

For information
on 28 March 2006

**LEGISLATIVE COUNCIL
PANEL ON PLANNING, LANDS AND WORKS**

**Review of Lease Modification
to permit Change of Use for Sites Previously Granted by Private Treaty**

Purpose

This paper presents the outcome of the review of lease modification to permit change of use for sites previously granted by private treaty (PTG) for Members' information.

Background

2. At the meeting of the LegCo Panel on Planning, Lands and Works on 22 March 2005, the Secretary for Housing, Planning and Lands undertook, at Members' request, to conduct a review of the current policy on lease modification to permit change of use for sites previously granted by private treaty.

Current Policy

Nature of PTG

3. Most land available for commercial, industrial or residential development is sold by public auction or tender. Apart from this, we also grant land by PTG to private or non-governmental organizations for specified use in justified circumstances, to comply with approved Government policies and to meet Hong Kong's economic, social and community needs. All such direct land grants have to be subject to stringent policy scrutiny and are thoroughly considered to be justified in the public interest, with specific approval granted by the Executive Council (ExCo) or by delegated authority exercised in accordance with the approval criteria set by ExCo, on a case by case basis.

4. PTGs are normally for a specific purpose with the land use specified in the grant. Premium payable varies from nominal, concessionary to full market value depending on the nature of the use. Examples of the different categories of PTGs classified by premium charged are as follows –

(a) nominal premium

- (i) education purpose: schools, tertiary institutions;
- (ii) welfare purpose : social welfare, residential care homes for the elderly;
- (iii) health use: clinics, hospitals;
- (iv) housing purpose: e.g. public rental housing by the Housing Authority.

(b) concessionary premium

- (i) charitable uses such as churches, temples;
- (ii) housing purpose: assisted housing (e.g. rental estates built by the Housing Society).

(c) full market premium

- (i) public utilities purpose;
- (ii) special industrial purposes; and
- (iii) housing purpose: e.g. property development by the railway corporations.

5. Other than the above-mentioned categories, there are a small number of PTG cases, where the relevant bureau / department will consider the merits of each case for submission to ExCo for approval, with regard to certain policy considerations, such as whether the development proposal for PTGs complies with approved Government policies or assists to meet pre-determined policy

objectives; the assessed economic or other benefits of the proposal, the strategic importance or otherwise of the proposal; whether it is the right timing to make the proposed PTGs; and the ability of the applicant in financing the implementation of the proposal etc.

6. To sum up, the number of PTG cases is not many, and these cases were approved only under rather special circumstances on individual merits. Development must conform to the current town plans at the time of grant or subsequent permissions granted or amendments of the relevant town plan by the Town Planning Board. Development must represent full use of the site having regard to the purpose of the grant. Grantees must demonstrate their financial capability to implement their projects. Unequivocal policy support from the relevant bureaux / departments must be secured before the application for land under PTGs can be processed. All PTGs have to be submitted to ExCo for approval or to the delegated authority for approval in accordance with the approved criteria set by ExCo. Restrictions as appropriate are included in the Conditions of Grant. The policy of grating land by private treaty is long established, and has worked well. It has proven to be effective in ensuring the timely and optimal development of our land resources to keep pace with our social and economic development, for the purpose of meeting economic, social and community needs in a timely and appropriate manner.

Process and considerations in the policy scrutiny of lease modification involving PTG

7. Hong Kong has undergone significant changes on economic, social and community fronts over the past few decades. As a result of economic restructuring, the continuous enhancement in the standard of living of our people and the infrastructural development of our city, the original specified purposes of some PTG sites granted in the early years have become obsolete and are no longer required. An application to the Government for a lease modification will be required, if the grantee wishes to use or develop a lot differently. However, the approval or otherwise of each and every case will be subject to stringent policy scrutiny and thoroughly considered on individual merits, have to be justified in the public interest, and then submitted to ExCo for consideration and approval (or where authority has been delegated by ExCo, to the Administration for consideration and approval) on a case by case basis. Generally speaking, applications for lease modification are usually favourably considered if the following conditions are met –

- (a) the former permitted use is already obsolete due to changing circumstances;
- (b) a change in the original land use of the PTG site is confirmed through the statutory town planning procedure for other better uses; and
- (c) the applicant is prepared to pay full market premium.

