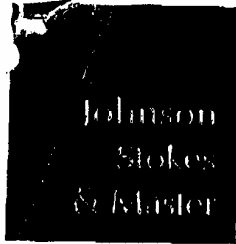


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Our Ref: AFK/S6/04/179527/1

Your Ref: LACO 11/316/2002 SF4 Pt VIII

Direct Tel: 2843 4225

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Date: 27th June 2005

Attn: Mr. A.L. Robertson

Dear Sir,

Re: Kowloon Inland Lot No. 11076: Hunghom Peninsula

We refer to your letter dated 18th May 2005.

We are referring the arguments put forward by you to Mr. Jonathan Sumption Q.C.

In the meantime, we have the following observations :-

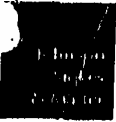
1. We have considerable difficulties in following your arguments and the logic behind the arguments.

2. You say that SC(6)(c) and (d) were deleted because they were spent of effect. If it had been the intention that SCs which were spent of effect were to be deleted in the modification exercise there would have been no good why the following SCs, among others, were not deleted as well :-

(i) SC(6)(a) containing the building covenant. This SC was replaced by the new SC(6)(a) set out in the First Schedule to the Modification Letter. The new SC requires the buildings to be completed not later than 22nd August 2002 in accordance with the Master Layout Plans ("MLP") submitted in accordance with the Tender Notice. The occupation permit was issued on 6th August 2002. The certificate of compliance was issued on 21st November 2002. The Modification Letter was entered into on 26th February 2004. SC(6)(a), whether in its original form, or as modified, was clearly spent of effect and no longer serves any purpose.

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- (ii) SC(6)(b) requires (i) building plans to be submitted for the approval of the Building Authority and the Director of Lands in accordance with the MLP submitted in accordance with the Tender Notice and (ii) the buildings to be completed within the time limits stipulated in the statement submitted in accordance with the Tender Notice. As the occupation permit and the certificate of compliance had already been issued when the Modification Letter was entered into SC(6)(b) was spent of effect and no longer serves any purpose.
- (iii) SC(3)(e), as replaced by the new SC(3)(e) set out in the First Schedule to the Modification Letter, provides that paragraphs 16 and 17 of the Tender Notice are expressly incorporated in and made part of the Conditions of Grant. Paragraph 16 deals with the provision of a parent or associated company guarantee for completion of the development. Paragraph 17 contains a prohibition against disposal of the shares of the grantee prior to the issue of the certificate of compliance. Both paragraphs 16 and 17 were spent of effect when the certificate of compliance was issued but they were expressly retained by the Modification Letter.
3. The above show clearly that the deletion of SC(6)(c) and (d), which contained restrictions on the number and sizes of units and efficiency ratio, was made not because the development was completed, nor because these SCs were spent of effect. They were deleted because it was intended that the lot and the buildings should be free from the restrictions contained in these SCs. The deletion of these SCs is not consistent with there being any subsisting right in the Director to insist on the restrictions. The buildings having been erected already, the deletion must have been intended to modify the grantee's obligations on the subsequent alteration or replacement of the buildings.
4. Various SCs which were clearly spent of effect long before the date of the Modification Letter were retained because they constitute a still relevant historical record of the contractual obligations and the development. The retention of these SCs and the deletion of SC(6)(c) and (d) show clearly the intention that the restrictions contained in SC(6)(c) and (d) are no longer to apply.
5. You accept that SC(3)(a) dealing with the developer's proposal was spent of effect. Yet it was not deleted. You seek to justify its retention by saying that it is relevant to SC(11)(a) which stipulates that the lot shall not be developed or redeveloped except in accordance with the MLP. This is a contrived argument which has no merits :-



