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本局檔號 OUR REF.: THB(T)CR 2/5591/75
來函檔號 YOUR REF.: LS/B/13/14-15

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29 May 2015

Ms Debbie Yau and Miss Evelyn Lee
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

Dear Ms Yau and Miss Lee,

Peak Tramway (Amendment) Bill 2015

At the meeting of the Bills Committee on 18 May 2015, some Members expressed concerns about whether the mandatory lease arrangement was a must, enquired about the details of the legal basis as to the compliance of the mandatory lease arrangement with the requirement stipulated under Article 6 (“BL 6”) and Article 105 (“BL 105”) of the Basic Law that private property should be protected in accordance with law, and asked whether laying down the mandatory lease arrangement through legislation would set an undesirable precedent. A Member also inquired about the possibility of implementing the mandatory lease arrangement through land lease conditions. On 19 May and 21 May, we received a letter each from the Assistant Legal Advisor (“ALA”) and the Bills Committee Secretariat (“the Secretariat”) for additional information. We are writing to respond to the concerns and enquiries of Members and to provide the information requested by ALA and the Secretariat.

2. Prior to the passage of the Peak Tramway (Amendment) Bill 1985, the Peak Tramway Ordinance (Cap. 265) had conferred to the Governor in Council the right to mandatorily buy back the undertaking of the peak tramway after the expiration of 28 years from the time when the Peak Tramways Company Limited (“PTC”) was empowered to construct the tramway and within six months after the expiration of every subsequent period of seven years. The relevant provision (available in English only) is extracted below:

“The Governor in Council may, within six months after the expiration of 28 years from the time when the company was empowered to construct the tramway, and within six months after the expiration of every subsequent period of seven years, ... by notice in writing require the company to sell, and thereupon the company shall sell, to the Government its undertaking on the terms of paying the then value (exclusive of any allowance for past or future profits of the undertaking or any compensation for compulsory sale or other consideration whatsoever) of the tramway, and all lands, buildings, works, materials, and plant, suitable to and used for the purposes of its undertaking...”

3. When the Government consulted the Legislative Council (“LegCo”) Panel on Economic Development and Panel on Transport on the two-stage legislative amendment exercise for the peak tramway in 2013, Members expressed two major concerns. Firstly, they wished to ensure that peak tramway service would not be disrupted. Secondly, they considered it necessary to introduce an exit mechanism to allow the operating right of the peak tramway to change hands where necessary so that a *de facto* monopoly would not be given rise to owing to the absence of an exit mechanism in the law. We have set out the above in detail in paragraph 4 of the discussion paper for the LegCo Panel on Economic Development on 23 March 2015 and paragraph 3 of the LegCo Brief issued on 22 April 2015.

4. Our proposed mandatory lease arrangement is meant to address these two concerns. When drafting the Bill, our primary consideration is that the arrangement must conform to the provisions concerning protection of private property under the Basic Law. The arrangement must also be made in an open and transparent manner to ensure that the relevant parties (including PTC, any party interested in operating peak tramway service and

the general public) can clearly understand their rights and responsibilities, both at present and in future. The rights and responsibilities must also be applicable to the present and future asset owners and tramway service operators.

5. The peak tramway is a unique facility in Hong Kong. Its ownership arrangement is also quite unique. The two terminus sites on Garden Road and at the Peak, the premises on the terminus sites, as well as the other assets essential to the operation of the peak tramway (e.g. tram tracks, tramcars, premises and facilities at the four intermediate stations, as well as power and haulage systems) are all owned by PTC. Meanwhile, the land on which the tram track and the four intermediate stations lie belongs to the Government. These land and assets are all essential to and indispensable for maintaining peak tramway operation.

6. As the law now stands, the Government lacks the legal power to compel PTC to sell or lease the two terminus sites and the other assets essential to peak tramway operation to the Government or other parties¹.

7. The Bill has introduced a provision stipulating that if the operating right is to expire or is to be terminated and no further operating right is to be granted to the operator, the Chief Executive in Council may require the owner of the “essential premises” to lease these “essential premises” to any party designated by the Chief Executive in Council (“designated party”). The designated party shall pay market rent for the leased “essential premises”.

