

Information Paper for Legislative Council Panel on Housing

Enhancement of Transparency in the Formulation of Deed of Mutual Covenant for Tenants Purchase Scheme Estates

Purpose

Further to discussion of the papers on “Maintenance and Management of Tenants Purchase Scheme Estates” (Paper No. CB(1)238/00-01(03) and CB(1)407/00-01(06)) and “Formulation of Vesting Order and Deed of Mutual Covenant for Tenants Purchase Scheme” (Paper No. CB(1)525/00-01(08)) on 4 December 2000 and 5 February 2001, this paper sets out the procedures for the formulation of Deed of Mutual Covenant (DMC) for Tenants Purchase Scheme (TPS) estates.

Background

2. The purpose of a DMC is to ensure proper building management in private residential developments. It is a legal instrument setting out the respective rights and obligations of owners and the manager of a development. It binds all signatories, assignees and the manager under the DMC.

3. The Legal Advisory and Conveyancing Office (LACO) of the Lands Department approves DMCs of developments which require the approval of the Director of Lands pursuant to the land grant conditions prior to the sale of interests in those developments. To ensure a fair balance of interests amongst all parties concerned, the LACO has promulgated through its Circular Memorandum No. 41 a set of drafting guidelines, at Annex.

Formulation of DMC for Tenants Purchase Scheme Estates

4. The procedures for the formulation of DMCs for TPS estates follow those for private developments. The DMCs for TPS estates are drawn up by the Housing Authority’s appointed legal consultants in accordance with the general principles and guidelines laid down in LACO’s Circular Memorandum No. 41 as far as possible. In drafting DMC, the Housing Authority ensures, to the best of its knowledge in managing the

estate, that existing authorized uses in respect of common areas and facilities by residents will continue to be protected, and that their management and maintenance responsibilities are fully reflected and fairly shared by all owners according to the “user-to-pay” principle. The Housing Authority as owner of unsold residential flats and commercial properties (such as shopping centres and carparks) would contribute to the management expenses for estate common areas and facilities together with all owners in proportion to the management shares it holds under the DMC.

5. Similar to that for private sector development, DMCs of TPS estates have to be approved by LACO to ensure compliance with the general principles and guidelines laid down in LACO Circular Memorandum No.41. LACO will scrutinize the DMCs and ensure that the DMC represents a fair balance among the interests of all parties concerned.

Access to DMC Prior to Sale

6. As described in paragraphs 4 to 6 above, there is a well-established mechanism for formulation of DMCs for TPS estates, which is intended to ensure proper management of TPS buildings and a fair balance of interests among all parties concerned. A copy of the approved DMC for each TPS estate will be kept in the estate office for inspection by prospective purchasers prior to commencement of and throughout the sale period. Interested parties may obtain a photocopy of the DMC for retention upon payment of a reasonable fee. Salient points in DMC will also be provided in the sales brochures when the estates are launched for sale. The purchasers’ solicitors have the responsibility to explain the DMC to purchasers in detail at the time of execution of the assignment deed. Such arrangements are in line with those for the sale of uncompleted residential properties in both the private and public sectors.

Housing Department
April 2001

GUIDELINES FOR DEEDS OF MUTUAL COVENANT (“DMC’s”)

To promote the concept of building management in private developments (with particular reference to residential developments) and to strike a fair balance of interests between purchasers and developers as co-owners as between owners and managers and as between owners themselves, Government has drawn up the following guidelines for the approval on behalf of the Director of Lands (the Director) of DMCs required under land grant conditions :-

1. (a) No provision in a DMC shall contravene the provisions of the Building Management Ordinance, Cap. 344 (the BMO).

