

LEGISLATIVE COUNCIL BRIEF

STANDARD RATES FOR CHARGING LAND PREMIUM ON LEASE MODIFICATIONS FOR REDEVELOPMENT OF INDUSTRIAL BUILDINGS

INTRODUCTION

At the meeting of the Executive Council on 23 February 2021, the Council **ADVISED** and the Chief Executive **ORDERD** that –

- (a) applicants of lease modification¹ for redevelopment of **pre-1987 industrial buildings**^{2,3} (IBs) should be allowed to **opt** for charging land premium at standard rates under a pilot scheme of **two years** (the Pilot Scheme);
- (b) differential standard rates should be set for: (i) **five broad regions in Hong Kong**, and (ii) within each region, **three uses**, namely: the **Before Use** being industrial/godown use permitted under the existing lease and **two types of After Use** being commercial/modern industrial use and residential use to be permitted under the modified lease, for calculation of the premium chargeable along the framework in **Annex A**; and
- (c) the level of standard rates should be kept unchanged for the duration of the Pilot Scheme.

¹ References to a lease modification in this brief include a land exchange.

² IBs refer to flatted factory buildings, industrial-office buildings and other buildings built for industrial uses where the leases governing the lots on which the buildings stand specify industrial and/or godown uses, or are unrestricted in terms of uses permitted under lease. Such IBs do not include special factories such as those located in industrial estates, storage premises in container terminals and flatted factories built by the Housing Authority, and those buildings on lots supporting special industries such as cargo handling uses, ship building and repairing, oil storage and refining and production of associated chemical by-product, manufacture of polystyrene plastics, manufacture and storage of chlorine, hydrogen and textile chemicals, etc..

³ Pre-1987 IBs refer to those IBs which were wholly or partly constructed on or before 1 March 1987, or those constructed with their building plans first submitted to the Building Authority for approval on or before the same date.

JUSTIFICATIONS

Latest progress of IB revitalisation

2. There are a total of about 1 500 IBs in the territory. Due to the restructuring of our economy, over the years suitable industrial land has been identified and rezoned into other uses more compatible with the prevailing socio-economic needs, such as commercial and residential uses. To facilitate the transformation of IBs on such rezoned land to realise the latest planning intention, the Government implemented a revitalisation scheme for IBs from 2010 to 2016 (hereafter the “2010 IB Revitalisation Scheme”) to incentivise redevelopment or wholesale conversion of these IBs (for details, please see **Annex B**). The 2010 IB Revitalisation Scheme resulted in 14 and 140 approved cases⁴ for redevelopment and wholesale conversion respectively, altogether providing a total of about 2 529 000 m² of gross floor area for non-industrial uses (such as hotels, offices and residential developments).

3. To further optimise the use of IBs, another round of IB Revitalisation Scheme was implemented in 2018 (hereafter the “2018 IB Revitalisation Scheme”). In particular, this round of measures gives a stronger push to encourage the redevelopment of pre-1987 IBs, which were constructed under a set of lower fire service installation requirements before the relevant code of practice on minimum fire service installations and equipment was revised by the Fire Services Department in 1987 (for example, many do not have automatic sprinkler systems)⁵ and thus of higher risk. The key incentive was a planning measure (hereafter the “2018 planning measure”) to allow relaxation of the maximum permissible non-domestic plot ratio by up to 20%, on a case-by-case basis upon application to the Town Planning Board (TPB), for a three-year period from October 2018 (more details of the 2018 IB Revitalisation Scheme are set out in **Annex B**). Up to December 2020, within an interval of slightly more than two years, 50 applications for redevelopment have already been received by the TPB, of which 42 applications have been approved. Of the redevelopment cases

⁴ As at end-September 2020, all 14 redevelopment cases and most of the 140 wholesale conversion cases have been executed.

