Bills Committee on Building Management (Amendment) Bill 2005

Apportionment of Management Fees

1. At the meeting of the Bills Committee on 20 June 2006[1], Members discussed, amongst other issues, the proposal to re-distribute management fees among owners in accordance with their respective undivided shares. Below are the responses of the Administration to the issue.

Background

2. The apportionment of management fees among owners is usually set out in the deed of mutual covenant (DMC) of the building. A DMC is a private contractual agreement among all the co-owners, the manager, and also the developer of a building. The Government is not a party to this private contract. As in other private contracts, any terms in a DMC could not be amended unilaterally without the consent of the parties to the contract. A DMC also sets out the rights and responsibilities of the owners, the developer and the building manager. Any amendment to a DMC will inevitably affect the rights and responsibilities of these parties.

3. The Government is aware that there are problems associated with some old DMCs, which were mostly drafted by the developer of the building without participation of the general owners. The Government had, therefore, since 1986 introduced a DMC clause in the land leases which requires all DMCs to be approved by the Legal Advisory and Conveyancing Office (LACO) of the Lands Department and that all DMCs have to be drawn up in line with the Guidelines for DMCs issued by LACO. In addition, some mandatory terms have been introduced into the Building Management Ordinance (BMO) (Cap.344) that must be impliedly incorporated into all DMCs (namely Part VIA and Schedule 7) since 1993.

Re-allocation of Management Fees

4. Members of the Bills Committee were concerned that some old DMCs have allocated management fees to owners on an unfair basis.

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[1] LC Paper No. CB(2)342/05-06(01) – The Administration's Response to the Views of the Deputations Attending the Meeting on 25 June 2005

5. To rectify the problem, LACO had required that both the undivided and management shares of a building should be allocated on gross floor area (GFA) basis. The relevant guideline[2] is set out below –

> "(a) Subject to sub-paragraphs (c) and (d) below, the allocation of undivided shares and management shares will be calculated by reference to the gross floor area of a unit in proportion to the gross floor area of the development as certified by the Authorized Person. For the purpose of this Guideline, gross floor area includes any gross floor area which has been exempted under the conditions of the land grant or the Buildings Ordinance. If any other basis is proposed for the allocation of undivided shares and management shares, full justification for the proposal must be produced.
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> (b) In the allocation of undivided shares and management shares, LACO will have to be satisfied that the use of any basis other than gross floor area will not result in disproportionate management charges being imposed on or voting rights being granted to e.g. the owners of any specific parts of a development or the prevention or hindrance of incorporation of an Owners' Corporation.
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> (c) The allocation of undivided shares and management shares to parking spaces, gardens, flat roofs, balconies, utility platforms and other similar spaces attached to a unit may be made on a nominal basis/lesser ratio than a strict gross floor area basis, provided that each type of these spaces is calculated on the same basis.
>
> (d) The undivided shares to be allocated to the common areas must be made on a nominal basis."

6. Furthermore, the Guidelines for DMCs also govern the management accounts for different parts of a building. The relevant guideline[3] is set out below –

> "For a development comprising residential units, non-residential units, parking spaces or any combination of them, the manager

[2] Guideline No.6 of Circular Memorandum No.56 of the Legal Advisory and Conveyancing Office
[3] Guideline No.24 of Circular Memorandum No.56 of the Legal Advisory and Conveyancing Office

must keep separate management accounts and budgets for each part. The owners of the residential units, non-residential units and parking spaces will only be liable to contribute to the management and maintenance costs of their respective parts (e.g. owners of residential units will only be responsible for residential common areas). All owners will be liable for development common areas."

7. The Guidelines for DMCs are applicable only to buildings constructed after the issuance of the Guidelines. As regards existing buildings, whilst unlike undivided shares, management shares do not signify ownership, any adjustments to the management fee level will alter the proportion and extent of the owners' obligations and liabilities to contribute towards the management expenses of the development as a whole. Such re-distribution will likely benefit one group of owners at the expense of another group of owners by subjecting the latter group to obligations which are more onerous than those provided for under the existing DMC. This could be regarded as having impact on the property rights of owners.

Legal Advice

8. We have sought advice from the Department of Justice on the issue. The proposal to re-allocate management fees among owners for existing buildings by a method that is not specified in the DMC will have substantial impact on the rights of the owners. The issue is primarily a private monetary issue between the owners and does not appear to serve any significant public interest. Whilst the proposal will not extinguish all the owners' legal rights in respect of their shares, it is likely to be regarded as an "interference"/"control" of the property which has to satisfy the "fair balance" test (i.e. whether it strikes a fair balance between the demands of the general interest of the community and the requirement of the protection of the owners' right). The proposal may raise strong objection on the ground of property right protection under Articles 6 and 105 of the Baisc Law.

