

**Report of the
Working Group on
Regulation of Estate Agents
Planning, Environment and Lands Branch
August 1994**

This is a Consultative Document.
The Working Group welcomes any views or
suggestions you may have on this Report.
These should be sent to:

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before 10 October 1994.

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EXECUTIVE SUMMARY

Malpractices

1. We note that although the present system in property transaction has a number of advantages such as speediness and cost-effectiveness, it is susceptible to abuse by unscrupulous estate agents. Common malpractices are usually committed through the following means :

- a) engagement of confirmors;
- b) double agency;
- c) illegal commissions;
- d) misrepresentation; and
- e) unfair Inspection Forms and Provisional Sale and Purchase Agreement.

2. We see that the main problem in the present system lies in the ambiguity of the role and obligations of estate agents.

Interim measures

3. The Working Group recommends that the following interim measures should be taken before regulation by legislation is introduced :

a) the Hong Kong Real Estate Agencies Association and the Society of Hong Kong Real Estate Agents, in consultation with the Consumer Council, the ICAC and the Law Society, should draw up for use by their members and promotion in the trade :

- a code of practice and practising guidelines; and

- standard documents which include a statement to disclose interest of the agent in the transactions.

b) the two trade associations should encourage estate agents to provide basic information to prospective purchasers such as the size, age and the permitted use of the property and the Crown lease tenure;

c) the ICAC and the Consumer Council should continue their publicity efforts to increase public awareness of common malpractices and to advise on how to avoid them; and

d) the two trade associations should take the initiative to promote corruption prevention in the trade in conjunction with the ICAC.

Positive Licensing

4 We recommend that a positive licensing system should be set up to regulate the trade. A self-financing regulatory authority should be established by legislation for licensing and enforcement.

Role and obligations

5. An estate agent should include any individual or corporation who carries out the business of an estate agent regardless of whether or not he receives any consideration.

6. The present practice of estate agents playing the role of an agent for both the vendor and purchaser has been long established and widely accepted by the public. We see practical advantages in this practice. We therefore do not recommend changing it.

7. In order to avoid any abuse of an estate agent's role specially as an agent for both parties, we recommend that the obligations of estate agents should be stipulated in law. They should include the obligatory disclosure of essential information as well as the agent's interest to his clients.

Categories of licences

8. There should be three categories of licences with different requirements applicable to individual estate agents, corporations and front-line estate salespersons. The objective of the licensing requirements is to ensure that an estate agent meets certain minimum standards of competence and knowledge.

9. An estate salesperson will work as an employee of an estate agent and under the latter's supervision. The licensing requirements for salespersons should be kept to the minimum so that they would not become an unnecessary barrier against entry to the trade nor would they cause problems in recruiting new staff.

10. The proposed regulatory system should apply to all individuals and corporations engaged in the sale of properties irrespective of where the properties are located.

Estate Agents Authority

11. We propose that the regulatory authority should be called the Estate Agents Authority and its Chinese name should be " in Chinese name".

12. It is important that the regulatory authority should command respect among the public as an impartial body that takes account of the interests of the trade and the consumer as well as the community in general. We recommend that the authority should be composed of members from the trade, related professions and the community. The authority should be included in the Schedule of Public Bodies in the Prevention of Bribery Ordinance.

13. The regulatory authority should have powers, subject to Government approval, to determine licensing requirements and prescribe rules of conduct and practice. It should also have powers to take disciplinary action against estate agents for breach of obligations and rules and to determine disputes over commissions and fees between an agent and his client.

14. It is estimated that the regulatory authority would require a staff of about 18 persons at an operating cost of about \$8 million in the first year of operation.

Written agreement

15. Many disputes and allegations of malpractice have arisen from the common practice of relying on verbal instructions or agreements. To rectify the situation, we recommend that an estate agent should have a prior written agency agreement between him and his client. The written agreement should contain essential items such as the agreed commission and the agent's other interests in the transaction. Estate agents and customers should be given ample time to adapt to the new requirement.

Commission

16. We do not recommend prescribing a standard scale of commission because such a scale tends to protect inefficiency and inferior services at the expense of those estate agents who provide efficient and good services.

Supply of information

17. We recommend that an estate agent should have in his possession certain essential information about the property before he introduces a property to a prospective purchaser. The estate agent can seek information from the owner, but he should be reasonably satisfied that the information is correct. This should include prima facie evidence of ownership, floor area, year of completion of the building, permitted use, land tenure and the property owner's statement about unauthorised alteration works.

Advertising

18. The regulatory authority should prescribe rules to govern advertising by estate agents to prevent false or inaccurate property advertisements.

Trust account

19. A trust money accounting system should be set up so that all trust money held by an agent can be accounted for at all times.

Indemnity

20. We do not see a need for a compensation fund. However, the regulatory authority should consider whether or not it should prescribe certain indemnity requirements to be met by estate agents.

Appeal panel

21. Government should appoint an independent appeal panel to deal with appeals against the regulatory authority's decisions.

Transitional arrangements

22. Transitional arrangements are necessary to bring estate agents within the regulatory system within a reasonable period of time. These arrangements should have due regard to practical considerations. They should not cause undue disruptions and anxieties in the trade as well as service to the public, or force many people out of work.

23. We recommend that the regulatory authority should invite all practising agents and salespersons to apply to it for a licence. A provisional licence will be issued initially.

24. The regulatory authority should then announce a date from which anyone operating as an estate agent or a salesperson must hold a licence first.

25. While their applications are being processed, estate agents and salespersons can continue to operate with a provisional licence. The licensing requirements for the regular licence should not be so stringent as to disqualify unnecessarily many practising agents. Applicants should be given adequate opportunities to meet the requirements.

Chapter I INTRODUCTION

1.1 The Working Group on the Regulation of Estate Agents was set up by Government in November 1993. Its terms of reference are :

- a) to assess the existing system and to identify problems;
- b) to recommend remedies to the problems identified;
- c) to draw up proposals for a regulatory system;

- d) to recommend a legislative framework for the regulatory system; and
- e) to examine the resource and enforcement implications.