⁵ The fire service installations in pre-1987 IBs are expected to be upgraded gradually with the commencement of the Fire Safety (Industrial Buildings) Ordinance (Cap. 636) in June 2020. The Fire Services Department and the Buildings Department will conduct inspections on each and every target building by phases, and issue directions to owners and/or occupiers on the necessary upgrading requirements for each building.

approved by TPB so far, 22 would require lease modifications. Furthermore, the Lands Department (LandsD) is processing lease modifications of 10 cases also involving redevelopment of pre-1987 IBs but not requiring TPB's approval. Expediting the execution of such cases in hand will help achieve the objective of revitalisation sooner.

4. Furthermore, apart from the above cases already on the radar screen, there are still around 900 pre-1987 IBs in Hong Kong. There is thus a case to give **a stronger push** to encourage revitalisation, particularly for redevelopment. A new option of premium assessment by way of standard rates would provide more certainty and encourage early execution of cases in the pipeline as well as motivate others to come forward, and thus expedite the transformation of IBs.

The case for Standard Rates

5. Under the established mechanism, LandsD assesses and negotiates with lease modification applicants on a case-by-case basis regarding the amount of land premium payable, being the value of the new lease after modification (After Value) less the value of the existing lease prior to modification (Before Value). In the process, LandsD takes into account market comparables (such as recent transactions) as well as case-specific circumstances (such as site location). It takes time to reach an agreement on the land premium payable, depending on such factors as the complexity of the issues involved and the gap between the offers of LandsD and those of the applicants as well as the readiness of the applicants to proceed with the projects.

6. While the conventional practice of premium assessment enables case-specific circumstances to be taken into account to ensure precision and fairness⁶ as well as safeguards premium receipts, there is a case for **piloting** the introduction of standard rates as an option for lease modification applicants **in the context of redevelopment of pre-1987 IBs** on land premium calculation, for the following reasons:

- (a) As traditional industries such as manufacturing diminish, many IBs have gradually accommodated various non-industrial uses, some of which are non-compliant with the permitted land uses in town planning

⁶ The value of a site, hence the premium, would depend on its location, size, configuration, accessibility, site conditions, lease restrictions, development intensity, height of the development, etc.

terms or under land lease conditions. The mixture of industrial and non-industrial uses in IBs (such as studios, party rooms, and even domestic flats) could pose serious safety risks to visitors who are not familiar with the means of escape and households residing in the premises. The problem is particularly acute in pre-1987 IBs as mentioned above. There is a need for intensified efforts to speed up the redevelopment of these IBs, which is a more fundamental way to address the fire safety problems in IBs than enforcement and upgrading of installations. Redevelopment also helps optimise the usage of IBs to create more commercial and residential floor space, and improve city environment.

- (b) Conventional premium negotiation takes time due to the disagreement between the applicants and LandsD. This is particularly challenging for cases involving IBs, given the different points of view in the assessment of the “Before Value”, such as whether market transactions of industrial premises, which often reflect the value of existing uses not permitted under the land lease, should be factored into the premium assessment. This may lead to rounds of appeals, deferring the conclusion of cases. While the introduction of standard rates would not change LandsD’s principle of not taking into account unauthorised uses in assessing the “Before Value” (which is in line with established valuation principles), it would be a **game changer** in that the standard rates would provide upfront certainty on the land premium payable. For applicants who see a business case for redevelopment, this saves the process of negotiation and the corresponding professional costs. For IBs still in multiple ownership, a certainty on the land premium payable could entice owners/developers to plan ahead in amalgamating the ownership of IBs to pursue redevelopment. All in all, more landowners may be induced to undertake redevelopment as a result.

Key parameters

7. The guiding principles for the Pilot Scheme are that the rules should be **clear and simple** for enhancing transparency and certainty. By design, standard rates are not tailor-made for individual cases, hence could not be expected to precisely reflect the merits of individual cases. Some applicants for lease modifications may be better off under the use of standard rates and others may not, depending on how the land premium assessed under the conventional

approach compares with that charged under the standard rates for the particular case in question. In this regard, it should be noted that for any one case in question, any “savings” in premium under the standard rates approach vis-à-vis the premium that would have been chargeable under the conventional approach would be incidental, and not the objective of the Pilot Scheme. The key parameters of the Pilot Scheme are as follows.

