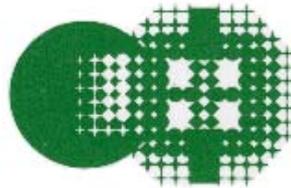


DIRECT INVESTIGATION REPORT

**GOVERNMENT'S REGULATION
OF GUESTHOUSES**



**Office of The Ombudsman
Hong Kong**

CONTENTS

<i>Chapter</i>		<i>Paragraph</i>
1	<i>INTRODUCTION</i>	
	<i>Background</i>	1.1 - 1.4
	<i>Process and Scope of Investigation</i>	1.5 - 1.12
2	<i>OUR FINDINGS</i>	
	<i>Licensing Regime</i>	2.1 - 2.10
	<i>Measures to Combat Unlicensed Guesthouses</i>	2.11 - 2.18
	<i>Public Views on the Existing Regulatory Regime</i>	2.19 - 2.23
	<i>Guesthouse Operation Violating Lease Conditions</i>	2.24 - 2.26
3	<i>THE CONSULTATION PAPER</i>	3.1
	<i>Enhancing the Licensing Regime</i>	3.2
	<i>Stepping Up Enforcement Against Unlicensed Guesthouses</i>	3.3
4	<i>COMMENTS AND RECOMMENDATIONS</i>	
	<i>Comments</i>	4.1 - 4.10
	<i>Recommendations</i>	4.11 - 4.12
	<i>Acknowledgements</i>	4.13

1

INTRODUCTION

BACKGROUND

1.1 In Hong Kong, operation of guesthouses is regulated by the Office of the Licensing Authority (“OLA”) under the Home Affairs Department (“HAD”). Pursuant to the Hotel and Guesthouse Accommodation Ordinance (“the Ordinance”), OLA assesses the fire and structural safety of the premises to be used for the guesthouse when processing a guesthouse licence application. Where a guesthouse is found to have violated any regulations or to be operating without a licence, OLA will prosecute the operator when sufficient evidence is to hand.

1.2 This Office has received, from time to time, public complaints about OLA loosely issuing licences to guesthouses in multi-storey buildings without taking into account the dangers and nuisances that those guesthouses may cause to other people living in the same building. In some cases, the complainants alleged that OLA had issued licences even though operation of guesthouses was in violation of the deeds of mutual covenant (“DMCs”) of the buildings.

1.3 Other complainants reproached OLA for its ineffective enforcement against unlicensed guesthouses, which had resulted in the proliferation of such unlicensed establishments. Many such cases appeared to pose fire risks and structural safety problems to the buildings.

1.4 In December 2013, a fire broke out at Continental Mansion in North Point, resulting in one death and more than 20 injuries, involving tourists staying in the guesthouses in the building. The incident revealed that there were not only licensed but also many unlicensed guesthouses in the building. The public were greatly concerned whether Government had been properly regulating the operation of guesthouses.

PROCESS AND SCOPE OF INVESTIGATION

1.5 Against this background, we initiated a direct investigation assessment (“DI assessment”) (in other words, a preliminary inquiry) in January 2014 to examine the need for a direct investigation to probe into the systemic and procedural inadequacies in the current regime for regulation of guesthouses.

1.6 During the DI assessment, we studied the Ordinance, the Administration’s guidelines on application for licences to operate guesthouses and other businesses, as well as relevant media reports. We also sought information from HAD direct.

1.7 Having examined the above information, we considered it necessary to delve into the following two areas:

- (1) whether the current system for guesthouse licensing is sufficient to protect the safety and interests of lodgers and the public; and
- (2) whether Government’s mechanism and measures are effective in combating unlicensed guesthouses.

1.8 Accordingly, on 5 June 2014, The Ombudsman declared her initiation of a direct investigation, under section 7(1)(a)(ii) of The Ombudsman Ordinance, against HAD, so as to obtain further information from the Department. On 12 June, we issued a press release on our commencement of the direct investigation to invite views and information from the public on the subject.

1.9 Since some guesthouses are allegedly operating in violation of not only the DMCs of the buildings but also the restrictions on land use stipulated in the land leases, we also made enquiries to the Lands Department (“Lands D”), which is responsible for enforcement of land lease conditions.

1.10 To better understand the actual operation of licensed and unlicensed guesthouses, our investigation officers conducted inspections in districts where the guesthouse business is particularly thriving, including Causeway Bay, North Point, Tsim Sha Tsui and Mong Kok.

1.11 On 4 July, HAD launched a public consultation exercise on the review of the Ordinance. On 10 July, we held a meeting with HAD officials to exchange views on the proposals in the consultation paper.