Discussion at the Ad Hoc Group under the Legislative Council

9. Members would like to re-visit the discussion of the subject during the scrutiny of the Multi-storey Buildings (Owners Incorporation) (Amendment) Bill 1992 by the Ad Hoc Group formed under the Legislative Council.

10. The Government set up an inter-departmental working group in 1987 to examine ways and means to remedy unfair provisions in DMCs. The working group proposed to introduce legislation containing a code of fair clauses based on the Guidelines for DMCs issued by the then Registrar General (i.e. LACO) which should apply across the board to all DMCs. The recommendations of the working group were published in the form of a consultative paper in February 1989 and all the views were subsequently examined by the Advisory Committee on Private Building Management.

11. Among the recommendations of the Advisory Committee on Private Building Management was that no owner may be called upon to pay more than his share of the management expenses either in proportion to the number of undivided shares vested in him or in accordance with the total area of his unit and no developer may evade his responsibility to pay all management expenses for those units unsold and both the owners and the developers should bear an appropriate proportion of the costs of management expenses in relation to the common parts.

12. In May 1991, the Government published the Multi-storey Buildings (Owners Incorporation) (Amendment) Bill 1991 as a White Bill for public comments. In the White Bill, there were two clauses which were relevant to the subject of this paper. The first one provided that the owner of any unsold share in the building is liable to pay the relevant management expenses as if he had purchased the share subject to the DMC[4]. The second one provided a formula for determining the maximum amount that an owner can be liable to pay as his share of the management expenses. The formula was based upon the proportion of shares in the building vested in the owner or the proportion of floor area vested in the owner, whichever is the greater. It was clearly stated in the White Bill that this provision would <u>not</u> apply to existing DMCs.

13. In relation to existing DMCs, the considerations then were that any proposal would upset the present arrangements for collecting management expenses. It then begged the question of what should be done with DMCs that have allocated management expenses in accordance with other formulae. If some but not all owners are required by an existing DMC to pay more than their fair share of management expenses, should their liability be limited according to the formula provided in the law? The effect of doing this would be either to create a shortfall in the contribution to management expenses or to increase the share of other

[4] This is now section 34G of the BMO.

owners. A shortfall did not seem to be a practical proposition. An increase in the shares paid by other owners would be difficult to quantify and be questionable from a legal policy point of view, since it would amount to an alteration of a fundamental obligation attaching to an existing right of property. It was also most important that the shares of all owners in any particular building were determined once and for all.

14. The consultation period for the White Bill ended in August 1991. Among the comments received, many considered there would be practical difficulties in adopting the formula for apportionment of management fees as provided in the White Bill. This was due to the peculiar circumstances of the different developments, particularly mixed commercial/residential developments. The clause was therefore taken out from the Multi-storey Buildings (Owners Incorporation) (Amendment) Bill 1992 which was subsequently introduced into the Legislative Council in July 1992. It was decided that the apportionment of management expenses should be determined by reference to the Guidelines for DMCs issued and regularly reviewed by LACO.

15. An Ad Hoc Group was formed under the Legislative Council to study the 1992 Bill. We are unable to locate any records showing detailed discussion about the apportionment of management expenses at the Ad Hoc Group. The Bill was passed by the Legislative Council in May 1993.

Administration's Views

16. We are aware that the problems of some old DMCs have caused difficulties in the owners' efforts in managing and maintaining their buildings. The Government generally does not have objection in principle to the introduction of a mechanism for amendments of provisions in DMC through legislative means for the purpose of facilitating effective building management and maintenance. The fundamental questions are to what extent should we authorize owners (presumably the majority owners) to seek to make changes to a DMC and at the same time, the level of protection to be offered to the minority owners who would be affected by or oppose such changes.

17. As advised by the Department of Justice, the issue of allocation of management fees among owners is primarily a private monetary issue between the owners. Given the implications of the proposal on property right protection and that we do not consider the issue is so fundamental as to have adverse impact on the proper management and maintenance of

buildings, we do not propose to introduce any provision in the BMO to mandate the re-allocation of management fees for existing buildings. We hope Members would appreciate that there is a limit to what the legislation could do to alter existing contractual (and property) rights.

Views Sought

18. Members' views are invited on the above.

Home Affairs Department
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