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Buying and Selling Real Estate in Hong Kong



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KEY FACTS OF REAL ESTATE ACQUISITIONS UNDER HONG KONG LAW

Introduction

Hong Kong is one of the most densely populated cities over the world. Due to historical reasons, almost all lands in Hong Kong are leasehold tenures. Over the centuries, the Government leased or granted to individuals or corporations pieces of land for use or for development. Therefore, a sale and purchase of landed property in Hong Kong is in fact a transfer or assignment of a lease. In a sale and purchase transaction, the vendor agrees to sell, and the buyer agrees to purchase both the legal estate and the equitable interest of and in the landed property. This article provides a brief introduction to land law in Hong Kong and sets out a summary of the procedures of the sale and purchase of landed properties in Hong Kong.

System of Deeds Registration

Unlike other common law jurisdictions, the Hong Kong registration system is not one of registration of title but a deeds registration system. Registration of instruments alone does not confer title but only serves as a notice of having an interest in the landed properties which are affected by the instruments. Instruments affecting landed properties are required to be registered at the Land Registry in Hong Kong in order to have priority over any other subsequent registrable interests in land. While the general rule is that the priority of the registrable instruments shall be determined by the sequence of their respective dates of registration, there is a special rule that priority shall take effect by reference to the date of execution instead of the date of registration if such registrable instruments (excluding charging orders and lites pendentes) are registered within one month after the date of execution. Failure to register a registrable interest will render the same to be null and void

against any subsequent bona fide purchaser or mortgagee for valuable consideration but will not affect the legality, validity, and enforceability of the instrument as between the parties of the unregistered registrable instrument.

The Procedures of the Common Sale and Purchase of Landed Properties in Hong Kong

Provisional Agreement for Sale and Purchase

Before a potential purchaser decides to purchase a landed property, he/she usually inspects the landed property (flat/apartment/house) through the arrangement by an estate agent first and considers if he/she requires any financing when purchasing the property. It is advisable that, at least, a rough estimate verbal valuation of the relevant property should be obtained beforehand in order to apply to bank(s) for mortgage loan. Nowadays, a mortgage loan of around 60%-70% of the market value of the property can be obtained. In the circumstance, a purchaser should consider carefully whether he/she can afford to pay for the remaining purchase price and the Ad Valorem Stamp Duty.

When a purchaser agrees to purchase and a vendor agrees to sell a landed property, both parties will enter into a written agreement. In Hong Kong, the preliminary agreement, also known as the provisional agreement for sale and purchase (the "PASP"), is not required by law but commonly used. Such written agreement is usually prepared by estate agents which contains the basic terms such as details of the subject property, parties, consideration, and completion date. Upon signing of a PASP, the purchaser will pay to the vendor or the vendor's solicitors (as stakeholders) a sum being the initial deposit (which is usually 3%-5% of the consideration) to show his/her sincerity



to purchase the landed property. The purchaser will usually register the PASP at the Land Registry (after stamping of the PASP).

The PASP generally contains, inter alia, a standard clause which gives both the vendor and the purchaser a chance to “get out” of the contract after signing the PASP. The vendor is entitled to forfeit the deposit paid by the purchaser if the purchaser decides not to proceed further, whereas the vendor shall refund the deposit to the purchaser and compensate the purchaser with a sum equivalent to the amount of the deposit paid if the vendor decides not to sell the property to the purchaser. However, both the vendor and the purchaser can choose to enter into a “binding” agreement without the chance to get out of the contract unless the title to the property is defective.

Ad Valorem Stamp Duty will be payable on the PASP only when the terms of the formal agreement for sale and purchase (the “Formal ASP”, as hereinafter defined) cannot be finalized and the Formal ASP cannot be signed within 14 days of the signing of the PASP. The Formal ASP is also required to be submitted for registration at the Land Registry.