Eligibility

8. Same as the 2018 planning measure, the Pilot Scheme shall apply to **pre-1987 IBs**⁷ to give a further push for redevelopment of those IBs not built to modern-day fire safety standards. For the avoidance of doubt, TPB’s approval of 20% additional plot ratio under the 2018 planning measure is **not** a prerequisite for joining the Pilot Scheme, as redevelopment of this pool of IBs should be encouraged irrespective of whether the redeveloped buildings would deliver increased floor area.

9. The following types of IBs will not be covered by the Pilot Scheme, because:

- (a) For pre-1987 IBs which have undergone wholesale conversion under the 2010 or 2018 IB Revitalisation Schemes, technically they are no longer pre-1987 IBs in terms of their form and building and fire safety standards.
- (b) For IBs under leases for special industries, they were excluded from the 2010 and 2018 IB Revitalisation Schemes, and will likewise be excluded from the Pilot Scheme. These leases carry more restrictive permitted user and are by nature different from conventional IBs. For instance, they are likely to attract a Before Value different from that of general industrial/godown use under the conventional premium assessment.

⁷ Irrespective of the zoning of the site under the Outline Zoning Plan (OZP).

Standard rates as an option

10. The standard rates approach is meant to be an alternative option to the conventional approach in land premium assessment. Applicants are required to opt **before** the commencement of land premium assessment (i.e. upon the acceptance of provisional basic terms offer of the lease modification⁸). Once the applicant chooses a particular premium assessment option, he is not allowed to change course midway, otherwise he would be required to submit a fresh application and make fresh payment of administrative fee.

Duration of the Pilot Scheme

11. The Pilot Scheme will run for a period of **two years** from the date of LandsD's promulgation of the Practice Note for the Pilot Scheme on 15 March 2021. Eligible IBs reaching the premium assessment stage (i.e. by way of acceptance of provisional basic terms offer) before the close of the two-year duration will be covered. A duration of two years would on the one hand encourage IB owners to come forth with redevelopment proposals in a timely manner, and on the other hand allow a timely review of the Pilot Scheme having regard to its efficacy in speeding up IB redevelopment and other experiences gained.

Different rates for different regions

12. To keep the Pilot Scheme simple yet pragmatic, we propose setting standard rates for the following five broad regions:

- (a) Hong Kong Island;
- (b) Kowloon East;
- (c) Kowloon West;
- (d) New Territories South; and
- (e) New Territories North.

Delineation of the five broad regions is shown in **Appendix to Annex A**.

⁸ Under established practice, LandsD would first offer the terms and conditions of the lease modification (known as "provisional basic terms") to the applicant for the latter's acceptance. Once accepted, LandsD will commence land premium assessment based on the terms and conditions so accepted.

13. The proposed tiering above has taken into account empirical evidence suggesting broadly discernible differences in the premium payable among these regions. To avoid complicating the scheme, the Pilot Scheme does not further sub-divide the regions into smaller localities.

Different rates for different uses

14. Standard rates have been set for the **Before Use**, i.e. industrial/godown use, and two types of **After Uses**, namely: commercial/modern industrial use, and residential use. The standard rates for Before Use reflect the land value of lots on which pre-1987 IBs are generally located⁹. In other words, in line with the established practice, any unauthorised uses in the IBs have not been taken into account.

15. In general, the common types of After Uses after redevelopment of IBs are commercial use, modern industrial use (such as data processing centres, media production centres, which are normally not regarded as falling within “industrial/godown” use under the land lease) and residential use, depending on the zoning of the site under the Outline Zoning Plan (OZP)¹⁰. As residential developments generally command higher market values than commercial and modern industrial developments, a different set of standard rates is set for residential After Use. Meanwhile, as commercial developments and modern industrial developments are both modernised business uses of similar market values, these two After Uses share the same set of standard rates, for the sake of simplicity.