1.2 The Working Group's membership is as follows :

Mr Leo KWAN Wing-wah,

- Deputy Secretary (Housing Policy),
- Planning, Environment and Lands Branch (Chairman)

Mr Michael CHOI Ngai-min,

- Representative of the Society of Hong Kong Real Estate Agents

Mr Joseph LEUNG Wai-kan,

- Representative of the Hong Kong Real Estate Agencies Association

Mr LIU Sing-cheong,

- Representative of the Hong Kong Institute of Surveyors

Mr Anthony CHOW Wing-kin,

- Representative of the Law Society of Hong Kong

Mr Charles WONG Kit-hung,

- Centre for Continuing Education, City Polytechnic of Hong Kong

Mrs Pamela CHAN Wong Shui,

- Representative of the Consumer Council

Mr CHAN Kam-pui,

- Representative of the Independent Commission Against Corruption

Mr William SHIU Wai-chuen,

- Principal Assistant Secretary (Housing Policy),
- Planning, Environment and Lands Branch (Secretary)

1.3 The Working Group has held nine meetings since its inception in November 1993.

1.4 In drawing up proposals for a regulatory system for estate agents in Hong Kong, we have studied the operation of real estate agents in Hong Kong. We have also made reference to regulatory systems for estate agents in other countries such as Australia, Canada, the United States of America and the United Kingdom. Regulatory experience in other local trades has also been taken account of as far as practicable. The public has been informed of our work through the press.

Chapter 2

THE PRESENT POSITION

Background

2.1 In the past few years, there have been a marked increase in the number of estate agencies in Hong Kong. According to the latest records of the Census and Statistics Department, there are about 4,730 establishments, employing over 15,500 people in the trade. Most of these establishments are fairly small companies run by people without formal qualifications in the property field.

2.2 The primary function of most estate agents in Hong Kong is to bring together vendors and prospective purchasers, lessors and prospective tenants. They accompany their clients to visit target flats and mediate between the two principal parties in price negotiations. Where an agreement is reached, an agent prepares a Provisional Sale and Purchase Agreement (PSPA) to be signed by the vendor and purchaser. The PSPA will then be passed to the respective solicitors of the vendor and purchaser for preparation of the formal Sale & Purchase Agreement. The estate agent is paid a commission for his service. In property transactions involving very large amounts of money, it is not uncommon that different agents are appointed by the vendor and the purchaser.

2.3 There are a number of estate agency associations but only two have a territory-wide coverage, namely the Hong Kong Real Estate Agencies Association (HKREAA) and the Society of Hong Kong Real Estate Agents (SHKREA), established in late 1991 and early 1992 respectively. In June 1994, about 2,600 practising agents were employed by corporations which were registered members of the SHKREA, whilst the membership of HKREAA was about 500, with roughly 3,000 practising agents affiliated with the association. The two associations have advocated to enhance the professional and ethical standard, encourage self regulation, improve the image of the trade and promote education and training for their members. Some associations have prepared standardized documents like tenancy agreements and provisional agreements for sale and purchase, drawn up codes of conduct for members and set up complaint mechanisms.

Existing legislative controls

2.4 There is at present no specific legislation on regulation of estate agents. However, certain ordinances may affect estate agents. For example, the Misrepresentation Ordinance enables a person to claim damages against an agent for misrepresentation. Under the Legal Practitioners Ordinance, a solicitor is prohibited from sharing fees with any person who is not a qualified solicitor, thereby preventing an agent from obtaining a commission for referring a transaction to a solicitor.

Complaints

2.5 At present, the Consumer Council, the Police and the ICAC deal with complaints on malpractice, fraud or corruption of estate agents involved in purchases and leasing of properties. The nature of complaints received by the Consumer Council and the ICAC in the past four years are set out in the tables below :

Table 1
complaints received by the Consumer Council
concerning estate agents

	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>
Sales Tactics	75	200	85	112
Non-Delivery	7	4	1	6
Overcharging	5	4	11	4
Quality of Services	19	16	8	12
Others	9	24	13	21
Total	115	248	118	155

Table 2
Corruption reports received by ICAC concerning estate agencies

	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>
Unauthorised commissions	19	18	28	55
Misrepresentation of price of property	2	25	15	18
Corruption involving estate agencies and staff of property developers	19	21	4	18
Corruption involving estate agencies and staff of solicitor firms	6	8	4	15
Corruption involving estate agencies and bank staff	2	4	-	2
Corruption involving estate agencies and management offices	2	2	1	4
Others	1	2	4	10
Total	51	80	56	122

Although the complaint figures may appear small when compared with the volume of property transactions, we believe that the extent of the problem is not accurately reflected by statistics as cases of malpractices may not be fully detected or reported.

The need for a regulatory system

2.6 Since 1990 there has been a solid body of public opinion advocating regulation of estate agents. There is a need to protect consumers' interests in property deals since a property purchase invariably involves a large amount of money and is likely to be the most significant purchase ever made by an average person. The professional competence and proper conduct of estate agents must be ensured and there must be a means for vendors and purchasers to seek redress against defaulting agents. In June 1993, Leg Co passed a motion urging Government to introduce legislation to regulate the operation of real estate agents through a licensing system.

Government's views

2.7 Government agrees in principle that legislation should be introduced to regulate estate agents. However, there are many aspects which require careful deliberations before a suitable proposal for a regulatory system can be drawn up. For instance, the introduction of a regulatory system should not cause undue disruptions to the trade which serves a large number of consumers and plays an important role in property transactions. It should not cause hardship to those estate agents who are honest and competent. If it is thought that a system of licensing should be introduced, then sufficient time should be allowed for existing and prospective agents to obtain the necessary qualifications; the system should not result in a shortfall of estate agents such that both the market and consumers will suffer from the consequences.

Chapter 3 **MALPRACTICES**

3.1 Malpractices in property transactions involving estate agents are usually committed through the following means:-

- a) engagement of confirmors
- b) double agency
- c) illegal commissions
- d) misrepresentation
- e) unfair Inspection Forms and PSPA

Engagement of confirmors

3.2 By introducing a "confirmor"* as an intermediary party to the transactions, an estate agent can sever contact between the seller and the buyer to enable the confirmor to pocket the difference between the higher offering price of the buyer and the lower asking price of the seller. In some cases, the confirmor is a relative or close associate of the estate agent who would first arrange the vendor to enter into a PSPA with the confirmor at an agreed price. The agent would then arrange the end purchaser who is willing to pay a higher price to enter into a second PSPA with the confirmor. Neither the vendor nor the end purchaser sees the other's PSPA.