Formal Agreement for Sale and Purchase

After signing the PASP, the parties have to appoint their respective solicitors as soon as possible. Solicitors for the respective parties will negotiate and agree on the terms and conditions of the Formal ASP. After execution of the Formal ASP, Ad Valorem Stamp Duty will be payable, and the Formal ASP will be presented for registration at the Land Registry.

Use of Power of Attorney in the Sale and Purchase

It is common for a purchaser or a vendor to execute a Power of Attorney (the “POA”) in the sale and purchase of a landed property,

especially when the purchaser or vendor is physically unable to be present in person when executing the Formal ASP and/or Assignment (as hereinafter defined). A POA is an instrument that allows a person (or corporation) to give power to an attorney to act for and on his/her/its behalf in performing certain acts or obligations, for example, for the purpose of enabling the sale or purchase of a landed property. To determine whether a POA is in order, a number of criteria has to be fulfilled:- (1) whether the POA has been properly executed; (2) whether the specified power(s) is/are clearly defined therein; and (3) whether the POA is still valid and not revoked as at the time when the relevant instruments such as the Formal ASP and/or Assignment is/are executed. Generally, the validity period for a POA is 12 months from its date of creation.

If a POA is being relied upon by any party in a sale and purchase transaction, it is important for the purchaser’s solicitors or the vendor’s solicitors to produce the POA to the other side for verification. More importantly, it is always advisable to consult your own solicitors before executing the POA to ensure that the proper procedures are observed, especially where the POA will be executed abroad for use in Hong Kong. For POA executed abroad, it is always a good conveyancing practice for the execution of the POA to be witnessed by a notary public and sometimes further authenticated/legalized depending on different jurisdictions.

Notwithstanding the foregoing, a POA might not be applicable or acceptable to all landed property transactions. For example, if a purchaser needs to obtain mortgage loan for financing the purchase of the property, a bank or financial institution may not accept POA when executing the mortgage deed. As such, it is advisable to obtain legal advice and/or consent from the relevant bank or financial



institution prior to the execution of a POA for use in a landed property transaction.

Title Requisitions: Proving & Investigating Title

The parties shall abide by the terms and conditions set out in the Formal ASP and prepare for completion after the execution of the Formal ASP. If the landed property is subject to any existing mortgage, the vendor will have to arrange for discharge or release of the existing mortgage before completion to ensure that the landed property shall be sold to the purchaser free from all encumbrances. The purchaser is advised to apply for mortgage loan from the relevant mortgage bank reasonably in advance of completion if he/she requires financing to pay the balance of the purchase price of the landed property.

Prior to completion, unless otherwise agreed by the parties, the vendor shall be under a duty to prove good title to the purchaser of the landed property by (1) delivering to the purchaser all relevant title deeds and documents in respect of the landed property; and (2) satisfactorily answering requisitions on title raised by the purchaser. As previously mentioned, one cannot prove his/her title of the landed property under the said deeds registration system. Hence, it is always the duty of the purchaser's solicitors to check the title to the landed property by perusing all the relevant title documents provided and delivered by the vendor's solicitors. This also explains why lawyers are actively involved in a sale and purchase transaction in Hong Kong. The rights of the purchaser's solicitors to investigate title and to raise requisitions are also generally set out in the Formal ASP. The vendor's solicitors have to satisfy the purchaser of the vendor's good title to the property or the vendor's title agreed to be delivered to the purchaser. The purchaser has the right to insist on a good title being proved and showed and the vendor is

obliged to clear all title encumbrances or to remedy all the title defects upon completion.

Mortgage Financing

In Hong Kong, if the purchaser requires financing for payment of the balance of the purchase price, the purchaser will apply for the mortgage loan as soon as practicable before completion and/or even get an indication from the bank(s) before entering into the PASP. When choosing a bank or financial institution for mortgage loan, the purchaser should consider the following (not exhaustive) :-

- (i) the landed property valuation and mortgage amount to be offered;
- (ii) the repayment term, number of installments and the amount of each installment;
- (iii) the criteria for determining interest rates; and
- (iv) the early redemption penalties and the notice period.