⁹ For IBs located on land whose lease is unrestricted in terms of uses permitted but carries restriction on other parameters, in case they apply for lease modification (mainly to seek an increase in development intensity), the same rate reflecting the value of an industrial/godown lot would apply for computing the premium payable under the standard rates approach.

¹⁰ In accordance with the established practice, LandsD will continue to designate the user restriction and development parameters in the modified lease with reference to uses and parameters permitted under the OZP. In the case where the site is zoned “Industrial” on the OZP, the permitted user in the modified lease will be updated into modern industrial use which are permitted under the OZP.

Level of standard rates

16. The standard rates, based on the above parameters, broadly reflect the variations in the land value of IBs across different regions as well as the land value of different uses upon redevelopment. The level of the rates (see Annex A with examples illustrating the land premium calculation) have been set by professional valuers in LandsD, with reference to market data, including results of land sales by the Government and by the private sector, land premium for lease modification cases, and having regard to the relativity of the sale prices of the different types of completed developments. Given the relatively short duration of the Pilot Scheme and to provide upfront certainty for landowners to plan ahead, no adjustment will be made to the rates during the two-year period.

17. In line with the established practice, the premium chargeable at standard rates will also be the difference between the After Value and Before Value. Under the standard rates approach, the two values will be computed by multiplying the standard rate(s) of the respective use(s) by the respective GFA(s). This framework will be able to reflect both the change in use and the change in development intensity of the lease modification. It is capable of catering for both scenarios with GFA loss and with GFA gain after lease modification. This framework is similar to the practice in other jurisdictions which charge similar land transactions at standard rates, e.g. Singapore.

Implementation

18. The Pilot Scheme will be launched by LandsD by way of a Practice Note to be issued on 15 March 2021. As a transitional arrangement, applicants of eligible cases which have entered into the premium assessment stage (i.e. already accepted the provisional basic terms offer), but yet to accept the binding premium offer from LandsD, will be allowed to switch to the “standard rates” route **once** without paying additional administrative fees. For cases which have already accepted the binding premium offer and hence paid 10% of the land premium as deposit but pending execution of the lease modification, their cases should be handled in accordance with the binding contract already entered into¹¹.

¹¹ In accordance with the terms of the said binding contract, upon acceptance of the binding premium offer, but pending execution of the lease modification, if the landowner wishes to unwind the accepted premium offer so as to go for the “standard rates” route, it would need to apply afresh and make fresh payment for administrative fee, and the 10% deposit already paid will be forfeited.

IMPLICATIONS

19. The Pilot Scheme has economic, financial and civil service, environmental, sustainability and family implications as set out in **Annex C**. The Pilot Scheme has no legal, productivity or gender implication, and is in conformity with the Basic Law, including the provisions concerning human rights.

PUBLIC CONSULTATION

20. Since the announcement in the Chief Executive's Policy Address (PA) in November 2020, we have been communicating with stakeholders in various contexts. The Land and Development Advisory Committee was consulted on development-related PA initiatives on 26 November 2020, and members welcomed the implementation of the initiative to expedite lease modification for redevelopment of IBs. We also met with representatives from the Hong Kong Institute of Surveyors after the PA to exchange views on possible directions for the initiative.

PUBLICITY

21. A press release will be issued on the same day as this Legislative Council Brief. LandsD will upload the Practice Note for the Pilot Scheme to its website on 15 March 2021. Briefings will be arranged for the industry for introducing the Pilot Scheme.

ENQUIRIES

22. Enquiries relating to this brief can be directed to Miss Polly Chong, Principal Assistant Secretary for Development (Planning and Lands) at 3509 8830.

Development Bureau
4 March 2021

Level of Standard Rates and computation examples**Level of standard rates**¹

Region ²	Before Use	After Use	
	Industrial/ godown	Commercial/ modern industrial	Residential
Hong Kong Island	\$40,000/m ²	\$75,000/m ²	\$130,000/m ²
Kowloon East	\$40,000/m ²	\$65,000/m ²	\$100,000/m ²
Kowloon West	\$35,000/m ²	\$60,000/m ²	\$110,000/m ²
New Territories South	\$35,000/m ²	\$50,000/m ²	\$75,000/m ²
New Territories North	\$20,000/m ²	\$30,000/m ²	\$55,000/m ²

¹ Given the relatively short duration of the Pilot Scheme and to provide upfront certainty for landowners to plan ahead, no adjustment will be made to the rates during the two-year period.

