

Bills Committee on Building Management (Amendment) Bill 2005

Proposed Formation of a Committee (not Owners' Corporation) For Owners of House Developments

Background

1. At the meeting of the Bills Committee of the Building Management (Amendment) Bill 2005 on 10 November 2005, Members discussed LC Paper No.CB(2)2017/04-05(02) – *Matters Arising from Meeting on 2 June 2005 (Formation of Owners' Corporations in House Developments)* and LC Paper No.CB(2)300/05-06(01) – *The Administration's Response to the Proposal by Hon Ronny Tong on the Incorporation of Owners of House Developments*. Members requested the Administration to consider setting up a mechanism to enable owners of house developments to form a committee so that they could have a greater say in the management of the common parts/facilities of the house developments. Members considered that such a committee might not necessarily possess the same powers and functions as those of an owners' corporation (OC) formed under the Building Management Ordinance (BMO). This paper sets out the Administration's views on the matter and seeks Members' views on the way forward.

Consideration

2. There are two fundamental issues for consideration if we were to provide for a mechanism for the owners of house developments to form a committee through legislative means: (I) what types of powers, duties and liabilities should this committee possess/bear; and (II) how should this committee be formed?

(I) What Types of Powers, Duties And Liabilities Should The Proposed Committee Possess/Bear?

3. As explained in LC Paper No.CB(2)300/05-06(01), the common parts in most house developments, notably Hong Lok Yuen, are not owned by the owners, or any owners of the individual subsections (or houses). These so-called "common parts" of house developments remain to be private properties of the developer. It follows that any committee to be formed could not have the right to manage and maintain these "common parts" (although it is the main function of the ordinary OCs) – which otherwise might amount to

interference of property rights. As long as the committee would not interfere with the property rights of the developer or any individual owner of the house developments, we consider that the proposal is legally viable.

4. Section 34 of the BMO provides that on the winding up of an OC, the owners shall be jointly and severally liable to contribute, according to their respective shares, to an amount that is sufficient to discharge the debts and liabilities of an OC. For owners of undivided shares in a multi-storey building, they in any case are co-owners of the land on which the building is erected – they are thus jointly and severally liable for the liabilities attached to the land whether they have incorporated or not. This is however not the case for owners of house developments who own individual lots/subsections/divided shares. An owner of an individual subsection (or house) of a house development, who does not own the land/development jointly with other owners, should consider whether he is prepared [and whether all the other owners of the individual subsections (or houses) in the development are prepared] to be subject to such additional liabilities.

5. The powers, duties and liabilities of an OC formed under the BMO are set out in Annex A. ***Members may like to consider whether any of these powers, duties and liabilities should be applicable to a committee for owners of house developments.***

6. In addition to OC, the BMO also provides for the operation of an owners' committee¹. According to section 34D, an "owners' committee" in respect of a building means (where a management committee has not been appointed) the committee of owners (howsoever named) formed under and in accordance with the deed of mutual covenant (DMC) in respect of the building.

7. The powers, duties and liabilities of an owners' committee are set out mainly in Part VIA of and Schedule 7 to the BMO. These are mandatory terms that must be impliedly incorporated into all DMCs and most of them are targeted at the building managers. In other words, whether owners of a building have incorporated or not, the manager must comply with the mandatory requirements in Schedule 7, including amongst others, the preparation of budget, keeping of accounts, etc.

8. The powers, duties and liabilities of an owners' committee referred to in section 34D of the BMO are set out in Annex B. ***Members may like to***

¹ Schedule 8 to the BMO provides for the operation of an owners' committee. The BMO, however, does not provide for its formation.

consider whether any of these powers, duties and liabilities should be applicable to a committee for owners of house developments.

(II) How Should The Proposed Committee Be Formed?

9. Once the owners of a building have agreed to incorporate, the OC will have a lot of statutory powers, duties and liabilities with regard to the management and maintenance of the development – and the exercise of such powers and sharing of such liabilities should definitely be based on a proper basis of shares among owners. That is one of the main reasons why house developments like Hong Lok Yuen, the DMC of which does not allocate any shares to owners, could not incorporate under the BMO.