Depending on the value of the landed property, the banks or financial institutions usually offer the purchaser a loan of up to 60%-70% of its market value.

Usually, the purchaser's solicitors also act for the purchaser's mortgagee in respect of the mortgage transaction by preparing all the relevant mortgage and security documents.

Preparation before Completion: Apportionment of the Outgoings

Before completion, purchaser's solicitors have to make enquiries with the management company or the incorporated owners of the building as to whether there is any outstanding management or other fees payable by the owner of the property. The vendor's solicitors will usually prepare an apportionment account to the purchaser's solicitors to show how all the



relevant outgoings will be apportioned between the vendor and the purchaser. It is common that management fee, rates and Government rent, and rental payment (if any) will be apportioned as at the date of completion. The vendor usually pays up to and inclusive of the actual date of completion. Nonetheless, utility payments such as electricity, gas and water will be dealt with by the vendor and the purchaser with the respective utility companies directly.

Preparation before Completion: Inspection of the Landed Property

Purchaser will make a final inspection of the landed property through the arrangement with the estate agent before the completion date if the property will be sold to the purchaser with vacant possession. There may be fixtures and fittings which have been agreed to be sold or delivered to the purchaser together with the landed property upon completion. One must note that even if the purchaser discovers that any or part of the fixtures and fittings which have been agreed to be sold to the purchaser is/are not available upon final inspection, he/she is not entitled to terminate the PASP/Formal ASP on this reason alone and the only claim which is available to the purchaser is a claim for damages.

Execution of Assignment

On completion, the vendor shall execute a deed of assignment (the "Assignment") upon receipt of the purchase money of the landed property. Assignment shall be in the form of a deed. It is required for transferring the legal estate of and in the landed property from the vendor to the purchaser upon completion. In usual practice, the purchaser will execute the assignment in escrow (i.e. to execute the completion documents before completion and the completion documents will only become

effective upon all the conditions having been satisfied).

Completion of the Sale and Purchase

Completion for sale and purchase of the landed property usually takes place by way of solicitors' undertaking. This form of completion places an important reliance on the solicitors by requiring the solicitors giving their professional undertakings (i.e., promises).

On the completion date, the purchaser's solicitors shall deliver the balance of the purchase money in exchange for an undertaking given by the vendor's solicitors to return (1) the assignment duly executed in the purchaser's favour by the vendor; (2) all original title deeds (which relate exclusively to the landed property and are required for giving good title to the landed property) including the release or discharge of the existing mortgage/legal charge (if any); and (3) the keys of the landed property (if vacant possession is agreed to be delivered to the purchaser on completion).

After the vendor has delivered a duly executed assignment to the purchaser, the purchaser's solicitors will then arrange to pay stamp duty on the assignment (which is a nominal sum of HK\$100) and register the assignment at the Land Registry.

Stamp Duty Implications

Under the Stamp Duties Ordinance (Cap.117) ("SDO"), the vendor and/or the purchaser may be liable for the payment of Ad valorem duty ("AVD"), Buyer stamp duty ("BSD") and Special stamp duty ("SSD") for the sale and purchase of a landed property. However, payments of AVD, BSD and SSD are not mutually exclusive. The following stamp duty implications will have to be carefully considered prior to entering into a sale and purchase transaction in relation to landed property:-



Ad Valorem Duty (“AVD”)

Unless specifically exempted or otherwise provided in the law, the sale and purchase or transfer of more than a single residential property under a single instrument executed on or after 12 April 2017 will be subject to AVD at a flat rate of 15% of the consideration or value of the residential property, whichever is the higher.

Any instrument executed on or after 5 November 2016 for the sale and purchase or transfer of **residential** property, either by an individual or a company will be subject to AVD at the rate set out under “Part 1 of Scale 1” under Schedule 1 to the Stamp Duty Ordinance (Cap.117) (i.e., a flat rate of 15% of the consideration or value of the residential property, whichever is the higher), unless specifically exempted or provided otherwise.

