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14 July 2009

Mr Anthony Shin
President
The Hong Kong Conveyancing &
Property Law Association Limited
c/o S.H. Leung & Co
Rm 502, Aon China Building
29 Queen's Road Central
Hong Kong

Dear Mr Shin,

Consultation on Land Titles (Amendment) Bill

I am writing to thank you for the submission that the Hong Kong Conveyancing & Property Law Association Limited 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.

Yours sincerely



(K.A.Salkeld)
Land Registrar

Encl.

Response to particular comments from Hong Kong Conveyancing & Property Law Association Limited

The covering letter has indicated how the Administration intends to respond to the main recommendation of the Law Society to retain the 'daylight conversion' mechanism. This supplementary note addresses some particular points raised in your submission.

It was suggested that the Administration had "exaggerated" the problems with the enacted conversion mechanism and was mainly concerned with its own financial liability. The Administration has not claimed that the problems are large. It has simply pointed out that there are certain known problems that the enacted mechanism does not make provision for, and some uncertainties that need to be managed prudentially to ensure the safe operation of the conversion mechanism. It is proper to give careful consideration to financial liabilities since it is the public that would end up paying for these.

With respect to the rectification and indemnity provisions we understand from your letter of 27 March 2009 that you would support the two exceptions to mandatory rectification that we are now considering to introduce. However, you object to the idea of introducing the doctrine of 'deferred indefeasibility'. Your attention is drawn to the recent submission from the Law Society on this point, a copy of which I attached. We would be grateful for your advice as to whether there is a prospect of a common position between the Law Society and the Association on this point.

We note your wish to see the specific provisions for addressing the various ambiguities in the operation of the indemnity provisions. As indicated in the covering letter, it is our intention to let you have a fresh draft of the LT(A)B incorporating all these provisions for consideration by the end of 2009.



THE LAW SOCIETY'S SUBMISSIONS ON THE ADMINISTRATION'S LATEST PROPOSAL ON AMENDMENTS TO THE LAND TITLES ORDINANCE – RECTIFICATION AND INDEMNITY ARRANGEMENTS

The Law Society has the following comments on the proposals put forward by the Development Bureau in its December 2008 paper ("*Consultation Paper*") on amendments to the "*Rectification and Indemnity Provisions*" in the Land Titles Ordinance ("*LTO*"):

Exceptions to Mandatory Rectification Rule

1. The Government has concern that the mandatory rectification rule will work to undermine confidence in the title register and the security and ease of conveyancing that the LTO aims to achieve.
2. The Law Society shares the concerns of the Government and believes that indefeasibility of title is an important feature of a title registration system. We support in principle the introduction of the proposed exceptions to the rule as set out in paragraph 26 of the Consultation Paper subject to review of the legislative provisions and introduction of further legislative changes to the Indemnity Provisions as set out in the succeeding paragraphs 3 & 4.
3. The mandatory rectification rule was introduced in the 2004 legislation in recognition of the fact that due to the effect of the cap on indemnity, unless rectification was made in favour of the former innocent owner being defrauded and lost his property, he might find himself worse off under the new

system. The Law Society is of the view that the Mandatory Rectification is an unfortunate political expediency arising out of the Administration's lack of commitment in capping the indemnity payment, otherwise it should have no place in our Land Titles Ordinance. The Law Society is strongly of the view that this deferred indefeasibility is the very minimum of any registered title system. The Law Society further believes that the cap on indemnity to the innocent former owner should be lifted in the proposed exceptional scenarios to the mandatory rectification rule.

4. Further, as the Administration has rightly pointed out in paragraph 29 of the Consultation Paper, the exclusion of indemnity for pre-conversion fraud to the innocent former owner under Section 84(4)(c) of the Land Titles Ordinance in the proposed exceptional scenarios should also be lifted as otherwise, a former innocent owner may be barred both from recovering the property or any indemnity if the fraud that removed him from the register occurred before conversion.

Other Proposed Amendments

5. The Law Society noted the Government has proposed other amendments with the view to clarify the ambiguities in the existing provisions and to ensure that the arrangements will work effectively.
6. The Law Society would like to reserve its overall comments on these other proposals upon sight of the draft legislative provisions. We would, however, highlight for the Administration's consideration the following observations:
 - (a) **Identity of the Persons Eligible to Claim Indemnity**
Section 84(1) of the LTO states that "...a person suffering loss by reason of an entry in the register or omitted from the register, where such entry has obtained, made or omitted,... as a result of (a) fraud...(ii) which affects the ownership of registered land... shall be indemnified by Government in respect of that loss."

The Administration was concerned there is some uncertainty over the

meaning of the term "*which affects ownership*" and proposed to replace it with "*which results in the loss of ownership*". The intention is to make clear that the indemnity fund will not be liable for claims in cases where there has not been any loss of ownership due to fraud.

The Law Society believes it is important to ensure all persons suffering loss as a result of fraud will be able to claim indemnity but noted the Section 84(1) has limited such claims to cases where there has been a "*loss of ownership*".

The Law Society also believes that the proposal should refer to "*title*" rather than "*ownership*" and has concern with the proposal as there are occasions or possibilities that someone having an interest in the registered land could suffer loss although the title of the owner has not been lost.

The Law Society noted with encouragement that similar stance was taken by the Hong Kong Association of Banks and the Consumer Council.

(b) **Proposed Apportionment where there are Multiple Claimants**

The Administration noted that where there are multiple claimants and the total value of their claims exceeds the cap, no provision exists now as to how the amount is to be apportioned among the various claimants.

The proposal is thus to include a provision to the effect that each claimant would be paid from the cap amount in proportion of the value of their loss.

The Law Society believes the proposal on the apportionment of the indemnity amount should be subject to any contrary intention expressed by the parties, particularly when in a Charge situation, the Chargee would probably wish to get everything up to the amount of the outstanding loan.

The Law Society of Hong Kong
23 June 2009