For the financial years between 2001-02 and 2005-06, a total of 745 lease modification/land exchange cases were executed with a total land premium of \$27.86 billion. Among these cases, only 6 cases concerned change of use involving PTG sites with a total land premium of about \$1.407 billion.

8. Based on the enhancement of value resulting from the proposed lease modification, the full market premium payable will be assessed. Permitting grantees to modify their leases after payment of the full market premium is a practical and flexible practice which helps achieve early realization of the planning intention. By allowing obsolete or under-utilized land to be put into optimal use, we can better cope with the rapidly changing social and economic demands and this will benefit the economic, social and community development. Without such flexible policy, the pace and scale of development to meet the needs for residential and commercial development and the early realization of the changing planning intentions of the areas would have been impeded.

9. Having examined various cases and categories approved and the policy considerations involved, and given the justifications set out in paragraphs 7 and 8 above, the Government has decided to maintain the current policy.

Practical difficulties in regaining re-possession of land for open sale

10. There has been a suggestion that the Government should consider taking back the PTG sites for open sale by auction or tender. We have examined three different ways of regaining re-possession of sites and concluded that none of them can ensure that the objective of regaining re-possession of land can be achieved within a reasonable period of time. Regaining re-possession of land can be a protracted process, which conflicts with the principle of making optimal use of land. The terms and conditions of PTGs (Conditions of Grant) commonly contain a cessation or diminution of

user clause and prohibitions on alienation. As landlord, the Government retains its right to re-enter, should the site cease to be used, or be used to a diminished extent, for the intended purpose. However, this is an extreme sanction, which should be preceded by efforts to ensure compliance with the Conditions of Grant or negotiate voluntary surrender of the lot by the grantee. The grantee has the right to apply to the Court of First Instance or petition the Chief Executive for relief against any re-entry under the Government Rights (Re-entry and Vesting Remedies) Ordinance (Cap. 126).

11. Although the Conditions of Grant of a site may contain a cessation or diminution of user clause such that in the event the grantee of the site no longer use it for the intended purpose, the Government may re-enter the site in accordance with the provision, in practice this will have to be established as a matter of fact on the evidence and have to be accepted by the Court. Resorting to re-entry action by invoking that clause has potential problems and can be protracted and result in long delay pending disposal of any application to the Court or petition to the Chief Executive for relief against re-entry, and only following the rejection of the petition or application will the land be made available for sale in the open market. For example, the site of a school in Ap Lei Chau was left vacant since the closure of the school in 1994. In the 10 years that followed, the grantee made several applications for change of use. As a result of rejection by the authorities or the grantee not having carried out the proposal, the development project could not proceed. Finally, the Government decided to re-enter the site in mid 2005. In November 2005, the grantee petitioned the Chief Executive for relief against re-entry and the case is still under processing. This process has already taken 12 years, without taking into account the time that will be needed subsequently for processing the petition. Therefore, the method of re-entering land has a lot of practical difficulties, and has rendered the future development of the land in question uncertain.

12. Particularly, pursuing the proposal on re-entering land for open bidding or tendering will be all the more unreasonable, if the original PTG includes private land already held by the grantee (the concerned private land being included in the PTG through surrender and regrant) or the proposed lease modification includes amalgamating the PTG sites with additional private land, in the form of land exchange. It would significantly reduce the incentive for developers to amalgamate ownerships and assemble land to secure worthwhile site for redevelopment according to the planning intention and achieve

revitalization of old dilapidated and over-crowded areas.

13. As for regaining re-possession of a PTG site by resumption, we do not have power to recommend resumption of PTG site under the Lands Resumption Ordinance or the Town Planning Ordinance unless the site is required for public purpose or that it interferes with the lay-out of town plans.