8. “Essential premises” and “essential equipment” are the assets essential to the operation of the peak tramway. Sections 11B(11) and 11C(9) proposed in the Bill provide for the definition of “essential premises” and “essential equipment” respectively. “Essential premises” means “*any land, structure or building that is considered by the Chief Executive in Council to be essential to operating the tramway*”. “Essential equipment” means “*any tramcar, motive power, works, plant, machinery, apparatus or article that is considered by the Chief Executive in Council to be essential to operating the*”

¹ Except under two specific circumstances as described in the Peak Tramway Ordinance, namely –
(a) discontinuance of peak tramway service for six months or more for reasons within PTC’s control; or
(b) when PTC becomes insolvent.

tramway". "Essential premises" mainly include the relevant parts of the two terminus sites on Garden Road and at the Peak, as well as the related premises on the two terminus sites. "Essential equipment" covers other assets essential to the operation of the peak tramway, such as tram tracks, tramcars, and power and haulage systems. What exactly "essential premises" and "essential equipment" should cover will be agreed upon with PTC (the incumbent operator) through discussion. This will become a term on which the operating right is to be granted in future.

9. Mandatory lease arrangement is an integral part of the exit mechanism. Without such an arrangement, peak tramway service will be disrupted if the operating right is to be transferred to a new operator and there is dispute between the two operators over the use of "essential premises". It would be uncertain as to how long such disruption may last pending the resolution of the dispute. If disruption or cessation of service is not acceptable to the public but no effective exit mechanism is in place, peak tramway service may then be effectively monopolised by the incumbent operator.

10. The purpose of the mandatory lease arrangement is to enable the new operator to have the right to use (not necessarily to own) the "essential premises" to minimise the risk of service disruption when the exit mechanism is triggered. Generally speaking, a mandatory sale arrangement would be more straightforward as opposed to a mandatory lease arrangement. However, a new operator would have to pay a hefty sum if he/she is required to purchase the two terminus sites and related premises upon entry. This would in turn raise the entry threshold and would not be conducive to introducing competition where necessary. If the Government is to fund the purchase of the "essential premises", a significant amount of public fund would be involved. Thus, we propose adopting a mandatory lease arrangement for the right to use the "essential premises".

11. It should be noted that the Bill does not forbid the owner from selling the "essential premises". In other words, if the owner intends to sell the "essential premises" and can reach an agreement with the new operator on their own accord, there would simply be no need for the Chief Executive in Council to exercise the power to order a mandatory lease. The matter can be

left to market force.

12. Indeed, as pointed out in paragraph 9 of the LegCo brief issued on 22 April 2015, PTC, as the owner of the two terminus sites, has indicated its willingness to lease (but not sell) the “essential premises” in case of an exit.

13. Rent payable for the use of the “essential premises” would be assessed at market rate. Dispute arising from the rental amount would be resolved at the Lands Tribunal or through arbitration. Pending settlement of the dispute, the law would provide for the new operator to take possession of the “essential premises” first to avoid service disruption.

14. The Department of Justice (“DoJ”) has confirmed that the mandatory lease arrangement conforms to the requirements in BL 6 and BL 105 for protection of private property. A detailed explanation is set out in our reply of 7 May 2015 to ALA.

15. DoJ now elaborates further. BL 105 reads “*the Government shall, in accordance with law, protect the right of individuals and legal persons to the acquisition, use, disposal and inheritance of property and their right to compensation for lawful deprivation of their property. Such compensation shall correspond to the real value of the property concerned at the time and shall be freely convertible and paid without undue delay.*” Since it is provided that “*in accordance with law, protect the right of individuals and legal persons to the use and disposal of property*”, the mandatory lease arrangement may be interpreted as imposing restrictions on the property rights of the asset owner. As noted in paragraph 102 of *Securities and Futures Commission v “C” & Ors* HCMP 727/2008, permissible restriction on the right to property guaranteed by the Basic Law must be “in accordance with law”. The expression “in accordance with law” in BL 105 mandates the principle of legal certainty and incorporates the requirement that the relevant law must be adequately accessible to citizens and formulated with sufficient precision to enable the citizens to regulate his conduct. Therefore, “in accordance with law” means that the Government cannot arbitrarily restrict the property rights of individuals or legal persons. Yet, BL 105 permits the Government to restrict property rights or deprive properties “in accordance with law” through legislation as and when necessary. The mandatory lease

arrangement is a restriction imposed “in accordance with law” by the Government on property rights through legislation.