3.3 As buying a property and selling it at a profit by the confirmor is not in itself illegal, the vendor and purchaser have no remedy unless deception or dishonesty on the part of the estate agent can be proved. Under the common law of agency, an agent owes a duty of absolute faith to his principal and is obliged to disclose any conflict of interest and not to make secret profits. Breach of a fiduciary duty in an agency relationship enables the principal to set aside the transaction and claim any profits and commissions acquired by the agent. Nevertheless, in many cases, it is unclear whether an estate agent is acting as an agent for the vendor in the legal sense or is just a middleman. In his latter capacity, an estate agent may have no legal obligation to protect the interests of his client even though his unscrupulous acts can be morally wrong.

Double agency

3.4 In Hong Kong, the primary functions of estate agents are to bring together vendors and prospective purchasers and facilitate their transactions. Their role as an agent for both parties gives rise to opportunities for unscrupulous estate agents to abuse their position. Cases of estate agents sharing profits with sellers at the expense of buyers or vice versa have been reported.

3.5 It may be arguable that estate agents are only middlemen and therefore may only have limited obligation and no fiduciary duty to vendors and purchasers. Consequently, they have no obligation to avoid conflict of interests and to disclose any personal interest which may affect the vendors or purchasers.

Illegal commissions

3.6 The malpractice of some employee estate agents may do harm to their employers. Common malpractices in this category include soliciting unauthorised commissions to facilitate the sale of a flat, pocketing the employer's commissions and conniving with clients to evade commissions due to the agency. An employee estate agent owes a fiduciary duty to his employer and should act for the interests of the latter in all property transactions. This fiduciary duty is clearly enshrined in the Employment Ordinance. An agent in breach of the duty is liable to prosecution.

3.7 An unscrupulous estate agent may refer his clients to a solicitor, a bank or an insurer in return for a commission not known to his clients. In some complaint cases, an estate agent unduly influences his clients to use the service of certain banks or solicitors with whom he has close connections.

3.8 Regarding acceptance of commissions as reward for referral of conveyancing business to banks and solicitors, it

will be an offence if the agent has not obtained prior permission from the purchaser. Moreover, a solicitor is forbidden under the Legal Practitioners Ordinance to share fees with any person who is not a qualified solicitor. Nonetheless, it is difficult to detect such corrupt practices of estate agents as it is often in the interest of parties concerned to conceal the payment of the illegal commission.

3.9 Most complaints in this category are related to breach of fiduciary duties which employee estate agents owe to their employers. As the present legislation already has provisions to cover this sort of malpractice, we have focused our attention on the prevention of corruption by employee estate agents.

Misrepresentation

3.10 Some estate agents conceal or fail to provide correct information about a property to prospective purchasers such as age, floor area, illegal alterations and ownership. According to complaint statistics of the Consumer Council, cases of estate agents exaggerating the size and understating the age of flats for sale are commonplace in Hong Kong. Misrepresentation of facts will induce prospective purchasers to make a wrong decision on the transaction. Having learnt the misrepresentation subsequently, the victim purchasers would have to face the dilemma of either proceeding with the transaction or forfeiting a substantial amount of initial deposit which has been paid upon signing the PSPA.

3.11 As the obligations of estate agents in Hong Kong are not clearly defined, there is at present neither control nor requirement as to the disclosure of information to prospective purchasers. The Misrepresentation ordinance cannot provide an effective remedy since description of flats are not normally set out in PSPAs.

Unfair Inspection Forms and PSPA

3.12 At present, the role and obligations of estate agents in a property transaction are not clearly spelt out, let alone their enforcement. To date, standardised Inspection Forms and PSPAs widely adopted by local estate agencies have yet to emerge. While many clauses in Inspection Forms and PSPAs are worded in favour of the agency, estate agents are not required to commit their obligations in these legally binding contracts. Most prospective purchasers do not have the necessary legal knowledge to identify the unfavourable clauses and inadequacies in these documents. As a result, unwary property purchasers may suffer from the unfair terms and conditions in these documents once they have signed them. Notwithstanding that most estate agents in Hong Kong are practising in an honest and scrupulous fashion, the lack of binding protective clauses in these contracts for prospective purchasers has engendered irresponsible acts of those unscrupulous agents. Over the years, the Consumer Council has received complaints from the public about the poor quality of service and irresponsible acts of some estate agents. In some complaint cases, the estate agents do not deserve commissions as they have failed to discharge their duties properly.

Conclusion

3.13 It is clear that the ambiguous role and obligations of estate agents is the main weakness in the present system that gives rise to the malpractices identified above. We shall therefore address these issues in the proposed legislative framework. We shall also recommend interim measures to help tackle the malpractices before a statutory regulatory system is in place.

Chapter 4 INTERIM MEASURES

4.1 It will take time to introduce legislation to regulate the trade so that the problems identified by us can be addressed effectively. In the meantime, we consider that some interim measures can be taken by the trade to tackle these problems. We have made recommendations on interim measures in this chapter.

Code of Ethics

4.2 We recommend that the HKREAA and SHKREA should draw up a code of ethics and practising guidelines in consultation with the ICAC and the Consumer Council and promote their use by the trade with a view to enhancing the service standard of estate agents.

Standard documents

4.3 We recommend that the two trade associations, in consultation with the Consumer Council, the ICAC and the Law Society, should review the present terms and conditions of Inspection Forms and PSPA and draw up standard documents for use by their members and other estate agents. The role and obligations of estate agents including the legal relationship between estate agents and their clients should be clearly spelt out in the new documents. Their terms should be fair to all parties concerned.

4.4 The standard documents should contain a clause that obliges estate agents to disclose their interests including profits or commissions to be earned by them. Making disclosure of interests a contractual obligation of estate agents will provide an effective safeguard against unscrupulous estate agents. Although these agents may refuse to sign a standard document with a disclosure clause, their so doing will alert their clients to possible malpractice.