10. Whether the Administration could agree, from the policy and legal point of view, to an alternative basis of shares among owners of house developments for the purpose of forming a committee will very much depend on the extent of powers, duties and liabilities to be vested with the proposed committee. After all, if owners who do not in the first place jointly own the common facilities, allowing them to form a legal entity might subject them to liabilities for which they should not be responsible before such an entity is formed. That said, for discussion purpose, we presume for the time being that such an alternative basis of shares among owners is acceptable.

11. Three options have been raised by Members for the formation of the proposed committee. They are the (i) “*one owner, one vote*” rule; (ii) “*one subsection, one vote*” rule; and (iii) “*vote depends on size of subsection*” rule.

12. Theoretically, the “*one owner, one vote*” rule could be adopted for owners of house developments. The proposal will not only resolve the concern about the lack of a basis of shares among owners, but will also resolve the problem of assignment of shares to the developer. Under the “*one owner, one vote*” rule, the developer who owns the so-called “common parts”, like any other owners, should have one vote only. Whether the proposal will be acceptable to the developer will of course be another matter.

13. We have, in LC Paper No.CB(2)300/05-06(01), set out our views that the “*one subsection, one vote*” rule; and the “*vote depends on size of subsection*” rule are not viable for the incorporation of owners of Hong Lok Yuen under the BMO. However, if we are no longer talking about incorporation but only the formation of a committee with limited powers, duties and liabilities, then these options could be open for discussion again.

That said, unlike in the “*one owner, one vote*” rule, the problem of how the developer’s shares could be calculated could not be solved.

14. ***Members may like to consider how the proposed committee for owners of house developments should be formed.*** Furthermore, Members may like to consider whether the same mechanism should be adopted for the future operation of the committee (i.e. the voting mechanism among owners for passage of resolutions).

Difficulties Envisaged

15. Aside from the two fundamental issues raised above, we have noted the following difficulties with the proposal –

- (a) It is doubtful whether owners of house developments, including those in Hong Lok Yuen, will embrace the proposal –
- The owners of Hong Lok Yuen have formed the Hong Lok Yuen Association, which is an advisory owners’ body². While the Hong Lok Yuen Association is not an owners’ committee recognized under section 34D of the BMO, it has a close and harmonious working relationship with the manager. The formation of a committee (unless with extensive powers as an OC) will not, in practice, change much of their existing position³.
 - In Hong Lok Yuen, the size of the subsections (or houses) varies to a great extent⁴. Whether owners of the larger houses/units will agree to just having one vote as owners of the smaller houses/units (i.e. both Options (i) and (ii) in paragraph 11) is in serious doubt.

² There is no provision for the establishment of an owners’ committee in the DMC of Hong Lok Yuen. The Hong Lok Yuen Association formed by some owners is thus not the “owners’ committee” referred to in section 34D of the BMO.

³ As a related matter, one of the key concerns of owners is on the level of management fees. According to information obtained from the Hong Kong Association of Property Management Companies Ltd, the management fees for the middle to high end properties range from \$1.5 to \$3.8 per sq ft. According to information obtained from the manager of Hong Lok Yuen, the current management fees of the estate is around \$1.1 to \$1.5 per sq ft. The management fees of Fairview Park, another similar house-type development, is around \$0.7 to \$1.1 per sq ft. Members may consider the scope for improvement in the level of management fees if an OC or a committee were to be formed in these two house developments.

⁴ Based on the Master Layout Plan obtained from the Land Registry, there are at least six types of houses in Hong Lok Yuen. Based on information obtained from real estate agents, the size of the houses (units) ranges from 879 to 3 500 sq ft.

