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13 July 2009

Ms Christine Chu  
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The Law Society of Hong Kong  
3/F Wing On House  
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*Dear Christine,*

### Consultation on Land Titles (Amendment) Bill

I am writing to thank you for the submission that the Law Society of Hong Kong 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 :

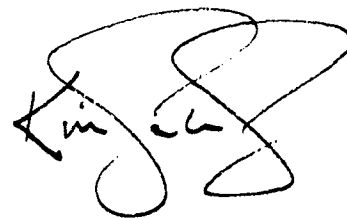
- (a) where land has been surrendered or resumed for a public purpose; and
- (b) where land had been redeveloped and had then passed into multiple new ownership.

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 Law Society of Hong Kong

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.

We note the Law Society's support for new provisions in the LRO for the Land Registrar to withhold particular properties from conversion. We are preparing detailed proposals for such a scheme for discussion with you. One of the most important points will be to give the assurance sought by the Legislative Council that any such power should be used only when essential. Our premise is 'that which the market has joined together, let no registrar put asunder'.

With respect to the rectification and indemnity provisions we understand from your letter of 24 June 2009 that you would support the two exceptions to mandatory rectification that we are now considering to introduce but that you would wish to go further, either adopting the 'deferred indefeasibility' position suggested in the consultation paper or, preferably, moving to immediate indefeasibility. Your attention is drawn to the submission from the Hong Kong Conveyancing and Property Association Limited (copy annexed) which rejects the idea of restoring indefeasibility in fraud cases. 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.

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**Submissions on Consultation on Amendments to Land Titles Ordinance  
Rectification and Indemnity Provisions**

**Proposed clarifications to various provisions set out in paragraphs 9 to 18 of the  
Consultation paper**

1. With reference to proposals set out in paragraphs 9 to 17, we accept all the proposed clarifications in principle.
2. In respect of paragraph 18, we accept the proposal regarding the Registrar's costs of processing applications for indemnity. However with regard to the applicant's costs, it would appear that if an applicant accepts the Registrar's offer in Land Titles Ordinance ('LTO') section 86(1)(b)(i), he cannot make an application to the Court under subsection (4). We submit that provision should be made for such cases that his costs should be payable from the indemnity fund automatically without further application either to the Registrar or to the Court.

**Proposed modifications to the Mandatory Rectification rule in paragraph 26**

3. We accept the proposed modifications in paragraph 26 except for paragraph 26(b)(i), which introduces the doctrine of deferred indefeasibility and therefore contravenes the fundamental principle that title of an assignee can be no better than that of his assignor. As such, if the first bona fide party to deal with the property after a fraud cannot enjoy indefeasible title, the second and subsequent ones should not be in a better position.
4. Paragraph 28 explains that a prospective owner have to exercise care in the transaction by which they themselves become owners since, if they have dealt with a fraudster, they are not given security against rectification in favour of the true owner affected by fraud. Using the illustration of owners A to E in the paper, where C is the fraudster, we accept that D, who deals with the immediate fraudster C, should exercise care in dealing with C, although it is not easy for D to detect that C has defrauded true owner B.
5. With deferred indefeasibility, it opens the loophole for fraudster C to procure sales in quick succession through D to E to perfect his fraud against true owner B,

thereby defeating the whole purpose of mandatory rectification.

6. For this reason, we submit that the proposed exception in paragraph 26(b)(i) should not be adopted.
7. As for paragraph 23(d) (deferred indefeasibility to be the rule for new land), which do not seem to be dealt with in paragraph 26, we consider that mandatory rectification should also apply to new land, and no modification is necessary. Even after the LTO takes effect, owners of new land may also be subject of fraud and they should also be entitled to the same mandatory rectification protection.

**The Hong Kong Conveyancing & Property Law Association Limited**  
**27 March 2009**