4.5 The two associations should promote acceptance of the new standard documents by the trade. We know that use of standard documents can only be on a voluntary basis. However, we believe that given suitable promotion by the two associations, estate agents will find that it will be in their interest to use a standard document that their clients have confidence in.

4.6 We are pleased to note that the two trade associations, in consultation with the Consumer Council, the ICAC and the Law Society, are in the final stage of preparing a revised Inspection Form entitled Engagement Agreement for Inspection of Premises. They also intend to review the standard PSPA currently in use by the two trade associations as the next project.

Supply of basic information

4.7 We consider that estate agents should be obliged to disclose fully and correctly basic but essential information of the property to prospective purchasers. To this end, we recommend that the two trade associations should encourage estate agencies to do a Land Registry search for the properties they handle and to provide prospective buyer clients with basic information in writing about the property such as the age, size, permitted use and Crown lease tenure provided that such information is available. The Rating & Valuation Department and the Land Registry have agreed to assist the two trade associations in identifying the scope of information that can be extracted from official records.

4.8 We note that the two trade associations are investigating how to tackle practical difficulties encountered by estate agencies in relation to the provision of information and will make practical proposals to their members.

Education and publicity

4.9 We recommend that the ICAC and the Consumer Council should continue their publicity efforts to advise the public how to avoid the pitfalls in relation to unscrupulous practices of some estate agents. We note that the ICAC has publicised a pamphlet advising prospective vendors and purchasers how to prevent pocketing of profits by unscrupulous agents. Similar precautionary measures are also set out in the Property Guide published by the Consumer Council.

4.10 The ICAC has been promoting corruption prevention measures among estate agencies. Brochures highlighting common corrupt practices of some unscrupulous estate agents and suggesting remedial measures are circulated in the trade. Corruption prevention seminars for management staff of estate agencies are also organised. These efforts will be more effective if there is a greater commitment and more forthcoming cooperation from the trade. We recommend that :

a) the two trade associations should take the initiative to foster a scrupulous and honest corporate culture in the trade by organising seminars and courses for managers and employees of estate agencies respectively in conjunction with the ICAC;

b) the trade associations should take the lead to suggest effective and practical cleaning-up measures to safeguard the

integrity and image of the trade; and

c) the ICAC should continue to organise corruption prevention seminars for bank employees and solicitors.

Chapter 5 **OBJECTIVES AND OPTIONS**

Objectives

5.1 We consider that the objectives of the regulatory system should be:

(a) to define the role and obligations of estate agents;

(b) to ensure that the operation of estate agents meets certain specified standards of competence and knowledge and obligations to their clients;

(c) to provide sanction against estate agents who fail to comply with those standards of competence and knowledge and obligations;

(d) to provide an avenue of complaints to consumers who suffer from an estate agent's unsatisfactory services or malpractices; and

(e) to establish a regulatory body to monitor the operation of estate agents and to enforce measures to achieve objectives (b)-(d).

5.2 In recommending measures to achieve these objectives, we are guided by the following :

(a) the regulatory system should not significantly increase the costs and time of property transactions;

(b) the introduction of the regulatory system should not cause a serious shortfall in the supply of estate agents to meet the needs of the public;

(c) the regulatory system should allow free entry to the industry and avoid the creation of effective monopoly of the trade by large establishments; and

(d) the regulatory system should be fair and reasonable to all parties concerned.

Options

5.3 We have considered the pros and cons of various regulatory measures for estate agents in Hong Kong. We have made reference to examples of regulatory systems in some overseas countries : British Columbia in Canada, California in the USA, Victoria and New South Wales in Australia and the United Kingdom.

5.4 Broadly speaking, there are three options of regulatory measures for estate agents, namely, self regulation, negative licensing and positive licensing. The operating mechanism and the pros and cons for each option are set out below.

Self-regulation

5.5 This requires self-policing by the trade. A new Organisation representing all practising agents, say, an estate agents council, will be formed by amalgamating various trade associations in the industry. A practising estate agent must be a member of the council. The council will regulate member estate agents by means of a code of practice and occasional directives. Members who breach the rules of self regulation risk losing their membership and their right to practise. An advisory committee appointed by Government may have to be set up to advise on and monitor the operations of the council. The pros and cons of this option are set out below :-

5.6 Pros

- a) This regulatory measure can be implemented with minimal legislation.
- b) The council being the exclusive regulatory body with pooled resources from the trade can gain more recognition from practising agents and the public than various trade associations in isolation.
- c) Relatively low administrative costs need to be incurred as no licensing arrangements will be required.

5.7 Cons

- a) It will take time and a great deal of organisation to amalgamate existing trade associations to set up a council.
- b) The policing and enforcement by a council comprising representatives from the trade alone will lack credibility in the eyes of the public.
- c) As many practising estate agents in Hong Kong do not belong to any trade associations at present, the council will have a formidable task to boost its membership, educate the practitioners and impose regulations on them.
- d) This regulatory measure runs counter to prevailing public expectations. The public will be skeptical about the impartiality and independence of a council which lacks a balanced representation of the community.

Negative licensing

5.8 Under this regulatory measure, it is not necessary for an estate agent to apply for a license to practise. Government will be empowered by legislation to regulate the conduct of practising estate agents. The legislation will prescribe the obligations for estate agents to follow and specify what constitutes undesirable practices. Any estate agent breaching these provisions will not be permitted to practise. The pros and cons of this option are set out below :-

5.9 Pros

- a) This option creates no barrier for entry to the trade and encourages free competition.
- b) It incurs relatively low administrative costs as no licensing arrangement will be required.
- c) Compared with self-regulation, the more elaborate legislation will more effectively deter the malpractice of some unscrupulous agents.
- d) Enforcement by a body independent of the trade is likely to foster greater public confidence in the regulatory measure.

5.10 Cons

- a) It requires new legislation and additional resources for effective enforcement.
- b) This measure cannot prevent unqualified personnel from practising. Consumers will be at the mercy of incompetent practitioners who should have been barred from the trade. A minimum standard of service cannot be assured.
- c) As the default rate of practising agents under this option is expected to be relatively high, effective enforcement will be very costly.
- d) Compared with positive licensing, this measure is less effective and offers less protection to consumers. Investigations can only be made after consumers have suffered from unscrupulous practice of agents. Also, this measure will have little practical effect on unscrupulous estate agents who practise on a temporary basis.
- e) This option will unlikely win support of the public who would attack its passive nature.