14. If the Government initiates the negotiation with the grantee on regaining re-possession of the site, the grantee could refuse, or will certainly negotiate with the Government for a high price even if they agree to consider the matter. The time needed for the negotiation process is not only beyond the control of the Government but also unpredictable. Perhaps more importantly, the pursuit of obtaining the land by voluntary surrender would merely substitute the negotiation process for a lease modification premium with another negotiation process concerning the surrender value. Also, the Government could not justify paying more than the existing use value as the surrender value. It will not be worthwhile for the Government to pay a very high price to obtain the land by voluntary surrender.

15. In the circumstances, it is clear that the only option is to either offer terms for a modification or land exchange, or not to. The former would allow implementation of the planning intent and the collection of premiums. The latter would result in lots continuing to be used for purposes which have become obsolete and early implementation of the planning intention would become unrealizable. Given the disappearance of the rationale for the original use of the grant, the land would not be fully utilized and the value would be significantly less than the optimum. It would be in nobody's best interest (be it the Government, the grantee, the community) nor would we be able to cope with the pace of development of Hong Kong, to continue to use the land for the purposes as restricted in the lease until its expiry.

Ensuring premium in the best interest of Hong Kong

16. PTG application, if approved, will be subject to the payment of full market premium by the applicant. On premium, we have a set of established mechanism and procedures to ensure that the outcome will be in the best interest of Hong Kong.

(a) Enhancing transparency

17. In the negotiation process, the Director of Lands is acting in the role of landlord in a private law and is negotiating contracts in that capacity, with all the commercial sensitivity implications that go with that. It would compromise the LandsD's position if the details of the negotiation process are disclosed. Nonetheless, the LandsD will disclose information as far as practicable, including –

(i) media briefings for introducing the premium assessment mechanism;

(ii) issuing practice note on premium assessment procedure; and

(iii) the LandsD has since January 2001 started to make available information on completed lease modifications and land exchanges on its web site. The public information database has from March 2005 been expanded to include land granted by PTG. The public can now have access to information on land transaction details such as site location, use, land grant execution date and premium paid.

(b) Premium assessment

18. Premiums for lease modifications and land exchanges are assessed by qualified professional valuers in the LandsD. The approach adopted for assessing enhancement in land value conferred by the change in the lease conditions accords with the policy reaffirmed by ExCo in July 1997. In arriving at the enhancement, the difference between the land value under the existing lease conditions and the land value under the modified lease conditions is assessed. Stringent guidelines on the policy, procedures and justifications have also been issued by the LandsD for its staff to ensure that each and every cases will be handled in a fair, reasonable and consistent manner. After the concerned application is approved, premium will be assessed by a Valuation Conference/Valuation Committee. The procedures are set out in a practice note issued by the Lands Department to the trade on 17 February 2006 (see appendix).

19. Under the current system, the Audit Commission will conduct audit on land sale proceeds from time to time, and the Public Accounts Committee will

also closely monitor. Furthermore, the ICAC and the Ombudsman also have a check and balance and monitoring role to play.

Strengthening the Cessation or Diminution of User Clause

20. There have been suggestions that the Lands Department (LandsD) should strengthen the cessation or diminution of user clause, whereby the land will automatically revert to the Government if in the opinion of the Director of Lands, the land has ceased to be used for the permitted use under the PTG. For new PTGs, the LandsD is strengthening the cessation or diminution of user clause which provides that the Director of Lands' opinion on whether a lot has ceased to be used for its permitted use will be unfettered, conclusive and binding on the grantee.

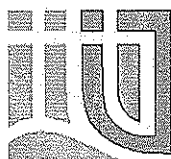
21. Where the cessation or diminution clause in the PTGs has been demonstrably breached and relevant policy justifications for the PTG remain valid, the Administration will re-enter the lot if the grantee refuses to purge the breach.

Presentation

22. Members are invited to note the content of this paper.

Housing, Planning and Lands Bureau
Lands Department

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Lands Administration Office
Lands Department

Practice Note

Issue No. 1/2006

Premium Assessment Procedure Relating to Lease Modification Transactions⁽¹⁾

Pursuant to discussions at the Land Sub-committee Meeting of the Land & Building Advisory Committee (LBAC) regarding measures to streamline and enhance the transparency of the premium assessment procedure in lease modification transactions, the Department has, in consultation with Hong Kong Institute of Surveyors (HKIS), reviewed its current procedure and has put in place a number of new practices.

