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LEGISLATIVE COUNCIL BRIEF

**MEASURE TO ENHANCE THE SMOOTH OPERATION
OF THE APPLICATION LIST SYSTEM**

INTRODUCTION

At the meeting of the Executive Council on 21 June 2005, the Council ADVISED and the Acting Chief Executive ORDERED that adjustment should be made to the triggering mechanism under the Application List System (ALS), whereby a bid reaching at least 80% of our assessed Open Market Value (our OMV) (i.e. within a 20% margin below our OMV) would be accepted as a trigger to initiate an auction or a tender, with the proviso that the site would not be sold unless the highest bid met or exceeded our OMV reserve price (i.e. 100% of our OMV) assessed on the day of auction/close of tender.

BACKGROUND AND ARGUMENT

Background

2. On 13 November 2002, the Secretary for Housing, Planning and Lands (SHPL) made a statement on Re-positioning of Housing Policy and announced a package of property market stabilisation measures. Sale of Government land had been suspended until the end of 2003, after which it would only be triggered through the ALS¹. Under the ALS, a developer who is interested in a site in the published list of available sites is required to submit his minimum bid which, if it meets our OMV, will trigger the site for an auction or a tender, all in accordance with a detailed published procedure. On 15 October 2003, SHPL made a statement on the Consolidation of Housing Policy and announced further measures, including resuming the ALS from January 2004.

3. Since then, we have observed the following phenomena –

¹ i.e. no scheduled auction programme operating in parallel except open tender for land for specific purposes such as petrol filling stations.

- (a) alleviation in the over-supply situation: the fall in the stock of completed flats pending sale from about 20 000 as at the end of June 2003 to about 15 000 as at April 2005;
- (b) construction of new private residential units has been on the decline, from a high level of over 30 000 units in 2000 to about 14 000 units in 2004; and
- (c) six sites (five residential and one commercial/business) had been successfully triggered and sold, after we resumed land sales from January 2004. However, no residential sites have been successfully triggered since the auction in October 2004² and there have been calls from the trade to enhance the smooth operation of the ALS.

4. We announced on 4 March 2005 the ALS for the 2005-2006 fiscal year, offering a total of 35 sites (29 residential and six commercial/business), and some measures to enhance the operation of the ALS. These measures comprised shortening the time required in bringing a triggered site to auction by three weeks³, revising the amount of deposit (subject to a cap of \$50 million) to a simple 10% of the specific bid amount, and announcing the number of failed bids received on a site-specific and monthly basis. Since announcing the new list and the enhancement measures, there have been four attempts to trigger two sites up to 31 May 2005. These bids fell short of our OMV.

Present Position

5. Notwithstanding the enhancement measures and a wider choice of sites, the market response has not been encouraging. Developers have openly expressed difficulties in being able to trigger sites on the AL. They attribute this mainly to what they see as Government's "high" trigger prices and lack of flexibility in accepting bids.

6. From the Government's point of view, further lack of successful triggers would affect the public's perception of the Government's reassurance of adequate and timely supply of land to meet market demand, and might encourage speculation which now appears to be re-emerging after the property market downturn in 1997. This may undermine public confidence in the ALS. The Economic Analysis and Business Facilitation Unit has also advised that there is

² The site sold at the auction on 22 February 2005 was commercial/business.

³ Further shortening the lead time between the successful trigger and the auction might be operationally difficult, and not preferred by other bidders (as in the interest of fairness and transparency, a reasonable time should be allowed for all to know about the exercise through gazetting and prepare themselves through seeking professional advice and making financial arrangements).

room for adopting a more flexible trigger price, at a reasonable level below our OMV.

7. While there are other sources of land supply⁴ which account for a significant proportion of the supply of private residential flats, we believe the operation of the ALS could be further enhanced to facilitate triggering of sites. This will demonstrate our responsiveness in taking appropriate action to render the smooth operation of the ALS which is one of the cornerstones of our housing policy.

Guiding Policy considerations and principles

8. In considering any changes to the ALS, we are guided by the following policy objectives and guiding principles -

- (a) upholding our economic philosophy of letting market forces thrive, with minimum Government's intervention;
- (b) providing a steady supply of land to ensure the continuation of a fair and stable environment for the free and efficient operation of the property market and to meet the market demand for community development in a timely manner; and
- (c) safeguarding public revenue through our time-honoured policy of not selling land cheaply and that the land goes to the highest bidder at a price which reflects the prevailing market value of the land concerned.

Relaxing the Trigger Price

9. Developers have argued that our present policy of setting the trigger price at our OMV is unnecessarily strict and sets a very high threshold for the purpose of triggering a site for sale. They consider that setting the trigger price lower than our OMV will encourage more bids and, once sites have been triggered, competitive bidding in the open auction will ensure that the full OMV on the day will be reached and there is no risk of public revenue being jeopardised by accepting triggers at less than our OMV.

