

**Hong Kong Bar Association's**

**Further Views on**

**Consultation Paper on the Contracts (Rights of Third Parties) Bill 2013**

1. In a paper dated 14<sup>th</sup> January 2013, the Hong Kong Bar Association (“the Bar”) has previously suggested that consideration be given to excluding obligations contained in Deeds of Mutual Covenants (“DMCs”) from the scope of the Contracts (Rights of Third Parties) Bill (“the Bill”).
2. The Bar is given to understand that the Law Reform Commission (“the LRC”) have since deliberated on whether to exclude DMCs from the scope of the Bill and decided not to recommend exclusion of DMCs from the scope of the Bill on the basis that the impact of the proposed legislation on the existing regime governing the enforcement of provisions contained in DMCs would be limited and hence, it cannot be said that allowing third parties to claim a right to enforce obligations contained in DMCs would contradict or prejudice the underlying policies of the area of law in question. Instead of excluding DMCs from the scope of the Bill, the LRC recommended that enforcement of DMCs should be governed by 2 parallel regimes – i.e., the rights newly conferred on third parties under the proposed legislation are to be additional to and operate alongside the existing regime governing the enforcement of DMCs by and against third parties (which will be preserved under Recommendation 16 of the LRC report).
3. By a letter dated 20<sup>th</sup> December 2013 from the Department of Justice, the Bar was invited to further comment on the LRC’s proposed treatment of DMCs and if the Bar considers that there is a need to exclude DMCs from the scope of the Bill, the Bar is further asked to consider whether *“the whole DMC (including non-land related provisions such as manager’s duties and owners’ meetings) should be excluded or is it sufficient for the land covenants contained in the DMC be excluded? Further, it appears that section 41 of the Conveyancing and Property Ordinance (Cap. 219) covers not only DMCs but other land covenants. Does the Bar consider that there are other instruments containing land covenants that should similarly be excluded from the application of the Bill?”*
4. In giving the Bar’s response, it would be useful to start by pointing out that in deciding not to recommend exclusion of DMCs from the scope of the Bill, the LRC appears to have been much influenced by the legal advice the LRC had obtained from “a counsel” who expressed the view that the additional right conferred upon third parties to enforce obligations contained in DMCs under the proposed legislation will have limited impact on the existing regime because *“third parties (whether as owners, visitors or the Government) already have enforcement rights under the existing regime”*. This is remarkable in that it is at variance with the true legal position.

5. Whilst a complete exposition on the existing legal mechanism which enables those who are not original parties to a DMC to enforce its provisions is beyond the scope of this paper, what needs to be pointed out is that not each and every provision found in a DMC is automatically enforceable by all third parties: provisions contained in a DMC are enforceable only to the extent that they “touch and concern the land” (i.e., affects the mode of enjoyment of the land) and (leaving aside special statutory provisions such as section 16 of the Building Management Ordinance which places Incorporated Owners in a unique position) only by those who are “successors-in-title” to the original covenantee (i.e., owner of an interest in land for the benefit of which the covenant was originally entered into, which would not include either visitors or the Government). Hence, it is not the case that *all* third parties already enjoy a general right to enforce *any* provision contained in a DMC and it cannot be said that the proposed legislation will have limited impact on the existing law.
6. Moreover, it is important also to note that from a conceptual point of view, there is an important distinction between the benefit of a contract (which is a mere right *in personam*) and the benefit of a covenant which runs with land (which has been judicially described as akin to an easement appurtenant to the land – i.e., a specie of “proprietary interest” amounting to a right *in rem*). The existing law which allows third parties to enforce covenants despite the absence of privity of contract (but which at the same time also limits the circumstances in which such covenants can be enforced) has developed specifically in response to needs of regulating the occupation of land, which are unique and not necessarily consistent with the policy arguments underlying the Bill, and extending a right to third parties to enforce a covenant in cases where they have no right of enforcement under the existing law may have far reaching and unintended consequences.
7. In the context of DMCs, experience has shown that the twin requirements under the existing law (that for a covenant to be enforceable by a third party, not only would the covenant have to “touch and concern” the land but the third party who seeks to enforce it must be a successor-in-title of the original covenantee) provide an important safeguard against exploitation by unscrupulous developers. Such safeguard will be substantially weakened if not lost if DMCs are not excluded from the scope of the Bill. For instances, someone (possibly an entity related to the developer) on whom a developer has sought to confer a valuable right (such as the exclusive use of a part of the building or the naming right of the building) *in gross* who cannot at present enforce those rights might in future be able to do so if DMCs are not excepted from the operation of the Bill. It is no answer to say that the parties are free to contract out of the Bill because in practice, freedom of contract seldom works well in situations involving DMCs.
8. In any event, given that there are clear limits set by the existing law on the enforceability of covenants which run with land (based on policy considerations which are unique to the regulation of land occupation) and that any relaxation of those limits would affect a large number of people, it is undesirable to effect a change in the law without full consultation specifically aimed at reform of that branch of the law.

9. It follows from the above that I am unable to subscribe to the view that the impact of the proposed legislation on the existing regime governing the enforcement of provisions contained in DMCs would be limited or that allowing third parties to claim a right to enforce obligations contained in DMCs would not contradict or prejudice the underlying policies of the area of law in question. And given that the law on the enforceability of provisions in DMCs largely follows the general law on the enforceability of covenants which run with land, for the purposes of deciding whether to exclude them from the scope of the Bill no sensible distinction can be drawn between the so-called “non-land related provisions such as manager’s duties and owners’ meetings” and “the land covenants” contained in a DMC, and for that matter, between covenants contained in a DMC and other covenants affecting land contained in other types of instruments.
10. To conclude, my suggested response to the questions raised in the letter dated 20<sup>th</sup> December 2013 from the Department of Justice can be summarised as follows:
- (a) The Bar is of the view that the LRC’s recommended treatment of DMCs appears to be based on flawed legal advice and contrary to that advice, the Bar does not believe it can be said that the additional right of enforceability under the proposed legislation will have limited impact on the existing law.
  - (b) The Bar does not believe that the problems caused by not excluding DMCs from the scope of the Bill can be adequately addressed simply by preserving the existing regime for enforcement of covenants by third parties or that the objections can be overcome by the ability of parties to exclude DMCs from the application of the legislation if they so wish.
  - (c) The Bar is of the view that all provisions included in a DMC, as well as all covenants the enforceability of which is currently limited by the rules which govern running of covenants with land should be excluded from the scope of the Bill.

**Dated: 15<sup>th</sup> January 2014**

**Hong Kong Bar Association**