A Proposal for

TASK FORCE ON LAND SUPPLY

Further Discussions on Tapping into the Potential of Private Land

Prepared by

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PURPOSE

In response to the discussion paper for the Task Force on Land Supply about tapping into potential of private land, dated December 9, 2017, the Ronald Coase Centre for Property Rights Research at HKU proposes a new public-private-partnership approach entitled “land readjustment” to speed up land development on agricultural land in the New Territories.

LAND READJUSTMENT

1. Land readjustment (LR) has been promoted by the United Nations and the World Bank aiming to release privately owned lands in the urban fringe for city expansion. It has been implemented as a policy in Germany, Spain, Israel, Turkey, Australia, Japan and South Korea. A number of development projects in the US, China, India, Nepal, Indonesia and Taiwan have also applied the concept for land assembly.

2. LR refers to the mechanism whereby private land owners voluntarily contribute their land parcels, usually irregular in shape and uncoordinated for future development, to the government. In return, after comprehensive planning efforts, they receive replotted sites of higher value in the vicinity. The replotted land parcels are usually smaller in size because a portion of the land will be used for public facilities such as roads, infrastructure, parks, affordable housing and other purposes.

(Sources: Walters 2016)
3. Conceptually, LR is to create marriage value for underutilized land parcels, and then redistribute the gains to major stakeholders including the landowners, original communities and society at large. It aims at and leads to win-win-win situations. LR is underpinned by robust theories in property rights and institutional design. There is a large body of literature documenting the remarkable experiences of LR. For instance, almost all the new urban land in Spain since the 1980s was developed through LR. About 370,000 ha of urban land in Japan was created by LR. In Seoul, LR has contributed around 14,600 ha of urban land since the 1930s.

4. Potentially, LR could unlock more than 1,000 hectares of privately owned land in the NT. Referencing the Outline Zoning Plan of Hung Shui Kiu, LR may contribute more than 300,000 new housing units in the NT, and hundreds of billions of dollars in land premiums to the Government. With a careful institutional design, LR can be a short-to-medium term measure to unleash land supply in HK.

5. By nature, LR is a public-private-partnership model. Representing public interests, the government seeks to facilitate land exchange, land use planning, essential infrastructure, environmental protection, heritage conservation and other provisions that benefit society as a whole, such as public housing and territory-wide facilities. The private parties contribute capital, know-how, understanding of any culturally valuable elements to be preserved. The shared aim is to make the new communities better places to live in for a sustainable future Hong Kong.

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1 In economics, LR can be construed as a Coasean bargaining (see Coase 1960) process. In a management context, major stakeholders of LR are playing a co-operation game (see Brandenburger and Nalebuff 1996).
2 See Hong and Needham 2007; Ingram and Hong 2012; Munoz and Van der Krabben, forthcoming; Van der Krabben and Lenferink, forthcoming; Van der Krabben and Needham 2008; Zamorano and Gielen 2017; and Li and Li 2007.
3 See Zamorano and Gielen 2017.
4 See Kim 2017.
5 Figure estimated by the discussion paper for the Task Force on Land Supply dated December 19, 2017.
6 S/HSK/1, gazetted on May 26, 2017. Plot ratios of residential development zonings in the OZP range from 3.8 to 6.5 for R(A) zonings; from 1.26 to 3.5 for R(B) zonings; 0.4 for R(C) zoning; and 4.5 for OU zoning. Majority of lands are with plot ratios of 2.5 or above. Take a plot ratio of the low side at 2.5 and a reduction rate of 40%, 1,000 ha of land will produce 150 million sq ft of floor spaces. Take the average flat size of 500 sq ft, it means 300,000 residential units could be produced from privately owned agricultural land in the NT.
6. LR serves as an alternative to conventional land assembly methods such as massive land taking[^7], which may be prone to disputes[^8], severe criticism[^9] and opposition. It enables all stakeholders to share the fruits of economic development. LR also takes into account the interests of minorities such as non-indigenous villagers, which could be safeguarded through more flexible arrangements, such as off-site resettlement or additional ex-gratia compensation etc.

7. In many countries, LR is designed as a value capture instrument to finance public infrastructure and facilities. In Hong Kong’s context, not only can LR save the public purse, it also unlocks the development potential of privately owned agricultural land in the NT. Adaptation will be required to make it operable in a high density, vertically expanding, complex property right structured and dynamic city. We contend that if LR can be implemented in countries with even more complicated historical, political and landownership settings like Israel[^10], there is no compelling reason to believe that it should not be considered in Hong Kong.

**MAJOR CONSIDERATIONS**

8. Based on international experiences, LR can be carried out through various models. Germany practices a top-down active model in which the government acts as the project initiator and land taking can be a last resort. In Japan, a bottom-up passive model is an option that, with the consent of at least two-thirds of landowners, allows private parties to be the project initiators. While an active model can be considered as a long-term solution, a passive model appears to be more responsive as far as a short-to-medium term solution is concerned. Nevertheless, the minimum thresholds to initiate a LR project can be a point for discussion.

[^7]: Known as resumption or compulsory purchase in HK and the UK; eminent domain in the US; expropriation in Australia. The New Development Areas (NDAs) developments in HK including the North East New Territories NDAs adopt this approach.
[^8]: In the US, although the State Supreme Court in Kelo vs City of New London (2005) ruled no violation of federal constitution on private property rights for land taking that entails public purposes, subsequently it led to legislation in 44 states forbidding the use of eminent domain for economic development.
[^9]: On Feb 22, 2018, Mr. Kenneth Lau Ip Keung, Chairman of Heung Yee Kuk, blamed the Government for paying far below market value compensation for resumption of rural land. He argued that the Government did not share the fruits of city development with indigenous villagers (see *The Standard*, Feb 23, 2018).
9. The LR model should operate administratively under the existing land management system. It should avoid any prolonged legislative process. On the one hand, while it honors the protection of private property rights under the Basic Law, on the other hand the sovereignty and authority of the HKSAR Government as the de jure land manager in Hong Kong will be respected.

