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Panel on Home Affairs

**Background brief prepared by the Legislative Council Secretariat
for the meeting on 12 December 2008**

Procurement of third party risks insurance by owners' corporations

Purpose

The Administration will seek members' views on the commencement date of the Building Management (Third Party Risks Insurance) Regulation (the Regulation) at the Panel meeting scheduled for 12 December 2008. This paper provides background information on the Regulation, as well as concerns and issues raised by members in their scrutiny of the Regulation.

Background

2. A new provision was introduced to the Building Management Ordinance (Cap. 344) (BMO) vide the Building Management (Amendment) Ordinance 2000 (section 28(1)) which requires all owners' corporations (OCs) to procure and keep in force in relation to the common parts of the building a policy of third party risks insurance. To implement this new provision which has yet come into operation, the Administration tabled the Regulation in the Legislative Council (LegCo) on 11 July 2007 to prescribe the requirements with which a policy must comply and to provide for related matters.

3. At its meeting on 12 October 2007, the House Committee appointed the Subcommittee on Building Management (Third Party Risks Insurance) Regulation (the Subcommittee) to study the Regulation. In response to the views and concerns of the Subcommittee, the Administration made a number of amendments to the Regulation. The amendments to the Regulation proposed by the Administration were passed by LegCo on 7 November 2007. In view of members' concern about the heavy financial burden of the mandatory insurance policy on the owners living in old buildings who might have very low income, the Administration also agreed to defer the commencement date of the Regulation.

Procurement of third party risks insurance

4. The Regulation (with the commencement date to be proposed by the Administration) provides, among other things, for an OC to procure an insurance of not less than \$10 million in respect of any liability that may be incurred in respect of the death or/and the bodily injury of a third party, arising out of one event. It is not a mandatory requirement for the OCs to take out third party risks insurance policy to cover any liability arising out of a breach of duty imposed by law in relation to unauthorised building works (UBWs). Should an OC fail to procure and keep in force in relation to the common parts of the building a policy of third party risks insurance, every member of the management committee shall be guilty of an offence and liable on conviction to a maximum fine of \$50,000.

Deliberations of the Subcommittee

Statutory minimum amount of insurance coverage

5. Members expressed diverse views on the statutory minimum amount of insurance coverage of the mandatory procurement of third party risks insurance by OCs. A member queried whether the proposed amount of \$10 million could offer adequate protection for owners and third parties. Other members were concerned about the possible impact on the financial burden of owners, particularly those in buildings with a small number of units. The Administration informed the Subcommittee that most public liability claims previously received were small to medium size.

Financial burden of owners to comply with the mandatory requirement

6. Some members expressed concern that the insurance premium would pose a heavy financial burden on owners of old buildings who might have very low income, and they might have to dissolve their OCs if the level of insurance premium was beyond their affordability. The Hong Kong Federation of Insurers was of the view that the change in the insurance premium might not be directly proportionate to the change in the insured amount, and might vary with different insurance companies and the conditions of the buildings. The Administration advised that out of the 15 000 buildings with OCs, 12% of OCs had not procured third party risks insurance. In this connection, the Urban Renewal Authority and the Hong Kong Housing Society had both introduced an incentive scheme whereby OCs which had completed the renovation works in the common parts of the buildings would be reimbursed for the third party risks insurance premium of up to \$6,000 per annum for three consecutive years.

Insurance coverage of UBWs

7. Some members expressed disappointment that UBWs would not be covered under the mandatory third party risks insurance under the Regulation, given that the problem of UBWs was prevalent and unlikely to be resolved in the near future. Such members considered that inclusion of UBWs in the insurance coverage would better protect third parties. Moreover, the increase in the premium due to such inclusion might encourage owners to consider demolishing UBWs. Some members, however, supported the proposal for not including UBWs, a view shared by the insurance industry. The Administration explained that to avoid high insurance premium for the poorly maintained buildings and to render it more possible for an OC to procure third party risks insurance, no mandatory requirement for coverage of liabilities arising out of UBWs was proposed under the Regulation. The Administration also advised that OCs should not be required to procure a third party risks insurance policy which covered liabilities relating to UBWs as otherwise it would imply that the Government condoned the existence of UBWs.

Obligation to procure insurance

8. Members noted that if OCs failed to comply with the mandatory requirement of procuring third party risks insurance, every member of the management committee (MC) would be guilty of an offence and liable on conviction to a fine at level 5, unless the MC member could prove that he had exercised all such due diligence to prevent the contravention of the mandatory requirement. A member was concerned that an MC might claim to have exercised due diligence to comply with such a requirement once the MC had put forward the procurement proposal to the meeting of the OC even though the motion was voted down by the OC. The Administration advised that the courts would determine whether reasonable diligence had been exercised, based on the facts of each case. The member suggested that the Administration should consider, for the next phase of implementation, the imposition of a penalty on an OC in addition to the MC concerned, for failure to comply with the mandatory requirement.

