

STATUTE LAW (MISCELLANEOUS PROVISIONS) BILL 1999

The Law Society's Property Committee has considered the proposed amendments to the *Conveyancing and Property Ordinance* (the "CPO") via the *Statute Law (Miscellaneous Provisions) Bill 1999* (the "Bill") and has the following comments and submissions:-

A PURPOSE

The primary aim of the proposed amendments is to provide the court with discretion to declare that a property is free of an encumbrance in the event that the mortgagee or the mortgage documents cannot be found.

B. GENERAL SITUATION IN HONG KONG

1. The type of dilemma which the proposed amendments are designed to counteract can be illustrated from the facts of *Fung Kam Cheung & ors v. Kwok Yiu Wing & ors* [1991] 1 HKC 321. In this case, a landowner sought a declaration from the court that a mortgage dated August 1939, where the last mortgage payment was payable in 1942, was discharged and/or null and void. Neither the mortgagee nor the mortgage could be found. Godfrey J. (as he then was) stated that he could not give such a declaration as there was no Hong Kong equivalent of S. 50 of the *English Law of Property Act* (the "LPA"). S. 50 of the LPA entitled the court to declare land to be free from an encumbrance on payment of sufficient money into court to meet the encumbrance, together with interest and costs.
2. It was noted in that case that the only method of dealing with such a "dead" mortgage in Hong Kong, which, only technically acted as a blot to title, was to take proceedings against the mortgagee and by seeking a declaration that the mortgage is no longer subsisting or capable of taking effect. One way of obtaining such a declaration would be to show that the mortgagee was barred by time limitation under the *Limitation Ordinance* (the "LO").
3. This exact type of situation is not novel in Hong Kong and has arisen in three other cases:
 - (a) *Tang Kun Nin Tony v. Tang Chun Chack* (MP 761/91, unreported) [1992] HKLY 588
 - (b) *Castle City Ltd. v. Choi Yue Development Ltd.* [1995] 2 HKC 593
 - (c). *Broada Ltd. & Another v. Chow Cheuk Yin* [1997] 3 HKC 168In each of these cases, the mortgagee was barred from taking action to enforce the mortgage by virtue of S. 7 and S. 19 of the LO. Although the court could not make an order that the mortgage was discharged and/or null and void,

nevertheless it could make an order that the mortgage was no longer subsisting or capable of taking effect.

4. Whether S. 7 and S. 19 of the LO can be readily invoked to assist the mortgagor in this regard is questionable as there are conflicting decisions as is examined in Part E of this paper. However, assuming that the section can be relied on, the existing approach has shortcomings. A Declaration that the mortgage is no longer subsisting or capable of taking effect does not absolutely clear the blot on the title to the property. As pointed out by the then Godfrey J. in the *Fung Kam Cheung* case:

"It must be appreciated that ... a declaration that the mortgage is no longer subsisting or capable of taking effect operated only as between the vendors and purchasers and does not bind the mortgagee. (Emphasis added) But I cannot see that that gives rise to any real difficulty. I would hope that no subsequent purchaser or lender will, in the future, seek to raise any objection to the title here based on the existence of the mortgage."

Moreover, the S. 7 and S. 19 relief may only assist a mortgagor in cases where the repayment date is specified in the relevant mortgage. Where no repayment date is specified, it is unclear when the right to receive the money accrued and thus the limitation period starts to run.

5. Clearly then, this present method of obtaining a declaration is inadequate as a remedy to cover all cases and as a definitive measure to erase all doubts as to the validity of the title which the purchaser is acquiring. Also, given the fact that this is a relatively common situation in Hong Kong with at least four adjudicated cases, it seems that it is right and proper that the situation be rectified so as to enable even the most theoretical blot on title to be removed.

C. SITUATIONS INVOLVING OLD MORTGAGES IN THE NEW TERRITORIES

1. In drafting the legislative amendments, one has to bear in mind the special features of old mortgages affecting land in the New Territories. Unlike conventional mortgages, these old mortgages have two peculiar features:
 - (a) no interest on the principal mortgage loan is provided;
 - (b) as a corollary of (a) above, the mortgagee is *in possession* of the mortgaged property during the mortgage period, so that the mortgagee enjoys the rents and profits arising from the land during the mortgage period
2. These special features can be observed from the facts of the *Fung Kam Cheung* case (see paragraph 2 of the Judgment) as well as a copy Schedule to a Block

Government Lease containing several old mortgages attached to this memorandum.

