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Panel on Housing

**Disposal of Hunghom Peninsula
Private Sector Participation Scheme Flats**

Background Brief

Purpose

This paper provides background to the disposal of the Hunghom Peninsula Private Sector Participation Scheme (PSPS) flats and summarized the views expressed by members on the subject.

Hunghom Peninsula PSPS project

2. PSPS is one form of subsidized ownership housing introduced by the Government in 1977 to supplement the Home Ownership Scheme (HOS) by inviting the participation of private developers. Unlike HOS flats which are owned by the Housing Authority (HA), PSPS developments are owned by the developer. Under the PSPS, private developers are invited to tender for housing sites on which they are required to build flats conforming to certain specifications stipulated by the Government. Like other Government land sales, the land title of a PSPS site is vested in the developer. The developer holds legal title to the land lot, owns the residential units, the car parking spaces and commercial facilities it builds under the same lease. The obligations of the contracting parties are stipulated in the Conditions of Sale for the housing site. Under the Conditions of Sale for PSPS projects, the HA is named to nominate eligible purchasers to purchase the flats from the developer concerned within a specified period. In the event that flats are unsold at the end of the specified period, the HA is obliged to purchase the flats at the guaranteed purchase price.

3. The Hunghom Peninsula PSPS flats comprised 2 470 flats, 494 car parking spaces and shopping facilities. The land lease was granted to the developer at a tender price of \$583 million on 24 September 1999. The flats

were completed in November 2002. The total saleable floor area was 123 500 square meter. The guaranteed purchase price was \$15,500 per square meter and the total guaranteed purchase prices for all the 2 470 residential units was about \$1,914 million. Under the Land Grant, the HA should nominate eligible home purchasers to purchase the flats within a period of 20 months from the date of the Consent to Sell, which was issued in November 2002.

4. In November 2002, the Government decided to cease indefinitely the production and sale of HOS/PSPS flats from 2003 onwards to address the imbalance between supply and demand of private residential flats, and to restore the confidence of the public and investors in the property market. Detailed information on the Government's decision is set out in the Background Brief entitled "Disposal of surplus Home Ownership and Private Sector Participation Scheme flats" in LC Paper No. CB(1) 350/04-05(03). The Hunghom Peninsula was one of the two PSPS projects that need to be disposed of pursuant to the decision to cease the production and sale of HOS and PSPS flats.

Disposal options

5. Following the decision to halt the sale and production of HOS and PSPS flats starting from 2003 onwards, the Government explored possible options to dispose of the Hunghom Peninsula PSPS flats. According to the Administration, it had explored several options. One of the options was for the HA to purchase all the flats from the developers and then to dispose of them as HOS flats. This option was discarded as the Administration considered that it ran contrary to the policy direction and would adversely affect the property market. Moreover, it was not possible to dispose and change the use of those flats without first obtaining the developer's agreement as the developer held legal title of the land.

6. Another option explored by the Administration was for the HA to purchase the Hunghom Peninsula PSPS flats for conversion into public rental housing. This option was not adopted on the ground that the flats were considered not suitable for conversion because they were excessive in size and of a provision standard higher than the existing public rental units.

7. The Administration had also examined the possibility of the HA nominating a single purchaser to take up all the flats from the developer so that the single purchaser can dispose of them in the private market. The legal advice from the Government solicitors and external Senior Counsel was that this could be considered as providing housing to the general public and the HA could be challenged for acting outside its authority and powers under the Housing Ordinance (Cap. 273). This option was also outside the terms of the Conditions of Sale and might be challenged by the developer.

Negotiation with the developer on the disposal arrangement

8. The Administration started negotiation with the developer in January 2003 to allow the developer to sell the flats in the open market, subject to payment of a lease modification premium. Owing to the huge differences between the positions of the two parties on the premium, negotiations broke off in March 2003. In July 2003, the developer initiated litigation against the Administration and the HA for breaches of the Land Grant and claimed for damages.

9. Having considered the various policy, legal and financial considerations and the various options, the Administration decided to re-open negotiation with the developer by way of mediation. The negotiation team comprised representatives from the Lands Department, Housing Department and Department of Justice. The mediation was concluded in December 2003 with the modification premium agreed before an independent mediator accredited by the Hong Kong International Arbitration Centre.

10. On 9 February 2004 the Government announced that it had reached an agreement with the developer, First Star Development Limited, to modify the Conditions of Sale to allow the 2 470 flats to be sold in the open market. The developer agreed to give up its right to receive the payment of a guaranteed purchase price at \$1,914 million from the HA and paid a premium of \$864 million to the Government for the lease modification. The Conditions of Sale restricts the development on the lot to a residential gross floor area of 144 300 square meter and any redevelopment would have to be in accordance with the Master Layout Plans approved for development of the lot as a PSPS development.

