

**Initial Views from the Law Society of Hong Kong, the Bar Association
and the Real Estate Developers Association**

<u>Comments</u>	<u>Response by Administration</u>
1. Conversion	
(a) Working Party on the Land Titles Ordinance (WP) of The Law Society of Hong Kong	
<p>(i) <u>Doubt on the effect of proposed conversion mechanism to solve the problem</u></p> <p>WP considered that the new proposed conversion mechanism would not assist to identify the problem registers but would just prolong resolution of the problem for 12 more years, allowing for more potential transactions to come onto the problem registers before these registers would be dealt with on an application for upgrading.</p>	<p>Under the proposed conversion mechanism, absolute title would not be vested in respect of problem cases on conversion. The position of the parties concerned would not be worse off than their existing position under the Land Registration Ordinance (Cap. 128) (LRO).</p>
<p>(ii) <u>Indefinite dual system</u></p> <p>WP found it difficult to accept the idea of provisional title when such title could be condemned in perpetuity and there would be no mechanism to ensure all provisional titles would mature into absolute ones.</p>	<p>Whether a property could be upgraded depended on whether the 'owner' had good holding title. It would be fundamentally wrong in principle to convert a bad or doubtful title to absolute title.</p>
<p>(iii) <u>Government should deal with problematic registers forthwith to prepare for automatic conversion 12 years later</u></p> <p>WP considered that the Government should be more proactive and try to identify and deal with the problematic registers forthwith to prepare for automatic conversion 12 years later.</p>	<p>There were currently around 2.8 million land registers kept in the Land Registry (LR). Given the volume of these registers and continuous activities in the property market, it would be impractical to go through all the registers within 12 years to identify all problem registers.</p>

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<p>(iv) <u>Lack of concrete examples of problem registers</u></p> <p>WP pointed out that the Administration had not given any concrete examples of the problematic registers and had not briefed it fully on what the risks were relating to the problem registers, or indeed whether or not there were such risks.</p>	<p>The Administration is arranging to meet the WP with examples of the problem registers by way of mock transactions.</p>
<p>(v) <u>Doubt on Government's liability for the problematic registers</u></p> <p>WP considered that the Government's liability for the problem registers would probably be very small. It would be hard to imagine a significant portion of the LRO registers involved conflicting claims but the interested parties were happy to ignore the conflicting claims.</p>	<p>The Administration could not safely assume that the Government's liability for the problem registers is small. We consider it necessary to screen all the 2.8 million land registers before upgrading.</p>
<p>(vi) <u>Reliance on the integrity of registration system and objection to late stage substantial change</u></p> <p>WP pointed out that the Government indicated on day one that it had confidence on the integrity of the registration system under the LRO; and the drafting of the LTO had proceeded on that basis. WP found it difficult to understand why the Government, having told the profession, the LegCo and the community that the registration system under the LRO could be relied on for daylight conversion, decided to go back and say at this late stage that there should be very substantial change on the conversion mechanism just because of the existence of an insignificant number of problem registers.</p>	<p>One of the purposes of the post-enactment review of the Land Titles Ordinance (Cap. 585) (LTO) was to give full consideration to the impact of the significant changes made to the Land Titles Bill at the committee stage. As part of the review, the LR has been tasked to review all risks involved in implementing automatic conversion.</p> <p>The Administration fully understood WP's concern at the suggestion of introducing a significant change to the conversion mechanism. But, given the potential liabilities to public fund, measures to manage the risk are necessary.</p>

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(b) Hong Kong Bar Association (Bar Association)	
<p>(i) <u>Agree to the benefits of the proposed conversion mechanism</u></p> <p>The Bar Association agreed that there would be some benefits in the proposed conversion of existing land to an interim status of ‘converted land’ after three years and upgrading to full title after a further period of 12 years.</p>	<p>The Administration noted this point.</p>
<p>(ii) <u>Caveat</u></p> <p>The Bar Association noted that under the enacted LTO, protection was given to unwritten equities by registration of caveats throughout the 12 years before automatic conversion. However, under the proposed conversion mechanism, there was no provision for registration of unwritten equities prior to conversion. The Bar Association was in favour of retaining the protection afforded to the unwritten equities even under the proposed conversion mechanism.</p>	<p>Under the proposed conversion mechanism, the holder of a pre-conversion unwritten equity might at any time after conversion but before upgrading of title record a warning note to protect his interest. The Administration did not wish to complicate the system by implementing a caveat system under the LRO for registering such interests, which would only be used for about three years. During this three-year period the holder of an unwritten equity might at any time take legal action and register a lis pendens under the LRO to protect his interest. His right remained unaffected under the proposed conversion mechanism.</p>
(c) The Real Estate Developers Association of Hong Kong (REDA)	
<p><u>No principle objection</u></p> <p>REDA replied that they had no in principle objection to the proposed alternative conversion mechanism.</p>	<p>The Administration noted the comment.</p>
2. Rectification and Indemnity Provisions	
(a) WP	
<p>(i) <u>Agree in Principle</u></p> <p>WP agreed with the proposals in principle regarding proposed changes to provisions on fraud affecting new land.</p>	<p>The Administration noted the comment.</p>

