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Buying and Selling Real Estate in Hong Kong

ILN REAL ESTATE GROUP



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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. With very little available land, real estate developers tend to build multi-storey buildings ranging from 30-to-70-storey high. 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 a piece 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 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. Under such deeds registration system, it provides a register of the instruments affecting a particular lot of land. Registration of instruments alone does not confer title. Only instruments affecting the landed property can be registered and registration serves as a notice of having an interest in the landed property. As such, documents such as deeds, conveyances, or other instruments in writing and judgments creating or dealing with an interest in land, or affecting land, are considered as registrable instruments. They 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, the special rule is 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 to consider 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. Around 60%-70% mortgage loan is the most of the market value of the property can be obtained nowadays. As such, a purchaser should consider carefully if he/she is affordable to pay for the remaining purchase price and also a lump sum of the Ad Valorem Stamp Duty.

When a purchaser agrees to purchase and a vendor agrees to sell a landed property, both parties will have to enter into a written agreement. In Hong Kong, 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 quite standard and usually prepared by estate agents which contains basic main terms such as the subject property, parties, consideration and completion date etc. in relation to the sale and purchase transaction. Upon signing of a PASP, the purchaser will pay to the vendor or to 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). It is advisable that both the vendor and purchaser should expressly set out the special agreed term(s) (if any) in the PASP since the PASP only contains the basic terms and parties should better let their own solicitors peruse/comment on the PASP before signing the same.

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 only be payable on the PASP when the terms of the Formal ASP (as hereinafter defined) cannot be finalized and the Formal ASP (as hereinafter defined) cannot be

signed within 14 days 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. (However, in the sale and purchase of firsthand property, separation of legal representation might not be necessary.) Solicitors for the respective parties will negotiate and agree on the terms and conditions of the formal agreement for sale and purchase (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. One should note that in the event that AVD is payable on the PASP in the circumstances as aforesaid, the Formal ASP will be stamped a nominal sum of HK\$100.00 before it is presented for registration at the Land Registry.

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 the completion so 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) answering requisitions on title raised by the purchaser satisfactorily. As previously mentioned, one cannot prove his/her title of the landed property under the said deeds registration system. Hence, it is always the purchaser's solicitors' duty 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 purchaser's solicitors' rights to investigate title and to raise requisitions are also generally set out under 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 remove 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 money, the purchaser will have to apply for the mortgage loan as soon as practicable before completion and even to get an indication from the bank(s) before entering into the PASP. When choosing a bank or financial institution for mortgage loan, purchaser should also 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 bank or financial institutions usually offer 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. The purchaser's solicitors will receive written instructions from the purchaser's mortgagee bank before completion, instructing them to prepare the mortgage document to secure the loan to be granted to the purchaser.

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 rent (if any) will be apportioned as at the date of completion. The vendor usually pays up to and inclusive of the actual day 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/delivered to the purchaser together with the landed property upon completion. One must note that if the purchaser discovers that any/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 upon receipt of the purchase money of the landed property. Assignment shall be in 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). The purchaser will deliver the balance of the purchase money in exchange for an undertaking given by the vendor's solicitors to return an assignment duly executed by the vendor within an agreed time limit.

On the completion date, the purchaser's solicitors shall deliver the balance of purchase

money in exchange for (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 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

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, irrespective of whether or not the purchaser/transferee is a HKPR who is 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 properties.



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. 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. 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 the purchaser, the vendor, and any person who uses the instrument, under the Hong Kong law, will be jointly and severally liable to pay AVD. In

other words, the purchaser, the vendor and any person who use the instrument will have the same extent of liability to pay for any AVD payable on the chargeable instruments, 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.