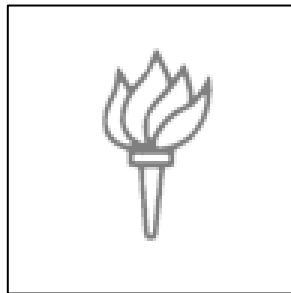


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### Land Options for Housing: How New Property Rights Can Break Old Land Monopolies

*Shitong Qiao and Roderick Hills, Jr.*

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## Land Options for Housing: How New Property Rights Can Break Old Land Monopolies

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### *Abstract*

The world today is afflicted by inequality of wealth created in large part by monopolistic ownership of land. Across the globe, in cities like Rio de Janeiro, Yangon, Johannesburg, and London, landowners in control of urban real estate in hot job markets have created a housing shortage. Hong Kong, with the least affordable housing in the world, provides a particularly apt example of how property law protects such monopolies – and also how the creation of new property rights can break them up.

In this paper we use Hong Kong as a case study to suggest both a diagnosis and a solution to two aspects of property law that slow down the creation of housing. First, the division of property rights between private owners and the government creates a bilateral monopoly that results in gridlock. Second, re-allocating property rights to end such gridlock is impeded by the reciprocal causation between property rights and political influence – what we will call a “constituency effect” of property law. Rather than attempt a frontal assault on existing holdings that would likely be foiled by such constituency effects, we suggest that the government should create entirely new property rights around which new interest groups could form. By giving every Hong Kong resident “land options for housing” (LOHs), the government could create a competitive market for development rights that simultaneously ends the gridlock of monopoly and creates a new constituency to lobby for more housing. Under our proposal, property owners would compete with each other to purchase LOHs from LOH holders in order to build high-density housing. Such a system would simultaneously give the LOH holders a stake in moving land from low-value to high-value uses while providing ample compensation to existing stakeholders.

The problem posed by Hong Kong’s mix of bilateral monopoly and constituency effects transcends Hong Kong. We also examine how these connected obstacles to housing construction can defeat or be defeated by land options in places ranging from Israel to New York City. There is a larger lesson for property theory at stake in the interaction of bilateral monopolies with constituency effects. The sense of entitlement generated by existing property rights limits politicians’ ability to design new, more flexible forms of property. There are, in other words, transaction costs generated by property that impede not only economic but also political transactions. Overcoming those transaction costs requires legislative proposals that create new constituencies but yet are also not blocked by the old ones.

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## I. Introduction

The world today is afflicted by inequality of wealth created in large part by monopolistic ownership of land. Thomas Piketty has famously shown how returns to capital have outstripped returns to labor.<sup>1</sup> The share of wealth accruing to the owners of land turns out to be at least as great an engine of inequality as ownership of finance capital.<sup>2</sup> The returns to land are driven by the unique value of parcels in cities where labor is most productive. Individuals and enterprises frequently depend on proximity to each other for their productivity. Gains in productivity from such proximity – what economists call “agglomeration economies” – are huge.<sup>3</sup> Because there is a fixed supply of parcels in cities with large agglomeration economies, landowners in such cities can levy immense tolls on everyone else by charging extraordinary premiums to buy or rent real estate.<sup>4</sup> Across the globe, in cities like Rio de Janeiro,<sup>5</sup> Yangon,<sup>6</sup> Johannesburg,<sup>7</sup> and London,<sup>8</sup>

<sup>1</sup> See generally THOMAS PIKETTY, *CAPITAL IN THE TWENTY-FIRST CENTURY* (Belknap Press 2017).

<sup>2</sup> See Matt Rognlie, *Deciphering the Fall and Rise in the Net Capital Share: Accumulation or Scarcity?*, in *BROOKINGS PAPERS ON ECONOMIC ACTIVITY: SPRING 2015* 1, 51 (David H. Romer & Justin Wolfers eds., Brookings Inst. Press, June 7, 2016) (“[C]oncern about inequality should be shifted away from the overall split between capital and labor and toward other aspects of distribution . . . . Although the net capital share has at times seen dramatic shifts both up and down, away from housing its long-term movement has been quite small.”).

<sup>3</sup> See David Schleicher, *Stuck! The Law and Economics of Residential Stagnation*, 127 *YALE L.J.* 78, 96 (2017) (explaining that according to agglomeration economics, “location matters. When people and capital congregate in particular cities and regions, they learn and trade more easily, and this creates wealth and generates economic growth”).

<sup>4</sup> See generally Roderick M. Hills, Jr. & David Schleicher, *Planning an Affordable City*, 101 *Iowa L. Rev.* 91, 115-16 (2015).

<sup>5</sup> See ERIC A. POSNER & E. GLEN WEYL, *RADICAL MARKETS: UPROOTING CAPITALISM AND DEMOCRACY FOR A JUST SOCIETY* xiii-xiv (Princeton Univ. Press 2018).

<sup>6</sup> See Khine Yin Htun, *Yangon’s Housing Inequality During the Covid-19 Pandemic*, *TEA CIRCLE OXFORD* (Jan. 13, 2021), <https://teacircleoxford.com/2021/01/13/yangons-housing-inequality-during-the-covid-19-pandemic>.

<sup>7</sup> See John Campbell, *Affordable Housing Crisis in Johannesburg*, *COUNCIL ON FOREIGN RELATIONS* (Jan. 6, 2017, 12:17 PM) <https://www.cfr.org/blog/affordable-housing-crisis-johannesburg>; Lerato Mogoatlhe, *The City of Johannesburg Is Turning 37 Factories into 3,000 Homes*, *GLOB. CITIZEN* (July 2, 2019), <https://www.globalcitizen.org/en/content/johannesburg-old-factories-into-homes-housing>.

<sup>8</sup> See Mark Townsend & Liam Kelly, *Thousands Gather in London to Protest Against Lack of Affordable Housing*, *GUARDIAN* (Jan. 31, 2015, 12:43 PM), <https://www.theguardian.com/society/2015/jan/31/hundreds-gather-london-march-for-homes-protest-city-hall-affordable-housing>.

landowners are reaping rents from their monopolistic position, creating a shortage of housing that divides residents between housing haves and have-nots.<sup>9</sup>

In this paper we use Hong Kong as a case study to suggest both a diagnosis and a solution to the problem of inequality driven by monopolistic property rights. Among cities dominated by real estate oligarchy, Hong Kong is a special case. Its housing market has been the least affordable in the world for a decade, easily beating out London, San Francisco, and Los Angeles for this dubious distinction.<sup>10</sup> Yet this housing crisis is a paradox of housing scarcity amidst plenty of land. Only about 24% of Hong Kong's land is built up, with the balance currently occupied by woodland, shrubland, and grassland.<sup>11</sup> Moreover, that 24% of built-up land includes warehouses and industrial facilities that are manifestly less urgently needed than more housing: 1,414 hectares (5.46 square miles) consist of brownfield sites containing old industrial facilities.<sup>12</sup> Despite this abundance of buildable land, Hong Kong's population is crammed into apartments with average living area per person of about 215 square feet -- much less than in New York City, Shanghai, or nearby Shenzhen -- and the waiting list for public housing is on average 5.7 years.<sup>13</sup> Unsurprisingly, Beijing -affiliated pundits have touted the idea of a communist-style land reform as a solution to the most severe housing crisis in the world and the deep social inequality and division caused by that crisis.<sup>14</sup>

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<sup>9</sup> Wendell Pritchett & Shitong Qiao, *Exclusionary Megacities*, SOUTHERN CALIFORNIA LAW REVIEW, VOL. 91, NO. 3, 467-522.

<sup>10</sup> Shawna Kwan, *Hong Kong Homes Ranked Least Affordable for 11th Year*, BLOOMBERG WEALTH (Feb. 22, 2021, 10:49 PM), <https://www.bloomberg.com/news/articles/2021-02-23/hong-kong-homes-ranked-world-s-least-affordable-for-11th-year>.

<sup>11</sup> Plan. Dep't, *Land Utilization in Hong Kong*, H.K. OFF. GOV'T CHIEF INFO. OFFICER (July 31, 2019), <https://data.gov.hk/en-data/dataset/hk-pland-pland1-land-utilization-in-hong-kong-statistics/resource/a7ad1fe5-a8a3-47a8-bf58-af11bbe04a4c>.

<sup>12</sup> Plan. Dep't, *supra* note 11.

<sup>13</sup> Shitong Qiao & Roderick M. Hills Jr., *Development Rights for All*, 1 U.S.-ASIA L. INST.: USALI PERSP. (June 17, 2021), <https://usali.org/usali-perspectives-blog/development-rights-for-all>.

<sup>14</sup> See Keith Zhai & Chun Han Wong, *China Targets Hong Kong Wealth Gap, Housing Woes After Political Purge*, WALL ST. J. (Mar. 15, 2021, 9:07 AM), <https://www.wsj.com/articles/china-targets-hong-kong-wealth-gap-housing-woes-after-political-purge-11615813651>.

We offer a different solution based on our diagnosis of the problem as rooted in two familiar aspects of property law theory. First, Hong Kong's division of property rights between private owners and the government creates a bilateral monopoly that results in gridlock – a kind of anti-commons in which an asset lies unused because each side enjoys a veto over its development.<sup>15</sup> Second, re-allocating property rights to end such gridlock can be impeded by the reciprocal causation between property rights and political influence – what we will call a “constituency effect” of property law. Property rights create a focal point around which owners can rally, reducing their costs of political organization and thereby enabling them resist changes in the property status quo. Governmental officials armed with apparently sweeping legal powers can be practically stymied by such constituency effects. In Hong Kong, for instance, villagers, tycoons, and activists are all inspired to vigorous litigation and lobbying by a sense of entitlement to the status quo that blocks any political change to that set of entitlements.

Hong Kong's housing crisis seems to emerge from this combination of anti-commons gridlock and entitlement-protecting constituency effects. Current entitlement-holders -- developers, indigenous villagers, land justice activists, and the government itself -- have for decades been locked in apparently endless dickering over how to divide the gains from converting land from low-value uses like warehouses and small homes to higher-value uses like residential high-rises.<sup>16</sup> Meanwhile, the beneficiaries of more housing – potential buyers and renters currently crammed in under-sized apartments -- are politically disorganized, scattered across the entire jurisdiction, without any networks to overcome collective action problems or

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<sup>15</sup> For an overview of the concept as an “anti-commons” as property that is under-developed as a result of having too many owners with veto rights over its development, see Michael Heller, *The Tragedy of the Anticommons: Property in the Transition from Marx to Markets*, 111 Harv. L. Rev. 621-688 (1998).

<sup>16</sup> Qiao & Hills, *supra* note 13.

the focused incentives in any particular housing project to exert themselves to lobby for new construction.