(b) No provision in a DMC shall be in breach of the Government grant or lease conditions.
2. The provisions of the Seventh and Eighth Schedules to the BMO shall be incorporated in and form part of the DMC either by reference or by setting them out in full.
3. (a) The DMC shall include a definition of the common areas including plans thereof which shall be annexed to the DMC. A copy of these plans certified as to their accuracy by or on behalf of the Authorized Person, shall be kept at the Manager’s office and shall be available for inspection by the owners during normal office hours. Undivided shares shall be allocated to the common areas and those shares together with all the common areas to which they relate shall be assigned to the manager as trustee for all owners, free of costs or consideration. The Manager shall assign the undivided shares free of costs or consideration to its successor as manager on termination of its appointment, or to the Owners’ Corporation (when formed), if so required by it.

The Definition of common areas shall where appropriate include reference to “common parts” as defined to in the BMO.

- (b) The accuracy of all plans annexed to the DMC as to the common areas shall be certified by or on behalf of the Authorized Person.

- (c) (i) Subject to sub-paragraph(ii) hereof, the whole of the car park areas, except those designated car parking spaces as shown on the carpark layout plan approved by the Building Authority, shall form part of the common areas.
- (ii) In the event that the developer retains ownership of the carpark areas as a whole, sub-paragraph (i) hereof shall not apply and the developer shall be solely responsible for the management and maintenance of the carpark. Upon the sale of designated car parking spaces, all areas other than the designated spaces, such as circulation areas, lifts and landings, shall be designated as carpark common areas by way of a sub-DMC.
4. The DMC may reserve rights to the developer to execute supplemental and sub-DMCs in respect of separate towers, phases etc. All supplemental and sub-DMCs (as well as the principal DMC) shall require the approval of the Director but where the Director is satisfied upon submission of the supplemental or sub-DMC to the Director, that the sub-DMC relates only to the internal sub-division of an existing unit and by the sub-DMC there would be no alteration to common areas under the principal DMC, the Director may waive the requirement of approval of such supplemental or sub-DMC.
5. The developer/manager may reserve the rights for itself, its licensees or other third parties to install or affix chimneys, flues, pipes or any other structures or facilities on or within the common areas provided that the written approval of the Owners' Committee (or Owners' Corporation if formed) is obtained prior to the exercise of such rights and that such installation shall not unreasonably affect the enjoyment of the development by the owners and occupiers. Any consideration received therefor shall be credited to the management account for the benefit of all owners.
6. (a) Subject to the provisions of the lease conditions and the DMC, the DMC may reserve the right for the developer to retain for his own use part or parts of the lot unsold not being common areas (" the Retained Areas") provided that: -
- (i) the Retained Areas shall be clearly defined and identified in the DMC; and

- (ii) the Retained Areas shall be allocated an appropriate number of undivided shares and management shares on a fair and reasonable basis, and the developer shall remain liable to contribute pro rata to management and other charges and payments.
- (b) Any use of the Retained Areas allowed to those who purchase shall be clearly specified as such in any sales brochure and pre-sale advertising.
7. The Director shall decide on a case by case basis whether or not the exercise of any other rights reserved to the developer should be subject to the approval of the Owners' Committee or the Owners' Corporation, if formed.
8. (a) The initial period of management by the first manager shall not exceed two years.
- (b) The DMC shall provide that, prior to the Owners' Corporation being formed that the Owners' Committee may terminate the manager's appointment by a resolution of the owners of not less than 50% of all undivided shares (excluding the undivided shares allocated to the common areas) and by giving the manager 3 months' notice in writing.
- (c) No provision of a DMC shall limit the application of the Seventh Schedule to the BMO by restricting or prohibiting termination of the first manager's appointment or his resignation during the initial period.
9. (a)(i) For residential developments, the manager's remuneration shall not exceed a percentage of the total expenditure necessarily and reasonably incurred in the management of the development. The percentage shall be based on the number of residential units in the estate and shall not exceed the following:-
- | | |
|--------------------------------|-----|
| 20 residential units | 20% |
| 21 to 100 residential units | 15% |
| 101 residential units and over | 10% |

