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13 July 2009

Ms Connie Lau
Chief Executive
Consumer Council
22/F, K Wah Centre
191 Java Road, North Point
Hong Kong

Dear Connie,

Consultation on Land Titles (Amendment) Bill

I am writing to thank you for the submission that the Consumer Council made in response to the two consultation papers on amendments to the Land Titles Ordinance (LTO). I would like to set out for your information how the Government, after consideration of all submissions, intends to proceed. I have also set out in an annex some responses to particular points or queries raised in your submission.

Conversion Mechanism

The first consultation paper dealt with the question of whether changes were needed to the mechanism under which existing land is to be brought under the LTO. The overwhelming response to the consultation paper was against making any changes to the main conversion mechanism contained in the LTO as enacted in 2004. Under this mechanism, almost all existing eligible land will be brought under the LTO automatically 12 years after commencement of the LTO. The only exceptions would be land against which a caution against conversion had been registered and land for which matters had been submitted for registration before the conversion date and had not yet

completed registration. However, there was recognition that the automatic conversion presented some risks. There was general understanding that the Government should make some changes to better manage these risks, provided that these changes kept to the essential framework of automatic conversion.

The Government has considered whether there are modifications that can be made within the existing automatic conversion mechanism that can deal with the problems that had been identified. It has been concluded that :

- (a) amendments can be made that will clearly manage the priority of interests claimed under caveats; and
- (b) new provisions can be added that allow known cases of indeterminate title to be withheld from conversion while allowing conversion of other land to proceed automatically.

No amendments can be made to the automatic conversion mechanism that remove all uncertainty about what liabilities may arise. However, the Government is of the view that some uncertainty has to be accepted in order to secure the wider public benefit that will come from the certain conversion of existing properties to the new title registration system. Assurance has been given that suitable measures will be put in place to ensure that, if any liabilities are found to have arisen out of the automatic conversion, they will be met in a way that will ensure reasonable stability in fees and charges faced by users of services provided by the Land Registry. The details of these measures are being considered and will be announced in due course.

On this basis, the Government intends to proceed with the Land Titles (Amendment) Bill (LT(A)B) without making any change to the underlying automatic conversion mechanism enacted in 2004. The only changes affecting conversion that will be put forward in the LT(A)B will be amendments to deal with the priority of interests under caveats after conversion and new provisions to withhold certain known problem cases from conversion. On the latter, we will issue a set of proposals for the new provisions for discussion with interested parties before drafting instructions are issued. The measures to handle any liabilities that may be found to arise from automatic conversion will not involve amendments to the LTO.

Rectification and Indemnity

In the second consultation paper, three exceptions to the existing mandatory rectification rule were proposed. These were :

- (a) when the land affected had been surrendered or resumed prior to discovery of the fraud;
- (b) when the land had passed into multiple new ownership; and
- (c) when the current owner was a bona fide purchaser who had not dealt with the fraudster.

On (a), there was general understanding of the need for exception to be made when it was a practical impossibility to return the affected land to the original owner. However, question was raised as to whether this was so in cases where the surrender was not for achieving a public purpose. Also, it was argued that the exception could only be accepted if the limitations on indemnity for a former owner currently laid down in the LTO are removed (these limitations being the cap on the amount of indemnity and the bar to indemnity if the fraud occurred before conversion). Otherwise, the risk that a former owner may be left without full compensation for loss of the property may again arise. It was this risk that the mandatory rectification rule was put forward to address in 2004.

On (b), most respondents questioned whether it was appropriate to make an exception simply because of the land having passed into multiple ownership. It was felt that unless redevelopment had taken place, the former owners should still be allowed to recover the property. As in the case of exception (a) it was argued that it was unacceptable to bar the former owner from recovery in case of redevelopment if the limitations on indemnity were to remain in place.

On (c), most responses were in favour of retaining the rule mandating recovery by the former owner, irrespective of the position of the current registered owner. The Consumer Council and Law Society recognized the arguments in favour of greater protection for purchasers, but tended to favour that the security should be given immediately to a bona-fide purchaser rather than accepting the idea of protection being deferred to the second bona-fide purchaser as proposed in the consultation paper. It was suggested that a 'deferred indefeasibility rule' might be open to abuse. Furthermore, acceptance of the idea of any form of indefeasibility was conditional on the limitations on indemnity for the pre-fraud owner being lifted.