16. In view of the considerations in paragraph 10 above, what we are proposing in the Bill is a mandatory lease arrangement. Upon passage of the Bill, any purchaser interested in purchasing the “essential premises” from the existing owner will continue to be entitled to the same right of selling the assets after the purchase. Moreover, the purchaser, when purchasing the “essential premises”, will become aware that the use and disposal of the premises are subject to the restrictions under the Bill. The Bill, however, does not impose any other new restriction on the purchaser. According to paragraph 33 of *Fine Tower Associates Ltd. v Town Planning Board* [2008] 1 HKLRD 553, property rights (particularly the land use rights) protected by BL 105 can be subjected to restrictions that may be lawfully imposed. For the new purchaser, such limitation will not constitute deprivation of property to him/her².

17. It should be pointed out that the mandatory lease arrangement will not constitute “deprivation” under BL 105. With reference to local case laws, there are two lines of authorities for interpretation of “deprivation”:

- (i) Formal expropriation: The Government formally expropriates the property for public use (*Harvest Good Development v Secretary for Justice & Ors* [2007] 4 HKC 1); or

² Local courts have not applied the “proportionality test” in “non-deprivation cases where there is interference with property rights”. Yet, for reference purpose, DoJ has reviewed whether the mandatory lease arrangement can satisfy the “proportionality test”.

Under the “proportionality test”, any interference with property rights would need to strike a balance between the general interest of society and protection of the individual’s rights. Regarding whether the “proportionality test” is applicable to “non-deprivation cases where there is interference with property rights”, according to *Hysan Development Co. Ltd. & Ors v Town Planning Board*, CACV 232 & 233 of 2012, the Court of Appeal expressed reservation towards whether the “proportionality test” under the common law should apply to the protection of property rights of individuals and legal persons. Therefore, the mandatory lease arrangement as proposed in the Bill is consistent with the protection of rights to use and dispose of property “in accordance with law” as required under BL 105. This case is being put to the Court of Final Appeal.

Even assuming that the “proportionality test” applies, since the mandatory lease arrangement is able to balance the general interests of society (to establish a mechanism to prevent monopoly by a single operator and to avoid disruption of peak tramway service) and the protection of the asset owner’s rights (to receive the rent of “essential premises” at market value), such an arrangement can satisfy the “proportionality test”. In fact, the asset owner (i.e. PTC) finds the mandatory lease arrangement acceptable.

- (ii) *De facto* deprivation: *De facto* deprivation involves the removal or denial of all meaningful use, or all economically viable use, of the property (*Fine Tower Associates Ltd. v Town Planning Board* [2008] 1 HKLRD 553).

DoJ has pointed out that the mandatory lease arrangement does not constitute any of the above types of “deprivation”. The fact that the Chief Executive in Council has the power to order the asset owner to handle the “essential premises” by way of lease does not constitute formal expropriation of property as the asset owner still retains ownership of the property. Since the asset owner still has the right to sell the “essential premises” or receive rent at market value under the mandatory lease arrangement, the arrangement does not constitute *de facto* “deprivation” either. It is clear that the mandatory lease arrangement under the Bill does not constitute “deprivation” under BL 105.

18. With regard to ALA’s enquiry as to whether the mandatory lease arrangement will be adopted under other circumstances through legislation, our response is that the Government will make decisions after considering all relevant factors on a case-by-case basis. There can be no one-size-fit-all answer. If legislative amendment is involved, we will consult LegCo on the amendment proposal as a matter of course, and the amendment bill has to be passed by LegCo.