What can be done to break the deadlock? Rather than attempt a frontal assault on the property rights of real estate tycoons and indigenous villagers, we suggest that the government would be better advised to create entirely new property rights around which new interest groups could form. Those new groups could break the bilateral monopoly of officials' dickering with current owners over the development of specific parcels. Specifically, we propose to give every Hong Kong resident "land options for housing" (LOHs). In such a regime, LOH holders rather than the government itself would sell these LOHs to developers and indigenous villagers. Those buyers would compete with each other to purchase LOHs in order to build high-density housing, simultaneously giving the LOH holders a stake in moving land from low-value to high-value uses while providing ample compensation to existing stakeholders.

The problem posed by Hong Kong's mix of bilateral monopoly and constituency effects transcends Hong Kong. It is a problem vexing both housing markets and property theory alike. Cities around the world are struggling to find ways to unlock urban real estate's development with innovative land entitlements. Done badly, however, such entitlements tend to be locked in place by the sense of entitlement created by the legal status quo. Fancy auctions, self-valuation for both tax and eminent domain, and complex liability rules are impressive but useless academic exercises unless one can figure out how to overcome the organizational advantages conferred on the constituents who benefit from the property rights that such rules seek to change. Bilateral monopoly and constituency effects are, in sum, two equations with two unknown variables that must be solved simultaneously.

Hong Kong's housing crisis illustrates this reciprocal causation between property law and public ordering. Our proposal to allocate the vertical dimension of property to LOH holders illustrates one such possible solution. By requiring current property owners to bid against each other for the purchase of LOHs, our proposal would simultaneously create a new interest group and eliminate the bilateral monopoly that has stymied land development in Hong Kong. The lessons of LOHs, however, can be extended beyond Hong Kong to any jurisdiction where the influence of existing rightsholders impedes the transfer of an asset to its most valued use.

There is also a larger lesson for property theory at stake in the interaction of bilateral monopolies with constituency effects. Bilateral monopolies are often the product of valuable entitlements that powerfully mobilize constituencies in their defense. "Homevoters," for instance, dominate zoning processes<sup>17</sup> in much the same way that developers and indigenous villagers dominate buildable land in Hong Kong.<sup>18</sup> The political influence generated by these entitlements prevent politicians from simply reshuffling the deck of private-law property allocations and starting anew, because those very allocations define who will effectively lobby, elect, or inform those politicians. Property theory, therefore, needs to integrate institutional politics into its theory of entitlements. Treating the political process or legislative politics as a *deus ex machina* that can step into redress the limits of private law ignores the ways that private law limits the political process.<sup>19</sup>

As economist Daren Acemoglu noted almost two decades ago, we need a political Coase theorem to define and overcome the transaction costs that block political re-assignments of

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<sup>17</sup> Roderick M. Hills Jr, and David Schleicher, Planning An Affordable City, Iowa L. Rev. 101 (2015): 91; David Schleicher, City Unplanning, Yale L. J. 122 (2012): 1670; Pritchett & Qiao, *supra* note 9.

<sup>18</sup> See *infra* Part II.

<sup>19</sup> On the need for property law scholarship to take into account the constituency effects of real property rather than assume that legislatures can re-allocate property rights with a free hand, see Hills & Schleicher, *supra* note 4; Hills & Schleicher, *Building Coalitions Out of Thin Air: Transferable Development Rights and "Constituency Effects" in Land Use Law*, 12 J. LEGAL ANALYSIS 79 (2020) [hereinafter *Building Coalitions Out of Thin Air*].



property rights.<sup>20</sup> The sense of entitlement that existing entitlements generate limits the ability of politicians to design new and more flexible forms of property. There are, in other words, transaction costs generated by property that impede not only economic but also political transactions.<sup>21</sup> Overcoming those transaction costs requires legislative proposals that create new constituencies but are not blocked by the old ones.<sup>22</sup>

The roadmap for our argument starts with a description of Hong Kong's housing crisis in Part II. In Part III, we diagnose this crisis's causes in the structure of property law, first by setting out the general theory that links property rights to negotiation-stalling bilateral monopoly in Part III(A), and, second, by showing in Part III(B) how constituency effects of property defeat some familiar solutions to such monopolies -- for instance, liability rules of various stripes, auctions, and self-valuation. In Part IV, we lay out our solution to this gridlock: LOHs, the purchase of which is both necessary and sufficient for the development of high-density residential structures. We will explain how LOHs simultaneously create a constituency for residential development, promote inter-parcel competition, and let bidding guided by self-interested predictions of landowners guide the location of housing. Part V concludes with some lessons for property monopolies in other settings, such as zoning in American cities.

## **II. The Landscape of the Problem: How Property Law Has Failed to Create Housing in Hong Kong**

Before plunging into any diagnosis, we will begin with a description of Hong Kong's housing problem. For decades, Hong Kong's government has acknowledged the undeniable fact

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<sup>20</sup> Daren Acemoglu, *Why Not a Political Coase Theorem? Social Conflict, Commitment, and Politics*, 31 J. COMP. ECON. 620 (2003).

<sup>21</sup> See *infra* Part III.

<sup>22</sup> See *infra* Part IVB.

that Hong Kong's citizens suffer from a debilitating shortage of housing.<sup>23</sup> Despite numerous efforts to solve the problem, however, land remains locked up in brownfields, small three-story residential structures, and empty grassland and forest a small fraction of which would suffice to build all of the housing the Hong Kong's residents need.

### **A. How Land in Hong Kong is Used**

The paradox of Hong Kong's housing shortage is epitomized by the absence of housing in an abundance of buildable land. The total land area in Hong Kong is approximately 1,111 square kilometers.<sup>24</sup> Within that total land area, only approximately 25% is built-up area, while the remaining 75% is non-built-up area, mostly consisting of woodland, shrubland, grassland, or wetland, including many country parks.<sup>25</sup> Only 3.8% is devoted to any sort of non-rural residential uses: 2.3% is private residential land, while 1.5% is public residential land.<sup>26</sup> By contrast, 3.2% is rural settlement, mainly so-called small-house and Tso/Tong land (祖堂地), also known as ancestral land; 1.5% is warehouse and open storage, mainly classified as "brownfields"; 4.5% is agricultural land most of which is unfarmed and of which developers own a big portion.<sup>27</sup> In sum, more than twice as much land in Hong Kong is devoted to warehouses, crops, and small village houses as higher-density residential uses.

In general, HK government, developers, and indigenous villagers control most of the developable land in Hong Kong. This land includes 391 hectares of unleased residential land,<sup>28</sup>

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<sup>23</sup> See Zhou Wenmin & Wang Duan, *What's Stopping Hong Kong from Fixing Its Housing Crisis?*, THINKCHINA (July 9, 2021), <https://www.thinkchina.sg/whats-stopping-hong-kong-fixing-its-housing-crisis> ("Improving housing affordability has been the top concern of every Hong Kong government.")

<sup>24</sup> Task Force on Land Supply, *Demand for Land* ¶ 2 (H.K. Dev. Bureau, Paper No. 02/2017, 2017), [https://www.devb.gov.hk/filemanager/en/content\\_1054/Paper\\_02\\_2017.pdf](https://www.devb.gov.hk/filemanager/en/content_1054/Paper_02_2017.pdf); *Hong Kong - the Facts*, GOVHK (May, 2021), <https://www.gov.hk/en/about/abouthk/facts.htm>.

<sup>25</sup> Task Force on Land Supply, *supra* note 24; *Hong Kong – the Facts*, *supra* note 24.

<sup>26</sup> Plan. Dep't, *supra* note 11.

<sup>27</sup> *Id.*

<sup>28</sup> *LCQ16: Vacant Government Sites Managed by Lands Department*, GOV'T H.K. PRESS RELEASES (Feb. 26, 2020, 2:52 AM), <https://www.info.gov.hk/gia/general/202002/26/P2020022600497.htm>.

3,380 hectares of village type development land,<sup>29</sup> 4,400 hectares of agricultural land, of which only 700 hectares are actively farmed,<sup>30</sup> and 1,600 hectares of brownfields.<sup>31</sup>

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<sup>29</sup> *RICS Calls on Hong Kong Government to Invest More Resources to Increase Land Supply*, BLOOMBERG (Sept. 26, 2018, 4:19 AM), <https://www.bloomberg.com/press-releases/2018-09-26/rics-calls-on-hong-kong-government-to-invest-more-resources-to-i>.

<sup>30</sup> *LCQ18: Statistics on Agricultural Lands and Development Plans*, GOV'T H.K. PRESS RELEASES (June 28, 2017, 3:10 AM), <https://www.info.gov.hk/gia/general/201706/28/P2017062800606.htm>.

<sup>31</sup> PLAN. DEP'T., *STUDY ON EXISTING PROFILE AND OPERATION OF BROWNFIELD SITES IN THE NEW TERRITORIES – FEASIBILITY STUDY 56* (Ove Arup & Partners H.K. Nov. 2019).

## B. How Land in Hong Kong is Owned

Formally speaking, all land in Hong Kong is owned by the government as “Crown Land.”<sup>32</sup> Under this system of public ownership, inherited from the British colonial period, the government provides for private control of real estate by leasing land to private lessors, usually for a period of 99 years.<sup>33</sup> While the government reserves the right to “resume” the lease on payment of just compensation for the balance of the lease’s term,<sup>34</sup> these leases operate much like any fee simple absolute: They are traded on the secondary market just like any other private property and are the basis for the lessors’ investment in improvements. Accordingly, we shall refer to such lessors as “lessee-owners” and long-term leases from the government to such owners as “ownership” for the sake of convenience and clarity.

In this system of quasi-private ownership, the vast majority of land suitable for new residential construction is held by private lessee-owners. Such lands can be classified into two categories: agricultural and brownfield lands, primarily held by land development companies, and village-type development land held by indigenous villagers either as households or village associations.

### 1. Agricultural Land and Brownfields

“Agricultural land” is a misnomer, describing the zoning rather than the use of the real estate: Of the 4,400 hectares (ha) of “agricultural land” in Hong Kong, only about 700 ha are

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<sup>32</sup> *Land Tenure System and Land Policy in Hong Kong*, H.K. LANDS DEP’T, <https://www.landsd.gov.hk/en/resources/land-info-stat/land-tenure-system-land-policy.html> (last visited Nov. 14, 2021).

<sup>33</sup> *Id.*; Edmond Chan & Shiu Man Wan, *Global Corporate Real Estate Guide: Hong Kong*, BAKER MCKENZIE, <https://resourcehub.bakermckenzie.com/en/resources/global-corporate-real-estate-guide/asia-pacific/hong-kong/topics/real-estate-law> (last visited Oct. 31, 2021).

<sup>34</sup> Chan & Wan, *supra* note 33.

actively farmed.<sup>35</sup> Whether farmed or fallow, nearly 80 per cent of this land is in private hands.<sup>36</sup> The four biggest developers in Hong Kong own around 940 ha or 21% of this agricultural land reserve.<sup>37</sup> Because developers are interested in real estate development, they generally let such land lie fallow, having purchased it from the government at a low price reflecting its low value for agriculture in hopes of eventually re-zoning the land for more valuable uses.