After consideration of the submissions, the Government is now assessing whether it is acceptable – in terms of managing the risks to the planned indemnity fund and the financial impact on property owners who will

finance the indemnity fund through a levy on transactions – to remove the limitations on indemnity for a former owner if exceptions to the mandatory rectification rule are made. If it is agreed that the limitations on indemnity can be removed, amendments may then be introduced in the LT(A)B that would allow for exceptions to mandatory rectification :

- (a) where land has been surrendered or resumed for a public purpose; and
- (b) where land had been redeveloped and had then passed into multiple new ownership.

Next steps

We will first be circulating detailed proposals for new provisions to withhold indeterminate titles from conversion. This will be done shortly with the aim of completing discussion on these by September 2009.

Subject to agreement on the new provision and a decision on whether the limitations on indemnity are to be amended to allow for some exceptions to the mandatory rectification rule, we will then prepare a final working draft of the LT(A)B for review by interested parties. We aim to have this working draft ready by the end of 2009, to allow reasonable time for consideration of the Bill and associated rules before they are put to the Legislative Council for deliberation in the second half of 2010.

With best regards

Kin.

(K.A.Salkeld)
Land Registrar

Encl.

Response to particular comments from Consumer Council

The intended way forward set out above corresponds closely with suggestions made by the Consumer Council in your letter of 14th April. I would like to take this opportunity, however, to respond to a number of points in your submission:

- (a) You queried why, under the alternative conversion mechanism set out in the consultation paper, there was no provision for registration of claims to unwritten equities before the 'initial' conversion. The reason for this was that pre-conversion unwritten equities would not have been affected by the proposed conversion. Any person claiming such an interest would have had at least 12 years after the initial conversion to register a warning note regarding their claim before the upgrading process began and put their interest at risk if not protected by a warning note. Putting provisions for registration of caveats back into the Land Registration Ordinance (LRO) for use during the period before initial conversion would have undermined one of the intended benefits of the alternative mechanism, that of avoiding complications on conversion over the priority of interests claimed under caveats registered under the LRO. Since the decision has been made to keep the 2004 Daylight conversion mechanism, this point is now moot. Amendments will be made in the LT(A)B to provide rules governing the priority of interests claimed under caveats after conversion;
- (b) You suggested that the Land Registry seek further funding from Government for the conversion process, in particular for building up a reserve for the Indemnity Fund. The Government has agreed that assurance of support be given to the Land Registry for handling any liabilities that may arise out of the conversion process. However, it is considered that, rather than alter the arrangements for the Indemnity Fund, which were designed to operate over the long term to deal with liabilities arising from fraud cases and mistakes or omissions of the Land Registry after land has been brought under the LTO, separate arrangements suitable for the particular liabilities that may arise from the conversion itself are more appropriate. These need not be permanent arrangements since, as time elapses after conversion, the possibility of any claim arising from the conversion itself will fall away. Since it is not possible in advance to make any reasonable estimate of what extent of liabilities might be found to have arisen, it is not possible to determine now a particular level of reserves or funding that might

cover them. Instead, the arrangements may take the form of an agreement such as a trigger point at which Government would act to ensure that the Land Registry is provided with the resources to meet any established liabilities and for the additional money to be provided on terms that allow for reasonable stability in setting fees and charges for users of Land Registry services. We will let you know the proposed arrangements once these have been drawn up;

- (c) The Consumer Council did not see justification for the idea of treating the 1st and 2nd or subsequent bona fide purchasers after fraud differently in rectification proceedings. Concern was raised at the risk of abuse and it was suggested that if the concept of indefeasibility in rectification after fraud was to be re-introduced it would be preferable to have immediate indefeasibility for the first bona-fide purchaser. While it is the present intention to proceed with the LT(A)B with only limited alteration to the mandatory rectification rule, we may wish to discuss further with you on this point. Most respondents were strongly opposed to giving greater protection to purchasers but the Law Society has argued in favour of indefeasibility and we remain concerned that, over time, the mandatory rectification rule is likely to lead to worries for purchasers that may impact on the conveyancing system;
- (d) The Council supported extending the indemnity provisions to cover any case of pre-conversion fraud. I would like to make clear that the Administration's consideration has only been to extend the coverage to pre-conversion fraud in cases where the exceptions to mandatory rectification would apply. This would be necessary, if it is decided to make the exceptions, in order to ensure that no former owner would risk being put in a position where they might be worse off (in money terms) under the new law than at present; and
- (e) The Council questioned whether the effect of replacing the term "affects ownership" with "loss of ownership" in section 84(1) of the LTO would be to restrict the class of persons who would be able to claim indemnity. The Administration's position is that where there has been loss of ownership, any other parties who have lost rights or interests due to the loss of ownership will also be eligible to claim for indemnity.