- (b) It is also doubtful whether the proposal (especially the formation procedures, be it Option (i), (ii) or (iii) in paragraph 11 above) will be acceptable to the developer⁵.
- (c) Neither Options (ii) nor (iii) in paragraph 11 is able to determine the shares to be allocated to the common parts (whether they are retained by the developer or not).
- (d) For Options (i) and (ii) in paragraph 11, it is for consideration whether owners of more than one house/unit/subsection should have one vote only.
- (e) In the case of Hong Lok Yuen, in addition to houses, there are also multi-storey blocks⁶. This group of owners could not be featured in Options (ii) and (iii) in paragraph 11.
- (f) As explained in LC Paper No. CB(2)1709/04-05(01) – *Incorporation of Owners of House Developments* and LC Paper No. CB(2)2017/04-05(02), the legal difficulties for the incorporation of owners in house developments under the BMO stems from the fact that there is the lack of a Master DMC to allocate shares to the individual owners and/or there is the lack of an undivided share of ownership in the land on which the building is erected. The proposal set out in this paper (which provides a mechanism for allocation of shares) will only work in house developments where there is at least a Master DMC. The existence of a Master DMC shows that the whole development, despite its being sold as subsections rather than undivided shares, is to be managed and maintained as a single estate. This applies to Hong Lok Yuen (about 1 000 houses/units), and also Fairview Park (about 5 000 houses/units). However, in most of the small-house or village-house developments in the New Territories, there is not necessarily a Master DMC. Some of the individual houses in these developments are covered by separate DMCs – showing that they are not supposed to be managed and maintained as

⁵ According to the Master Layout Plan obtained from the Land Registry, the whole lot of Hong Lok Yuen has a total of 51 097 hectares, of which 38 472 hectares are housing areas. A rough calculation shows that some 25% of the whole lot are owned by the developer.

⁶ Of the 12 sections in Hong Lok Yuen, two of them (totaling ten subsections) contain multi-storey buildings (all of them are four-storey buildings). The ten subsections are governed by their respective sub-DMCs. According to the sub-DMCs, the joint owners of these subsections (there should be 62 such co-owners) are allocated with undivided shares – like ordinary multi-storey buildings. It is for consideration how these 62 co-owners should stand in the owners' meeting to agree to form the proposed committee.

a single development in the first place. In such cases, the above proposal for owners of house development is not applicable to them⁷. It begs the question on whether the above proposal, which is tailor-made for Hong Lok Yuen and Fairview Park, should be pursued in terms of overall public interest.

Drafting Matters

16. Whether the above proposal should be included in the existing BMO or implemented through a separate legislation will again depend on the extent of the powers, duties and liabilities of the committee. If the former is viable, then it would be necessary to make corresponding amendments and additional provisions in the BMO. These amendments involve substantial or fundamental changes to the definition of the terms “owner”, “building”, “flat”, “share”, etc. in section 2 and the introduction of new provisions and/or a new Schedule to the BMO to set out the formation procedure, composition and operation of the proposed committee, terms of appointment of the committee members, the powers, duties and liabilities of the committee, and the relationship between the committee and the persons or bodies (if any) who are managing the house development for the time being, etc.

Way Forward

17. Subject to Members’ views, we will continue to work on the implementation details in consultation with the departments concerned. Consultation with the owners of house developments, the real estate and property management industries and the professional bodies will need to be conducted. Given the complexity of the proposal and also the need for extensive consultation, we do not propose to incorporate the amendments into the Building Management (Amendment) Bill 2005. Subject to an agreement reached among Members and the Administration on the legislative framework, we estimate that the consultation process will take some six months and depending on the results of the consultation, the drafting work will take some six to nine months.

Views Sought

18. Members’ views are invited on the above.

⁷ The Administration is separately preparing another paper on a proposal to allow owners of buildings which are covered by more than one DMC to incorporate under the BMO.