Positive licensing

5.11 Under this option, all estate agents must obtain a licence in order to practise. To be eligible for a licence, applicants will be required to meet certain objective standards of competence by having certain relevant knowledge and working experience. A self-financing regulatory authority will be established by legislation to advise Government on regulatory matters, determine licensing requirements, deal with licensing, set standards of practice, inquire into alleged breaches of rules and regulations and impose penalties on defaulting agents. Members of the regulatory authority will be appointed by Government and its major policy decisions, e.g. licensing requirements, will be subject to Government approval. Government will monitor the operations of the regulatory authority and investigate criminal acts which are outside the purview of the authority. The pros and cons of this option are set out below :-

5.12 Pros

- a) This will be the most thorough means of regulating estate agents as it can effectively weed out dishonest, unscrupulous and incompetent practitioners.
- b) This regulatory measure will enhance the estate agents' level of competence thereby improving the standard of service provided by the trade.
- c) It provides an opportunity for the trade to raise their professional status and polish the image of the industry.
- d) Public interests will be taken into consideration by the regulatory authority by virtue of a balanced membership.
- e) This option will be most acceptable and credible to the public at large.

5.13 Cons

- a) Transitional arrangements in relation to licensing requirements are necessary. Practising agents need to be given time and avenue to acquire the necessary qualifications.
- b) Some estate agents who fail to meet a minimum standard of competence may be forced out of work.
- c) Government financial assistance to the authority may be required to fund its operation in the early stage of its inception.
- d) It requires relatively more resources to administer this option.

Other regulatory systems

5.14 We have studied the regulatory frameworks for other industries in Hong Kong. It is noted that travel agents in Hong Kong are subject to positive licensing. The Travel Agents Registry set up under the Trade and Industry Branch is empowered by legislation to administer licensing operations and inspect travel agents' accounts. Insurers operating in Hong Kong subject to supervision by the Insurance Authority under Insurance Companies Ordinance.

Recommendation

5.15 Having thoroughly considered the pros and cons of the various options of regulatory measures, we conclude and recommend that it would be in the best interest of the trade and the public to place estate agents under a positive licensing system. This will serve the purposes of ensuring minimum service standard and sanctioning incompetent and dishonest agents.

Chapter 6 ROLE AND OBLIGATIONS

6.1 Most of the problems identified in the present operation of estate agencies arise from the ambiguity of the role and obligations of estate agents. We believe that it is important to define the role and obligations of estate agents in the

legislation.

Definition of estate agents

6.2 We recommend that an estate agent should be defined as follows:

a) the business of an estate agent is

* selling, buying, exchanging, letting or taking on lease of or otherwise dealing with or disposing of; or

* negotiating for the sale, purchase, exchange, letting or taking on lease or any other dealing with or disposition of any real property on behalf of any other person;

b) any individual or corporation who carries on or holds himself out to the public as ready to undertake the business of an estate agent is an estate agent;

c) any individual or corporation within the definition of a) is an estate agent whether or not he carries on any other business, or obtains any consideration in a property transaction; and

d) someone who indirectly engages himself in estate agent work via a third party should be deemed as an estate agent.

Role of estate agents in Hong Kong

6.3 In most instances, an estate agent in Hong Kong serves as an agent for the vendor as well as the prospective purchaser in a property transaction. Estate agents carry out a number of tasks in relation to their clients as set out below :-

a) seek out properties for sale and establish connections with vendors who agree to list their properties through the agents' firms;

b) advertise vendors' properties including their key features such as description of the property, floor area and asking price;

c) verify or find out the salient features and ownership status of the properties through preliminary on-the-spot surveys and counter-checking at the Land Registry;

d) explain to clients the range of services provided by the agencies;

e) present information of the property to prospective purchasers and answer their enquiries;

f) discuss with and understand the needs of prospective purchasers and introduce a short-list of suitable properties to the latter;

g) make appointments with vendors for inspection of the properties, accompany prospective purchasers to inspect the properties and request them to sign Inspection Forms after explaining the terms therein;

h) mediate in the negotiation process between vendors and prospective purchasers with a view to facilitating transactions between them;

i) arrange vendors and purchasers to sign proforma PSPA after filling in details such as the agreed transaction prices, dates of signing the formal Agreement for Sale and Purchase, accessories like furniture and appliances to be assigned with the property, etc;

j) settle or follow up disputes arising from revocation of PSPAs according to the terms set out therein;

k) facilitate clients in passing, e.g. by fax, the PSPA to their solicitors; and

1) follow up miscellaneous requests and queries of purchasers and vendors until acquisition of legal title to property and occupation by the purchaser.

6.4 The present practice of estate agents playing the role of an agent for both parties has a number of advantages. Through their contacts with purchasers and their expertise in marketing and advertising, agents can ensure that the maximum number of potential purchasers view a vendor's property. This should speed up the selling process for a vendor and increase the likelihood that a flat will be sold to the purchaser willing to pay the highest price. Similarly, agents can also expedite the search process for purchasers by making information about the price and descriptions of flats centrally available. Furthermore, the present role of estate agents has enabled property transactions to be carried out in a generally cost-effective manner.

6.5 It is noted that the dual role of estate agents has the disadvantage of potential conflict of interest. However, given the long established and widely accepted role of estate agents as an agent for both the vendor and purchaser and the advantages it brings about, we recommend that the role of estate agents in Hong Kong as described above need not be changed in the future regulatory framework.

6.6 We also recommend that in order to avoid any abuse of an estate agent's role, the obligations of estate agents should be clearly stated in legislation.