10. The sales prices for the six sites sold since January 2004, which ranged between 48% and 200% higher than the trigger prices, do not seem to support the developers' claim that trigger prices are set too high. For the reasons set out at paragraphs 5, 6, and 7, we consider some relaxations are justified.

⁴ Other sources of land supply include modification of lease conditions of developers' existing land holdings, purchase of land from the private market, property developments from the two railway corporations and the Urban Renewal Authority.

11. Our considerations are as follows -
- (a) the justification for setting the trigger price at our OMV under the ALS is to guarantee that the site will be sold at our OMV to the successful triggerer, in the event there is no other bid when the site is put to auction or tender. Provided that we can maintain a separate undisclosed reserve price at our OMV assessed on the day of auction or close of tender, which must be met or exceeded before the site will be sold, public revenue regardless of at what level the trigger price is set can be protected. We will make it clear that if the highest bid fails to meet or exceed the reserve price, the auctioneer will withdraw the site from sale; and
 - (b) with regard to the extent of relaxation or margin compared to our OMV, in accord with common acceptance in the valuation field, a 10% variation in value constitutes a permissible “margin of error” or range between two valuation experts. Various suggestions received from members of the Land and Building Advisory Committee and its Land Sub-Committee, individual developers and financial analysts range from 15% to as much as 40%. We understand that in Singapore where a broadly similar land sale system is being operated, the trigger price is set at within a 15% margin below OMV. Sales are by tender rather than auction, and there is no reserve price.
12. We propose that the margin be set at the maximum of 20% having regard to the need to establish a genuine commitment not too remote from our OMV. Setting the margin greater than 20% might potentially result in a protracted and tedious auction in reaching the OMV reserve price, and a higher possibility of withdrawals.
13. In summary, we recommend allowing triggering if the trigger price reaches at least 80% of our OMV (i.e. within a 20% margin below our OMV). Successful triggering does not guarantee sale of the site. Sale will only be accepted if the highest bid meets or exceeds 100% of our OMV assessed on the day of auction/close of tender. In accordance with existing principles, provided that there is an opening bid at the successful trigger price, be it made by the triggerer or another bidder, we would return the deposit to the triggerer (as against forfeiture of the deposit), if the site is eventually sold to another bidder other than the triggerer or is withdrawn.

IMPLICATIONS OF THE PROPOSAL

14. The proposal has economic, financial and sustainability implications as set out at Annex.

15. The proposal is in conformity with the Basic Law, including the provisions concerning human rights, and has no civil service, productivity or environmental implications.

PUBLIC CONSULTATION

16. We have consulted key industry players through the Real Estate Developers Association of Hong Kong from time to time, the Land and Building Advisory Committee on 18 November 2004 and its Land Sub-Committee on 11 November 2004. The Legislative Council Panel on Planning, Lands and Works also met on 26 April 2005 to discuss issues relating to the ALS. The current proposals have been formulated after taking into account views expressed at those meetings.

PUBLICITY

17. A public relations plan has been worked out. The plan includes briefings for stakeholders, members of political parties and the media. Legislative Council brief and press release will be issued. A spokesman is available for answering media enquiries.

BACKGROUND

18. Sale of Government land by auction has been a long established practice. To stabilize the property market, scheduled auction was suspended for ten months in 1998-99. The ALS was only introduced after the 1998-99 moratorium. In November 2002, the Government decided that to facilitate the efficient operation of the property market, scheduled auctions would be stopped until further notice. Following the Government's announcement in October 2003, the AL has been resumed since January 2004.

ENQUIRIES

19. For enquiries, please contact Miss Diane Wong, Principal Assistant Secretary for Housing, Planning and Lands (Planning and Lands)¹ at 2848-2266.

Planning and Lands Branch
Housing, Planning and Lands Bureau
21 June 2005

Financial, Economic and Sustainability Implications of the Proposals

Financial Implications

If the proposed measure is introduced, this would facilitate more successful triggers. Assuming this to be the case and that the reserve price is reached at auction, more land revenue will be generated as a result. The increase in the number of transactions may relieve the pressure towards the feverish bidding of land as was the case in the land auctions held in 2004 and the unit price (i.e. per square foot) of sites may not be inflated. Taken together, the two factors may bring a moderate increase in the land revenue. However, given the volatility of the property market, it would be impractical to estimate the additional land revenue generated as a result of the implementation of the proposed measure.

Economic Implications

2. The low level of Government land sale activity under the existing ALS has heightened market concerns about the adequacy of new land supply and future land production. This could result in unduly upward pressures on property prices. The proposed measure would enhance the market-driven mechanics of the ALS and is conducive to steady supply of land. This is beneficial to the healthy development of the property market.

Sustainability Implications

3. The proposal brings about more flexibility to the ALS, and helps ensure a stable supply of land that is responsive to market demand. It is in line with the sustainability principle of achieving a market-based economy which provides the resources to meet the needs and aspirations of the population, both now and in the future.