- (ii) For non-residential developments, the manager's remuneration shall not exceed 15% of the total expenditure necessarily and reasonably incurred in the management of the development.
 - (iii) For a composite development comprising both residential and non-residential units, sub-paragraph (a)(i) shall apply as if each non-residential unit is a residential unit.
 - (b) The DMC shall provide for a review of the percentages by resolution at meetings of owners, the Owners' Committee or the Owners' Corporation if formed.
 - (c) For the purposes of this Guideline only, "Unit" shall have the same definition as "flat" under the BMO.
 - (d) For the purpose of calculating the manager's remuneration, the total expenditure incurred in the management of the estate or any portion of it shall exclude (i) the manager's remuneration itself and (ii) any capital expenditure provided that the Owners' Committee (or the Owners' Corporation, if formed) may be empowered to decide to include, at its own discretion, any capital expenditure for calculating the manager's remuneration at the rate applicable under paragraph (a) or (b) of this Guideline, or at such lower rate as the Owners' Committee (or the Owners' Corporation, if formed) may consider appropriate. "Capital expenditure" shall mean expenditure of a kind not incurred annually.
10. The manager shall call the first meeting of owners as soon as possible, but, in any event, not later than 9 months after the date of the DMC, which meeting shall appoint a chairman and committee of owners or shall appoint a management committee for the purpose of forming an Owners' Corporation under the BMO.
11. During the existence of an Owners Corporation, the general meeting of the Owners' Corporation shall take the place of the meeting of owners under the DMC, and the management committee of the Owners' Corporation shall take the place of the Owners' Committee under the DMC.

12. Subject to the provisions of the BMO, the DMC shall provide for the appointment of a manager who shall have the authority to act for and on behalf of all owners in accordance with the provisions of the DMC.
13. House rules and any amendments thereto may be made by the manager with the approval of the Owners' Committee or the Owners' Corporation, if formed, but they must not be inconsistent with the DMC.
14. The Owners at an owners' meeting shall have power to require the annual accounts to be audited by an independent auditor of their choice.
15. (a) Provisions shall be made for each owner to pay the following amounts:
 - (i) a refundable or transferable deposit of not more than $\frac{3}{12}$ of the first year's budgeted management expenses;
 - (ii) an advance payment of management fees of not more than $\frac{2}{12}$ of the first year's budgeted management expenses;
 - (iii) a debris removal charge/decoration charge of not more than $\frac{1}{12}$ of the first year's budgeted management expenses (to be paid by owners of residential units) in the case of residential shares or $\frac{3}{12}$ (to be paid by owners of commercial units) in the case of commercial shares;
 - (iv) contributions during the first year towards a special fund (for capital expenditure) totalling not more than $\frac{2}{12}$ of the first year's budgeted management expenses.
- (b) All payments, deposits, charges and contributions payable by first purchasers under the DMC which are non-transferable and non-refundable shall be of an aggregate amount not exceeding $\frac{5}{12}$ (or $\frac{7}{12}$ for commercial units) of the first year's budgeted management expenses, and if the initial contribution under sub-paragraph (a)(iv) hereof is

transferable or refundable, such an aggregate amount shall not exceed 3/12 (or 5/12 for commercial units) of the first year's budgeted management expenses.