1.12 On 25 July, we issued a draft investigation report to HAD and relevant parts to Lands D, to invite their comments. Having considered such comments, we finalised the report on 14 August 2014.

2

OUR FINDINGS

LICENSING REGIME

Origin of the Licensing Regime

2.1 In 1988, a fire broke out in a guesthouse in Chungking Mansions in Tsim Sha Tsui, causing the death of a tourist. The incident aroused wide public concern. In the wake of the incident, Government decided to establish a licensing regime through legislation to regulate the hotel and guesthouse business. The Ordinance was enacted in June 1991.

2.2 In drafting the legislation, Government had consulted various stakeholders and the then Legislative Council. In the paper presented to the Council, the Administration stated that:

- (1) The primary objective of legislation was to ensure, through a licensing regime, that the premises used as guesthouses meet the prescribed standards in respect of **building structure** and **fire safety** so as to protect the lodgers and the public.
- (2) Compliance with the provisions of the **land lease** or **DMC** is **not** a licensing requirement. Any breach of such provisions should be dealt with by the relevant Government department or owners of the building through exercising their legitimate powers to take appropriate action.

Relevant Legal Provisions

2.3 As stipulated in section 8(3) of the Ordinance, the Hotel and Guesthouse Accommodation Authority (i.e. the Secretary for Home Affairs; with OLA

delegated the authority to perform the relevant functions) may refuse to issue a licence in respect of a guesthouse if it appears to him:

- (a) that for reasons connected with –
 - (i) the situation, means of ingress or egress, design, construction, size, equipment, or type of building; or
 - (ii) the protection of life and property under the Fire Services Ordinance,

the premises to be used for the guesthouse are not fit to be used for the purposes of a guesthouse;
- (b) that such premises do not comply with any requirement relating to design, structure, fire precautions, health, sanitation and safety set out in the Buildings Ordinance; or
- (c) that the operation, keeping, management and other control of the guesthouse would not be under the continuous and personal supervision of the person to whom the licence is issued.

2.4 Section 8(4) of the Ordinance provides that where the Hotel and Guesthouse Accommodation Authority refuses to issue a licence, he shall make a written order to that effect stating the ground in the above paragraph on which he has refused to issue a licence.

Factors Not Considered in Licensing

2.5 HAD has explained to us that it is not empowered by the Ordinance to reject a licence application for reasons other than those specified in section 8(3) of the Ordinance (**para. 2.4**). The Department, therefore, will not refuse to issue a licence to a guesthouse on the grounds that its operation is in breach of the provisions of the land lease or DMC, or has met with public objection.

2.6 HAD has also pointed out that the DMC is a private covenant among the owners, the property manager and the developer of the building. Those parties are entitled to exercise their powers conferred by the DMC and take appropriate

actions against those who have breached the DMC provisions. The contents of DMCs differ from building to building. Whether a DMC contains any provisions restricting operation of guesthouses in the building involves interpretation of a private agreement. HAD is not in a position to intervene.

2.7 Nonetheless, guesthouse licences issued by OLA will not waive any conditions in any lease, tenancy agreement or other licence granted by Government, nor will they affect or change the provisions of the DMC of the building or other private agreements. OLA has clearly reminded all licensees that they are liable for any consequences if operation of guesthouses on the premises concerned is in violation of the terms and conditions of the relevant lease or covenants.

Licensing Procedures

2.8 Upon receipt of a licence application, the professional staff of OLA, seconded from the Buildings Department (“BD”) and the Fire Services Department (“FSD”), will inspect the premises concerned to conduct surveys relating to building structure and fire safety. OLA may require the applicant to carry out improvement works. With reference to the requirements on means of escape in the Buildings Ordinance and the layout plans approved by BD, OLA will specify in the licensing conditions the maximum number of lodgers that the guesthouse may accommodate, so as to ensure that the total number of occupants expected within the building after the establishment of the guesthouse will not exceed the maximum capacity specified in the approved plans.

2.9 In processing an application for licence renewal, OLA officers will likewise conduct site inspections. Licence renewal will only be approved after OLA has confirmed that the premises concerned still comply with the safety standards.

Statistics

2.10 Between 2011 and 2013, the numbers of licensed guesthouses and new guesthouse licences issued are as follows:

Year	2011	2012	2013
Number of licensed guesthouses	1,400	1,493	1,600
Number of new guesthouse licences issued	64	125	145

MEASURES TO COMBAT UNLICENSED GUESTHOUSES

Inspection and Investigation

2.11 Since 2011, FSD officers with law enforcement experience have been seconded to the Enforcement Team of OLA to step up enforcement against unlicensed guesthouses. OLA has also increased its manpower and recruited frontline officers with law enforcement experience to achieve this end. Where suspected cases of unlicensed guesthouse operation are found or reported, OLA will conduct inspections. If there is sufficient evidence that the premises in question involve unlicensed guesthouse operation, OLA will institute prosecution. Moreover, OLA will concentrate its efforts on inspecting buildings with higher risk of fire.