For the same motivation, developers also hold significant amount of brownfields.<sup>38</sup> There are about 1,600 hectares of brownfields, more than 80% of which are privately owned, mainly by the major developers.<sup>39</sup> “Brownfield” is an imported term from the UK and the US and generally refers to agricultural land in the New Territories which have been converted to low-cost uses since the decline of agricultural activities decades ago.<sup>40</sup> Current uses include port back-up uses, open storage, logistics operations, vehicle parking, vehicle repair workshops, recycling yards, rural workshops, construction machinery and materials storage.<sup>41</sup> These lands occupy relatively flat areas in the New Territories<sup>42</sup> and are often intermingled with villages, squatter structures, and active or fallow farmland.<sup>43</sup>

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<sup>35</sup> See *supra* note 30 and accompanying text.

<sup>36</sup> PLAN. DEP'T., *supra* note 311, at 56.

<sup>37</sup> Lin Yueqian (林樂謙) Meiyin: Sida Dichanshang Yong Yu Yifangchi Nongdi Hengdi Zhan Jinban (美銀：四大地產商擁逾億方呎農地 恒地佔近半) [Meiyin: Four Biggest Developers Own Agricultural Land of More Than 100 Million Square Feet, Nearly a Half Belonging to Henderson Land], H.K. 01 (Sept. 25, 2019, 7:38 PM), <https://www.hk01.com/地產樓市/375584/收回土地條例-美銀-四大地產商擁逾億方呎農地-恒地佔近半>.

<sup>38</sup> See Fazhan Zongdi Xu Fang Mingyi Dichanshang (發展棕地須防明益地產商) [Development of Brownfields Requires Attention to Profitting Property Developers], Ta Kung Pao (大公報) (Jan. 12, 2019, 3:17 AM), <http://www.takungpao.com.hk/opinion/233119/2019/0112/233073.html>.

<sup>39</sup> PLAN. DEP'T., *supra* note 311, at 56.

<sup>40</sup> 何謂棕地? [What is Brownfield?], 香港經濟日報 [H.K. ECON. TIMES] (Aug. 8, 2018, 8:15 PM), <https://service.hket.com/knowledge/2133284/何謂棕地?>.

<sup>41</sup> *Id.*

<sup>42</sup> Task Force on Land Supply, *Brownfield Sites* ¶ 3 (H.K. Dev. Bureau, Paper No. 05/2017, 2017), [https://www.devb.gov.hk/filemanager/en/content\\_1054/Paper\\_05\\_2017.pdf](https://www.devb.gov.hk/filemanager/en/content_1054/Paper_05_2017.pdf).

<sup>43</sup> *Id.*

## 2. Indigenous Villagers' Rights to Small Houses and Village-Type Development Land

Roughly 3,380 hectares of land is held for the current or eventual use by indigenous villagers, either as low-density small-property houses, ancestral temples, or vacant land on which small-property houses will eventually be built.<sup>44</sup> The special place of the indigenous villagers is a product of the British colonizers' acquiring the New Territories under a 100-year lease from the government of the Qing Dynasty.<sup>45</sup> Unlike Hong Kong Island, which was turned over as a permanent concession to the British that was governed entirely by British law, the New Territories were governed by Qing Dynasty era Chinese law and custom.<sup>46</sup> British colonial government reenforced the role of Chinese law in an effort to co-opt support from the villagers living in the New Territories by preserving those villagers' traditional rights and powers over their land.<sup>47</sup> That land, which is called "village-type development land," is contained within 642 recognized villages, mostly in the New Territories, encompassing a total area of around 3,380 ha.<sup>48</sup> Indigenous villagers control 64% of such land, with the government controlling the remaining 36% (1201 hectares).<sup>49</sup> Much of the land controlled by indigenous villagers are the so-called Tso/Tong land.<sup>50</sup> While the government does not have information on the existing

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<sup>44</sup> See *supra* note 31 and accompanying text.

<sup>45</sup> See Lisa Hopkinson & Mandy Lao Man Lei, *Rethinking the Small House Policy*, CIVIC EXCHANGE 31 (Sept. 2003), [https://civic-exchange.org/dev/wp-content/uploads/2003/09/47-200309LAND\\_RethinkSmallHouse\\_en.pdf](https://civic-exchange.org/dev/wp-content/uploads/2003/09/47-200309LAND_RethinkSmallHouse_en.pdf).

<sup>46</sup> See *id.*

<sup>47</sup> LIU RUNHE (劉潤和), XINJIE JIAN SHI (新界簡史) [BRIEF HISTORY OF NEW TERRITORIES] (Sanlian Shudian (三聯書店) 1999).

<sup>48</sup> See *supra* note 31 and accompanying text.

<sup>49</sup> Shifang Tudi Zuo Fangwu Guihua Keburonghuan Zhengfu Zhongxu Miandui Dingquan Wenti (釋放土地作房屋規劃刻不容緩 政府終須面對「丁權」問題) [Release of Land for Housing Planning is Urgent and the Government Will Sooner or Later Face the Problem of New Territories Rights], H.K. 01 (Feb. 21, 2019, 7:19 PM), [https://www.hk01.com/01\\_觀點/297875/釋放土地作房屋規劃刻不容緩-政府終須面對-丁權-問題](https://www.hk01.com/01_觀點/297875/釋放土地作房屋規劃刻不容緩-政府終須面對-丁權-問題).

<sup>50</sup> For an official definition of tso/tong land and explanation for the lack of official data, see generally *LCQ21: Tso/Tong Lands*, H.K. PRESS RELEASES (Jan. 15, 2020, 2:15 AM), <https://www.info.gov.hk/gia/general/202001/15/P2020011500371.htm?fontSize=1>; It is not clear by definition whether the village-type development land includes Tso/Tong land, and the government does not provide data about the latter. However, such land is likely to be located within those 642 villages. We also find evidence that two plots of tso/tong land resumed by the government lie within the boundaries of village-type development land. See 評估為

number and area of Tso/Tong parcels, some chambers of commerce have suggested that there are currently around 2,000 hectares Tso/Tong land.<sup>51</sup> For the 36% controlled by the government, because the Hong Kong Basic Law requires the government to use this land only to satisfy indigenous villagers' "traditional right" to build small houses,<sup>52</sup> the government has to leave such land vacant to satisfy future claims by indigenous villagers' to their "small house" rights.<sup>53</sup>

The Basic Law's "small house" requirement continues a British colonial policy dating from 1972, when the colonial government created a "small house policy" (SHP) modeled on Qing law.<sup>54</sup> Under the SHP, a male indigenous villager aged 18 years old or older who is descended through the male line from a resident in 1898 of a recognized village in New Territories may apply to the Lands Department of the Hong Kong government for permission to build for himself a small house -- a residential structure no higher than three stories with each floor limited to 700 square feet -- on a suitable site within his own village once during his lifetime.<sup>55</sup> In most cases, the eligible villager builds a small house merely by applying for a building license to construct a structure on the villager's own land, but villagers also have the right to build a house on government-owned land in exchange for the villager's property or, if the villager is landless, apply for a Private Treaty Grant on government land purchasable at a

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適合作高密度資助房屋發展的用地列表 [List of Potential High-Density Development Plots], [https://gia.info.gov.hk/general/202105/13/P2021051300383\\_367366\\_1\\_1620896483258.pdf](https://gia.info.gov.hk/general/202105/13/P2021051300383_367366_1_1620896483258.pdf);

<sup>51</sup> Zutangdi Zhi Zheng (祖堂地之爭) [The Battle of Tso/Tong Land], Tudi Zhengyi Lianmeng 土地正義聯盟 [LAND JUST. LEAGUE] (Sept. 29, 2018), <https://landjusticehk.org/2018/09/29/tsotongland-2>.

<sup>52</sup> Kwok Cheuk Kin v. Dir. Lands, [2021] 1 H.K.L.R.D. 737.

<sup>53</sup> See generally Justin Ng, *The Importance of Land Reclamation in Hong Kong and Its Impacts*, EARTH.ORG (Dec. 14, 2020), <https://earth.org/land-reclamation-hong-kong> ("Between 1877 and 2020, over 70 sq km of land has been reclaimed in Hong Kong.").

<sup>54</sup> See Hopkinson & Lei, *supra* note 46, at 31.

<sup>55</sup> Task Force on Land Supply, *Village Type Development in the New Territories* ¶ 2 (H.K. Dev. Bureau, Paper No. 14/2017, 2017), [https://www.devb.gov.hk/filemanager/en/content\\_1054/Paper\\_14\\_2017.pdf](https://www.devb.gov.hk/filemanager/en/content_1054/Paper_14_2017.pdf).

two-thirds of the land's market value.<sup>56</sup> From 1972 to 2017, the Lands Department executed a total of 42,131 small house grants.<sup>57</sup>

### C. How Hong Kong Land is (Not) Developed: The Failure of Lease Modifications and Land Resumption

With 11,780 ha of land sitting semi-idle, Hong Kong has no shortage of land on which high-density residential building could easily be constructed. It is estimated that the 900 hectares of village-type development land currently reserved by the government alone could supply up to 500,000 housing units if ten-floor buildings (rather than the current 3-floor buildings) were permitted on them.<sup>58</sup> Moreover, the current occupants of this land are hardly satisfied with the status quo or resistant to their land's conversion to high-density residential uses. Indigenous villagers, in particular, seem utterly dissatisfied with their "small house" entitlement that is ostensibly designed for their benefit. Heung Yee Kuk, the organization that represents the indigenous inhabitants' view, supports the idea of high-rise small house development by using the public-private partnership model.<sup>59</sup> The "Kuk's" view is reenforced by a 2014 survey

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<sup>56</sup> Dingquanan Shangsuting Caijue Dingwu Bu Weixian Dan Nengfou Hushi San Da Biduan? (丁權案 | 上訴庭裁決丁屋不違憲 但能否忽視三大弊端?) [The New Territories Rights Case | The Court of Appeals Ruled New Territories Rights Constitutional, But Could the Three Main Drawbacks be Ignored?] (Jan. 25, 2021), H.K. 01 (Jan. 25, 2021), <https://www.hk01.com/周報/578941/丁權案-上訴庭裁決丁屋不違憲-但能否忽視三大弊端>.

<sup>57</sup> Task Force on Land Supply, *supra* note 56, at ¶ 3.

<sup>58</sup> 團體倡丁屋放寬建十層 [Groups Advocate the Relaxation of the Building of Ten-Storey Small House], Dongfang Ribao – Xiri (東方日報 - 昔日) [Oriental News], ORIENTAL ENTER. (May 19, 2014), [https://orientaldaily.on.cc/cnt/news/20140519/mobile/odn-20140519-0519\\_00176\\_028.html](https://orientaldaily.on.cc/cnt/news/20140519/mobile/odn-20140519-0519_00176_028.html).