3. S. 26 of the *New Territories Ordinance* (since repealed) owes its origin to S. 38 of the *New Territories Regulation Ordinance* (Ordinance No. 34 of 1910). Such section appears to codify the customary law of mortgage and allows mortgagees under a mortgage (Chinese Customary Mortgage) executed in Form C to enter into possession of the mortgaged land until redemption.
4. Under S. 14 of the LO, a landowner's right of redemption is extinguished after the mortgagee has been in possession of the mortgaged land for a period of 12 years or more. In such circumstances, the mortgagee will become the owner of the land.
5. Care should thus be taken to ensure that the proposed legislative amendments will not, when enacted, prejudice the entitlement of a mortgagee, its successors in title and assigns under S. 14 of the LO.

D. LEGISLATIONS IN OTHER JURISDICTIONS

1. The proposed legislation gives Hong Kong courts the discretion to order that various encumbrances on the land can be removed by means of a payment into court. It is very simple and uncomplicated, unlike the provisions in other jurisdictions such as England and Australia.
2. The following are comments on the proposed legislation in Hong Kong in light of the precedents from the other jurisdictions:

The UK Position

Amount to be Paid into Court

- a. S. 50 of the LPA is somewhat more complex than the provisions proposed for Hong Kong. As to the definition for "*encumbrance*" under the Bill, it is exactly the same as that given in S. 205(1) of the LPA save for a different spelling. S. 50 of LPA requires the applicant to pay into court *a sum to account for future contingencies* which is not to exceed one-tenth part of the amount originally paid in, and *the court has discretion to order an even greater sum to be paid in*.
- b. Under the Bill, the amount to be paid in is stated simply as "*an amount sufficient to meet the encumbrance and any interest due thereon*". This does not seem to be a mere linguistic variation.
- c. S. 50 of LPA does not limit the court's discretion on the amount to be paid in to just the capital, or capital and interest outstanding, but the Court can require such sum as when invested in government securities would be adequate to meet the

capital charge and interest thereon. The English provision allow the court to require a greater sum to be paid while the Hong Kong provision allows for the bare minimum.

Discretion of the court to declare other affected land to be freed from the encumbrance

- d. One other significant variation between S. 50 of LPA and the Bill is that under the LPA, the court has the added power to *declare all other land, affected by the encumbrance, to be freed from the encumbrance*. The legislators and law draftsmen in Hong Kong have not seen fit to give the court such a wide discretion for whatever reason.

Overall Effect of Differences between the UK and HK Provisions

- e. The overall effect of these differences is that the discretion granted to the Hong Kong courts is framed in narrower terms than under the corresponding legislation in the UK. It is certainly in the vendor's interest, when trying to clear the land of such encumbrances, that the discretion of the courts be framed in the narrowest terms possible, and therefore, the Hong Kong legislation tends to favour the applicant applying to discharge the encumbrance.

The Australian Position

Circumstances entitling the Court to Exercise the Statutory Discretion

- f. The Australian provision is considerably more complex than both the UK and the Hong Kong provisions. S. 98 of the *New South Wales Conveyancing Act* limits the "*facilitation of redemption in case of absent or unknown mortgagees*" to situations, in which the mortgagee is out of the jurisdiction, cannot be found or if it is uncertain as to who he is.

Costs of the Application

- g. S. 98 provides that if the court makes a determination as to whether monies are left owing under the mortgage, it is the mortgagee, to the extent set out in the provisions, who is liable to pay the costs of the applicant incurred in obtaining the determination. The applicant can then deduct the cost of the application from the amount that he is required to pay to discharge the mortgage. Obviously, this provision has the effect of lightening the load of the applicant and it seems highly sensible that the mortgagee should bear the costs of the application rather than saddling the applicant with excessive expenses. In Hong Kong, presumably it is the applicant who would bear the costs of the application, although the legislation is silent on this point.

Effect of the Court's Determination

- h. One weak point in the operation of S. 98 is that any determination is not conclusive as between the mortgagee and the mortgagor and "*that the*

determination does not prejudice any right conferred by the mortgage for the recovery of an amount due thereunder." The certificate given by the court under a successful application under S. 98 "*operates as a discharge of the land from the amount due under the mortgage, and as a deed of conveyance*".