2.12 In recent years, some unlicensed guesthouses have tried to camouflage their operations by advertising and conducting transactions on the Internet only. In view of this trend, OLA has formed a dedicated Internet enforcement team to closely monitor websites, discussion forums, blogs, etc., to collect intelligence on suspected unlicensed guesthouses as well as to advise tourists to choose licensed guesthouses.

2.13 According to HAD, in case of OLA officers' repeated failures to enter a suspected unlicensed guesthouse for inspection, OLA will write to the owner of the premises and the guesthouse operator to request their cooperation to enable its officers to enter the premises.

Penalty and Statistics on Enforcement

2.14 Any person who operates an unlicensed guesthouse commits a crime and is, upon conviction, liable to the maximum penalty of a fine of \$200,000 and imprisonment for two years, as well as a fine of \$20,000 for each day during which the offence continues.

2.15 For the period 2011-2013, the statistics in connection with enforcement actions against unlicensed guesthouses are as follows:

	Year	2011	2012	2013
(1)	Number of complaints about unlicensed guesthouses	696	1,418	1,225
(2)	Number of inspections of unlicensed guesthouses	3,125	6,791	9,889
(3)	Number of prosecutions against unlicensed guesthouses	53	128	171
(4)	Number of convictions	39	110	161
(5)	Highest fine imposed	\$20,000	\$50,000	\$20,000
(6)	Longest term of imprisonment imposed	3 months	2 months	2 months

2.16 HAD attributes the low albeit rising prosecution figures (**item (3) of para. 2.15**) to the very high standard of proof (i.e. beyond reasonable doubt) required by the court in prosecutions against unlicensed guesthouse operations because operation of unlicensed guesthouses is a criminal offence, conviction of which can lead to imprisonment and constitute a criminal record. Therefore, OLA must prove that the premises in question are providing rent-charging short-term accommodation before bringing a prosecution against the operator. OLA officers can often find circumstantial evidence (including subdivisions of the premises, receipts for daily rental provided by tourists, etc.) during inspections. However, most tourists refuse to give a witness statement or are reluctant to travel to Hong Kong again to give evidence in court. Legal advice from the Department of Justice is that mere circumstantial evidence is not sufficient to prove unlicensed guesthouse operations on the premises on the material day and, therefore, prosecution is not recommended in such cases.

2.17 HAD also indicated that the successful convictions of unlicensed guesthouse operations between 2011 and 2013 (**item (4) of para. 2.15**) were all achieved by decoy operations by OLA officers enabling their collection of sufficient evidence for prosecution.

Findings from Our Site Inspections

2.18 During site inspections (**para. 1.10**), our officers noticed that it was not unusual for licensed guesthouse operators to also run unlicensed guesthouses in other units within the same building (commonly known as “shadow guesthouses”). Our officers actually witnessed staff of the licensed guesthouses unscrupulously showing visitors to those “shadow guesthouses”, which had been subdivided into a number of guestrooms connected by only one narrow corridor. Such units were clearly not on the list of licensed guesthouses on OLA’s website.

PUBLIC VIEWS ON THE EXISTING REGULATORY REGIME

2.19 Based on the public comments received during our direct investigation (**para. 1.8**) and relevant newspaper reports, we note the following views of residents and guesthouse operators.

Views of Residents / Owners’ Corporations

2.20 People residing in multi-storey buildings where guesthouses exist have found their daily lives adversely affected by the increasing number of guesthouses in recent years. Problems include:

- environmental hygiene condition deteriorates due to the increasing amount of refuse, with additional cleaning costs to be borne by all owners of the building;
- conflicts often arise between residents and guesthouse lodgers over the use of lifts;
- frequent repairs are required due to over-use of lifts, with all owners having to share the costs;
- water and electricity supply and sewage are also affected; and
- the large number of strangers entering the building causes security concern.

2.21 Some residents consider it irresponsible of HAD to suggest owners of the building to take legal action against guesthouse operators for violating the provisions of the DMC (**paras. 2.6 and 2.7**). They criticise Government for creating conflicts by issuing licences to guesthouse operators in full knowledge that such operations may be in violation of DMC provisions. The owners of the buildings are left with the problem and the associated legal costs.