<sup>59</sup> 丁權上訴案 鄉議局劉業強形容全勝 冀政府盡快處理積壓丁屋申請 [New Territories Appeals Case: Liu Yeqi from Heung Yee Kuk Described as Full Victory, Hoping that Government Soon Deal with the Backlog of New Territories Applications], ORANGE NEWS (Jan. 13, 2021), <https://www.orangenews.hk/hongkong/147930/%E3%80%90%E4%B8%81%E6%AC%8A%E4%B8%8A%E8%A8%B4%E6%A1%88%E3%80%91%E9%84%89%E8%AD%B0%E5%B1%80%E5%8A%89%E6%A5%AD%E5%BC%B7%E5%BD%A2%E5%AE%B9%E5%85%A8%E5%8B%9D-%E5%86%80%E6%94%BF%E5%BA%9C%E7%9B%A1%E5%BF%AB%E8%99%95%E7%90%86%E7%A9%8D%E5%A3%93%E4%B8%81%E5%B1%8B%E7%94%B3%E8%AB%8B.jhtml>.



showing that 88% of the indigenous inhabitants agreed that three-floor small houses were a huge waste of land and supported the development of high-rise small house.<sup>60</sup>

How, then, is it possible that the land has not been converted from current uses that none of the land's current users want? As explained below, the government and these users cannot reach agreement about the premium that should be charged to the lessees for conversion from low- to higher-value uses. Dickering over this premium has stalled this conversion for decades. In theory, the government could either resume leases after paying just compensation to the lessees or accede to the villagers' and developers' view of a proper premium. But the former option is foreclosed by the government's lack of information, and the latter option is foreclosed by politics. Lease resumption is a slow process made intractable by the predictably persistent litigation of developers with the best knowledge of the land's actual value. As for giving into villagers and developers, the government is under pressure from "land justice" activists and mortgage holders not to confer windfalls on groups regarded as excessively privileged by many in Hong Kong.<sup>61</sup> By contrast with the robust activism to prevent windfalls for villagers and developers, there are few protests seeking to increase the supply of housing. The under-housed are simply missing from the public housing discussion, despite hundreds of thousands of under-housed Hong Kong residents who are now crammed into tiny apartments rented at exorbitant prices.<sup>62</sup>

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<sup>60</sup> Groups Advocate the Relaxation of the Building of Ten-Storey Small House, *supra* note 58.

<sup>61</sup> See e.g., Peace Chiu, *Protesters Storm Elite Hong Kong Golf Course, Call for Land to be Used for Homes*, S. CHINA MORNING POST (Mar. 31, 2018, 6:52 PM), <https://www.scmp.com/news/hong-kong/community/article/2139769/protesters-storm-elite-hong-kong-golf-course-call-land-be>.

<sup>62</sup> See e.g., Nikki Natividad, *What Can be Done About Hong Kong's Ridiculously Tiny Flats?*, VICE (Mar. 30, 2021, 6:22 AM), <https://www.vice.com/en/article/v7m5md/hong-kong-housing-small-subdivided-apartments> ("A subdivided flat can range from 18 to 160 square feet, with a 100-square-foot unit with a bathroom costing anywhere from HK\$4,000 (\$516) to HK\$5,000 (\$645) per month.").

## 1. Rezoning and Lease Modification: Endless Haggling Over the Gains from Land Conversion

Because Hong Kong's system of property rests on the government's leasing Crown lands to private lessees, any conversion of land from its current uses to high-density residential purposes requires both a regulatory change and a lease modification. The first step requires lessee-owners to apply to the Town Planning Board for a plan amendment – basically, a modification of the land's zoning.<sup>63</sup> The second step requires those owners to apply to the Lands Department for a lease modification.<sup>64</sup> Because the government has a duty to obtain a fair stream of revenue from any lease modification, the second stage requires the government to negotiate a “premium” from the lessee-owner in exchange for the increase in value conferred by broadening the range of permissible uses under the lease.<sup>65</sup>

Neither of these two stages is easy, but negotiations over that lease premium have been the primary cause of delay in conversion of land.<sup>66</sup> Regulatory change by itself is also time consuming, as a larger number of stakeholders have been participating in the plan amendment process. Between 2009 and 2018, filings of public comments have grown from 4,352 to 39,000,

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<sup>63</sup> See *LCQ21: Amendment of Plans and Modification of Land Leases*, H.K. PRESS RELEASES (May 5, 2021, 2:30 AM), <https://www.info.gov.hk/gia/general/202105/05/P2021050500311.htm>.

<sup>64</sup> Xianggang Jizhe Xiehui Gongzuo Fang (香港記者協會工作坊), *Xinjie Xiang Jiao Tudi Gaikuang* (新界鄉郊土地概況) [Profile of the New Territories Rural Lands], DEV. BUREAU, PLAN. DEP'T & LANDS DEP'T 18 (Nov. 18, 2017), [https://www.landsd.gov.hk/doc/en/smo/HKJA\\_20171118.pdf](https://www.landsd.gov.hk/doc/en/smo/HKJA_20171118.pdf).

<sup>65</sup> See *LCQ21: Amendment of Plans and Modification of Land Leases*, *supra* note 63.

<sup>66</sup> See Jimmy Chow, *Land-use Conversions in Hong Kong to Make Areas Available for Housing Developments Present Many Challenges*, S. CHINA MORNING POST (Sept. 2, 2016, 1:00 PM), <https://www.scmp.com/property/article/2012934/land-use-conversions-present-many-challenges-process-making-areas-available> (“[L]and premium negotiations are typically a lengthy back-and-forth process . . .”).

peaking at 115,000 in 2014.<sup>67</sup> This growth in public comment has imposed a mammoth burden of the Board as it has a legal duty to consider each comment.<sup>68</sup>

The delay imposed by the plan amendment process, however, is compounded by the even more serious delay created by negotiations over the premium payment to the government that is required by lease modification. This premium equals the difference between the value of land before and after the modification.<sup>69</sup> Premium assessments are centrally processed by the Valuation Section of the Lands Department and are communicated to the applicant by the District Lands Office by way of a binding basic terms offer.<sup>70</sup> If applicants disagree with the premium demanded by the Government, they may launch an appeal against the premium to the Appeal Team of the Valuation Section and seek further judicial review of the Appeal team's decision on procedural grounds.<sup>71</sup> The government cannot compel the lessee-owner to accept the government's terms for lease modification, so the disagreement over lease premiums may continue indefinitely, without any conclusion being reached.<sup>72</sup>

Both developers and the Hong Kong government have become frustrated by the time and cost of going through plan amendment and lease modification process, including premium negotiation. Developers have manifested such frustration by forgoing lease modification of their

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<sup>67</sup> 兩條路線加快造地（上）：加強地區協調 理順改劃分歧 [Two Routes to Speed Up Land Reclamation (Part 1): Strengthening Regional Coordination and Straightening out Differences in Rezoning], BAUHINIA FOUND. RSCH. CTR. (Apr. 18, 2020), <http://www.bauhinia.org/index.php/zh-HK/analyses/966>.

<sup>68</sup> See Chengshi Guihua Tiaoli (城市规划条例) [Town Planning Ordinance] §§ 6B(1), 6F(1); *Plan Making*, TOWN PLAN. BD. (Aug. 22, 2019), [https://www.info.gov.hk/tpb/en/plan\\_making/participate.html](https://www.info.gov.hk/tpb/en/plan_making/participate.html).

<sup>69</sup> See *Land Disposal and Transaction: Premium/Rental Assessment*, H.K. LANDS DEP'T, <https://www.landsd.gov.hk/en/land-disposal-transaction/premium-rental-assessment.html> (last updated Mar. 31, 2021).

<sup>70</sup> *Id.*

<sup>71</sup> *Premium Assessment Procedures Relating to Lease Modification Transactions*, H.K. LANDS DEP'T ¶ 2(iv)-(v) (2006), [https://www.landsd.gov.hk/doc/en/practice-note/lpn/2006-1e\\_text.pdf](https://www.landsd.gov.hk/doc/en/practice-note/lpn/2006-1e_text.pdf).

<sup>72</sup> See *LCQ19: Pilot Scheme for Arbitration on Land Premium*, H.K. PRESS RELEASES (Nov. 7, 2018, 1:30 AM), <https://www.info.gov.hk/gia/general/201811/07/P2018110700354p.htm>.

own properties and instead bidding in the government's auctions to acquire entirely new leases.<sup>73</sup> The government has manifested its frustration with various subtle schemes to speed up the negotiation process.<sup>74</sup> These schemes have attracted little developer interest as they do not break the gridlock of bargaining between the government which controls the right to develop and developers who control the actual land.

The government's auctioning off completely new leases of unleased Crown land could, in theory, sidestep the obstacles posed by the lease modification process. In practice, however, the government does not have much land left for such auctions<sup>75</sup> whereas it controls 1,200 hectares of "village-type development land" for generations of indigenous villagers' future claim to their small-house rights. In the 2020-2021 fiscal year, the Hong Kong government did not sell a single plot of private residential land.<sup>76</sup>

The government has faced analogous obstacles in increasing the permitted densities on the 3,380 ha of village land held by indigenous villagers or their associations. As noted above, the villagers are eager to convert the land to higher-density residential uses, but other Hong Kong residents are less enthusiastic: Only 25% of survey respondents who were not indigenous villagers supported such conversion.<sup>77</sup> Part of the reason for such reluctance might be a popular sense that indigenous villagers already enjoy an unjust windfall in the form of the government's

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<sup>73</sup> Roger Nissim & John Corrigan, *Land Supply – Why and How We Need to Unlock the Private Sector's Land Banks to Help Meet Current Housing Need*, REAL EST. DEV. ASS'N H.K. ¶ 3 (Sept. 2016), <https://www.reda.hk/wp-content/uploads/2016/04/Lease-modifications-2016.pdf>.

<sup>74</sup> See generally *Information Note Relating to the "Pilot Scheme for Arbitration on Land Premium"*, H.K. LANDS DEP'T (2020), [https://www.landsd.gov.hk/doc/en/exc\\_mod/arbitration/Arbitration\\_Doc3.pdf](https://www.landsd.gov.hk/doc/en/exc_mod/arbitration/Arbitration_Doc3.pdf); *Land Sharing Pilot Scheme and Guidance Note on Applications*, H.K. DEV. BUREAU ¶¶ 1, 3, 24 (2020), [https://www.devb.gov.hk/filemanager/en/content\\_1152/LSPS\\_GN\\_e.pdf](https://www.devb.gov.hk/filemanager/en/content_1152/LSPS_GN_e.pdf).

<sup>75</sup> See *Transcript of Secretary for Development Bureau's Media Interview*, H.K. PRESS RELEASE (Dec. 17, 2014, 8:24 AM), <https://www.info.gov.hk/gia/general/201412/17/P201412171139.htm>.

