

**For discussion
on 23 December 2010**

**LEGISLATIVE COUNCIL
PANEL ON DEVELOPMENT
AND
PANEL ON ADMINISTRATION OF JUSTICE AND LEGAL SERVICES**

**JOINT SUBCOMMITTEE ON
AMENDMENTS TO LAND TITLES ORDINANCE**

Amendments to the Land Titles Ordinance

PURPOSE

This paper updates Members on the following issues relating to the preparation of the amendments to the Land Titles Ordinance (Cap. 585) (LTO) : (i) rectification and indemnity arrangements; and (ii) determination of land boundaries.

RECTIFICATION AND INDEMNITY ARRANGEMENTS

Background

2. As reported at the Joint Subcommittee meeting held on 28 June 2010 (LC paper No. CB(1)2352/09-10(01)), the Law Society of Hong Kong (the Law Society) has indicated its opposition against the mandatory rectification rule under section 82(3) of the LTO. According to the Law Society, since an innocent former owner will, under the LTO, be restored as owner if (i) he lost his title by or as a result of fraud and (ii) the relevant entry in the Title Register was procured by a void instrument or a false entry, this might encourage a purchaser to go behind the Title Register to investigate previous transactions in order to obtain greater assurance that his title would not be at risk. This would undermine the certainty of title and would work against the objective of simplifying conveyancing procedures. The Law Society has advocated the adoption of the principle of immediate indefeasibility of title instead. They have further suggested that the cap on indemnity (currently proposed at \$30 million) and the bar on indemnity for pre-conversion fraud be removed. The Law Society's latest views disrupt the difficult consensus reached in the LTO,

and have drawn mixed reaction from other stakeholders.

Follow-up with the Law Society

3. To take the matter forward, we have invited the Law Society to provide further information on the additional conveyancing procedures and steps envisaged to be undertaken by solicitors acting for purchasers if the mandatory rectification rule is adopted, and how the procedures and steps would assist in identifying fraud. In the light of the divergent views held by stakeholders on the Law Society's latest stance, we have also invited the Law Society to reconsider the matter.

4. On the issue of fraud identification, the Law Society considers that the scope of application of the mandatory rectification rule is not entirely clear since "fraud" is only defined in the LTO to include dishonesty and forgery and the Court has not laid down any exhaustive definition of the term. Instead of considering in every case whether there is fraud and whether the document involved is a void instrument, solicitors would adopt a prudent approach by way of checking old title documents and raising requisitions to find out if any fraud and/or void or false entry in the Title Register is involved. As such, solicitors would in essence be doing more or less the same things as they have been doing now.

5. As regards the rectification and indemnity arrangements under the LTO, the Law Society remains strongly opposed to the mandatory rectification rule and continues to call for the adoption of the immediate indefeasibility principle. As an alternative, however, they would be prepared to accept limited discretion by the Court to rectify in favour of an innocent former owner, by either retaining sections 82(1) and (2) of the LTO, or following the model adopted in the United Kingdom's Land Registration Act 2002. Likewise, the Law Society maintains that the cap on indemnity and the bar on indemnity for pre-conversion fraud should be uplifted. They consider that the risk exposure of the Land Titles Indemnity Fund (LTIF) to claims could be limited by adopting suitable fraud prevention measures (e.g. requiring presentation of the title certificate before registering a change of ownership, conducting identity check by estate agents and solicitors before purchase of property, etc.). Nevertheless, the Law Society would be prepared to accept the cap provided it is reviewed regularly so as to cover the majority of properties in Hong Kong.

6. In view of the strong objection of the Heung Yee Kuk (HYK) against changes to the mandatory rectification rule, the Law Society has proposed that an option be given to the HYK to consider whether to have lands in the New Territories held by indigenous villagers excluded from the title registration system at the initial stage of the LTO's implementation. A mechanism should be put in place whereby the owners of those lands could opt into the new system at a later stage upon title being proved to the Land Registry at their own expenses.

The Administration's Considerations

7. We have considered the views and suggestions expressed by the Law Society, as well as the implications of abolishing the mandatory rectification rule. We note that when the Land Titles Bill was introduced in 2002, it was then proposed that the Court should be given the discretion to rectify the Title Register in favour of an innocent former owner if the Court considered that it would be unjust not to do so. The arrangement was similar to the United Kingdom model under the Land Registration Act 2002 as recently suggested by the Law Society. In the course of the Bills Committee's examination, however, there were concerns from stakeholders that an indefeasible title for a purchaser, together with a cap on indemnity payable to an innocent former owner in the case of fraud, might amount to deprivation of property if the Court did not rectify in favour of the former owner. The mandatory rectification rule was eventually introduced at the final stage of the Bill's deliberation in 2004 in order to address the concerns of stakeholders.

8. Since there would not be any title checking under the LTO's automatic conversion mechanism, removing the cap on indemnity and the bar on indemnity for pre-conversion fraud could subject the LTIF to tremendous financial risks and could result in substantial increase in the levy to be charged. In this connection, we note that *none* of the major common law jurisdictions¹ that operate a title registration system with indefeasible title for purchasers and indemnity for fraud would follow the arrangement of converting historical land registers to the title registration system automatically without appropriate measures to mitigate the associated risks. We also note that fraud prevention measures (such as the requirement to present the title certificate of the seller

¹ Examples include England and Wales, Scotland, Ontario and New Zealand. Singapore does not provide indemnity payment for fraud cases.

before registering a transfer under section 29 of the LTO) can only be applied to *new* transactions under the title registration system. Such measures will not relieve the LTIF from potential liabilities arising from pre-conversion fraud.