2.22 In general, residents of buildings are of the view that HAD should, when processing guesthouse licence applications, examine whether the operation of guesthouses is in violation of the DMC provisions of the buildings concerned, and that HAD should consult residents on each licence application.

Views of Guesthouse Operators

2.23 However, in guesthouse operators' view, the existing regulatory regime is adequate to ensure the safety of lodgers of licensed guesthouses and residents of the buildings concerned. All Government has to do is to combat unlicensed guesthouses. DMC provisions and residents' views should not be included as conditions for guesthouse licensing, since there is no difference between the operation of guesthouses and that of other businesses like coffee shops, hair salons and tutorial schools in multi-storey buildings in terms of their impact on residents. It would be unfair to guesthouse operators if Government imposes additional licensing requirements only on this trade.

GUESTHOUSE OPERATION VIOLATING LEASE CONDITIONS

2.24 As regards whether guesthouse operation may violate the land use restrictions stipulated in the land leases of some premises, Lands D has explained to us that, generally speaking, if the land lease stipulates that the premises are designated for "private residential use" or "industrial use" only, guesthouse operation will be considered to be in breach of the land lease.

2.25 Lands D has also told us that it will conduct an investigation whenever it receives a complaint or referral about violation of lease conditions by guesthouse operation. Where such violation is confirmed, Lands D will seek legal advice if necessary and then take appropriate lease enforcement action. It may first issue a warning letter to the offender and have it registered with the Land Registry. If the

warning is not heeded, Lands D may consider re-entering the site.

2.26 According to the information provided by Lands D, it received a total of 12 relevant complaints/referrals between 2011 and 2013. After investigation, the Department confirmed that none of those cases had violated the lease conditions.

3

THE CONSULTATION PAPER

3.1 After we publicly declared our commencement of this direct investigation, HAD, in view of the concerns of different sectors of the community about the existing regulatory regime for guesthouses, launched on 4 July 2014 a public consultation exercise on review of the Ordinance (**para. 1.11**). In its consultation paper, HAD made a number of improvement proposals, which focus on two areas:

- (1) enhancing the licensing regime; and
- (2) stepping up enforcement against unlicensed guesthouses.

ENHANCING THE LICENSING REGIME

3.2 Regarding the licensing regime, HAD made, *inter alia*, two proposals of amending the Ordinance to allow the Department in processing applications for guesthouse licences:

- (1) to refuse to issue/renew licences or cancel existing licences on the ground that the DMC provisions of the building concerned explicitly prohibit the operation of guesthouses; and
- (2) to take into account residents' views collected through local consultation.

STEPPING UP ENFORCEMENT AGAINST UNLICENSED GUESTHOUSES

3.3 As regards enforcement against unlicensed guesthouses, HAD made, *inter alia*, three proposals of amending the Ordinance:

- (1) to add “deeming provisions” to the Ordinance for admission of “circumstantial evidence”, such that the standard of proof by OLA can be lowered to facilitate prosecution against owners and operators of unlicensed guesthouses;
- (2) to make provisions empowering OLA to apply for a court warrant for entry into, and breaking in if necessary, any suspected unlicensed guesthouses for inspection; and
- (3) to increase the maximum penalty for operating unlicensed guesthouses to a fine of \$500,000 and imprisonment for three years, in the hope that the court would impose heavier sentences compared with the present.

4

COMMENTS AND RECOMMENDATIONS

COMMENTS

4.1 Based on our findings in Chapter 2, we have the following comments on the current licensing regime for guesthouses and enforcement measures against unlicensed guesthouses.

Licensing Regime for Guesthouses

4.2 Given the legislative intent of the Ordinance (**para. 2.2**) and the relevant provisions (**paras. 2.3** and **2.4**), this Office considers that HAD, in processing applications for guesthouse licence, has been acting in accordance with the law and within the powers conferred by the Ordinance when it takes into account only such factors as building structure and fire safety but not the provisions of the land lease or DMC. From an administrative point of view, we cannot say that there is impropriety.

4.3 Nevertheless, the number of guesthouses has been continuously on the rise in recent years owing to tourists' surging demand. Understandably, some residents feel that their daily lives have been affected by the operation of guesthouses in their buildings (**para. 2.20**). They clearly expect that Government's regulation of guesthouses should address not only safety concerns, but also the basics of their daily lives. The fact that DMC provisions and residents' views are left out in the current licensing regime is an issue that Government must tackle. We consider that HAD, as the licensing authority for guesthouses, should have much earlier reviewed the issue and introduced improvement measures or even legislative amendments, so as to address the community's concerns.