<sup>76</sup> See «東方» 助覓地紓房困 政府懶理硬推填海 [Oriental Helps Find Land to Relieve Housing Difficulties; The Government Pushes Reclamation], ORIENTAL ENTER. (Dec. 15, 2020, 11:15 AM), [https://hk.on.cc/hk/bkn/cnt/news/20201215/bkn-20201215001520600-1215\\_00822\\_001.html](https://hk.on.cc/hk/bkn/cnt/news/20201215/bkn-20201215001520600-1215_00822_001.html).

<sup>77</sup> Groups Advocate the Relaxation of the Building of Ten-Storey Small House, *supra* note 58.

“small house policy.” This policy not only discriminates against female villagers (because only male villagers are entitled to a small house under the traditional Qing Dynasty custom) but also provides a housing windfall to a small group of Hong Kong residents. Motivated by such concerns, a citizen activist, Kwok Cheuk Kin, filed an unsuccessful lawsuit to revoke the policy.<sup>78</sup> Wary about being blamed for colluding with the rich, the government has chosen the safest path of simply maintaining the “small house” status quo. Although this status quo sometimes involves clearly illegal transactions<sup>79</sup> of small house rights involving powerful indigenous politicians and developers, the government continues to insist in the face of a serious housing shortage that all such buildings be no taller than three floors.<sup>80</sup>

## 2. Feeble Leviathan: The Failure of Land Resumption in Breaking the Deadlock

The government, of course, need not rely on developers or villagers to produce housing. At least in theory, the government could simply acquire the land over the objections of its current lessee-owners through the forced resumption of leases.<sup>81</sup> The lessee-owners would be entitled to just compensation, but that price would be objectively defined by courts that could, again in theory, sidestep the endless haggling that has stalled lease modifications.

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<sup>78</sup> See Kwok Cheuk Kin v. Dir. Lands, *supra* note 52.

<sup>79</sup> See Wah Hing Strategy Co. v. Tang Wai Hung [2014] H.K.C.U. 1200.

<sup>80</sup> See Wu Wanying (吳婉英), Jie 9,878 Zong Yisi Taoding Gean (揭9,878宗疑似「套丁」個案) [Uncovering 9,878 Suspected Cases of Illegal Selling of Rights of New Territories], Zhong Xinwen (眾新聞) [CITIZEN NEWS] (Jan. 5, 2018), <https://www.hkcnews.com/article/9241/%E5%A5%97%E4%B8%81-%E6%9C%AC%E5%9C%9F%E7%A0%94%E7%A9%B6%E7%A4%BE-%E5%9C%B0%E6%94%BF%E7%B8%BD%E7%BD%B2-9248/%E6%8F%AD9878%E5%AE%97%E7%96%91%E4%BC%BC%E3%80%8C%E5%A5%97%E4%B8%81%E3%80%8D%E5%80%8B%E6%A1%88-%E4%BD%94%E6%96%B0%E7%95%8C%E4%B8%81%E5%B1%8B%E7%B8%BD%E6%95%B823-%E6%9C%AC%E5%9C%9F%E7%A0%94%E7%A9%B6%E7%A4%BE%E6%89%B9%E6%94%BF%E5%BA%9C%E8%A6%96%E8%8B%A5%E7%84%A1%E7%9D%B9> .

<sup>81</sup> Lands Resumption Ordinance, Hong Kong SAR; Can the Lands Resumption Ordinance offer a way out of Hong Kong’s housing crisis and quell protests?, <https://www.scmp.com/news/hong-kong/hong-kong-economy/article/3027209/can-lands-resumption-ordinance-offer-way-out-hong>.

The theoretical possibility of the government's acting as an all-powerful Leviathan, however, has been largely a practical failure. The reason seems to be fear on the part of judges and other officials that the government's too aggressively attacking private property rights would ruin Hong Kong's reputation as an enclave protective of investors. The result has been a cautious and glacially slow use of land resumption, almost exclusively to convert some brownfields into more valuable uses.

The legal obstacles to quick and aggressive land resumption are baked into the Hong Kong Basic Law and implementing ordinances. Article 105 of the HK Basic Law obliges the Hong Kong government to protect individuals' and legal persons' rights to property and just compensation.<sup>82</sup> Section 3 of the Land Resumption Ordinance<sup>83</sup> ("the LRO") further authorizes the Chief Executive to order land resumption only for a "public purpose," term that both the government and the courts have construed narrowly and excluded private housing development.<sup>84</sup> While the government has exercised the resumption power authorized under the LRO more than 160 times since the 1997 handover, these resumption cases have been painfully slow: Five land resumption for public housing cases in the past 10 years took an average of 7.1 years from publication of the notice in the Gazette until final completion of the project.<sup>85</sup> Moreover, the government has been reluctant to use its resumption power outside a narrow definition of "public purpose," emphasizing that Hong Kong, "as a free economy, respects the

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<sup>82</sup> HONG KONG BASIC LAW, art. 105.

<sup>83</sup> Land Resumption Ordinance, (1900) Cap. 124, § 3 (H.K.).

<sup>84</sup> Section 2 of the Land Resumption Ordinance; *Fok Lai Ying v. Governor Council*, [1997] 1 H.K.L.R.D. 111; *How to Receive Compensation for Private Land Resumed in the New Territories by the Government*, H.K. LANDS DEP'T (May 2006), [https://www.landsd.gov.hk/doc/en/land-acq-clearance/land-resumption-clearance/acq-compensation/reccomp\\_e.pdf](https://www.landsd.gov.hk/doc/en/land-acq-clearance/land-resumption-clearance/acq-compensation/reccomp_e.pdf).

<sup>85</sup> Shouhui Tudi Tiaoli Shi Shenme? (《收回土地條例》是甚麼?) [What is the Land Resumption Ordinance?], XIANGGANG JINGRI RIBAO (香港經濟日報) [H.K. ECON. TIMES] (Oct. 3, 2019), <https://ps.hket.com/article/2461652>.

right of private ownership of property.”<sup>86</sup> Accordingly, the government has never used land resumption to create purely private market-rate housing.

The slow pace of land resumption has been reinforced by litigation over just compensation, guaranteed by section 6 of the LRO. In theory, the compensation rules give the government significant advantages. *Director of Lands v Yin Shuen Enterprises Ltd*<sup>87</sup> held that Section 10 of the LRO, which bases the amount of compensation on the loss or damage resulting from the resumption of the lease, only provides for the value of land uses permitted by the lessee’s deed, even when it is probable that the deed would be modified by the government absent resumption. This doctrine would theoretically permit the government to acquire land leased to tycoons for agricultural or warehouse purposes at a much lower value than the residential value that the government would earn by resuming the lease and converting the land to residential high-rises. Despite this theoretical capacity for the government to resume leases with minimal compensation, however, there has been frequent and time-consuming litigation over the compensable value of resumed leases.<sup>88</sup> For instance, in the case of *Nam Chun Investment Co Ltd*,<sup>89</sup> the company, dissatisfied with the statutory compensation awarded in 1999, launched a series of appeals that were not resolved until 2007.

The expense and time required for lease resumption has led the government to use it sparingly. Carrie Lam, the Chief Executive, advised the Legislative Council during a Question and Answer Session that the Lands Resumption Ordinance should not be invoked arbitrarily

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<sup>86</sup> *LCQ5: Use of Lands Resumption Ordinance by Government*, H.K. PRESS RELEASES (June 27, 2018, 4:02 AM), <https://www.info.gov.hk/gia/general/201806/27/P2018062700628.htm>.

<sup>87</sup> *Dir. Lands v. Yin Shuen Enterprises*, [2013] 2 H.K.L.R.D. 399 (C.F.A.).

<sup>88</sup> See Shouhui Tudi Tiaoli Buchang Tudi Fazhan Qianli de Feihei Jibai (《收回土地條例》補償——土地發展潛力的非黑即白) [Compensation under the Land Resumption Ordinance – the Development Potential of Land is Either Black or White], HONG KONG BAR ASSOCIATION (May 2015), <https://www.hkba.org/node/13844>.

<sup>89</sup> *Nam Chun Investment Co. v. Dir. Lands*, [2005] 4 H.K.L.R.D. 480 (C.F.A.); *Nam Chun Investment Co. v. Dir. Lands*, [2017] 10 H.K.C.F.A.R. 523 (C.F.A.).

because “owners whose private ownership is being infringed upon ... will apply for judicial review against the Government,” with such lawsuits lasting as long as eight to nine years.<sup>90</sup> The Wan Chai Outline Zoning Plan (OZP), for example involved multiple JR applications since 2011: With follow-up work still in progress, the OZP has yet to be submitted to the Chief Executive in Council for approval, impeding the development of various sites within the district.<sup>91</sup>

### **3. The Bias of Hong Kong’s Political Process for Locking in the Status Quo**

These failures of voluntary bargaining, land auctions, or lease resumptions to produce housing naturally leads to the question: What about political pressure from Hong Kongers suffering from inadequate, over-crowded, and expensive housing? There has been substantial political activism concerning housing over the last quarter-century— but the activists have opposed rather than supported the construction of new housing.

The most dramatic example of such opposition was the defeat of Chief Executive Tung Chee-hwa’s “85,000 Plan” between 1997 and 2000.<sup>92</sup> In his 1997 Policy Address, Tung Chee-hwa announced to build at least 85 000 flats a year in the public and private sectors (Known as the “85,000 Plan”).<sup>93</sup> This plan to enlarge housing supply, however, ran aground on the 1997 financial crisis in which a bubble in housing prices, which inflated rapidly since 1995, suddenly burst, trapping hundreds of thousands of mortgage buyers in negative equity.<sup>94</sup> The collapse of

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<sup>90</sup> *LCQ5: Use of Lands Resumption Ordinance by Government*, H.K. PRESS RELEASES (June 27, 2018, 4:02 AM), <https://www.info.gov.hk/gia/general/201806/27/P2018062700628.htm>.

<sup>91</sup> *Id.*

<sup>92</sup> See Gary Cheung, *Why Ties Between Beijing and Hong Kong’s Property Bosses Are Unraveling*, INKSTONE NEWS (Sept. 25, 2019), <https://www.inkstonenews.com/politics/why-ties-between-beijing-and-hong-kongs-property-bosses-are-unraveling/article/3030300>.