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<p>The proposals were (a) the mandatory rectification rule in section 82(3) would be maintained, subject to specific exceptions; and (b) an innocent former owner not restored to the title register due to the operation of any of the exceptions would be eligible for indemnity.</p>	
<p>(ii) <u>Inconsistency between converted title property and registered title property</u></p> <p>Regarding the proposal that a property with converted title would be subject to subsisting interests and that, prior to upgrading, the mandatory rectification rule and the rectification exceptions would not apply to fraud committed before conversion, WP was concerned that there would be inconsistencies if common law principles were to apply before upgrading.</p>	<p>Prior to upgrading of title, interests under LRO and common law remain undisturbed. Existing common law principles would continue to apply to converted properties as if they had not been converted. For pre-conversion fraud, LTO rectification provisions and proposed exceptions would not apply. Common law principles would continue to apply.</p>
<p>(iii) <u>Limiting the right of indemnity to ‘loss of ownership’</u></p> <p>Regarding who would be entitled to claim indemnity, WP noted that it would be limited to cases where there had been a ‘loss of ownership’. The WP believed the proposal should refer to ‘title’ rather than ‘ownership’ and had concern as there would be occasions that someone having an interest in registered land could suffer loss although the title of the owner had not been lost.</p>	<p>It had always been the Administration’s intention to compensate a person who suffered loss by or as a result of fraud which affected ownership of registered land. ‘Title’ was not defined whilst ‘owner’ was a well-defined word under LTO. Ownership is an easily understandable concept in LTO context.</p>
<p>(iv) <u>Apportionment amongst multiple claimants</u></p> <p>WP believed the proposal on the apportionment of the indemnity amount should be subject to any contrary intention expressed by parties, in particular chargor and chargee.</p>	<p>The proposed apportionment did not affect distribution of indemnity between owner and his chargee. It applied to apportionment of indemnity between an owner and other claimants such as tenants.</p>

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<p>(v) <u>Finance for starting off indemnity fund</u></p> <p>WP noted the Government’s concern that indemnity fund would be accepting liabilities without income to offset them. WP recalled that the Government agreed earlier to provide seed money to start off the indemnity fund.</p>	<p>The Government agreed to provide a loan as seed money to start off the indemnity fund. The loan had to be repaid to the Government. The indemnity fund would be self-financing with income generated from the levy. The Government could not accept unquantifiable and unlimited liabilities without income to offset them.</p>
<p>(vi) <u>Application to daylight conversion system</u></p> <p>WP could not see why the proposed exceptions to mandatory rectification rule should not equally apply to the daylight conversion system.</p>	<p>The proposed exceptions could not apply to daylight conversion as no indemnity would be payable for pre-conversion fraud discovered after conversion under daylight system. If proposed exceptions were to apply, a former owner who lost property due to pre-conversion fraud might not be able to recover his property and no indemnity would be payable. His position would be worse than his existing position under the common law.</p>
<p>(b) Bar Association</p>	
<p>(i) <u>Cap on indemnity</u></p> <p>The Bar Association restated its strong objection to the upper limit on indemnity payable to an innocent owner whose interest was extinguished by reason of the rectification provisions under the LTO.</p>	<p>The concern with upper limit on indemnity in fraud cases was noted. In considering any changes to the rectification and indemnity provisions, the Administration appreciated that these concerns would need to be taken fully into account before a decision was made on how to proceed.</p>
<p>(ii) <u>Arbitrary exceptions</u></p> <p>The proposed exceptions to mandatory rectification seemed rather arbitrary. The different treatment of the first registered owner after the fraud and subsequent registered owners (albeit both innocent) may be perceived as unfair or arbitrary.</p>	<p>Some jurisdictions adopt ‘immediate indefeasibility’ whilst others adopt ‘deferred indefeasibility’. It was proposed to adopt ‘deferred indefeasibility’ in Hong Kong because the first registered owner when acquiring a property from a fraudster would</p>