4.4 At long last, HAD has embarked on a public consultation exercise on review of the Ordinance and proposed in the consultation paper that explicit restrictive provisions in the DMC (**para. 3.2(1)**) (“proposal (1)”) and residents’ views (**para. 3.2(2)**) (“proposal (2)”) be taken into account when the Department processes applications for guesthouse licence.

4.5 We support proposal (1), as it would spare the owners of the building the hassles and costs of litigating with the guesthouse operator after the latter has been issued a licence by HAD (**para. 2.21**).

4.6 As for proposal (2), we also find it worthy of support in principle. However, we note the concern of the guesthouse operators about the likely impact of imposing such an additional licensing requirement on the trade. We, therefore, consider it necessary for details of the proposal to be carefully worked out. For those licence applications that have fully met the legal requirements (including the possible new requirements of compliance with the DMC and even the land lease after legislative amendment (**para. 4.7**)), HAD should exercise prudence when conducting local consultation and considering residents’ views on licence applications. To this end, the Department is recommended to devise a set of reasonable and workable criteria for assessing the objections raised by residents so as to ensure fair and impartial vetting of licence applications.

4.7 In its consultation paper, HAD has not proposed that it can refuse to issue/renew licences or cancel existing licences on grounds of the restrictions on land use stipulated in the land lease. HAD does not consider that necessary as cases of breach of land lease conditions are few and far between. Indeed, the information provided by Lands D indicates that there were no proven cases of breach of land lease between 2011 and 2013 (**para. 2.26**). Nevertheless, one cannot rule out the possibility of such cases in the future. In our view, Government should seriously consider taking this opportunity of legislative amendment to include compliance with land lease conditions as a licensing requirement, such that any cases of breach of land lease can be prevented.

4.8 We understand that Lands D has all sorts of land administration matters to deal with. Some of those matters can be rather complex. It may take the Department a long time to take lease enforcement action. If HAD could at the outset consult Lands D when processing licence applications, any breach of land lease can

thereby be averted. That can save residents of the buildings concerned the troubles of complaining to Lands D against such breach later on and of waiting for the Department to take lease enforcement action.

Enforcement Measures against Unlicensed Guesthouses

4.9 Although OLA has, in the past few years, increased manpower and stepped up inspections and investigations of the proliferating unlicensed guesthouses (**paras. 2.11** and **2.12**), the seriously low prosecution rates (**item (3) of para. 2.15**) show that its enforcement actions have been largely ineffective. The main reasons are:

- (1) currently, Government cannot institute prosecutions merely based on “circumstantial evidence” (**para. 2.16**);
- (2) uncooperative owners and operators of guesthouses make it difficult for OLA officers to enter the premises for investigation (**para. 2.13**);
- (3) the penalties are too lenient (**paras. 2.14** and **2.15**); and
- (4) more decoy operations for collecting evidence are called for (**para. 2.17**).

4.10 We consider that HAD should have sought to change its enforcement strategy much earlier in the face of the abovementioned unsatisfactory situation (e.g. to redeploy resources to conduct more decoy operations for collecting evidence). In fact, in our previous investigations of complaint cases, we had already suggested that HAD devise new strategies to counter the ever-changing ploys of unlicensed guesthouses. The consultation paper recently released by the Department has included several proposals for improvement in the right direction, including: the introduction of “deeming provisions” that will allow admission of “circumstantial evidence”; the empowerment of OLA to apply to the court for entry warrants, as well as the imposition of heavier penalties (**para. 3.3**). We believe that those measures will enhance the effectiveness of HAD’s enforcement actions. Since HAD has acknowledged that admissible evidence can be collected by decoy operations (**para. 2.17**), we would suggest that OLA further extend its use of decoy operations.

RECOMMENDATIONS

4.11 In sum, this Office generally supports the improvement proposals in HAD's consultation paper. The Ombudsman, however, urges the Department:

- (1) if it decides to conduct local consultation during the licensing process, to draw up a set of reasonable and workable criteria for assessing residents' objections (**para. 4.6**); and
- (2) to consider including compliance with land lease conditions as a licensing requirement (**paras. 4.7 and 4.8**).

4.12 We appreciate that the legislative amendments proposed by HAD would take time. The Ombudsman, therefore, also urges that HAD should in the interim:

- (3) further enhance OLA's investigation of unlicensed guesthouses by conducting more decoy operations to obtain evidence in order to increase the effectiveness of its enforcement actions (**para. 4.10**).

ACKNOWLEDGEMENTS

4.13 The Ombudsman is grateful to HAD for its full cooperation and to Lands D for the assistance rendered during the course of this investigation.

Office of The Ombudsman

Ref: OMB/DI/354

August 2014