2. This Practice Note (PN) sets out the revised premium assessment procedure is as follows : -

(i) Initiation of Premium Assessment

Generally speaking, the acceptance by the applicant of the offer of provisional basic terms (PBTO) and conditions for the proposed lease modification transaction issued by the District Lands Office (DLO) concerned together with the draft Special Conditions as approved by the District Lands Conference will trigger the premium assessment procedure. *(Note: For cases such as those requiring the completion of statutory procedure as a condition for execution of the lease modification document, the actual timing of the premium assessment will be adjusted to take into account the progress of the statutory process involved).*

To facilitate preparation of the premium assessment, applicants or their agents are invited to submit to the DLO concerned such information as they consider relevant to the premium assessment as soon as possible after their formal acceptance of the PBTO. The finalised premium assessment will then be submitted to the Valuation Section in LandsD/HQ for action under (ii) and (iii) below.

⁽¹⁾ The reference to lease modification transactions includes lease modifications to be effected by way of land exchanges.

(ii) **Vetting of the Premium Assessment Submission**

Upon receipt of a submission from the DLO, the Valuation Section will notify the applicants/agents and vet all submissions before referring them to the Valuation Committee (V. Com.)/Valuation Conference (V. Conf.) for consideration. During this period, applicants/agents may submit additional information and/or clarifications they consider relevant to the premium assessment direct to Valuation Section. It is important that this be done without delaying the referral of the premium assessment to V. Com./V. Conf. No negotiation on the premium assessment would be permitted.

(iii) **Consideration of the Premium Assessment**

Depending on the amount of the premium involved, the assessment will be referred to and decided by either V. Com. or V. Conf. V. Conf. will also consider appeals to assessments previously approved by V. Com.

(iv) **Communication of the Premium Assessment and the Issue of Binding Basic Terms Offer**

The premium will be communicated to the applicant by the DLO concerned by way of a binding basic terms offer. If the applicant disagrees with the amount of the premium, he or she may appeal against it. However, any revised assessment to be carried out will be at value current at the time of re-assessment, which could be the same as, or higher or lower than, the premium originally offered.

(v) **Consideration of Appeal against Premium Assessment**

On receipt of an appeal against the premium assessment, the DLO concerned will submit the case to the Appeal Team of the Valuation Section. Prior to submission of the premium appeal to V. Conf., the case officer in the Appeal Team will communicate with the applicant/agent on a non-committal and without prejudice basis. The case officer will exchange views with the applicant/agent on matters relevant to the premium assessment, including the basis of valuation, gross development values, construction costs of the development, comparables and relevant transaction evidence etc. Normally, at the final stage of this process, the case officer will also enquire if the agent has received any instruction from his/her clients as regards the latest counter-offer of premium for the proposed lease modification transaction for incorporation into a submission to V. Conf.

(vi) **Attendance at Valuation Conference**

The applicant/agent will be invited to attend the meeting of the V. Conf. to consider his/her premium appeal. The case officer will present the case to Members of V. Conf. in the presence of the applicant/agent who will then have the opportunity to elaborate on any arguments which he/she may have already put forward in any written submissions in support of a revised assessment. Deliberation of the case by Members of the V. Conf. will take place after the applicant/agent has left the meeting.

(vii) **Issue of Revised Offer on Premium Assessment**

After a decision has been made by V. Conf. on the premium appeal and a binding offer of the revised premium assessment has been issued, the case officer may, upon request of the agent, advise him/her of the major parameters adopted by V. Conf. in the premium assessment, which are substantially different from those put forward by the agent including any major arguments/comparables contained in the agent submission that have not been accepted by V. Conf. The purpose of the above is to facilitate the consideration of the revised assessment by the agent clients.

3. A flow chart highlighting the key steps referred to above is attached.

(Patrick L. C. LAU)
Director of Lands
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Flow Chart
(Premium Assessment Procedure Relating to Lease Modification Transactions)