² Delineation of the five broad regions is shown in **Appendix** to this Annex.

Computation examples

Case A – With reduction of GFA upon redevelopment

Case background

Region	Hong Kong Island
Before GFA	Industrial/godown: 8,000 m ²
After GFA	Residential: 6,000 m ²

Premium assessment

Based on the table of standard rates, the Standard Rate for the Before Use is \$40,000/m², and the Standard Rate for the After Use is \$130,000/m².

$$\begin{aligned} \text{Premium payable} &= \text{Standard Rate}_{\text{After Use}} \times \text{After GFA} \\ &\quad - \text{Standard Rate}_{\text{Before Use}} \times \text{Before GFA} \\ &= \$130,000/\text{m}^2 \times 6,000 \text{ m}^2 \\ &\quad - \$40,000/\text{m}^2 \times 8,000 \text{ m}^2 \\ &= \$780 \text{ million} - \$320 \text{ million} \\ &= \mathbf{\$460 \text{ million}} \end{aligned}$$

Case B – No change in GFA upon redevelopment

Case background

Region	Kowloon East
Before GFA	Industrial/godown: 12,000 m ²
After GFA	Commercial/modern industrial: 12,000 m ²

Premium assessment

Based on the table of standard rates, the Standard Rate for the Before Use is \$40,000/m², and the Standard Rate for the After Use is \$65,000/m².

$$\begin{aligned}\text{Premium payable} &= \text{Standard Rate}_{\text{After Use}} \times \text{After GFA} \\ &\quad - \text{Standard Rate}_{\text{Before Use}} \times \text{Before GFA} \\ &= \$65,000/\text{m}^2 \times 12,000 \text{ m}^2 \\ &\quad - \$40,000/\text{m}^2 \times 12,000 \text{ m}^2 \\ &= \$780 \text{ million} - \$480 \text{ million} \\ &= \mathbf{\$300 \text{ million}}\end{aligned}$$

Case C – With increase of GFA upon redevelopment

Case background

Region	New Territories South
Before GFA	Industrial/godown: 10,000 m ²
After GFA	Commercial/modern industrial: 18,000 m ²

Premium assessment

Based on the table of standard rates, the Standard Rate for the Before Use is \$35,000/m², and the Standard Rate for the After Use is \$50,000/m².

$$\begin{aligned} \text{Premium payable} &= \text{Standard Rate}_{\text{After Use}} \times \text{After GFA} \\ &\quad - \text{Standard Rate}_{\text{Before Use}} \times \text{Before GFA} \\ &= \$50,000/\text{m}^2 \times 18,000 \text{ m}^2 \\ &\quad - \$35,000/\text{m}^2 \times 10,000 \text{ m}^2 \\ &= \$900 \text{ million} - \$350 \text{ million} \\ &= \mathbf{\$550 \text{ million}} \end{aligned}$$

Measures under the 2010 and 2018 IB Revitalisation Schemes

Redevelopment

2010 IB Revitalisation Scheme	2018 IB Revitalisation Scheme
<ul style="list-style-type: none">- Land premium assessed based on the optimal use and proposed development density (i.e. pay for what you build)¹- allowing owners to opt for payment of 80% of lease modification premium by annual instalments up to five years at a fixed rate of interest, if the premium exceeded \$20 million- no restrictions on building age- non-industrial zones	<ul style="list-style-type: none">- No land premium related measure under package announced for the 2018 scheme
-	<ul style="list-style-type: none">- subject to approval of the Town Planning Board on a case-by-case basis and the maximum non-domestic plot ratio (PR) allowed under the Building (Planning) Regulations, allowing relaxation of maximum permissible PR by 20% to incentivise redevelopment of pre-1987 IBs for sites located in non-residential zones² (i.e. in “C”, “OU(B) and “I” zones) of the Main Urban Areas and New Towns. The approved cases are required to have their lease modification (if any) executed within three years from the date of Town Planning Board’s approval of the planning application.

