it will be important to ensure that service standards are maintained. The current management system of PMAs will therefore be reviewed and enhanced, by including output specifications and re-vamping performance monitoring. Customer satisfaction and bench-marking will also be introduced into the appraisal system in order to drive the EMM services to a higher level.

Conclusion

28. The Department agrees that increasing PSI would provide a more flexible and potentially more cost-effective way of procuring EMM services; and that the most practicable means is by a phased service transfer approach. The major advantages over the other options are -

- (a) it effectively builds in immediate viability through competitive tendering from the outset;
- (b) the phasing will ensure that the private sector is able to digest the new workload in a predictable and progressive manner;
- (c) the proposed condition on taking on the Department's staff will allow the latter to transfer in an orderly manner on terms negotiated with new employers who will be competing with each other to hire expertise; and
- (d) it will enable the HA to manage risk effectively.

However, the Department also considers that the door should be left open for any management buy-out proposal. If staff can come forward with an equitable and workable business model, then this should be considered in a positive way, and support and assistance should be afforded where possible.

29. The Department shares the Consultant's view that it is important to establish a suitable pace for transferring services to the private sector in order both to enable a smooth transition and to avoid a long drawn out contraction of the Department. It will also be necessary to catch up with and then develop a momentum which keeps the process ahead of the rate of sell-off of flats under the TPS. This suggests a rate of no fewer than 25,000 units in the first year and 50,000 thereafter from the existing PRH stock. However the Department is at the same time conscious of the complexities involved in getting the process underway.

30. Thus while endorsing the broad direction of greater PSI, the Department acknowledges that much work will need to be done to translate the proposed phased transfer of services to the private sector into action. Many implementation details including the scale and progress of the service transfer, the qualifications for tendering, the batching of tenders and the terms of the new contracts, all remain to be decided. So also do the terms of the package for staff willing to transfer. It is therefore proposed that a Task Force under the HA be immediately formed to consider the implementation issues, with terms of reference as proposed at **Annex F**. The Task Force should report back to the HA on its deliberations within six months.

FINANCIAL IMPLICATIONS

31. The Consultant estimates that there would be potential annual savings of roughly \$1 billion (or about \$0.9 billion after allowing some necessary recurrent costs, e.g. contract management and monitoring costs, to be incurred after the transfer) if the entire current PRH stock were placed under the management of PMAs. However, this has not taken into account the transition costs for HD staff to transfer to the private sector. It is not possible to accurately ascertain the transition costs at this stage in the absence of details about the number of staff who opt to leave the Civil Service and the release package to be offered to them. Subject to Members' decision on the broad direction, the related staff transfer packages together with the financial implications will be worked out and submitted to the HA for endorsement in due course.

DEPARTMENT'S RECOMMENDATIONS ON PSI

32. The broad direction on PSI is recommended as follows -
- (a) to enhance and accelerate PSI in the HA's EMM services, and to continue to explore other opportunities for PSI;
 - (b) to adopt the phased service transfer approach in transferring the EMM services to the private sector;
 - (c) to leave the door open to staff who wish to put forward a viable management buy-out proposal; and
 - (d) to set up a Task Force under the HA to consider issues on implementation of greater PSI in the EMM services and to report back to the HA on its deliberations within six months.

WAY FORWARD

33. Subject to the HA's endorsement of the proposal put forward in Paragraph 6 above, an independent consultant will be immediately commissioned to advise on further streamlining of the Department's service provision with a view to commencing implementation of any proposed recommendations by mid 2000.

34. Subject to the HA's endorsement of the broad direction on PSI as recommended in Paragraph 32 above, the action plan is as follows -

- (a) consult the Government (in particular Civil Service Bureau and Finance Bureau) and develop the release package and bridging-over arrangements and commence formal consultation with staff as soon as possible;
- (b) submit proposals to the HA Task Force on the new form of contract, the batching of contracts and transfer arrangements for staff, with a view to seeking endorsement from the HA and the Government before implementation; and
- (c) implement the first batch of phased service transfer by mid

2000.

ADVICE SOUGHT

35. At the HA meeting on 6 May 1999, Members will be asked to discuss and endorse the proposal for examining ways of further streamlining service delivery in general as recommended in Paragraph 6, and the broad direction on phased transfer of EMM functions as recommended in Paragraph 32 above in particular.

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