Obligations

6.7 We recommend that the future legislation should provide that an estate agent whether acting for both parties or for one party only should have the following main obligations :

- a) an estate agent shall report and present to a prospective purchaser, who is his client, to his best knowledge essential information about the property as prescribed by the regulatory authority;
- b) an estate agent shall inform the vendor of any offer made by a prospective purchaser until the vendor is bound by contract, e.g. signing of a provisional sale and purchase agreement;
- c) an estate agent shall disclose fully to his client, i.e. the prospective purchaser, the vendor or both, as the case may be, his interest in the property transaction, e.g. any commission or profit or him becoming the purchaser;
- d) an estate agent shall disclose fully to his client any conflict between his duty to his client and his interest;
- e) an estate agent shall inform his client if he is representing both the vendor and the purchaser; and
- f) an estate agent shall conduct negotiations in a fair manner when he is acting for both the vendor and purchaser.

6.8 We also recommend that the regulatory authority should prescribe rules of conduct and practice to elaborate these statutory obligations.

Chapter 7 LICENSING CATEGORIES

7.1 We have considered the question whether individuals and corporations operating as an estate agent should be licensed, and whether licensing should also extend to frontline personnel i.e. salespersons.

7.2 We recommend that individuals and corporations operating as an estate agent should be licensed. The objective of the licensing requirements is to ensure that an estate agent meets certain minimum standards of competence and knowledge. The work of raising the standards of service of estate agents over and above the licensing requirements should be a matter for the trade itself.

Estate agent's licence

7.3 An individual applying for an estate agent's licence should meet the following requirements:

- a) he must meet a minimum age requirement as specified by the regulatory authority;
- b) he must be a fit and proper person, e.g. he should have no record of criminal convictions or complaints that, in the view of the regulatory authority, render him unsuitable to be an estate agent;
- c) he has demonstrated to the satisfaction of the regulatory authority that he has a good understanding of the rules of conduct and practice prescribed by the regulatory authority; and
- d) he proves to the satisfaction of the regulatory authority that he has a minimum standard of competence, knowledge and experience, as specified by the authority, necessary for carrying out the duties of an estate agent.

Corporation licence

7.4 A corporation which operates an estate agent business must obtain a corporation licence first.

7.5 We recommend that the requirements for a corporation licence should be:

- a) the corporations' directors must be fit and proper persons;
- b) the corporation should have as its directors a number of licensed estate agents as specified by the regulatory authority (e.g. the regulatory authority may specify that at least half of the corporations' directors should be licensed estate agents); and
- c) the corporation has a licensed estate agent acting as the officer-in-effective-control of its estate agent business.

Officer-in-effective-control

7.6 A principal office, a branch office or a sub-office of an estate agent business operated either by an individual or a corporation should have a licensed estate agent in effective control and a licensed estate agent should not be an officer-in-effective-control of more than one business or office. There is concern that in the early stage of licensing, there may not be sufficient licensed estate agents to fulfil this requirement. If this should happen, the regulatory authority should exercise flexibility in regard to the number of offices for which a licensed estate agent is responsible.

Salesperson's licence

7.7 To differentiate an estate salesperson from other employees of an estate agency, we recommend that a salesperson should be clearly defined in legislation. Anyone working for an estate agent as an estate salesperson must hold an estate salesperson's licence unless he already holds an estate agent's licence. An estate salesperson will perform the function of an estate salesperson only as an employee of an estate agent and under the latter's supervision. That means a licensed salesperson cannot operate an estate agent business. His employer will be responsible for the estate salesperson's business conduct.

7.8 We recommend that an estate salesperson should be defined as an individual whose duties as an employee of an estate agent include :

- a) introduces a prospective buyer/lessee or seller/lessor of a property for or on behalf of his employer; or
- b) induces or negotiates with any person to buy, sell or lease a property.

7.9 A salesperson is the basic entry point to the trade. The licensing requirements for an estate salesperson should be kept to the minimum so that they would not become an unnecessary barrier against entry to the trade nor would they cause problems in recruiting new staff. We recommend the following licensing requirements for an estate salesperson :

- a) he must meet a minimum age requirement as specified by the regulatory authority;

b) he is a fit and proper person, i.e. he has no record of criminal convictions or complaints that render him unsuitable to be an estate salesperson; and

c) he has demonstrated to the satisfaction of the regulatory authority that he has a good understanding of the rules of conduct and practice prescribed by the regulatory authority.

Exemptions

7.10 We recommend that the licensing legislation should not apply to Government departments. The regulatory authority should have power to exempt certain organisations, e.g. the Housing Society, or classes of persons from licensing.

Licensee Register

7.11 The regulatory authority should keep a register of licenced estate agents and salespersons and a register of those whose licences have been suspended and revoked. These registers should be available for public inspection.

7.12 An individual or corporation operating as an estate agent or estate salesperson without a licence or employing an unlicensed salesperson will commit an offence in law.

Sale of overseas properties

7.13 We note concerns expressed by the public about the sale of overseas properties in Hong Kong. We recommend that the regulatory system we propose should apply to all individuals or corporations engaged in the sale of properties irrespective of where the properties are located. The regulatory authority may introduce rules of conduct and practice specific for overseas properties.

Chapter 8

THE REGULATORY AUTHORITY

8.1 We propose that the future regulatory authority should be called the Estate Agents Authority. Its Chinese name should be "in Chinese name".

Composition

8.2 It is important that the regulatory authority should command respect among the public as an impartial body that takes account of the interests of the trade and the consumer as well as the community in general. We recommend that the authority should be composed of members from the trade, related professions and the community. Estate agents should be sufficiently represented on the authority. During its early stages, it would be preferable to have a government representative on the authority to provide a link between the authority and Government. The authority should be included in the Schedule of Public Bodies in the Prevention of Bribery Ordinance*.

Powers of the Regulatory Authority

8.3 We recommend that the regulatory authority should have the following powers :

(a) subject to Government's approval, make regulations:

(i) to set licensing requirements;

(ii) to exempt certain organisations and classes of persons from licensing;

(iii) to prescribe rules of conduct and practice for estate agents and salespersons; and

(iv) to prescribe penalties for breach of rules of conduct and practice; and

- (b) issue licence to estate agents and salespersons;
- (c) prescribe fees for the issue and renewal of licences and for services it provides;
- (d) prescribe standard forms, agreements and documents to be used by agents and salespersons;
- (e) inquire or appoint somebody to inquire into alleged breach of legal obligations and rules of conduct and practice by an agent or salesperson, institute disciplinary proceedings and impose any of the specified penalties (the inquiry power should include power to require an estate agent to provide information and records related to the case under investigation);
- (f) delegate powers to a committee or an officer of the authority; and
- (g) review evidence and make a judgement on the reasonable amount of commissions and fees in response to an application by a party to a dispute between an agent and his client.