19. The Secretariat and ALA have also enquired if there is any local and overseas legislation providing for a similar mandatory lease arrangement. We have found several local examples relating to transport services, namely Part IV of the Public Bus Services Ordinance (Cap. 230), Part V of the Ferry Services Ordinance (Cap. 104), and Part IV of the Mass Transit Railway Ordinance (Cap. 556). These ordinances contain similar provisions providing for the Government to take possession of properties of individuals or legal persons under certain circumstances for a period of time specified. Besides, our search findings also suggest that the “Rent Stabilization Code” of New York and “Telecommunications Act of 1986” of the United States provide for similar mandatory lease arrangements, and in the court case of “*The Greystone Hotel Co. v. The City of New York, Edward Hochman*”, the

“Rent Stabilization Code” of New York was considered. It should be noted that there are differences between the mandatory lease arrangement under the Bill and the examples of the mandatory possession arrangements quoted above. There are also differences among the quoted examples themselves. It should be also noted that the peak tramway is somewhat unique as mentioned in paragraphs 5 and 6 above. The transfer of its “essential premises” has to be handled in a practical and practicable manner. This can be achieved through the mandatory lease arrangement. Indeed, the existing asset owner (i.e. PTC) finds the mandatory lease arrangement acceptable.

20. We have consulted the Lands Department (“LandsD”) on Member’s enquiry about whether the mandatory lease arrangement can be achieved by way of lease modification (instead of legislative amendments), and the answer is in the negative. Putting in place the mandatory lease arrangement through legislative amendments will turn the arrangement into a legal provision and make the requirements contained therein (including the requirement for the lessee under the mandatory lease arrangement to pay market rent so as to comply with the requirement under BL 105 that private property should be protected) legally binding on all lessees under the mandatory lease arrangement in future. Instituting the mandatory lease arrangement by way of a land lease cannot have such an effect. This is because as with all land leases, the land leases for the terminus sites are contracts between the Government and the lessee of the terminus sites. The lease provisions do not have any binding effect on non-contracting parties. In other words, even if the lessee of the sites agrees to modify the leases of the two terminus sites, we cannot write the provisions on the rights and obligations of the lessee of the mandatory lease arrangement under the proposed Section 11B into the land leases. This means that the most critical requirement – that the lessee under the mandatory lease arrangement must pay market rent – cannot be enforced. Even if the provisions on the dispute resolution mechanism for the terms of the mandatory lease as specified in the proposed Section 11D are provided for in the leases of the terminus sites, they will again not be binding on the lessee under the mandatory lease arrangement. This would render the dispute resolution mechanism, and consequentially the exit mechanism, ineffectual. In fact, the empowerment of the Lands Tribunal to handle disputes over the terms of the mandatory lease can only be effected through legislative means.

21. In response to the enquiry about the lease terms of the sites owned by PTC, LandsD advises that the relevant lease terms (available in English only) are as follows:

The terms of the site on which the Peak Terminus is located –

“... the lot or any part thereof or any building or buildings erected or to be erected thereon shall not be used for residential or industrial purposes except:-

- (a) For purposes in connection with the operation of the Peak Tramway; or*
- (b) For such public entertainment or recreational purposes as the Director [of Lands] may approve.”*

The terms of the site on which the Garden Road Terminus is located –

“The lot shall not be used for any purpose other than non-industrial purposes and for purposes in connection with the maintenance and operation of the Peak Tramway only.”

22. The mechanism under the proposed sections 11B(7) and 11C(b) will be invoked when the Chief Executive in Council has issued an order for mandatory lease or sale in accordance with the proposed sections 11B(1) and 11C(1), and the order has not been complied with. The Secretary can then apply to the Court of First Instance to enforce such an order.

Yours sincerely,



(Miss Carrie Chang)

for Secretary for Transport and Housing

c.c. Department of Justice
(Attn: Mr Gilbert Mo, Ms Daphne Siu and Mr Llewellyn Mui)

Hon Jeffrey LAM Kin-fung, Chairman of the Bills Committee