<sup>93</sup> *See id.*

<sup>94</sup> Between the fourth quarter of 1995 and the third quarter of 1997, the property price in Hong Kong recorded a 66% increase. Accordingly, the property price dropped drastically by mid-2000 to around 50% of peak prices in October 1997. Victor Jing Li, *Housing Policies in Hong Kong, China and The People’s Republic of China* 4 (Asian



housing prices in 1997 provoked substantial opposition from the Hong Kong real estate industry and property owners. The Hong Kong Institute of Real Estate Administration, the professional body of representing the real estate sector, urged the government to reduce the housing supply to boost property prices.<sup>95</sup> Likewise, Thomas Kwok Ping-kwong, the vice chairman of Sun Hung Kai Property, warned that bringing 85,000 new units onto the market could cause the bottom to drop out of the housing market.<sup>96</sup> In June 2000, the Liberal Party, a pro-Beijing, pro-business political party, mobilized a substantial protest (1,000 people)<sup>97</sup> in opposition to the 85,000 Policy, with the ostensible aim of protecting people's assets.<sup>98</sup> By the summer of 2000, Tung Chee Hwa surrendered to this anti-housing campaign, saying in a June 29<sup>th</sup> interview that the “85,000 Policy” no longer existed.<sup>99</sup>

The campaign against the “85,000 Plan” was self-consciously a narrowly self-interested effort by the real estate industry and mortgage holders to boost land prices by restricting supply. Other more public-spirited activists, however, have not made promotion of higher land prices as their goal. They have instead aimed at protecting non-indigenous farmers from unjust

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Dev. Bank Inst., ADBI Working Paper No. 566, 2016),  
<https://www.adb.org/sites/default/files/publication/183031/adbi-wp566.pdf>.

<sup>95</sup> See Hong Kong Legislative Council, LC Paper No. CB(1)1900/99-00(01) (2000), <https://www.legco.gov.hk/yr99-00/chinese/panels/hg/papers/1-1900c01.pdf>.

<sup>96</sup> YUEMAN-YEUNG (杨汝萬), ANJU LEYE ZHAN MINGTIAN (安居乐业展明天) [BETTER HOUSING TOMORROW] 7, 18 (1998).

<sup>97</sup> Zhongchan Nahan Fu Zichan (中產吶喊負資產) [Middle Class Protests of Negative Assets], TELEVISION BROADCAST LIMITED (June 26, 2000), [http://ifiles.tvb.com/ifiles/20000626/f\\_more/20000626\\_445.html](http://ifiles.tvb.com/ifiles/20000626/f_more/20000626_445.html).

<sup>98</sup> Huiyi Guocheng Zhengshi Jilu (会议过程正式纪录) [Official Records of Meeting], H.K. LEGIS. COUNCIL (July 12, 2002), <https://www.legco.gov.hk/yr01-02/chinese/counmtg/hansard/cm0712ti-translate-c.pdf>.

<sup>99</sup> Ricardo Saludo, *A Bit Too Much in Hong Kong*, ASIaweek (July 5, 2000, 3:30 AM), <http://www.cnn.com/ASIANOW/asiaweek/intelligence/2000/07/05/#lede2>.

dispossession<sup>100</sup> and preserving county parks and historic landscapes and buildings.<sup>101</sup> All these efforts have had the same effect: They prevent the government from enlarging Hong Kong's housing supply.

The political strength of anti-development forces is powerfully illustrated both by their vote-getting influence in Legislative Council elections and their capacity to block the government's development initiatives. Eddie Chu Hoi-dick, the charismatic head of the Land Justice League, won the legislative council election with 84,121 votes in 2016, making him Hong Kong's "King of the Vote."<sup>102</sup> The development-blocking power of anti-development groups is also well-illustrated by the inability of the government to adjust the boundaries of county parks to provide land for housing development. Country parks cover roughly 40% of Hong Kong's total land area – more than ten times the total area occupied by any sort of residential use<sup>103</sup> Efforts to convert any parkland to housing, however, has met with vociferous resistance from environmental groups and neighbors abutting the parks. When the South East New Territories Landfill ("the SENTL") proposed to use 5 hectares of land in the Clear Water Bay ("CWB") Country Park, for instance, nearby Tseung Kwan O residents and district councils fiercely objected, provoking the Legislative Council to "veto" the proposal despite support from

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<sup>100</sup> See Olga Wong, *Non-indigenous Villagers Lose Out in Compensation for Loss of Their Homes*, S. CHINA MORNING POST (July 7, 2014), <https://www.scmp.com/news/hong-kong/article/1548175/non-indigenous-villagers-lose-out-compensation-loss-their-homes>; *No Eviction for Wang Chau Villagers Before Lunar New Year, but Further Compensation Unlikely, Officials Say*, S. CHINA MORNING (Nov. 6, 2017), <https://www.scmp.com/news/hong-kong/community/article/2118664/no-eviction-wang-chau-villagers-lunar-new-year-further>.

<sup>101</sup> Junren Zhou (周峻任), *Dushi Jianshe Bentu Shenfen yu Shehui Yundong* (都市建設、本土身份與社會運動) [Metropolis Construction, Local Identity and Social Movement], 29 LINGNAN YANJIU (嶺南研究) 6 (2012); Tanna Chong & Gary Cheung *Protesters Storm Legco over Northeastern New Territories Plan*, S. CHINA MORNING POST (June 7, 2014), <https://www.scmp.com/news/hong-kong/article/1526945/protesters-storm-legco-over-northeastern-new-territories-plan>.

<sup>102</sup> See Kris Cheng, *Interview: 'King of Votes' Eddie Chu Says It's Time for a Real Hong Kong Democratic Movement*, H.K. FREE PRESS (Dec. 25, 2016, 12:01 AM), <https://hongkongfp.com/2016/12/25/interview-king-of-votes-eddie-chu-says-its-time-for-a-real-hong-kong-democratic-movement/>.

<sup>103</sup> Task Force on Land Supply, *Developing Country Parks*, H.K. DEV. BUREAU ¶ 2 (Dec. 5, 2017), [https://www.devb.gov.hk/filemanager/en/content\\_1054/Paper\\_11\\_2017.pdf](https://www.devb.gov.hk/filemanager/en/content_1054/Paper_11_2017.pdf).

the Chief Executive.<sup>104</sup> Although there was uncertainty over whether the Legislative Council actually had the power to repeal an order of the Chief Executive,<sup>105</sup> the government eventually backed down in the face of such vehement and well-organized opposition.<sup>106</sup>

The inability of the government to overcome resistance to development of existing land is highlighted by the government's preferring to reclaim entirely new land from the ocean in spite of reclamation's gargantuan cost. Carrie Lam's signature project is to reclaim 1,700 hectares of land from the ocean at a cost of 600 billion Hong Kong dollars.<sup>107</sup> Lam favored this proposal, dubbed "the Lantau Tomorrow Vision," over the recommendations of her own Task Force of Land Supply, which had identified development of brownfield sites and agricultural land as superior options.<sup>108</sup>

The government, in sum, is trapped between anti-development activists powerful developers and indigenous landowners. The government cannot let developers and indigenous landowners develop their land for free without provoking the activists' ire at an apparently corrupt giveaway. But the government also cannot induce the developers and villagers to pay a premium acceptable to those activists. As for using its theoretical power simply to take over the land using lease resumption, the government and courts are both fearful of deterring investors with disrespect for private property rights. Seeking land in which no interest group currently has any stake, therefore, the government pins its hopes on a fantasy of dredging up earth from the

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<sup>104</sup> *Protection of Country Parks and Special Areas*, H.K. AUDIT COMMISSION ¶ 3.37 (Oct. 30, 2013), [https://www.aud.gov.hk/pdf\\_e/e61ch05.pdf](https://www.aud.gov.hk/pdf_e/e61ch05.pdf).

<sup>105</sup> Gu Min Kang (顧敏康), *Lun Xianggang Lifahui Dui Fushu Fagui de Foujue Quan (論香港立法會對附屬法規的否決權)* [On the Veto Power of the Hong Kong Legislative Council over Subsidiary Legislation], 8 *Yiguoliangzhi Yanjiu (一國兩制研究)* [JOURNAL OF ONE COUNTRY TWO SYSTEMS STUDIES] 127, 129-30 (2011).

<sup>106</sup> *Protection of Country Parks and Special Areas*, *supra* note 104 at ¶ 3.38.

<sup>107</sup> *Lantau Tomorrow Vision*, S. CHINA MORNING POST, <https://www.scmp.com/topics/lantau-tomorrow-vision> (last visited Nov. 21, 2021).

<sup>108</sup> *The Chief Executive's 2017 Policy Address: We Connect for Hope and Happiness*, H.K. CHIEF EXEC.'S POL'Y ADDRESS ¶ 143, Annex 2, <https://www.policyaddress.gov.hk/2017/eng/pdf/PA2017.pdf>.

ocean. But “Lantau Tomorrow Vision” likely is all too literally described by its name: It is likely nothing more than an effort to postpone for another day the conundrum by proposing something that cannot be done within the Chief Executive’s own term of office.

### **III. Diagnosing the Problem: How Bilateral Monopoly and Constituency Effects Together Block Housing Development**

Here, then, is the mystery in need of explanation. Everyone agrees that Hong Kong faces a colossal crisis in its shortage of affordable housing. Moreover, both the Hong Kong government and the current lessee-owners of the land want to convert three-story small houses, fallow farmland, and warehouses and other brownfield uses into high-density housing. Yet somehow neither the negotiations between the lessee-owners and the government nor the politics of Hong Kong will allow for that conversion. Instead, Hong Kong is stuck with “agricultural” land that has never been farmed, tiny rural homes that even their occupants think are wasteful uses of land, and an eyesore of parking lots, warehouses, and other brownfield uses manifestly less necessary than residential apartments.

What has locked Hong Kong into such a perverse use of its ample real estate? We argue in this section that Hong Kong’s housing predicament is the foreseeable result of some dynamics familiar from property theory. Because the government and lessee-owners negotiate over the zoning and leases of each parcel one at a time, their negotiations are afflicted by bilateral monopoly that encourages each side to misrepresent their actual valuation of current and prospective uses. Since Calabresi and Melamed published *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*,<sup>109</sup> property theorists have offered a lot of now-familiar solutions to the problem of bilateral monopoly. An impartial arbiter might, for instance,

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<sup>109</sup> See generally Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972).

simply enforce some sort of liability rule, forcing a sale at an objectively determined price. Those liability rules have gotten increasingly exotic: Scholars have concocted a dizzying number of fancy mechanisms -- call options, taxes, auctions, etc. – to force tight-lipped negotiators to reveal how much they actually value an asset.<sup>110</sup> As we explain in Part III(B) below, however, all of these solutions assume away the problem of property’s “constituency effects.” The “constituency effects” of a law are the law’s promotion of a politically effective constituency through the creation of a focal point around which that constituency can rally. By creating a sense of common entitlement, property law helps mobilize and organize otherwise politically ineffective constituents to defend that legal assignment. The result of this sense of entitlement is that the exotic mechanisms of self-valuation, auctions, or objective appraisal of assets’ values are, politically speaking, off the table.

Somehow the law must sidestep the power of existing entitlement holders to protect their entitlements in the political process by creating a new constituency capable of breaking the gridlock that paralyzes negotiations over those entitlements. We will offer one such possible solution in Part IV. In this section, we merely lay out the gravity and pervasiveness of the problem created by the interaction of bilateral monopolies and constituency effects that protect such monopolies from political correction.