8.4 We have not recommended to give powers to the regulatory authority to investigate allegations of people operating as estate agents without a licence. We are of the opinion that these cases should be referred to the police for investigation.

Resources and financial implications

8.5 We recommend that the regulatory authority should be a financially autonomous body which is expected to fund its day-to-day operations by its own revenues such as licence fees, penalties and miscellaneous charges. It should have its own executive arm to carry out its function. To ensure smooth inception of the authority, Government should identify practicable means to help the authority during its start-up. It is estimated that to cope with the work in the first year, for issue of provisional licences in particular, the executive arm of the regulatory authority will require a staff of about 18 persons, at an estimated operating cost of around \$8 million a year.

Chapter 9 WRITTEN AGENCY AGREEMENT

9.1 At present in most cases an estate agent relies on verbal instructions or agreements with his clients. This has given rise to disputes and allegations of malpractice.

9.2 We recommend that an estate agent should have a prior written agency agreement between him and his client where:

- (a) he charges a purchaser a commission or fee for introducing a property;
- (b) he charges a vendor a commission or fee for selling the vendor's property; or
- (c) he seeks to find a purchaser on behalf of the vendor, whether or not he charges the vendor a commission or fee.

9.3 The regulatory authority should prescribe a standard agency agreement. The agreement should state the main obligations of an estate agent, the agreed commission or fee and the validity period of the agreement. In the case of an agreement with a potential purchaser, it should state the obligations of the purchaser if he subsequently purchases the property without going through the estate agent. The written agreement should also state whether the estate agent is acting as an agent for a third party (vendor or purchaser) or intends to do so and whether he will receive any remunerations from the third party and the amount.

9.4 There will be resources implications for estate agencies, particularly those smaller ones, to make sure that agency agreements are signed by their clients. Customers will not be familiar with this new practice. Therefore, it is important that estate agents and their customers should be given ample time to adapt to this new requirement before it is enforced fully.

9.5 References made to sales in this chapter apply to lettings as well.

Chapter 10 COMMISSION

10.1 In return for providing services to vendors and purchasers, an estate agent is normally entitled to a commission. While there is at present no standard commission rate in the trade, most estate agencies charge purchasers a commission equivalent to 1% of the property transaction price. Many estate agencies do not charge vendors a commission while others do.

10.2 Some estate agents are of the view that the proposed legislation should stipulate standard commission rates for estate agents as in some professions in Hong Kong. On the other hand, there are merits to maintain the current practice of not prescribing a fixed commission rate for the trade : it encourages free market competition, helps promote better services in the trade and enables flexibility among estate agencies to target at different market segments. A standard scale of commission rates tends to become the charging norm of the trade and protect inefficiency and inferior services at the expense of those estate agents who provide efficient and good services.

10.3 We recommend that the regulatory authority should not prescribe a standard scale of commission but should take up a positive role in resolving disputes over commissions and fees between an agent and his client. We have recommended in chapter 8 that the regulatory authority should be given powers to review evidence and make a judgement on the reasonable amount of commissions and fees in response to an application by a party to a dispute between an agent and his client.

Chapter 11 SUPPLY OF INFORMATION AND ADVERTISING

Supply of information

11.1 We are of the view that, in principle, an estate agent should supply certain information to a potential purchaser. There is concern that it will take time to obtain the necessary information so as may cause delay to property transactions. Having regard to this concern, we have come up with the following recommendations.

11.2 An estate agent should have the following information in his possession before he introduces a property to a prospective purchaser:

- (a) prima facie evidence of ownership e.g. the name of the vendor and the name of the last owner as shown on an up to date Land Registry record of the property;
- (b) the saleable floor area of the property;
- (c) the year of completion of the property as evidenced by, for example, an Occupation Permit;
- (d) the permitted use of the property;
- (e) the expiry date of the land lease of the property and any right of renewal; and
- (f) a statement by the owner of the property as to whether he has done any unauthorised alteration works to the property and to the best of his knowledge whether the property has any other unauthorised alteration works; and whether there are any current orders or plans to carry out repairs or improvements to the property or common areas that will incur costs to the new owner of the property.

11.3 The estate agent can seek information items (a) to (e) from the owner, but he should be reasonably satisfied that the information is correct. For example, he should have sight of the original computer printout of the Land Registry record. Or, the estate agent can obtain the information on behalf of the owner; he may charge the owner for the service provided. It should be part of the licensing requirements for an estate agent that he knows how to obtain these items of

information.

11.4 Item (a) is to give the estate agent prima facie evidence of ownership of the property so that he is reasonably satisfied that he is dealing with a bona fide owner. This will prevent false owners from cheating potential purchasers and estate agents.

11.5 Item (b) can be obtained directly and quickly by actual measurement if the information is not readily available elsewhere. A sub-committee of the Law Reform Commission has proposed a standard definition for saleable floor area. We appreciate the fact that gross floor area has been the commonly used measurements in advertisement. Therefore we agree that the gross floor area can still be quoted in advertisements, but potential purchasers should be also informed of the saleable floor area when an estate agent introduces the property to him.

11.6 When an estate agent introduces a property to a potential purchaser, e.g. when he takes the latter to inspect the property, he should provide information items (b) to (f) to the potential purchaser.

11.7 It is believed that this arrangement should overcome the concern over the time it takes to obtain some of the information. If an owner wants to sell his property, we consider it fair and reasonable to require him to produce the essential information concerning the property. If he has the information ready before going out to seek a purchaser, it will not affect the time taken for completing a transaction.