10. A coordination unit can be setup by the public authority to facilitate LR exercises. A good reference for the setup of this unit is the Energizing Kowloon East Office. The project initiators will prepare the LR plans with the help of the coordination unit, which should strike a balance between the interests of the landowners and those of the general public. Since the LR model must fit into the existing development control system in HK, if there are statutory requirements the LR plans may form the blueprints of the master layout plans (MLP) to be approved by the Town Planning Board (TPB). This should save considerable time in the planning application process.

11. In the past, missing owners, speculative holdouts and communal interests collectively owned by the indigenous villagers were the major challenges to carrying out comprehensive development in the NT. The LR model in HK should enable the public authority to take custody of those fair interests without the need to proceed to land taking.

12. In cases where preservation of tangible or intangible heritage elements are needed, the LR model should enable the stakeholders to raise their concerns. TPB and the public authority should act as the gatekeepers.

13. To incentivize the minority landowners to take part in LR, two proposals can be considered. First, the size of land lots of the minority owners after readjustment can remain those of the status quo, or even increase marginally. Second, all replotted land can be connected to roads such that future development can meet all requirements of the Buildings Ordinance. Bonus land parcels to minority landowners may even be given for other considerations such as the preservation of heritage and community. To realize the bonus, in cases where the replotted lands are intended for village type house development, houses higher than 3 storeys may be permitted.

14. While the allocation of replotted lands to minority landowners may cause certain technical issues such as choices of location etc., the majority landowners and the public authority should assure that the LR plan is attractive to them, or else the LR proposal may fall through. In addition, the minority landowners should be encouraged to make arrangement for further LR among themselves or,
for a future option in the completed project, or other collaborative arrangements, tag along with the majority landowners by entrusting their minority development rights to them.

15. For missing owners or those who prefer a simplistic approach to LR, a development entitlement scheme that was previously used for new town development can be considered. Minority landowners may exchange their lands for a redemption certificate of a square-footage determined in para 13 above. A trust can be setup by the public authority to hold the beneficial interests or redemption certificates of the missing owners. The certificates would be freely transferrable in the market for future land purchase or exchange exercises.

16. The sizes of the replotted land parcels for the majority landowners will depend on the reduction rates, i.e. the levy for public infrastructure and facilities etc., adopted in the LR model. Reduction rates in overseas countries vary widely, but usually range from 30 to 40%. Two key considerations, however, should be taken into account to determine the reduction rate in HK. First, compared to overseas countries, generally there are less surface roads in massive housing development type projects in HK. Second, the reduction rate in overseas countries is levied for value capture purpose, while in HK the majority landowners are still subject to premium assessment after readjustment. Thus, a suitable reduction rate to be adopted in HK can be discussed, which should not sacrifice the benefits of comprehensive planning, or defeat the purpose of LR – redistribute the gains among all stakeholders.

17. For illustrative purposes, assuming there are 1,000 ha of privately owned agricultural land taking part in LR, if a 40% reduction rate is to be implemented in HK, it means there will be about 400 ha of land available for public housing, recreational and other facilities to benefit the general public. Assuming one-quarter of that land, i.e. 100 ha, is to be used for public rental housing development, it will create about 76,000 additional housing units, which could almost absorb half of the public housing application queue as that stood in December 2017!

Another key consideration of the LR model is the premium for lease modification. While the existing premium assessment mechanism for land exchange can be applied for the replotted land parcels, a more facilitating approach can be adopted given the fact that a certain reduction rate has been levied to the majority landowners already. Premium assessment should be

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1 Estimations based on Hung Fuk Estate in Hung Shui Kiu where 4,900 units are produced from a site of 6.4ha.
prudent but flexible and could be charged in cash or in kind. Any premium in kind could be in terms of developer obligations such as provisions of public housing, roads, schools and public recreational facilities.

18. Based on overseas experience, LR is all about arriving at optimal “trade-offs” among stakeholders over the marriage value\(^{12}\). Hence, successful LR schemes require among all stakeholders open-mindedness, collaboration and, in some cases, innovative ideas. Some pre-LR experimental\(^{13}\) or consultative sessions conducted by independent bodies or professionals may ease the bargaining process. Mediation or even arbitration mechanisms can be put in place if necessary.

19. Conceptually the public authority can cluster government land and land owned by the minority together as a single entity, and then negotiate with the majority landowners as in a typical private land exchange application. In other words, the land exchange exercises carried out in HK for decades can actually be construed as LR. The proposal made in this paper is merely adding one more dimension to the system – the minority landowners.

20. We propose that LR is another alternative to the current land assembly methods such as private acquisition and land taking for NDAs etc. It is not intended to replace any existing mechanism. A passive model based on voluntary initiatives from the private sector in conjunction with a facilitating role for the public authority will release considerable privately owned agricultural lands in the NT for housing development in the short-to-medium term. Whether or not an active LR model led by the public sector should be introduced in the long term, which may entail legislation, can be reviewed further.

**Team Members**

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\(^{12}\) In economics, it is about Pareto Optimality which suggests the parties are better off while no one will be worse off. Hick-Kaldor’s efficiency further suggests that if there exists a mechanism in which the worse off parties can be compensated by the better off ones, optimality can be arrived at. This paper proposes that LR is the mechanism to achieve Hick-Kaldor efficiency.

\(^{13}\) One of our team members, Professor Van der Krabben, has extensive experience in conducting experimental studies for LR and transit-oriented-development in Europe and China.
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