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LegCo Panel on Home Affairs

**Subcommittee on review of the
Building Management Ordinance**

**Minutes of meeting
held on Tuesday, 22 January 2002 at 2:30 pm
in Conference Room B of the Legislative Council Building**

- Members Present** : Hon Albert CHAN Wai-yip (Chairman)
Hon Andrew WONG Wang-fat, JP
Hon Emily LAU Wai-hing, JP
Hon Andrew CHENG Kar-foo
- Member Attending** : Hon LAU Ping-cheung
- Members Absent** : Hon Cyd HO Sau-lan
Hon Albert HO Chun-yan
Hon NG Leung-sing, JP
Hon IP Kwok-him, JP
- Public Officers Attending** : Ms Esther LEUNG
Principal Assistant Secretary for Home Affairs (5)
- Mr T E BERRY
Deputy Director of Lands (Legal)

Mrs Kenny WONG
Assistant Director of Home Affairs (4)

Miss Stella CHANG
Assistant Secretary for Home Affairs (5)2

Mr MA Kam-ki
Senior Liaison Officer (Building Management)
Home Affairs Department

Clerk in Attendance : Miss Flora TAI
Chief Assistant Secretary (2)2

Staff in Attendance : Mr Stephen LAM
Assistant Legal Adviser 4

Miss Irene MAN
Senior Assistant Secretary (2)7

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I. Confirmation of minutes
[LC Paper No. CB(2) 934/01-02]

The minutes of the meeting held on 18 December 2001 were confirmed.

II. Proposals to improve the Building Management Ordinance
[LC Paper Nos. CB(2)671/01-02(01) and 696/01-02(01)]

2. The Chairman welcomed representatives of the Administration. He suggested members to discuss the issue in respect of the mechanism to amend provisions in deeds of mutual covenant (DMCs) because the Deputy Director of Lands (Legal) had specifically been invited to join the discussion.

Administration's position

3. Responding to the Chairman, Principal Assistant Secretary for Home Affairs (5) (PAS(HA)5) said that DMC was defined in section 2 of the Building Management Ordinance (Cap.344) (BMO). As DMC was a private contract

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executed between the developer and owners, the Administration was not a party to the contract and was not in a position to meddle with its terms and conditions. However, BMO did contain statutory provisions which should be incorporated into a DMC to protect the interests of the parties concerned. A DMC was intended to define the property rights and obligations of owners between themselves and to provide for the allocation of management charges according to the circumstances of developments on individual lots. The Lands Department (LANDs) considered applications for DMC approval according to the current Legal Advisory and Conveyancing Office (LACO) Guidelines.

Background of DMC approvals

4. Deputy Director of Lands (Legal) (DD of L(L)) briefed members on the background of the DMCs approval. He advised that the then Registrar General's Department (RGD) had started looking into DMCs in late 70s to early 80s in the context of the new towns in the New Territories (NT) to ensure their compliance with the lease conditions. In the early 80s, a standing committee on building management was set up within the Administration and made several recommendations. In October 1987, the then Register General Department (RGD) had drawn up the Guidelines for DMCs on the basis of the recommendations of the standing committee. Since the lease conditions required approval of DMCs by RGD, it had become a prerequisite to the granting of consent by RGD (new LACO) to pre-sales.

5. DD of L(L) said that although not all the recommendations of the standing committee had been incorporated into the BMO when it was enacted by LegCo, RGD had based its original 1987 Guidelines on the standing committee's recommendations, including those which had not eventually been adopted by LegCo in the BMO and enforced them administratively through the mechanism of approving the DMC under the land grant conditions. Since 1987, based on experience gained in the typical provisions in DMCs, LANDs had revised the Guidelines and issued these in June 1999. The Guidelines for DMCs were drawn up to promote the concept of building management in private developments and to strike a fair balance of interests between purchasers and developers, between owners and managers and among owners themselves.

[Post-meeting note: the "1999 Revised Guidelines for Deeds of Mutual Covenant" provided by the Administration was tabled at the meeting and subsequently circulated to members vide LC Paper CB(2)981/01-02 for retention.]

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Uneven distribution of shares between residential and commercial units or common area

6. The Chairman said that in some DMCs, the percentage of shares allocated to the common area or commercial units was unreasonably high but the percentage of shares allocated to residential units was very low.