#### **A. The Problem of Bilateral Monopoly and Its Theoretical Solutions**

Consider, first, how the endless haggling between the government and lessee-owners follows the typical pattern of parties’ concealing their preferences because of a bilateral monopoly. The government and lessee-owners are locked into such a “monopoly,” because there are no

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<sup>110</sup> For a summary of sixteen such mechanisms, see generally Saul Levmore, *Unifying Remedies: Property Rules, Liability Rules, and Startling Rules*, 106 YALE L.J. 2149 (1996-1997). For an example of some exotic varieties of such rules, see, e.g., Abraham Bell & Gideon Parchomovsky, *Pliability Rules*, 101 MICH. L. REV. 1 (2002).

competing suppliers of the items (uses of parcels, lease modifications) that each is buying or selling. If villagers or real estate tycoons turn down the government's offer of a lease modification, there are no alternative buyers of lease modifications to which the government can turn. Likewise, if the government demands an extortionate premium to modify a lease, then the lessee-owners cannot seek out another seller of lease modifications who might offer a more reasonable price. Forced to deal only with each other, each side has incentives to bargain deceptively, dragging out negotiations interminably.<sup>111</sup>

The problem posed by lease modification in Hong Kong is familiar from many other property settings. The assembly of land through eminent domain, for instance, is the product of an identical sort of strategic concealment of valuations. Sellers who know that their parcel is essential for a larger project have incentives to misrepresent the price that they will accept to sell to a land assembler. Buyers who are assembling the land have an incentive to misrepresent the benefits created by assembly in order to exclude the seller from getting a share of those benefits. Because there are not competing buyers and sellers who offer competing offer and asking prices, negotiations stall and sometimes breakdown entirely.<sup>112</sup>

Just as the problem of strategic holdouts is familiar, there are lots of familiar solutions to that problem, all of which limit, in one way or another, the absolute power of one or the other side to demand any price they please. Guido Calabresi and Douglas Melamed famously set the terms for all such solutions with the idea of a "liability rule" under which one side could force a sale of the

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<sup>111</sup> The problem of bilateral monopoly, a specific case of buying in a thin market where efficient outcomes cannot be insured by purely voluntary bidding between a seller and buyer, is described by Roger B. Myerson & Mark A. Satterthwaite, *Efficient Mechanisms for Bilateral Trading*, 29 J. ECON. THEORY 265 (1983). Carol M. Rose has characterized such bilateral monopoly as a special form of transaction cost blocking Coasean bargains in *In the Shadow of The Cathedral*, 106 YALE L.J. 2175, 2184 (1997), calling them "Type II Transaction Costs" to distinguish them from the costs of identifying the parties with a legally protected interest in property.

<sup>112</sup> For an overview of this "holdout" problem, see Thomas Merrill, *The Economics of Public Use*, 72 Cornell L. Rev. 61 (1986).

asset at some objectively determined price.<sup>113</sup> Eminent domain and nuisance damages are two examples of such liability rules, but, in the half-century since Calabresi & Melamed's seminal article, scholars have proposed a profusion of exotic liability rules to force parties to show their hand. The basic idea underlying all such solutions is that some impartial arbiter will calculate the actual value of the asset to one side, charging that value to the other side who will, by rejecting or accepting it, honestly reveal that they value the asset more than the other side does.<sup>114</sup>

The basic challenge of any liability rule, however exotic, is that determining the actual value of an asset to a person is difficult. If the price is set too high, then it functions just as an injunction, blocking transactions that ought to occur; if the price is set too low, then it forces transactions that ought to be blocked.<sup>115</sup>

Legal scholars and economists have proposed a variety of cleverly designed liability rules to improve the accuracy of that objectively determined price. Ian Ayres and Jack Balkin, for instance, laid out a theory of "higher-order liability rules" in which an asset can be purchased by a party who matches the initial price set by an impartial arbiter.<sup>116</sup> That initial price, in effect, serves as the starting price in an auction between two bidders whose bids improve the accuracy of the initial award. For example, under Ayres & Balkin's proposal, the condemnee who was forced to sell their house to a land assembler for a judicially determined price could buy back the right to preserve the house by offering the assembler a higher price, and the assembler could respond in turn with yet another yet higher price to re-acquire the right of assembly. Economists

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<sup>113</sup> Calabresi & Melamed, *supra* note 109.

<sup>114</sup> For a comprehensive analysis of the theory that liability rules can force parties to reveal information about how much they value an asset, see Louis Kaplow & Steven Shavell, *Property Rules Versus Liability Rules: An Economic Analysis*, 109 HARV. L. REV. 713, 726–27 (1996).

<sup>115</sup> A. Mitchell Polinsky, *Resolving Nuisance Disputes: The Simple Economics of Injunctive and Damage Remedies*, 32 Stan. L. Rev. 1075 (1980) (first setting out this basic challenge).

<sup>116</sup> Ian Ayres & Jack M. Balkin, *Legal Entitlements as Auctions: Property Rules, Liability Rules, and Beyond*, 106 YALE L.J. 703, 749 (1996-1997).

and legal scholars have also enlisted uncertainty about the consequences of a party's valuation to improve the valuation's accuracy. Several such proposals rely on some sort of shared ownership of an asset with an obligation to buy each other's share at some valuation reflecting both parties' valuation.<sup>117</sup> Other scholars have suggested that making a self-declared valuation simultaneously the basis for property tax liability as well as compensation in eminent domain would give owners incentives to be honest in their self-valuation of assets, because owners who over-stated the value of their property for tax purposes would thereby risk losing their property for a low price if it were condemned.<sup>118</sup> Eric Posner and Glen Weyl have generalized from such self-valuation to urge a "common ownership self-assessed tax" (or "COST") in which owners are taxed on the value that they themselves declare, with that value simultaneously constituting the tax base as well as a price at which any buyer, not only the government, could purchase the asset in a forced sale.<sup>119</sup>

Whatever the details of the particular scheme, all such proposals share the idea that owners and buyers can be prodded into revealing how much they truly value an asset so that it ends up in the hands of the party who values it the most. It is easy, at least in theory, to imagine applying

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<sup>117</sup> See generally Peter Cramton, Robert Gibbons & Paul Klemperer, *Dissolving a Partnership Efficiently*, 55 *ECONOMETRICA* 615 (1987) (suggesting a "Texas Shoot-Out" in which each party would be obliged to purchase the other's share at an average of the two parties' bids); Ian Ayres & Eric Talley, *Solomonic Bargaining: Dividing a Legal Entitlement to Facilitate Coasean Trade*, 104 *YALE L.J.* 1027, 1073–80 (1994-1995) (arguing for (among other possible rules) a probabilistic division of assets, such that each party is uncertain about whether they will be the buyer or seller at a price based on each party's self-valuation of the asset). For a criticism of this proposal, see Louis Kaplow & Steven Shavell, *Do Liability Rules Facilitate Bargaining? A Reply to Ayres and Talley*, 105 *YALE L.J.* 221, 233 (1995). For an overview of division of an entitlement as a way to ensure accurate revelation of preferences, see Ilya Segal & Michael D. Whinston, *The Efficiency of Bargaining under Divided Entitlements*, 81 *U. CHI. L. REV.* 273 (2014).

<sup>118</sup> The idea of self-valuation by landowners for property taxation in which the government would reserve the option of purchasing the landowner's land at the value declared by the owner was proposed by Sun Yat-sen in 1905 and later implemented in Taiwan. See generally Emerson M. S. Niou & Guofu Tan, *An Analysis of Dr. Sun Yat-Sen's Self-Assessment Scheme for Land Taxation*, 78 *PUB. CHOICE* 103 (1994). It has been revived and refined by, among others, Saul Levmore, *Self-Assessed Valuation Systems for Tort and Other Law*, 68 *VA. L. REV.* 771 (1982), Lee Anne Fennell, *Revealing Options*, 118 *HARV. L. REV.* 1399 (2005) (providing an overview of such self-valuation systems, which she characterizes as "customizable callable calls").

<sup>119</sup> POSNER & WEYL, *supra* note 5, at 21.



one of these liability rules to the problem of property gridlock in Hong Kong. Indeed, the Hong Kong government's system of lease resumptions is the most basic form of liability rule: An impartial arbiter sets an objective price for the lessee-owners' lease, theoretically revealing that the government values the resumption more than the lessee-owner's value of the lease.

Following Ayres and Balkin, this simple liability rule might be refined by (for instance) giving the lessee-owners the right to buy back their lease from the government by offering a counter-price exceeding the court-defined price. Likewise, the government might invite lessee-owners to declare how much their lease is worth and then raise revenue by imposing a tax of some percentage of that value. Or the government might use the "Texas Shoot-Out" method of a divided entitlement under which the Hong Kong government and lessee-owners would each offer their own estimate of a fair premium for modifying leases to allow high-density housing, and each side would thereby obtain the option to force the other side either to pay the option holder the average of the two premiums or to accept such payment in exchange for surrendering such control.

And so forth: There is no shortage of policies that could theoretically be used to nudge each side into revealing its true valuation of Hong Kong land. So why have none of these clever proposals ever been suggested, let alone used, to break the Hong Kong impasse on housing?

#### **B. The Problem of Constituency Effects: How Property Rights Create A Sense of Entitlement That Blocks Political Change.**

The reason, we argue below, is the constituency effect created by property law. As a matter of practical politics, it would be impossible to transform existing property rights with these sophisticated liability rules, because they would be regarded by one or another politically powerful constituency as an unjust attack on existing property rights. Put another way, existing

property rights have fostered a sense of entitlement among the politically organized part of Hong Kong's residents that foils such reconfiguration of property law.

To better explain the obstacle posed by constituency effects, we will first review in Part III(B)(1) how law more generally can create focal points rooted in a sense of entitlement among the law's beneficiaries. We will then apply this literature in Part III(B)(2) to suggest how the sense of entitlement created by Hong Kong's existing system of property rights makes wholesale adoption of new liability rules extremely unlikely.

### **1. How Property Law Can Entrench Itself through Constituency Effects**

Laws create effective constituencies by uniting otherwise unorganized individuals into interest groups with a common stake in defending those laws. This unification of otherwise disorganized individuals occurs through a variety of mechanisms. Simply by singling out one characteristic of individuals as the legal basis for some entitlement the law can make those individuals identify as members of a group defined by that characteristic. The Social Security Act, for instance, made salient the characteristic of being over the age of 65, because this age triggered eligibility for Old Age insurance under the statute.<sup>120</sup> A law might also create a sense of entitlement by characterizing itself as a contract in which benefits are provided in return for some action from the beneficiaries. Again, the Social Security Act was self-consciously designed as such a contract by linking payment of benefits to covered individuals' paying payroll taxes while participating in the workforce.<sup>121</sup> The law might also inspire elite communication about benefits or direct education to beneficiaries from governmental officials or procedural

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<sup>120</sup> ANDREA CAMPBELL, *HOW POLICIES MAKE CITIZENS: SENIOR POLITICAL ACTIVISM AND THE AMERICAN WELFARE STATE* (Princeton Univ. Press 2003).