Advertising

11.8 To ensure clear identification of publishers and to avoid misrepresentation in advertisements by estate agents, we recommend that the regulatory authority should make the following rules of practice to govern advertising by estate agents :-

(a) an estate agent who publishes any advertisement in respect of any property should specify therein his approved name, licence number and the address of his business. In case of small advertisements, stating the name of the agency and its licence number will suffice;

(b) an estate agent should not wilfully or recklessly put up false or inaccurate property advertisements and should not advertise without having a written agency agreement with a vendor or lessor; and

(c) an estate agent should not put up or authorise to put up as part of any advertisement any false, inaccurate or misleading statement concerning any property for sale or leasing.

Chapter 12 TRUST MONEY AND INDEMNITY

Trust Money

12.1 Estate agents hold a significant position of trust within the community in the course of carrying out their business. A purchaser usually pays his initial deposit through an estate agent to the vendor.

12.2 Complaint statistics do not point to a problem of estate agents' misappropriation of client money. However, it is prudent to introduce measures to prevent a problem from occurring.

12.3 We recommend that a trust money accounting system should be set up so that all trust money held by estate agents can be accounted for at all times. An estate agent should be required by legislation to :-

(a) pay all trust money into a bank account (trust account) separate from his own account as soon as practicable after receiving such money;

b) retain all trust money in the trust account until it is paid to persons entitled thereto or such persons' solicitors;

(c) use the trust money only for the purpose authorised by the client, e.g. to pay a deposit to the vendor;

(d) keep, maintain and arrange to audit periodically at each business location trust documents and records as prescribed by the regulatory authority; and

(e) produce trust documents and records for inspection by the regulatory authority as and when necessary.

Indemnity

12.4 Since misappropriation of client money is not a problem, it does not appear necessary to set up a compensation fund for the trade. A compensation fund is cumbersome and expensive to administer as it inevitably entails fund management and monitoring of fund managers' performance. The costs will ultimately be passed on to the consumer. However, when misappropriation of client money does occur or when a successful claim for damages against an agent is made, a client should be duly compensated for his financial loss.

12.5 We recommend that the, regulatory authority should consider whether or not it should prescribe certain indemnity requirements to be met by estate agents.

Chapter 13 PENALTIES, OBJECTIONS AND APPEALS

Penalties

13.1 we recommend that the regulatory authority should be able to impose penalties on rule-breaking estate agents or salespersons.

13.2 If an allegation is made against an estate agent or salesperson that he has acted improperly by breaching statutory rules and regulations, the regulatory authority may after initial inquiry hold a hearing and summon the agent or salesperson to appear before the authority. If the authority considers that the allegation against the estate agent or salesperson is proven, the authority should be able to impose one or more the following penalties on the offender:-

(a) admonish or reprimand the licence holder;

(b) require the licence holder to pay the costs arising from the inquiry;

(c) impose a fine not exceeding a certain maximum amount to be prescribed by the authority;

(d) suspend the estate agent or salesperson's licence for a certain period of time;

(e) impose conditions or limitations on the estate agent's or salesperson's licence; and

(f) cancel the estate agent's or salesperson's licence and disqualify him from holding a licence either permanently or temporarily.

Objections and appeals

13.3 To ensure credibility of the regulatory authority, its processing of licensing applications should be transparent to the public. We recommend that the legislation should allow any person to object to the granting of a licence to an applicant by the authority on the ground that the applicant fails to satisfy licensing requirements prescribed by the authority. If the objection is proved to be valid and legitimate by the authority, a hearing should be arranged for the objector and applicant to present their cases. After reaching a decision in the case, the authority will decide what costs, if any, should be paid by the licence applicant or the objector.

13.4 To avoid contravention with requirements of the Bill Of Rights Ordinance, it is essential that any licence applicant or holder who is aggrieved by the decision of the regulatory authority concerning licence application and renewal and imposition of penalties should have a right to appeal. We recommend that the legislation should provide for the setting up of an independent appeal panel which comprises members to be appointed by Government. The appeal panel should

be seen to be independent and impartial in order to satisfy the requirements of the Bill of Rights Ordinance.

Offences

13.5 The legislation should state certain offences with appropriate maximum penalties for serious breach of the law. These cases will be dealt with by prosecution in court.

Chapter 14 TRANSITIONAL ARRANGEMENTS

14.1 Transitional arrangements are necessary to bring estate agents into the regulatory system within a reasonable period of time. These arrangements should have due regard to practical considerations. They should not cause undue disruptions and anxieties in the trade as well as service to the public. Nor should they force many people out of work.

14.2 We recommend that following its establishment, the regulatory authority should take the following steps:

(i) openly invite all practising estate agents, including corporations, and salespersons to come forward to the authority to apply for a licence. They will initially be issued with provisional licences. The whole process should preferably be completed as soon as practicable;

(ii) announce and publicise the effective date of the licence provision i.e. anyone operating as an estate agent or estate salesperson without a licence (either a provisional or regular licence) after the effective date will commit an offence;

(iii) prescribe the rules of conduct and practice for estate agents and estate salespersons;

(iv) determine licensing requirements for converting a provisional licence into a regular one. To assist applicants to meet the licensing requirements, the authority may have to publish information materials, e.g. text books, or to organise briefing seminars.

14.3 Since the proposed licensing requirements for salespersons are minimal, they should not cause major problems. For estate agents, it should be accepted that while a minimum standard of competence and knowledge is expected, the requirements should not be so stringent as to disqualify unnecessarily many practising agents. This will not be in the interest of the trade or the consumer. Due regard should be given to experience as opposed to formal education and training. Applicants should be given adequate opportunities to meet the requirements; this includes allowing repeated attempts within a reasonable period of time.

14.4 These transitional arrangements will allow screening out unsuitable estate agents to take place in a gradual and a planned manner without causing unnecessary anxieties in the trade. They will unlikely cause any undue disruptions to the trade and hence service to the public.

14.5 Once the licence provision has come into effect, any person who wants to operate as an estate agent or to work as a salesperson must obtain a licence first. This should only affect new comers to the trade, as existing estate agents and salespersons would have been covered in the transitional arrangements.

** Footnote : A confirmor is a person who purchases a property with a view to re-selling it for a profit before the completion of the assignment.*

** Footnote :The Corruption Prevention Department of the ICAC is empowered by the ICAC Ordinance to examine the practices and procedures of those public bodies listed in the Schedule to identify and recommend changes to reduce any corruption opportunities.*