Part 1 of Scale 1 does not apply to an agreement /conveyance for a residential property where the purchaser/transferee is a Hong Kong permanent resident (“HKPR”) (or he/she is a tenant or an authorized occupant of the Housing Authority who acquires the residential property under the Tenants Purchase Scheme) acting on his/her own behalf and does not own any other residential property in Hong Kong at the time of acquisition of the subject property. In those circumstances, only the rate set out under “Scale 2” under Schedule 1 to SDO (i.e., a rate ranging from \$100 to 4.25% of the consideration or value of the residential property, whichever is the higher) will apply to such agreement/conveyance.

Any agreement executed on or after 23 February 2013 for the sale and purchase or transfer of **non-residential** property, either by an individual or a company will be subject to AVD at the rate set out under “Part 2 of Scale 1” under Schedule 1 to SDO (i.e., a rate ranging

from 1.5% to 8.5% of the consideration or value of the residential property, whichever is the higher), unless specifically exempted or provided otherwise.

While it is typical for the purchaser to agree to bear the AVD, it is important to note that under the Hong Kong law, the purchaser, the vendor, and any person who uses the instrument will be jointly and severally liable to pay AVD, irrespective of any agreement to the contrary made between them.

Buyer’s Stamp Duty (“BSD”)

Unless specifically exempted or provided otherwise, BSD is chargeable on an agreement/conveyance for the sale and purchase or transfer of any **residential** property acquired on or after 27 October 2012, except where the purchaser or transferee is a HKPR acquiring the subject property on his/her own behalf. It is the purchaser (not the vendor) who is liable to pay BSD, the rate of which is 15% of the consideration or value of the residential property, whichever is the higher.

Special Stamp Duty (“SSD”)

SSD is chargeable on a transaction involving the sale and purchase or transfer of a **residential** property if the subject property is acquired on or after 27 October 2012 and resold within 36 months after acquisition. The rate of the SSD payable varies from 10% to 20% of the consideration or value of the residential property, whichever is the higher, depending on when the subject property was resold within those 36 months. The purchaser and the vendor to the property transaction and any person who uses the instrument will be jointly and severally liable to pay SSD.



Sale and Purchase of Property by way of Transfer of Shares

On the other hand, it has now gradually become a common practice for potential purchaser in Hong Kong to acquire property by way of transfer of shares in a limited company. Under such arrangement, the vendor, who is actually the shareholder of the limited company, agrees to sell and the purchaser agrees to purchase all the issued share capital and liabilities of and in that limited company. As a result, the purchaser will acquire the property through becoming the shareholder of that limited company in place of the vendor.

Unlike the usual PASP as aforesaid, an agreement for the sale and purchase of shares of limited company is a more complicated legal document. Apart from taking over the shares of a limited company, the purchaser will also have to take over the debts and liabilities of that limited company which is associated with the share transfer transaction. However, such debts and liabilities of the limited company may not be easily discovered by the purchaser unless a thorough due diligence examination of the accounting records and corporate documents of that limited company has been conducted. Further, complications may arise from the share transfer transaction if financing is required by the purchaser. The approach will be totally different from applying for mortgage loan for financing the purchase of a property through a simple sale and purchase as aforementioned.

From a tax perspective, a purchaser may prefer making his/her purchase through a company in order to enjoy lower stamp duty. As mentioned above, purchase of property in Hong Kong may be subject to three types of Stamp Duties, namely, AVD, BSD and SSD. Meanwhile, a share transaction is subjected to a significantly lower stamp duty, which is 0.13% of the amount of

consideration or the underlying net asset value of those shares, whichever is the higher.

If parties intend to sell and purchase a property by way of transferring shares of a limited company, it is important that the parties' interests are adequately protected, and comprehensive legal documentation is required. It is advisable to obtain legal advice before acquiring a property by way of share transfer.