Home Affairs Department
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Powers, Duties and Liabilities of an Owners' Corporation

The main powers, duties and liabilities of an owners' corporation (OC) formed under the Building Management Ordinance (BMO) are set out below –

- (a) With effect from the date of issue of the certificate of registration, the owners for the time being shall be a body corporate with perpetual succession and shall in the name of the corporation specified in the certificate of registration be capable of suing and being sued and, subject to the BMO, of doing and suffering all such other acts and things as bodies corporate may lawfully do and suffer. (Section 8(2)(a))
- (b) At a meeting of a corporation any resolution may be passed with respect to the control, management and administration of the common parts or the renovation, improvement or decoration of those parts and any such resolution shall be binding on the management committee and all the owners. (Section 14(1))
- (c) The rights, powers, privileges and duties of the owners in relation to the common parts of the building shall be exercised and performed by, and the liabilities of the owners in relation to the common parts of the building shall be enforceable against the corporation to the exclusion of the owners. (Section 16)
- (d) The corporation shall maintain the common parts and the property of the corporation in a state of good and serviceable repair and clean condition. (Section 18(1)(a))
- (e) The corporation shall carry out such work as may be ordered or required in respect of the common parts by any public officer or public body in exercise of the powers conferred by any Ordinance. (Section 18(1)(b))
- (f) The corporation shall do all things reasonably necessary for the enforcement of the obligations contained in the deed of mutual covenant (DMC) (if any) for the control, management and administration of the building. (Section 18(1)(c))

- (g) A corporation may engage and remunerate staff for any purpose relating to the powers or duties of the corporation under the BMO or the DMC (if any). (Section 18(2)(a))
- (h) A corporation may pay the chairman, vice-chairman, secretary, treasurer and other holders of office of the management committee. (Section 18(2)(aa))
- (i) A corporation may retain and remunerate accountants for the purposes of auditing the corporation's books of accounts and preparing the annual income and expenditure accounts and balance sheets. (Section 18(2)(b))
- (j) A corporation may retain and remunerate a manager or other professional trade or business firm or person to carry out on behalf of the corporation any of the duties or powers of the corporation under the BMO or the DMC (if any). (Section 18(2)(c))
- (k) A corporation may insure and keep insured the building or any part thereof to the reinstatement value thereof against fire and other risks. (Section 18(2)(d))
- (l) A corporation may purchase, hire or otherwise acquire movable property for use by the owners in connection with their enjoyment of the common parts or to satisfy any requirement of a public officer or public body for the purpose of any Ordinance. (Section 18(2)(e))
- (m) A corporation may establish and maintain lawns, gardens and playgrounds on the common parts. (Section 18(2)(f))
- (n) A corporation may carry out any renovation, improvement or decoration work, as the case may be, to the common parts. (Section 18(2)(fa))
- (o) A corporation may act on behalf of the owners in respect of any other matter in which the owners have a common interest. (Section 18(2)(g))
- (p) If a DMC provides that if an owner fails to pay any sum which is payable under the DMC, a person may sell that owner's interest in the land or register a charge against such interest in the Land Registry,

then, notwithstanding the provisions of the DMC, the corporation may, to the exclusion of such person, exercise such power of sale or register such charge in the same manner and subject to the same conditions as if it were the person referred to in the DMC. (Section 19(1))

- (q) A corporation shall establish and maintain a general fund. A corporation may establish and maintain a contingency fund. A corporation shall maintain an interest-bearing account and shall use that account exclusively in respect of the management of the building. (Section 20)
- (r) The procurement of all supplies, goods or services required by a corporation in the exercise of its powers and the performance of its duties under the DMC (if any) or the BMO shall comply with such standards and guidelines as may be specified in a Code of Practice relating to such procurement. (Section 20A(1))
- (s) If any amount payable by an owner who is not occupying a flat in the building concerned remains unpaid for a period of one month after it has become due to the corporation, the corporation may, without prejudice to any right of action against the owner, by notice in writing addressed to the occupier of the flat demand such amount from the occupier, who shall thereupon be liable to pay the same to the corporation. (Section 23(1))
- (t) A management committee shall maintain proper books or records of account and other financial records and shall prepare an income and expenditure account and a balance sheet and laid before the corporation at the annual general meeting of the corporation. (Section 27(1))
- (u) A corporation shall procure and keep in force in relation to the common parts and the property of the corporation, such policy of insurance with an insurance company in respect of third party risks. (Section 28 – not yet commence)
- (v) A corporation may be wound up under the provisions of Part X of the Companies Ordinance as if it were an unregistered company within the meaning of that Ordinance. In the winding up of a corporation, the owners shall be liable, both jointly and severally, to contribute, according to their respective shares, to the assets of the corporation to an amount sufficient to discharge its debts and liabilities. (Sections 33

and 34¹)