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	<p>have opportunity to conduct the necessary enquiries to avoid the fraud. The second registered owner had no such opportunity. This principle represented a fair balance of interests among innocent parties in case of fraud.</p>
<p>(iii) <u>Exception relating to multiple purchasers</u></p> <p>As a matter of principle, it would be difficult to justify the exception where property had been divided up and sold to multiple purchasers. It would seem unfair that a defrauded former owner whose property was sold to one purchaser would have his title restored whereas a defrauded former owner whose property had been divided and sold to two purchasers would not be restored to ownership of the property.</p>	<p>The exception would only apply in very limited circumstances. It would only apply when a property acquired by fraud was redeveloped or divided up and sold <u>directly</u> by fraudster to two or more purchasers. The proposal represented a fair balance of interests among innocent parties in case of fraud.</p>
<p>(iv) <u>Inconsistency between converted title property and registered title property</u></p> <p>For pre-conversion fraud, distinction between converted title properties and registered title properties could lead to anomalies. In case of pre-conversion fraud, owner of converted title property would be displaced by innocent former owner and would not be entitled to indemnity. However, if the claim was made/established after upgrading, the owner would be entitled to indemnity. The right of registered owner to claim indemnity would depend entirely on the date that the claim of the innocent former owner was made/established.</p>	<p>For pre-conversion frauds, common law rules would continue to apply prior to upgrading. Purchaser would take property subject to subsisting interests. An innocent former owner would recover property in case of void transaction while an innocent purchaser would lose the property without indemnity. After upgrading of title, full benefit of title registration system would be afforded to purchaser. The Administration was prepared to extend the protection of indemnity to pre-conversion fraud after upgrading as the LR would have had the opportunity to check title prior to upgrading.</p>

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<p>(v) <u>Limiting the right of indemnity to ‘loss of ownership’</u></p> <p>There would be no reason for limiting the right of indemnity to ‘loss of ownership’ and that loss of other kinds of interests especially encumbrances ought similarly to give rise to a right of indemnity.</p>	<p>It had always been the policy intent to limit the right of indemnity to cases where there had been a ‘loss of ownership’. Where there were parties who suffered loss in consequence of displacement of an owner, those parties might also be eligible to claim indemnity for their loss.</p>
<p>(c) REDA</p>	
<p>(i) <u>Cap on indemnity</u></p> <p>REDA restated the objection to the cap on indemnity. REDA accepted the cap only on the basis that innocent original owner would be entitled to have title restored under mandatory rectification rule. The proposed exceptions would substantially abrogate the mandatory aspect of the rule.</p>	<p>With the mandatory rectification rule, no purchaser would be protected by the title register against the effect of fraud committed prior to the transaction in which he was involved and he risked losing his property at any time during his ownership. The security and ease of conveyancing that LTO aimed to achieve would be severely undermined.</p>
<p>(ii) <u>Exception relating to deferred indefeasibility</u></p> <p>Exception (1) (registered owner in possession not the first person registered as owner since fraud) was very widely drawn. This amounted to a fundamental departure from the spirit of the mandatory rectification rule and the philosophy behind it. No justification was provided as to why the rights of innocent original owner should be fundamentally altered simply because the property had changed hands.</p>	<p>The integrity and conclusiveness of the title register is the cornerstone of a title registration system. Some jurisdictions adopt ‘immediate indefeasibility’ while other adopt ‘deferred indefeasibility’. The concept of ‘deferred indefeasibility’ was considered to be more appropriate for adoption in Hong Kong.</p>
<p>(iii) <u>Exception relating to resumption or surrender</u></p> <p>Regarding exception (2) (resumption or surrender property to Government), REDA had difficulties in understanding</p>	<p>Where a property was resumed or surrendered to Government, the resumption or surrender would be for a specific purpose and the property would no longer be held under a lease. The property could</p>

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<p>why an innocent original owner should stand to lose his property simply because the property had been resumed or surrendered to Government. An application of exception (2) might result in the loss to the innocent original owner of his property or had the effect of appropriation of property without compensation or adequate compensation. The Administration needed to address whether exception (2) would be contrary to Articles 6 and 105 of the Basic Law.</p>	<p>not simply be handed back to a former innocent owner. It would be impractical to rectify the title register in such circumstances. REDA's concern about compliance with the Basic Law was noted and the LR would maintain close liaison with the Department of Justice.</p>
<p>(iv) <u>Exception relating to multiple purchasers</u> The protection of the innocent purchasers should not be made at the expense of the innocent original owner whose remedy should not be limited by the cap. If exception (3) (property sold into multiple ownership) were to apply, certain criteria had to be set and satisfied. It would be difficult to see why the exception should apply simply because the land was developed into two town houses one of which had been sold.</p>	<p>The concern regarding the cap on indemnity was noted. The determination of 'sufficient number of bona fide purchasers' was arbitrary. The only effective rule was that once the land was divided up and two or more innocent purchasers were involved, it would be just and reasonable for the exception to apply.</p>
<p>(v) <u>Costs payable by Land Registrar (Registrar)</u> Whilst REDA accepted that as a general rule, the Registrar's costs should be paid out of the indemnity fund, there might be circumstances where due to the conduct of the Registrar or some other person, the costs should be borne either by the Registrar or by some other person. The provision should be qualified such that it would be so 'unless otherwise ordered by the court'.</p>	<p>Registrar's costs in handling application for indemnity did not involve court proceedings unless the applicant rejected the indemnity offered. It should be made clear that the Registrar's costs of processing application be charged to the indemnity fund. The Administration agreed that the Registrar's costs should be paid out of the indemnity fund unless otherwise ordered by the court.</p>