Members' concerns

11. Following the public announcement of the outcome of the negotiation, the Panel on Housing, together with the Panel on Planning, Lands and works, held two special joint meetings to discuss the subject. Many members expressed grave concern about the agreement reached by the Administration with the developer of the Hunghom Peninsula PSPS project concerning the disposal of flats. The major concerns of members are as follows:

- (a) It was inappropriate for the Administration to negotiate with the developer behind closed doors. The flats could be sold through open tender or auction so that other developers could have a chance to participate. The approach taken by the Government benefited only the developer concerned at the expense of public interests;
- (b) The agreement to modify the relevant Conditions of Sale to allow

the 2470 flats to be sold in the open market was against the Administration's stated housing policy of ceasing the production and sale of HOS and PSPS flats;

- (c) The agreed premium of \$864 million was pathetically low, taking into account the fact that the property market was picking up; and
- (d) The agreement did not settle the issue once and for all as there was still pending litigation for damages filed by the developer.

12. To address members' query about the basis for accepting the agreed premium and in response to members' request, the Administration provided to the Panels the valuation report compiled by the Lands Department for the negotiation and mediation. The Administration also secured the developer's consent to disclose the pertinent information about the mediation, including the developer's estimates of the premium for the lease modification. The details of the discussions on the premium provided by the Administration are in **Appendix I**.

13. Since some members were unconvinced of the approach taken by the Government to settle the issue by means of negotiation and mediation and at members' request, the Administration made available on a confidential basis the legal advice on the disposal options for the Hunghom Peninsula PSPS project for members' inspection.

14. A chronology of relevant events and the relevant papers with their hyperlinks are in **Appendices II and III** respectively.

Appendix I

Details of the discussions on the premium for lease modification provided by the Administration

The mediation was conducted and concluded between 8 December and 23 December 2003 before an independent mediator who is accredited by the Hong Kong International Arbitration Centre. During the course of mediation, both parties carefully examined each other's figures in the presence of the mediator. There were differences on the estimated sale price of the flats after upgrading works, developer's profit/bulk discount, marketing cost, upgrading cost and period for sale of flats after completion of upgrading works. Our position was vigorously challenged by the developer. In particular, the developer argued that a greater profit/bulk discount was appropriate to reflect the substantial number of flats, and the developer adopted a comparatively lower estimated sale price of the flats.

After several rounds of exchange of details, we proposed, as a basis for settlement and bearing in mind the inherent difficulties in valuing 2 470 upgraded PSPS flats as one lot, a premium of \$1,310 million based on an estimated sale price of \$38,000/m² net (\$3,021/sq.ft gross) for the flats and a 15% bulk discount/profit. The developer rejected our proposal and counter-offered a modification premium of \$864 million, which we understood, was based on, among other things, a selling price of \$35,218/m² net (\$2,800/sq.ft gross) and a profit margin of 20%. Despite further intensive discussions between the two sides, the developer declined to move from this position.

Appendix II

Chronology of events relating to the Disposal of Hunghom Peninsula PSPS flats

| Date | Event |
|-----------------------|--|
| 24 September 1999 | Land lease was granted to the developer at a tender price of \$583 million |
| 22 October 1999 | The developer commenced construction |
| 3 September 2001 | The Chief Secretary for Administration made statement on housing and announced moratorium of all sales of HOS and PSPS flats until end of June 2002 |
| 6 August 2002 | Construction completed |
| 13 November 2002 | The Secretary for Housing, Planning and Lands gave a statement on housing policy at the Council Meeting and announced the cessation of the production and sale of HOS and PSPS flats |
| 15 November 2002 | The Panel on Housing discussed the statement on housing policy |
| 20 November 2002 | The Lands Department issued the Consent to Sell to the developer and the 20-months prescribed period for the HA to nominate purchasers for the completed PSPS flats commenced |
| 14 January 2003 | The Panel on Housing received a policy briefing from the Secretary for Housing, Planning and Lands |
| 18 March 2003 | The Panel on Housing discussed the disposal of surplus HOS/PSPS flats |
| January to March 2003 | The Administration carried out initial negotiation with the developer |
| 6 March 2003 | HA's Strategic Policy Committee approved the disposal arrangement of the surplus HOS/PSPS flats and was informed that negotiation with the developer was underway |

| Date | Event |
|------------------------|--|
| End March 2003 | Negotiation with the developer halted since both sides were unable to reach any agreement upon encountering difficulties |
| 25 July 2003 | The developer initiated litigation by issuing a Writ of Summons |
| August to October 2003 | The Administration revisited various possible disposal options and decided that further negotiation with the developer through mediation should proceed |
| 9 October 2003 | Hon LEUNG Yiu-chung raised a question at the Council meeting concerning problems arising from cessation of the production and sale of HOS and PSPS flats. The Council was informed that the developer had filed a writ against the Government and the HA |
| 3 November 2003 | The Panel on Housing discussed the updated progress of the disposal of surplus HOS/PSPS flats |
| 8 to 23 December 2003 | Lands Department, Housing Department and Department of Justice conducted mediation with the developer with the facilitation of an independent mediator accredited by the Hong Kong International Arbitration Centre |
| 26 January 2004 | The Administration formalized preliminary agreement on lease modification with the developer |
| February 2004 | Completion of lease modification process |
| 17 February 2004 | The Panel on Housing and the Panel on Planning, Lands and Works discussed the disposal of Hunghom Peninsula PSPS flats |
| 8 March 2004 | The Panel on Housing and the Panel on Planning, Lands and Works further discussed the disposal of Hunghom Peninsula PSPS flats |