E THE DECISION OF COMMON LUCK INVESTMENT LTD. v. CHEUNG KAM CHUEN FACV No. 22 OF 1998

1. While deliberating on the existing approach of relying on the provisions of the LO to seek a declaration that the mortgage is no longer subsisting or capable of taking effect where either the mortgagee, the mortgage document or both cannot be located, members of the Property Committee noted that the judicial interpretation of the provisions of LO concerning the relationships between parties to a mortgage is confused or unclear. Whereas mortgagors in cases mentioned in paragraph B3 could successfully rely on S. 7 and S. 19 of LO to bar the claims of the mortgagees, the Court of Final Appeal in a recent decision in the case of Common Luck Investment Ltd. v. Cheung Kam Chuen FACV No. 22 of 1998 adopted a different approach to interpret the Mortgagor's right under the LO and came to a totally different conclusion.
2. Briefly, the Mortgagor in the CFA case defaulted in repayment of the mortgage loan in 1965. Canton Trust and Commercial Bank Limited, the Mortgagee, was then in liquidation and had done nothing to enforce the terms of the mortgage. The property was sold by the Official Receiver as liquidator of the Mortgagee to a purchaser in 1970s. In 1991, the Government resumed the land. Both the purchaser and the Mortgagor claimed to be entitled to the compensation money. The Mortgagor's case was that as he had defaulted in repayment in 1965, a right to recover possession had accrued to the then Mortgagee and he was thus in adverse possession starting 1965. By the time the resumption took place in 1991, the right of action of the Mortgagee and hence the purchaser who was claiming through the Mortgagee was barred under S. 7 and S. 19 of the LO.
3. The Mortgagor won both in the Court of First Instance and in the Court of Appeal. However, on appeal, the CFA allowed the appeal in favour of the purchaser. The CFA took the view that until foreclosure by order of the court, or sale by the mortgagee in realizing his security, the Mortgagor in default has an equitable right to redeem. The mere act of default does not convert the Mortgagor into a trespasser. The Mortgagor's right of possession flows from the mortgage itself and he remains on the property upon default with an implied licence. He cannot be regarded as "*a squatter of his own home*".
4. The Committee is concerned that if the CFA decision is right and the defaulting Mortgagor in possession is to be regarded as occupying the property as a licensee so long as the mortgagee has done nothing to enforce its right, the mortgagee's right to take possession vis-a-vis the mortgagor can never be statute-barred under the provisions of the LO. On the other hand, if the mortgagee in possession is

entitled to rely on S. 14 of the LO to claim that the Mortgagor's equity right of redemption is statute-barred, this will lead to an unsatisfactory position when the mortgagor will always be the loser in all circumstances.

5. The Committee finds it difficult to reconcile the CFA decision with the other decisions and with the provisions of the LO. Members believe that this is a good time to raise the concerns with the Administration so that the implications of the CFA decision on the provisions of the LO could be carefully reviewed.

F. CONCLUSION

1. **The proposed amendments to the CPO are to be welcomed in Hong Kong** as they represent a significant step to alleviate the hardship of proving a perfect title in cases of old, outdated, meaningless mortgages which cannot be found, yet, which remain as a blot on the title. In the past, the courts of Hong Kong have been prevented from declaring such mortgages to be null and void with the result that aggrieved persons have had to resort to other courses of action such as an action under the LO. One extreme example of this was evidenced with a headline in the *South China Morning Post* to the effect that "*Law blocks bid to pay back \$210 mortgage*". The simple reality is that there are many mortgages in Hong Kong which were paid off and forgotten about without the proper steps being taken to discharge them. This new legislation enables the courts to "*take the broom and dust away these fossilized mortgages which are cluttering up the closets in Hong Kong*".
2. The Property Committee has the benefits of considering the recommendations put forward by the Hong Kong Conveyancing and Property Law Association Limited. The Committee supports the view that relief should be extended to situations involving "*other than*" a sale and exchange of land.
3. As noted above, any prejudicial effect the proposed Legislation would have on the right of a mortgagee over New Territories land under S. 14 of LO should be avoided. **It is proposed that a new Subsection (4) be added to the end of the proposed S. 12A of the CPO as follows:**

"(4) Nothing in this Section shall prejudice the right of the encumbrancer under Section 14 of the Limitation Ordinance, (Cap. 347)."

To furnish an opportunity for the encumbrancer to enforce or assert its right under S. 14 of the LO, **it is also suggested that the requirement of notice under Subsection (2) of S. 12A be at the discretion of the court in the manner as provided in S. 50(2) of the LPA.**
4. The provisions of the new CPO legislation are, however, excessively vague on whom the burden of the costs of the application should rest. **The Australian**

legislation is superior in allowing the costs of the application to be deducted from the amount to be paid into court. This is an excellent initiative that should be followed in Hong Kong.

5. The new provisions are to be lauded for their attempt to mitigate the hardships caused to applicants by allowing the court only to order payment of the bare minimum.
6. This legislation is long overdue and it is to be hoped that it will be enacted with the suggested modifications sooner rather than later.
7. The Administration is urged to study the implications of the CFA decision on the provisions of the LO and make amendments to the LO to clarify the legislative intent as appropriate.

**The Property Committee
The Law Society of Hong Kong
2 March 2000**