7. Addressing the Chairman's query on why the common area with a large portion of undivided shares was usually given to the developer or their trustee, DD of L(L) clarified that under the current Guidelines for DMCs, shares of common area had to be assigned to the management company as a trustee for the owners. This was to prevent the manager from making use of the shares for the interest of the developer. As such, he advised that owners could always take actions against the management company if the common areas were being misused for some other purposes. The manager had to comply with its legal obligations as a trustee for the owners.

8. DD of L(L) assured members that since the 90s, it was a common practice to specify in DMCs that the management company as trustee or the owners' corporation (OC) should take control of the shares of the common area. Nevertheless, he understood that the situation might vary depending on when individual DMCs were approved. DD of L(L) pointed out that RGD (now LACO) only started to approve DMCs since early to mid 80s for developments built on newly sold government land where the land grant conditions required a DMC to be executed subject to the approval of RGD/LACO. The specification was contained in the DMCs of about two-third of the property developments and did not apply to the rest of older estates.

Unproportionate distribution between undivided shares and management shares of a development

9. The Chairman pointed out that it was common in DMCs that the allocation of undivided shares (ownership shares) was very disproportionate to that of management shares (which usually regulated owners' contribution). In some cases, the developers might take control of the decision-making power of the management because two-third of the undivided shares had been allocated to the common areas or commercial units they owned. However, these developers were only required to pay a much smaller proportion of management fees as only one-third of the management shares were allocated to the common areas or commercial units. The Chairman cited Discovery Park as an example, saying that the problem of unproportionate allocation of undivided shares and management shares also applied to the DMCs of some new developments.

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10. DD of L(L) said that in approving DMCs, the Administration had all along upheld the principle that no one should be required to pay more than his fair share of the overall management cost. He pointed out that the proportion of the management shares could be different from that of the undivided shares due to the value, location and nature of the property. Nevertheless, the management shares should be distributed on a broadly fair basis between the developers and owners.

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11. The Chairman asked whether the Administration would consider imposing a ceiling to cap the discrepancy between the allocation of undivided shares and the management shares, say the discrepancy should not exceed 20 or 30%. DD of L(L) undertook to explore the feasibility from both the policy and technical perspectives. He would consider devising a mechanism to balance between the allocation of undivided shares and management shares.

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12. In response to Ms Emily LAU's enquiry on the time needed to devise the said mechanism, DD of L(L) said that the Administration would have to consult professional bodies and other relevant organisations from the policy point of view and take a few weeks to explore the feasibility. At members' request, DD of L(L) undertook to provide an information paper reporting on the matter to facilitate members' further discussion.

13. Ms Emily LAU further asked whether legislative amendments would be required for the operation of the mechanism. DD of L(L) responded that the mechanism if devised could apply to future DMCs only. Members might need to consider legislation so that it would apply with retrospective effect to existing DMCs. DD of L(L) pointed out that amendments had been made to BMO in 1993 with retrospective effect by imposing up-to-date conditions on existing DMCs, especially for those of the old buildings built in the 50s and 60s. At present, DMCs for all estates built in the 90s had been drawn up in compliance with the current Guidelines for DMCs.

14. The Chairman said that while he appreciated the Administration's positive response, he was very concerned about how the interests of owners affected by existing DMCs could be protected. DD of L(L) said that LANDs was in the process of approving a new Sub-DMC for the current phase of development of a new village in Discovery Bay and had been negotiating with the developers to ensure that the DMCs would comply with the current Guidelines for DMCs.

15. In response to Ms Emily LAU's enquiry, DD of L(L) explained that there were not many phase developments such as the Discovery Bay which were old but still continued to be developed. The developer of Discovery Bay had agreed that the current Guidelines should be adopted to approve DMCs of future phases in the

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development of Discovery Bay so long as there was no legal conflict with the original DMC.

The length of service of management companies

16. Although it was stipulated in most of the new DMCs that the initial period of service by the first management company should not exceed two years, the Chairman said that many management companies continued their service for the estate year after year following the expiry of the initial period. Owners could only terminate the appointment of the management company after the two-year period with the consent of owners of at least 50% of the management shares at an owners' meeting. However, it was very difficult, if not impossible, to achieve such a high percentage in most cases. The Chairman remarked that as most of the management companies were subsidiaries or closely linked to the large developers, owners might not have the resources to take actions against them even if they found the services unsatisfactory.

17. The Chairman gave an example that the management company might rent out certain areas in the carpark (which was against the land use as approved by LANDs) and transfer the rental to the developer direct instead of contributing it to the management fund of the development. DD of L(L) responded that any practice against the lease conditions could be reported to the district lands offices so that enforcement actions under the land grants might be taken.