Disposal of Hunghom Peninsula Private Sector Participation Scheme Flats

List of relevant papers

| Council/Committee | Date of meeting | Paper |
|---|-------------------|--|
| Housing Panel | 10 September 2001 | <p>A Statement on Housing http://www.legco.gov.hk/yr00-01/english/panels/hg/papers/cs-e.pdf</p> <p>Appendix II to LC Paper No. CB(1)251/01-02 http://www.legco.gov.hk/yr00-01/chinese/panels/hg/papers/251ce-a.pdf</p> <p>LC Paper No. CB(1)1983/00-01(01) http://www.legco.gov.hk/yr00-01/english/panels/hg/papers/a1983e01.pdf</p> <p>Minutes http://www.legco.gov.hk/yr00-01/english/panels/hg/minutes/hg010910.pdf</p> |
| Council meeting | 13 November 2002 | <p>Hansard http://www.legco.gov.hk/yr02-03/english/counmtg/hansard/cm1113ti-translate-e.pdf</p> |
| Housing Panel and Planning, Lands and Works Panel (PLW Panel) | 15 November 2002 | <p>LC Paper No. CB(1)301/02-03(01) http://www.legco.gov.hk/yr02-03/english/panels/hg/papers/hgplw1115cb1-301-1-e.pdf</p> <p>Minutes http://www.legco.gov.hk/yr02-03/english/panels/hg/minutes/hgpl1115.pdf</p> |

| Council/Committee | Date of meeting | Paper |
|-----------------------------|------------------|---|
| Housing Panel | 6 January 2003 | LC Paper No. CB(1)591/02-03(03) http://www.legco.gov.hk/yr02-03/english/panels/hg/papers/hg0106cb1-591-3-e.pdf Minutes http://www.legco.gov.hk/yr02-03/english/panels/hg/minutes/hg030106.pdf |
| Housing Panel | 14 January 2003 | LC Paper No. CB(1)704/02-03(01) http://www.legco.gov.hk/yr02-03/english/panels/hg/papers/hg0114cb1-704-1-e.pdf Minutes http://www.legco.gov.hk/yr02-03/english/panels/hg/minutes/hg030114.pdf |
| Housing Panel | 18 March 2003 | LC Paper No. CB(1)1129/02-03(04) http://www.legco.gov.hk/yr02-03/english/panels/hg/papers/hg0318cb1-1129-4-e.pdf Minutes http://www.legco.gov.hk/yr02-03/english/panels/hg/minutes/hg030318.pdf |
| Housing Panel | 3 November 2003 | LC Paper No. CB(1)190/03-04(03) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hg1103cb1-190-3e.pdf Minutes http://www.legco.gov.hk/yr03-04/english/panels/hg/minutes/hg031103.pdf |
| Housing Panel and PLW Panel | 17 February 2004 | LC Paper No. CB(1)990/03-04(01) (English version only) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-990-1e-scan.pdf |

| Council/Committee | Date of meeting | Paper |
|-----------------------------|-----------------|--|
| | | <p>LC Paper No. CB(1)995/03-04(01) (English version only) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-995-1e-scan.pdf</p> <p>LC Paper No. CB(1)1000/03-04(01) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-1000-1e.pdf</p> <p>LC Paper No. CB(1)1000/03-04(02) (English version only) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-1000-2e-scan.pdf</p> <p>LC Paper No. CB(1)1000/03-04(03) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-1000-3e.pdf</p> <p>LS44/03-04 http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217ls-44-e.pdf</p> <p>LS46/03-04 http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217ls-46-e.pdf</p> <p>Minutes http://www.legco.gov.hk/yr03-04/english/panels/hg/minutes/hgpl0217.pdf</p> |
| Housing Panel and PLW Panel | 8 March 2004 | <p>LC Paper No. CB(1)1160/03-04(01) http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0217cb1-1160-1e.pdf</p> |

| Council/Committee | Date of meeting | Paper |
|-------------------|-----------------|--|
| | | LC Paper No. CB(1)1212/03-04(01) (http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0308cb1-1212-1e.pdf) LC Paper No. CB(1)1238/03-04(01) (http://www.legco.gov.hk/yr03-04/english/panels/hg/papers/hgplw0308cb1-1238-1e.pdf) Minutes (http://www.legco.gov.hk/yr03-04/english/panels/hg/minutes/hgpl0308.pdf) |

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