- (c) The Director will not object to a provision requiring the owners to further contribute to the deposit referred to in subparagraph(a)(i) hereof so as to make it up to 25% of any subsequent current year's budgeted management expenses per unit.
 - (d) Any monies paid as debris/decoration charges not used for debris/decoration are to be paid into management funds.
16. Interest at a rate not exceeding 2% per annum above the prime rate from time to time specified by the Hong Kong and Shanghai Banking Corporation Limited and a collection charge not exceeding 10% of the amount due may be imposed on any owner failing to pay sums due under the provisions of the DMC within 30 days of demand and the amounts of such interest and collection charge plus any legal costs (on a solicitor and own client basis) involved in recovering them may be the subject of a charge on the owner's undivided shares. All interest and collection charges received shall be credited to the management account.
17. Where any consent is required from a manager by an owner of a unit any fees charged by the manager as consideration for the granting of such consent shall be held by the manager for the benefit of all owners and paid into the management account. The manager shall be entitled to charge no more than a reasonable administration fee for processing and issuing the consent.
18. The manager will on reasonable notice (except in an emergency) be allowed to enter any units for the purpose of effecting necessary repairs to the estate/building. The DMC must also provide for the remedying of damage and liability for the negligent, wilful or criminal acts of the manager, his staff, contractors, etc.
19. The manager shall be responsible for effecting and updating insurance to the full new reinstatement value in respect of loss or damage by fire and other perils in respect of the common areas and also for insurance covering public liability, occupier's liability and employer's liability in respect of employees employed within or exclusively in connection with the management of the development. The Director will not object to provision for the manager procuring

block insurance for the entire development including those areas which are not the common areas.

20. (a) There shall be no provision in the DMC for interrupting the supply of electricity, water, gas or other utilities which are provided by public utility companies to any unit or to prevent access to the unit by reason of the owner of that unit failing to pay any fees or to comply with any other provisions under the DMC.
- (b) The manager may discontinue providing management services to owners who fail to pay fees or to comply with any other provisions under the DMC and the manager may, if the DMC so provides, register and enforce a charge against the interest of an owner who fails to pay any sum which is payable to the manager under the DMC.
21. The manager's rights and duties to manage the estate/building shall not include effecting any improvements to facilities or services which involves expenditure in excess of 10% of the current annual management budget except with the prior approval of the Owners' Committee or Owners' Corporation if formed.
22. The DMC may provide for the manager to appoint or employ agents, contractors or sub-managers, who may include professional property management companies, to carry out certain aspects of the management works or management works in respect of certain area(s) of the development but the manager shall not transfer or assign his rights or obligations under the DMC to any such persons: such persons must remain answerable to the manager. The manager shall at all times be responsible for the management and control of the whole development (including any part thereof) and no provision in the DMC shall attempt to take away or reduce such responsibility.
23. The DMC shall not exclude the liability of the manager to the owners for any act or omission involving criminal liability, dishonesty or negligence on the part of the manager or its servant or agent and no owner shall be required to indemnify the manager or its servant or agent from and against any action, claim, etc. arising out of any such act or omission.

24. The allocation of undivided shares should normally be on a gross floor area (“gfa”) basis. If any other basis is proposed for allocation of undivided shares such proposal may be required by the Director to be justified. The Director shall be concerned that any basis other than gfa adopted, will not result in disproportionate voting rights being granted (e.g. to the owners of commercial parts of a development) and the prevention or hindrance of incorporation of an Owners Corporation.
25. (a) No owner may be called upon to pay more than his fair share of management expenses, and no developer may evade his responsibility to make payments and contributions for those expenses which are of recurrent nature for those undivided shares unsold, provided, however, that a developer shall not be obliged to make such payments and contributions in respect of undivided shares allocated to a building the construction of which has not been completed except to the extent that building benefits from provision in the DMC as to management and maintenance (e.g. as to the costs of managing and maintaining slopes or as to security etc afforded by the management of the completed parts) of a development.
- (b) For a composite development comprising residential and commercial parts, the manager shall be required to keep separate management accounts and budgets for each part. The owners of the residential parts and of the commercial parts will be responsible for the management and maintenance costs of their respective parts (e.g. owners of commercial units will alone be responsible for commercial common areas). All owners will, however, be equally liable for estate common areas.
- (c) The developer shall make the initial contribution to the special fund for capital expenditure and pay the management fee deposit, debris removal/decoration charges if he remains the owner of those undivided shares allocated to units in that part of the development the construction of which has been completed and which remain unsold 3 months after (i) execution of the DMC or (ii) the date when he is in a position validly to assign those undivided shares (i.e. when the consent to assign or certificate of compliance has been issued), whichever is the later.