¹ This is a relaxation over the established practice where LandsD would designate the user restriction and development parameters in the modified lease with reference to the uses and parameters permitted under the OZP.

² For IBs located in “Residential” zones, a similar measure for 20% increase in domestic plot ratio has been implemented since 2014.

Wholesale Conversion

2010 IB Revitalisation Scheme	2018 IB Revitalisation Scheme
<ul style="list-style-type: none"> - nil waiver fee - for IBs aged 15 years or above - in non-residential zones, namely: “OU(B)”, “C” or “I” zones 	<ul style="list-style-type: none"> - nil waiver fee - for IBs aged 15 years or above - in non-residential zones, namely: “OU(B)”, “C” or “I” zones - in return, 10% of the converted floor space to be designated by owners for specific uses prescribed by Government after the conversion
<p style="text-align: center;">-</p>	<p>Transitional housing</p> <ul style="list-style-type: none"> - facilitating proposals from the community for providing transitional housing in portions or entire blocks of IBs (without any age limit) located in non-industrial zones, namely: “C”, “CDA”, “OU(B)” and “R” zones, after wholesale conversion into non-industrial uses, by exercising flexibility in the application of planning, land lease and building design requirements, including charging a nil waiver fee for this specific use of transitional housing

Permitting Non-industrial Uses in Existing Buildings Without Wholesale Conversion

2010 IB Revitalisation Scheme	2018 IB Revitalisation Scheme
-	<ul style="list-style-type: none"> - in respect of individual units at existing IBs, relaxing the waiver application policy to permit uses for the arts and cultural sectors, creative industries, and innovation and technology sectors in an orderly manner so long as such uses are permitted under the planning regime in the first place - broadening the permissible uses of buffer floors, with due regard to public safety, to cover (among other permitted uses at present) “telecommunications exchange centres” and “computer/data processing centres”, to facilitate conversion of lower floors of some IBs into non-industrial uses - promulgating a broader definition for “godown” uses under the land lease, covering “cargo handling and forwarding operation” and “recyclable collection centre” uses

Implications of the Pilot Scheme

Economic Implications

The Pilot Scheme would provide the transparency on land premium payable in advance and / or expedite the process for the redevelopment of existing IBs, though the attractiveness of the Scheme to the owners of eligible IBs may also hinge on the relativity between the standard rates (which are fixed over the two-year period) and the prevailing market prices. This may help attract more applications and if so, in turn increase the commercial and residential floor space supply for meeting the socio-economic needs of Hong Kong.

Financial and Civil Service Implications

2. Individual applications opting for land premium assessment at standard rates may end up paying less land premium as compared to that under conventional land premium assessment approach. However, a reasonable set of standard rates might induce more IB owners to apply for IB redevelopment in overall terms, including those which might otherwise not come forward, and the overall financial implications to the Government cannot be ascertained. The Lands Department will absorb any extra workload caused by an increase in lease modification applications under the scheme.

Environmental Implications

3. Whilst redevelopment of IBs may provide opportunities to ease or eliminate some existing interface problems between industrial and non-industrial use, increase in development intensity upon redevelopment in some cases may add some burdens on the environmental infrastructures. The speedier redevelopment of IBs may also generate construction waste. The environmental implications will be dealt with in accordance with the relevant environmental legislation, standards and guidelines.

Sustainability Implications

4. The Pilot Scheme would help facilitate better use of valuable land resources to meet the housing, economic and social development needs and inject vibrancy into former industrial areas.

Family Implications

5. The Pilot Scheme would increase land supply for residential use to help meet the keen demand for housing space in Hong Kong, and would be conducive to promoting better living environment and family harmony in society in general.