- (i) The argument was put forward to support your argument that SC(6)(c) and (d) were deleted because they were spent of effect. You therefore have to find a way to explain why SC(3)(a) (which was also spent of effect) was not deleted.
 - (ii) You attempt to found the explanation on the basis that SC(3)(a) was needed because there was a need to identify the MLP referred to in SC(11)(a).
 - (iii) The problem is that for the purpose of identifying the MLP there was no need to refer to or retain SC(3)(a) at all. This is amply demonstrated by the new SC(6)(a) set out in the First Schedule to the Modification Letter : the MLP was identified in that SC as being the "Master Layout Plans submitted in accordance with paragraph 3(d)(ii) and (iii) of the Tender Notice".
6. It has never been the practice of the Government to charge a premium for approving alterations to a MLP, particularly where the Land Grant itself provides for a mechanism for approval of alterations to the MLP and the alterations do not result in a breach of the development restrictions. SC(3)(a) specifically refers to alterations not to be made "without the consent of the Director" and for a record of any amendments to the proposal to be deposited with the Director. The intention was to put in place an alteration mechanism consistent with the long-standing practice of the Lands Department.
 7. By saying that the power to consent to alterations of the MLP under SC(3)(a) has fallen away, the Director is contriving a case to justify his departure from the Lands Department's long-standing practice that no premium will be charged for changes in the MLP where the changes are consistent with the development restrictions in the Land Grant. Your argument was an attempt to justify the desire of the Director to charge a premium when there is no good justification.
 8. You say that the primary objective of the Modification Letter was to free the developer from the restrictions of the PSPS Scheme and that it is not necessary for the achievement of this objective that the developer should be free to change the sizes or layout of the flats or depart from the MLP. This is, again, a contrived argument and is contradicted by the facts and the plain words of the Modification Letter:-
 - (i) When the parties negotiated the Modification Letter and the premium payable for the modification, Government was fully aware that the design, sizes and layout of the PSPS flats were substantially below private sector standards and that substantial alterations would need to be carried out in order to



make the units marketable in the private sector housing market.

- (ii) For this reason, and to enable the upgrading proposal to be effected, the Modification Letter made the following changes to the Land Grant :-
- (a) The deletion of SC(6)(c) and (d) restricting the number and sizes of the units and the efficiency ratio.
 - (b) The deletion of the Technical Schedule detailing the architectural design, the fixtures and fittings and the building services installations.
 - (c) The addition of a new SC(69) to enable recreational facilities not accountable for gross floor area calculations to be included.
9. The changes to the Land Grant effected by the Modification Letter point irresistibly to the conclusion reached by Mr. Jonathan Sumption Q.C. that the upgrading proposal is permitted as of right. The refusal by the Director to permit the upgrading proposal would amount to a derogation of grant for which the Government is liable to our client for substantial damages.
10. We are unable to see how you can on the one hand accept that the developer is entitled to build recreational facilities in accordance with SC(69) without payment of a premium but, on the other hand, maintain that if the developer were to carry out the upgrading proposal it would have to pay a premium :-
- (i) In either case, the works would result in the buildings not conforming to the original MLP.
 - (ii) In either case, the carrying out of the works would be based on the changes effected by the Modification Letter : in the case of the recreational facilities by the addition of SC(69) permitting recreational facilities and in the case of the upgrading proposal by the deletion of SC(6)(c) and (d) containing restrictions on the number and sizes of units and the efficiency ratio.
 - (iii) The construction of recreational facilities was as much part of the negotiations in the mediation and modification process as the alterations to the number and sizes of the units and, as a matter of fact, the recreational facilities will form part of the upgrading proposal.

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- 11. You suggest that the position taken by our client is consistent with the position of Government simply because the developer requested for modification additional to those provided in the Modification Letter and the additional modification was not agreed by Government. This, with the greatest respect, is irrelevant to the construction of the Land Grant, as modified by the Modification Letter.
- 12. We are unable to follow your argument that the submission in March 2005 of a revised MLP not showing any external or internal walls on the floor plans shows that the position taken by our client is consistent with the position of Government. We would have thought that the submission of such an MLP clearly shows that the developer does not consider that it is restricted in any way in so far as the number and sizes of the units are concerned.

No doubt you would put our observations to your Counsel.

Our client reserves all its rights against the Government, including its rights to damages in respect of the delays of Government in approving the revised MLP or in insisting that our client is not entitled to carry out the upgrading proposal.

Please let us know, within the next 10 days, whether Government still insist on the position so far taken by it on the upgrading proposal.

Yours faithfully,

Johnson Stokes & Master

[SHKProperties/8604/L14/mc]