18. In response to the Chairman's query about the initial period of appointment of the first building manager, DD of L(L) explained that the initial two-year period should be a fixed contract. Upon expiry of the contract, it should be up to the OC to decide whether re-appointment for a further term should be offered to the management company concerned. PAS(HA)5 supplemented that the two-year initial period stated in Guideline no.8 had been drawn up on the basis of paragraph 7 of the Seventh Schedule to BMO. She undertook to seek legal advice and revert to the Subcommittee to clarify whether a resolution of the owners of not less than 50% of all management shares would be required to terminate the appointment of the first building manager after the initial two-year period under the DMC.

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Calculation of undivided shares in DMCs

19. In response to Mr LAU Ping-cheung's enquiry about the ways to calculate undivided shares in DMCs, DD of L(L) explained that the undivided shares were generally calculated on the gross floor area (GFA) basis. At one time, undivided shares had been calculated on a valuation basis as well. However, the alternative was too complicated and had not been used by the developers for a long time. He pointed out that LANDs also did not have the expertise to determine whether a

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valuation schedule was justified. As a result, the GFA basis was widely adopted in almost 99% of the existing DMCs.

20. DD of L(L) added that although it was advised in the current Guidelines for DMCs that undivided shares should be allocated on a GFA basis, developers and professional bodies were welcome to submit alternative basis, such as using valuation or saleable area etc for consideration.

Possible proposals to address the problem of provisions in DMCs which were unfair to owners

21. The Chairman said that the following three possible proposals to address the problem of provisions in DMCs which were unfair to owners had been brought up for consideration at previous meetings -

- (a) a mechanism should be set up so that the provisions of a DMC could be amended by a resolution of an OC and with the approval of the Secretary for Home Affairs (S for HA) or the Court;
- (b) BMO should be amended to the effect that a DMC might be amended by a resolution of owners of not less than 75% of the shares at an OC meeting; and
- (c) Overriding provisions should be added to BMO in order to protect the interest of owners against provisions in a DMC which were unfair to them.

He invited views on these possible proposals.

22. DD of L(L) remarked that it would be inappropriate for the Secretary for Home Affairs, as an administrator, to play a role in the mechanism because he would receive all sorts of representation from different groups of owners in favour or against the proposed amendments to the DMC and it would be difficult to make a fair decision. It was also doubtful whether the Court would have the expertise to make such decision. Regarding the second proposal, he pointed out that if the percentage of shares was set at a very high level, it would be difficult to meet the requirement but a low level could not really represent the wish of the majority owners and the mechanism could be easily abused.

23. Given the controversies of the two possible proposals, PAS(HA)5 said that legislative amendments to BMO had been used to override certain provisions of DMCs. The Administration would welcome members' suggestions along the line of adding overriding provisions to BMO.

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24. Mr Andrew WONG considered that it was dangerous to allow amendments to DMCs by means of an owners' resolution because the interests of the minority would be sacrificed. He pointed out that even the Court could hardly determine whether a certain amendment was fair or not unless specific standards or criteria were stipulated in BMO under which the DMC should be drafted. As such, Mr WONG took the view that if problems in DMCs which were unfair to owners had been identified, overriding provisions should be added to BMO to protect the interest of owners against provisions in DMCs which were unfair to them.

25. The Chairman shared Mr Andrew WONG's view. He pointed out that the mechanism of amending the DMC by a resolution of an OC might affect the interest of the minority. For example, even if a DMC did not forbid dog keeping, 98% of owners might pass a resolution to amend the DMC so that the 2% of owners might not be able to keep their dogs. According to his understanding, as the grievances of most owners only focused on the distribution of shares which was unfair to owners and the proportion of management fees payable by developers, adding overriding provisions to BMO should be able to address the grievances. He stressed that it was necessary to ensure that interests of the minorities would not be sacrificed in any proposal.

26. Mr Andrew CHENG held a different view. He said that it was almost impossible to have the consent of 100% of owners to amend the DMC, and the Administration had little role to play on the ground that the DMC was a private contract. Mr CHENG considered that BMO should be amended to the effect that a DMC could be amended by a resolution of about 60 to 70% of owners. To protect the interests of the minority, if the interests of the minority of owners were affected by the proposed amendment to the DMC, a mechanism should be provided to allow them to file their objection to S for HA or the Court on the condition that the number of these owners reached a certain percentage. The Chairman expressed reservations about Mr CHENG's suggestion.