- (w) A member of a management committee may, on reasonable notice to the owner or occupier, enter a flat at any reasonable time for the purpose specified in the BMO. (Section 40)
- (x) The tribunal shall have jurisdiction to hear and determine any proceedings specified in the Tenth Schedule. A corporation is a person specified to be competent to commence any proceedings. (Section 45)
- (y) A corporation may decide, by a resolution of the owners, to reject the budget prepared by the manager. The total amount of management expenses for the financial year shall, until another budget is sent or displayed and is not so rejected, be deemed to be the same as the total amount of management expenses (if any) for the previous financial year, together with an amount not exceeding 10% of that total amount as the manager may determine. (Schedule 7, paragraph 1)
- (z) If the corporation decides, by a resolution of the owners, that any income and expenditure account and balance sheet should be audited by an accountant or by some other independent auditor, the manager shall without delay arrange for such an audit to be carried out by that person. (Schedule 7, paragraph 2)
- (aa) A corporation shall determine, by a resolution of the owners, the amount to be contributed to a special fund by the owners in any financial year, and the time when those contributions shall be payable. (Schedule 7, paragraph 4)
- (bb) A corporation may, by a resolution of the owners of not less than 50% of the shares, terminate by notice the manager's appointment without compensation. (Schedule 7, paragraph 7)

¹ Sections 33 and 34 of the BMO are more concerned with the liabilities of the owners upon winding up of an OC.

Annex B

Powers, Duties and Liabilities of an Owners' Committee

The main powers, duties and liabilities of an owners' committee referred to in section 34D of the Building Management Ordinance are set out below –

- (a) No person may convert any part of the common parts of a building to his own use unless such conversion is approved by a resolution of the owners' committee (if any). (Section 34I)
- (b) In respect of each financial year, the manager shall prepare a draft budget setting out the proposed expenditure during the financial year and send a copy of the draft budget to the owners' committee. The manager is also required to send to the owners' committee a copy of the budget (which should be revised taking into account the views of the owners) after the end of 14 days from the date the draft budget was sent or displayed in the building. (Schedule 7, paragraph 1(2))
- (c) The financial year may not be changed more than once in every five years, unless that change is previously approved by a resolution of the owners' committee (if any). (Schedule 7, paragraph 2(7))
- (d) The manager may, out of money received by him in respect of the management of the building, retain or pay into a current account a reasonable amount to cover expenditure of a minor nature, but that amount shall not exceed such figure as is determined from time to time by a resolution of the owners' committee (if any). The retention of a reasonable amount of money or the payment of that amount into a current account and any other arrangement for dealing with money received by the manager shall be subject to such conditions as may be approved by a resolution of the owners' committee (if any). (Schedule 7, paragraph 3)
- (e) Except in a situation considered by the manager to be an emergency, no money shall be paid out of the special fund unless it is for a purpose approved by a resolution of the owners' committee (if any). (Schedule 7, paragraph 4(5))

- (f) No resignation of the manager shall take effect unless he has previously given not less than three months' notice in writing of his intention to resign by sending such a notice to the owners' committee. (Schedule 7, paragraph 6(1)(a))

- (g) If the manager's appointment ends for any reason, he shall within two months of the date his appointment ends prepare an income and expenditure account and a balance sheet and shall arrange for that account and balance sheet to be audited by an accountant or by some other independent auditor specified in a resolution of the owners' committee (if any). The manager shall also within two months deliver to the owners' committee (if any) or the manager appointed in his place any books or records of account, papers, documents and other records in respect of the control, management and administration of the building that are under his control or in his custody or possession. (Schedule 7, paragraph 8)