- (d) Subject to Guideline 15, the Director will not raise any question as to the actual amount of the initial deposit of management fee, debris removal fee or the number or variety of capital funds.
 - (e) All outgoings including management fees up to and inclusive of the date of assignment of the unit shall be paid by the developer.
26. "Owner" shall be as defined in the BMO.
27. No owner shall be allowed to make any structural alteration which will interfere with or affect the rights of other owners. No provision shall be made to prevent an owner from taking legal action against another owner in this respect.
28. (a) Provisions shall be included in the DMC specifying clearly that the owners shall at their own expense maintain and carry out all works in respect of any and all slopes, slope treatment works, retaining walls and other structures within or outside the lot or estate as required by the Government Grant (collectively referred to in this guideline as "the slope structures") and in accordance with the "Geoguide 5 - Guide to Slope Maintenance" issued by the Geotechnical Engineering Office (as amended from time to time).
- (b) If there is one or more "slope structures", a plan of a scale of not less than 1:500 showing all the slope structures (for identification purposes only), certified by the Authorised Person as to the inclusion of all the structures on the plan shall be annexed to the DMC. The plan shall also be attached to a sub-DMC under which undivided shares reserved to a phase of the development are allocated.
- (c) The manager (which for this purpose shall include or Owners' Corporation, if formed) shall be given full authority by the owners to engage suitable qualified personnel to inspect, keep and maintain in good substantial repair and condition, and carry out any necessary works in respect of the structures in compliance with the Government Grant and in particular in accordance with all guidelines issued from time to time by the appropriate Government department regarding the maintenance of slopes, retaining walls and related

structures.

- (d) The DMC shall have adequate provisions for the payment to the manager by all owners of all costs lawfully incurred or to be incurred by the manager in carrying out such maintenance repair and any other works.
 - (e) The manager shall not be made personally liable for carrying out any such requirements of the Government Grant, which shall remain the responsibility of the owners if, having used all reasonable endeavours, the manager has not been able to collect the costs of the required works from all owners.
29. (a) No owner including the developer shall have the right to convert any of the common parts to his own use or for his own benefit or to convert any of his own areas to common parts unless approved by the Owners' Committee or Owners' Corporation.
- (b) The developer shall have no right to designate retained areas as common areas unless such areas are for the beneficial use of all owners and unless the approval of the Owners' Committee or Owners' Corporation has been obtained. Neither the developer nor the manager shall have the right to redesignate common areas.
30. The DMC shall provide that the undivided shares allocated to the common areas shall not carry any voting rights or liability to pay fees under the DMC, nor shall such undivided shares be taken into account for the purpose of calculating the quorum of any meeting.
31. The DMC shall provide for a resolution on whether or not to rebuild or reinstate any part of the estate/building having been damaged by fire, typhoon, earthquake, subsidence or other causes rendering it substantially unfit for use or habitation shall be a resolution of not less than 75% majority at a meeting of the owners of not less than 75% of the undivided shares allocated to that part of the estate/building that has been damaged (excluding the undivided shares allocated to the common areas).
32. The DMC shall provide for all owners of undivided shares who do not occupy the units to which those shares relate to provide the manager with an address in Hong Kong for service of notices under the DMC.

33. The developer shall at its own cost provide a direct translation or summary in Chinese of the DMC within 3 months of the date of the DMC, and shall ensure that it is available for inspection at the management office and for the taking of copies by owners at their expense. The DMC shall specify which version shall prevail in the event of a dispute as to the effect of the Chinese translation and the English language document.
34. The Director will not be concerned whether or not pets are permitted or subject to any controls.
35. The Director will not be concerned as to any arrangements or restrictions on the design, decoration or colour schemes of any external parts of the development.

Notes to Guidelines

- (1) These Guidelines shall apply to all developments regardless of user and size.
- (2) These Guidelines are not required to be incorporated into DMCs verbatim, but the wording may be suitably adapted for particular cases.