Way forward

27. In the light of the divergent views expressed, the Chairman suggested and members agreed that the Subcommittee should discuss the issue at a later stage and focus its future discussion on the issues which the Administration had undertaken to follow up.

28. At the request of the Chairman, PAS(HA)5 briefed members on the latest Administration's position of the six major issues identified earlier by the Subcommittee.

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Formation of OCs by owners of house developments holding divided shares

Adm 29. PAS(HA)5 said that Department of Justice (D of J)'s initial view was that since the objectives of BMO was to facilitate the incorporation of owners of multi-storey buildings and to provide for the management of such buildings, the formation of OCs in house developments would unlikely be provided through a simple technical amendment relating to definition of undivided shares under the BMO. PAS(HA)5 undertook to continue to explore the feasibility for the owners of house developments to form OCs with D of J.

Specific exemption of members of an OC from legal liabilities

30. PAS(HA)5 said that it was inappropriate to give a blanket exemption from legal liabilities to individual members of an OC. However, the Administration would consider any concrete proposals from members regarding granting OC members exemption from a specific liability if warranted.

Adm 31. The Chairman reiterated members' request raised at the last meeting that the Administration should make reference to the Company Law so that OC should operate as a corporate body and members of a MC could enjoy the status similar to that of directors of a limited company. With reference to sections 16 and 17 of BMO, PAS(HA)5 said that D of J had pointed out that members of a MC should not be held personally liable for the action taken in the name of an OC. Nevertheless, she undertook to request D of J to study the details of the cases mentioned by members at the last meeting and find out whether action could be taken against individual MC members in respect of duties undertaken in the name of an OC.

Adm 32. The Chairman referred to paragraphs 16, 21 and 24 of the minutes of the meeting held on 18 December 2001 and requested the Administration to take appropriate follow-up actions. Mr Andrew CHENG urged the Administration to provide the information as requested before the next meeting to facilitate members' discussion.

Voting rights of the shares allocated to the common parts of a building

Adm 33. DD of L(L) clarified that according to the current Guidelines for DMCs which had been in force since mid 1999, owners of common areas were not entitled to any voting rights. For the DMCs approved before mid 1999, the management company was required to hold the shares allocated to the common parts of a building for the owners in the form of a trustee. However, he admitted that holders of the undivided shares of the common parts of a building might have voting rights in some old DMCs. The Chairman requested the Administration to

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examine the cases quoted by members in paragraphs 30 to 35 of the minutes of the meeting held on 18 December 2001 and explore ways to address the problems found in the DMCs before the 90s.

Formation and election procedures of an OC

Adm 34. PAS(HA)5 confirmed that the Administration would consider adding a schedule to BMO setting out the appropriate procedures for the formation of OCs.

Percentage of shares required for the termination of the appointment of building manager

35. PAS(HA)5 considered that it was reasonable to require owners of not less than 50% of the shares liable to pay management fees to terminate the appointment of the manager by a resolution. She expressed reservations about further lowering the percentage. Members agreed to pursue the issue at a later stage.

Mediation mechanism to resolve building management disputes

Adm 36. Upon the Chairman's enquiry on whether a mediation system could be established to resolve minor disputes to share the workload of the Lands Tribunal, Assistant Director of Home Affairs (4) (AD of HA(4)) advised that the Home Affairs Department (HAD) had recently liaised with two mediation centres to explore the feasibility of setting up a non-statutory mediation mechanism through making arrangements for mediation bodies to provide voluntary service at HAD's Building Management Resource Centres for resolving management disputes among owners. At the Chairman's request, AD of HA(4) undertook to revert to the Subcommittee on the progress.

Adm 37. To facilitate members' future discussion, Ms Emily LAU requested the Administration to provide a paper setting its position on the issues and the timing for the submission of relevant legislative proposals for the Subcommittee to consider.

III. Date of next meeting

38. Responding to the Chairman, PAS(HA)5 said that the Administration would need about one and a half months to provide the requisite information for the Subcommittee's further consideration. Members agreed that the meeting would be scheduled in due course.

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[Post-meeting note: With the concurrence of the Subcommittee Chairman, the next meeting has been scheduled for Wednesday, 20 March 2002, at 10:45 a.m.]

IV. Any other business

39. There being no other business, the meeting ended at 4:15 p.m.

Council Business Division 2
Legislative Council Secretariat
18 March 2002