Other related issues

Anti-avoidance provision

9. Section 6(3) of the proposed Regulation provided that, if the insurance policy purported to restrict the insurance of an OC by reference to the condition or maintenance of the building, the use of the building and the existence of a statutory instrument in relation to the building, such restrictions would be of no effect, unless the policy also required the OC to exercise reasonable diligence and that the death or bodily injury that gave rise to the liability was directly caused by the OC's contravention of that requirement. Members were concerned that an insurance company might easily refuse to pay compensation

to third parties under the mandatory insurance policy of an OC on the ground that the OC had not exercised reasonable diligence to keep the building concerned in good condition and maintenance, or to comply with any statutory instrument in relation to that building, etc. In the light of members' strong view that the phrase "to exercise reasonable diligence" would lead to numerous legal disputes and delays for third parties to receive judgment compensation, the Administration had repealed section 6(3).

Non-disclosure of a material fact

10. Some members expressed concern that an insurance company might refuse to pay compensation to third parties under the mandatory insurance policy of an OC on the grounds that the OC had failed to disclose a material fact. They considered that an OC might not know about the existence of a UBW and hence make a false statement in procuring an insurance policy to the insurance company. The Administration explained that the insurance company had the burden to successfully obtain a declaration from the court before it could avoid the policy. It was therefore for the court to decide whether there was a non-disclosure or misrepresentation of a material fact to the extent that it warranted the avoidance of the insurance policy by the insurance company.

Notice of insurance

11. Some members considered that the failure to display the notice of insurance in respect of the new mandatory requirement to procure third party risks insurance should not lead to a penalty at level 2 (\$5,000) under section 5(7), which was too severe. In response to the members' views, the Administration had lowered the level of the fine to level 1 (\$2,000).

Latest development

12. The Administration will report to the Panel the progress of procurement of third party risks insurance by OCs and seek members' views on the commencement date of the Regulation at the Panel meeting on 12 December 2008.

Relevant papers

13. A list of relevant papers with their hyperlinks at the LegCo website is in the **Appendix**.

Council Business Division 2
Legislative Council Secretariat
9 December 2008

Panel on Home Affairs

Relevant documents on procurement of third party risks insurance
by owners' corporations

Date of meeting	Meeting	Motion/Paper/Minutes	LC Paper No.
5.10.2007	House Committee	Legal Service Division Report on subsidiary legislation tabled in the Legislative Council on 11 July 2007	LS121/06-07 http://www.legco.gov.hk/yr06-07/english/hc/papers/hc1005ls-121-e.pdf
12.10.2007	Subcommittee on Building Management (Third Party Risks Insurance) Regulation	Legislative Council Brief on Building Management (Third Party Risks Insurance) Regulation issued by the Home Affairs Department on 5 July 2007	File Ref: HAD/HQ/CR/20/3/1(C) http://www.legco.gov.hk/yr06-07/english/subleg/brief/146_brf.pdf
		Background brief prepared by the Legislative Council Secretariat	CB(2)26/07-08(02) http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/papers/sc611012cb2-26-2-e.pdf
		Minutes of meeting	CB(2)269/07-08 http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/minutes/sc611012.pdf
16.10.2007		Minutes of meeting	CB(2)298/07-08 http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/minutes/sc611016.pdf
		Administration's response to issues raised at the Subcommittee's meeting on 16 October 2007	CB(2)127/07-08(01) http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/papers/sc611023cb2-127-1-e.pdf
23.10.2007		Minutes of meeting	CB(2)364/07-08 http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/minutes/sc611023.pdf

Date of meeting	Meeting	Motion/Paper/Minutes	LC Paper No.
29.10.2007		Minutes of meeting	CB(2)572/07-08 http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/minutes/sc611029.pdf
		Administration's response to issues raised by the Subcommittee at its meeting on 29 October 2007	CB(2)240/07-08(01) http://www.legco.gov.hk/yr06-07/english/hc/sub_leg/sc61/papers/sc611029cb2-240-1-e.pdf
2.11.2007	House Committee	Report of the Subcommittee on Building Management (Third Party Risks Insurance) Regulation to the House Committee	CB(2)207/07-08 http://www.legco.gov.hk/yr07-08/english/hc/papers/hc1102cb2-207-e.pdf

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