9. In view of the inter-relationship between conversion, rectification and indemnity, any modifications to these core elements of the LTO would have to be considered in a holistic manner. The exclusion of lands in the New Territories held by indigenous villagers would not absolve us from the need to reconsider all the core elements of the LTO if the mandatory rectification rule were to be modified or abolished. It would also complicate the land registration regime by creating three classes of lands (new lands, existing lands eligible for automatic conversion and existing lands in the New Territories held by indigenous villagers to be excluded from automatic conversion) governed by different sets of legislation, which might cause considerable confusion to the public. In addition, we would need convincing justifications for partial application of a policy, and there could be legal implications as well.

Discussion with Stakeholders

10. A meeting of the Land Titles Ordinance Steering Committee (LTOSC) chaired by the Land Registrar was held on 16 December 2010 for stakeholders to consider the inter-relationship among the three core elements of the LTO, and the potential risks and liabilities to the LTIF if the mandatory rectification rule were to be removed. The views and suggestions put forward by the Law Society in its letter of 10 December 2010 (LC Paper No. CB(1)790/10-11) were also considered. At the meeting, LTOSC Members took note of the following points -

- (a) while immediate indefeasibility was commonly adopted in other jurisdictions, none of them followed the automatic conversion mechanism under the LTO. As such, the question of whether to replace the mandatory rectification rule with immediate indefeasibility could not be considered alone. All the three core elements of the LTO, i.e. the conversion, rectification and indemnity arrangements had to be considered together;
- (b) the Administration had therefore invited the Law Society to reconsider its position. In this regard, the Administration noted the Law Society's

concern on title checking that might arise out of the mandatory rectification rule, and was prepared to discuss with the Law Society and other stakeholders on any proposal that the Law Society might have regarding the repositioning of the three core elements under the LTO, so as to address the concerns of stakeholders and to balance the interests of the general public;

- (c) an actuarial consultant was engaged by the Land Registry in 2006 to assess the risks that would be borne by the LTIF. Based on the conversion, rectification and indemnity provisions under the LTO, the consultant recommended a levy rate of 0.017% on property value for the LTIF. The consultant further recommended the Administration to review the assumptions adopted in the study based on the latest available data closer to the implementation of the LTO;
- (d) if the mandatory rectification rule was to be removed, it might also be necessary to remove the cap on indemnity and the bar on indemnity for pre-conversion fraud. As advised by the actuarial consultant, however, the probability of insolvency of the LTIF would increase significantly if the cap on indemnity was removed, rendering it susceptible to bankruptcy if more high-valued claims were payable. Furthermore, it would not be possible to assess or contain the risks associated with pre-conversion fraud;
- (e) the experience of other jurisdictions indicated that there was a marked increase in the number and magnitude of property fraud in recent years. There was also evidence of syndicates involved, targeting multiple properties at a time; and
- (f) in view of the recommendations of the actuarial study and the rising trend of property fraud, it would be necessary to reassess the risks of the LTIF and its levy rate, having regard to any amendments made to the relevant provisions of the LTO.

11. The views offered by Members of the LTOSC were as follows –

- (a) the Law Society reiterated the views as set out in their submission dated 10 December 2010. The Law Society indicated that they appreciated

the Administration's concern on risks and liabilities to the LTIF and the implications on ordinary home buyers if the cap on indemnity and the bar on pre-conversion fraud were to be removed. On the other hand, they considered that parties to property transactions had already been bearing considerable risks and costs under the existing deed registration system, and the title registration system with indemnity payment would represent a significant improvement. The benefits of the new system should outweigh the associated costs;

- (b) the HYK remained strongly opposed to any changes to the mandatory rectification rule. They pointed out that as a statutory advisory body on New Territories affairs, the HYK's purview was not confined to lands held by indigenous villagers. They were concerned about the impact of the removal of the mandatory rectification rule on *all* New Territories lands and properties. Under common law, the former owner would recover the property in case of fraud. An innocent former owner in the New Territories might be worse off under the new system if the mandatory rectification rule were to be removed. This was particularly so with the cap on indemnity. They did not agree with the Law Society's proposal to exclude lands in the New Territories held by indigenous villagers from the application of the LTO at its initial stage of operation, as it would vastly complicate the land registration system in Hong Kong. In the event that the mandatory rectification rule were to be abolished, however, the cap should also be removed so that an innocent former owner could be fully compensated; and
- (c) the Real Estate Developers Association of Hong Kong reiterated its support for a system of indefeasible titles without any mandatory rectification rule or cap on indemnity. If the cap was to be preserved, however, the mandatory rectification rule should be maintained in order to preserve the interests of the innocent former owner.

12. We will continue to maintain close liaison with stakeholders and explore viable options to take forward the land titles exercise.

DETERMINATION OF LAND BOUNDARIES

13. The determination of land boundaries has been discussed by the Joint Subcommittee at its previous meetings. We have been carefully examining Members' concerns which involve complex legal and policy implications, as well as the views expressed by stakeholders at the Joint Subcommittee held on 29 April 2010. The Government had further consulted the relevant stakeholders at the Cadastral Survey Consultative Committee, in August 2010. Their views remained diverse.

14. To avoid complicating matters, we consider it appropriate to examine the proposal on determination of land boundaries as a separate exercise from the amendment of the LTO. Under this approach, the momentum for taking forward both exercises would be sustained.

ADVICE SOUGHT

15. Members are invited to comment on the contents of the paper.

Development Bureau
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