<sup>121</sup> See Paul Romer, *Preferences, Promises, and the Politics of Entitlement*, in *INDIVIDUAL AND SOCIAL RESPONSIBILITY: CHILD CARE, EDUCATION, MEDICAL CARE, AND LONG-TERM CARE IN AMERICA* 195, 195-200 (Victor R. Fuchs ed., Univ. Chicago Press 1996).

mechanisms by which beneficiaries can overcome obstacles to collective action, such as notices and hearings especially directed to beneficiaries of the law.<sup>122</sup>

The legal status quo can create an effective constituency simply by defining a single focal point around which the beneficiaries of that status quo can rally. Such focal points solve a collective action problem created by a population with multi-dimensional preferences and, therefore, multiple possible majority coalitions.<sup>123</sup> In such a population, citizens may waver between numerous possible bundles of benefits without coalescing around any single package. By picking out one such package on which citizens can focus, the legal status quo enables a stable coalition to form in defense of that status quo.<sup>124</sup> It helps, of course, that such status quo is plausibly defended as morally “correct” according to some widely accepted set of values.<sup>125</sup> There might, however, be several such “correct” answers: The legal status quo helps people overcome disagreement by picking out one such answer among many as the legally privileged “correct” answer.

Land-use regulation can be a powerful creator of constituencies through all such mechanisms. Landowners – especially homeowners -- often have large and undiversified investments in real estate the value of which is protected by such regulations.<sup>126</sup> By defining a

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<sup>122</sup> See generally Suzanne Mettler, *The Only Good Thing Was the G.I. Bill: Effects of the Education and Training Provisions on African-American Veterans' Political Participation*, 19 *STUD. AM. POL. DEV.* 31 (2005) (describing GI Bill's effect on political participation); Jacqueline Chattopadhyay, *Can Health Insurance Regulations Generate Citizen Constituencies?* 44 *J. HEALTH POLIT. POL'Y & LAW* 455, 462–63 (2019) (describing how poor visibility of complex and obscure programs can be reduced through elite communication).

<sup>123</sup> Peter Ordeshook, *Constitutional Stability*, 3 *CONST'L POL. ECON.* 137, 148 (1991). The point has made in the legal literature frequently since the 1990s, especially to justify judicial review. See, e.g., Tom Ginsburg & Richard H. McAdams, *Adjudicating in Anarchy: An Expressive Theory of International Dispute Resolution*, 45 *WM. & MARY L. REV.* 1229 (2004); David S. Law, *A Theory of Judicial Power and Judicial Review*, 97 *GEO. L. J.* 723 (2009).

<sup>124</sup> Barry R. Weingast, *The Political Foundations of Democracy and the Rule of Law*, 91 *AM. POL. SCI. REV.* 245, 263 (1997).

<sup>125</sup> *Id.*, at 258.

<sup>126</sup> WILLIAM FISCHER, *THE HOMEVOTER HYPOTHESIS: HOW HOME VALUES INFLUENCE LOCAL GOVERNMENT TAXATION, SCHOOL FINANCE, AND LAND-USE POLICIES* (Harv. Univ. Press 2005).

specific set of protections against neighboring uses that could lower property values, zoning regulations give neighbors a common focal point around which to rally to defend that investment. By entitling persons living close to proposed re-zonings to posted notice in the neighborhood and to protest land-use changes through a referendum, zoning laws further reenforce a sense of solidarity among homeowners that converts them into neighborhood defenders who dominate zoning hearings.<sup>127</sup> The zoned status quo can also be plausibly defended as a morally appropriate focal point around which homeowners can rally, because such owners can claim reliance on existing zoning restrictions when they purchased their homes. Thus, zoning is often regarded as a form of de facto property in political discourse, regardless of what constitutional doctrine says.<sup>128</sup>

Constituency effects can make creative liability rules politically impossible to enact. Consider, for example, Eric Posner and Glen Weyl's "common ownership self-assessed tax" or "COST." Their COST would require owners of property to declare a value of such property on the basis of which such property would not only be taxed but also subject to forced sale by any buyer. The history of American real property taxation, however, indicates that it is politically impossible to enact any such tax. Out of deference to the political influence of homeowners, virtually every state in the United States has adopted a system of fractional assessment under which residential real property is under-assessed relative to its actual value. Judicial efforts to alter such favoritism towards residential property have been handily rebuffed by legislatures

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<sup>127</sup> *Building Coalitions Out of Thin Air*, *supra* note 19, at 108–10 (2020); KATHERINE EINSTEIN, MAXWELL PALMER & DAVID GLICK, *NEIGHBORHOOD DEFENDERS* (Cambridge Univ. Press 2019).

<sup>128</sup> Courts occasionally recognize the popular understanding of zoning as a kind of contract in construing state statutes if not in enforcing formal constitutional doctrine. *See, e.g.*, *Neighbors in Support of Appropriate Land Use v. County of Tuolumne*, 68 Cal. Rptr. 3d 882, 1009–10 (Cal. Ct. App. 2007) (characterizing zoning as "similar in some respects to a contract" insofar as "each party foregoes rights to use its land as it wishes in return for the assurance that the use of neighboring property will be similarly restricted, the rationale being that such mutual restriction can enhance total community welfare").

fearful of provoking anger from homeowners.<sup>129</sup> Moreover, there is a durable psychological foundation for this political reality: Americans tend to oppose taxation of non-realized capital gains.<sup>130</sup> Posner and Weyl devote a few pages to speculations that people might eventually adopt a sort of “optimal Buddhism” that would eliminate their “fetishistic attachment” to property that causes them to resist such forced sales.<sup>131</sup> If the reform of property rules depends on such a “Buddhist” change of heart, however, then it hardly seems obvious why the change in property rules would be necessary in the first place: Presumably these “optimal Buddhists” who have such a relaxed attitude towards their possessions also would not strategically exploit private information to outwit the people with whom they bargain.

The same objections apply to other exotic forms of liability rules: To the extent that they contradict a sense of entitlement created by the existing property status quo, they will have no chance at being enacted by any legislature. Forced sales at prices set by novel auctions or liability rules, therefore, have only academic interest unless those sales can somehow be made politically palatable by side-stepping the constituency effects of the very property law that these rules hope to change.

## **2. The Constituency Effects of Hong Kong’s System of Property law**

Hong Kong’s system of property law has the hallmarks of self-entrenching constituency effects described above. The existing stakeholders hold powerful positions in Hong Kong politics, and they defend their stakes with entitlement-based rhetoric rooted in promise and

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<sup>129</sup> For a description of the arbitrary discriminations produced by fractional assessment in New York, see Alan Finder & Richard Levine, *Unequal Burden: New York's Property Tax; Hodgepodge of Home Valuations Produces Disproportionate Taxes*, N.Y. TIMES (July 6, 1991), <https://www.nytimes.com/1991/07/06/nyregion/unequal-burden-new-york-s-property-tax-hodgepodge-home-valuations-produces.html>.

<sup>130</sup> Zachary Liscow & Edward Fox, *The Psychology of Taxing Capital Income: Evidence from a Survey Experiment on the Realization Rule 3* (Tax Law and Policy Colloquium, working paper 2021), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3848064](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3848064).

<sup>131</sup> POSNER & WEYL, *supra* note 5, at 79–80.

history. The track record of the Hong Kong government's failed effort to alter these entitlements when confronted with such rhetoric suggests the futility of the sorts of exotic liability rules that are standard fare for improving bargaining over assets.

Consider how Hong Kong's unsuccessful experience with land resumption, the simplest liability rule, suggests the likely failure of more sophisticated versions of forced sales. As described above in Part II(C)(2), land resumption has been a failure because litigation over just compensation and public purpose has been too time-consuming and expensive. Under existing law, leases cannot be resumed by the government to produce private market-rate housing, because such housing is deemed by courts not to be a "public purpose" under the Land Resumption Ordinance. Even for such public purposes, the government is obliged to pay compensation that is the subject of apparently interminable litigation. Of course, the Legislative Council or the National People's Congress might amend the Lease Resumption Ordinance or even the Basic Law to modify these rules. The Hong Kong government has, however, been extraordinarily reluctant to play hard ball with lessee-owners, apparently out of deference to Hong Kong's reputation for having "a free economy" which "respects the right of private ownership of property." Behind this rhetoric is a sense that land development companies sitting on thousands of acres of now-useless land purchased at low prices nevertheless have a moral expectation of a return on their investment that more aggressive lease resumption would disrupt. Such worries might be framed in terms of moral hazard: By resuming leases in defiance of those developers' expectations of eventual development, the government would deter further investment in Hong Kong.

Whatever the economic merit of these worries, they are backed by the powerful political influence of the lessee-owners. Developers, in particular, are politically influential. Since the

handover, tycoons with large investments in real estate have in effect controlled about a quarter of the appointments to the election committee that chooses the territory's top leader.<sup>132</sup> A member of Legco elected by one of the "functional constituencies" that represent a specific business sector expresses shame at his role, saying that "I'm a mercenary for the rich."<sup>133</sup> Such votes may not be sufficient to dictate who is going to be Hong Kong's chief executive, but they are sufficient to embarrass Beijing, who relies on a stable pro-Beijing coalition to govern. Key members of that coalition are developers and indigenous villagers. Taking the 2012 Chief Executive Election as an example, the four biggest developers and Heung Yee Kuk, which represent indigenous villagers, backed Henry Tang, who won 390 nomination tickets, much more than the 305 nominations won by Leung Chun-ying,<sup>134</sup> who was backed by Beijing. Lee Ka Shing, the Chairman of CK holding limited, said publicly that he supported Henry Tang on the election day.<sup>135</sup> Eventually, with Beijing's coordination and backing, Leung obtained 689 votes (65.62% of the total number of votes), merely 88 votes higher than the election threshold, whereas Tang obtained 285 votes (27.1% of the total number of electoral vote).<sup>136</sup>

Like Hong Kong's great land companies, the indigenous villagers are armed with both powerful political rhetoric and political influence against the liability rules that would force any

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<sup>132</sup> *China's Communist Party Chips Away at Hong Kong Business Houses*, ECONOMIST (May 22, 2021) <https://www.economist.com/leaders/2021/05/22/what-to-do-about-a-labour-crunch>.

<sup>133</sup> *China Is Not Just Shackling Hong Kong, It Is Remaking It*, ECONOMIST (Mar. 18, 2021), [https://www.economist.com/briefing/2021/03/20/china-is-not-just-shackling-hong-kong-it-is-remaking-it?itm\\_source=parsely-api](https://www.economist.com/briefing/2021/03/20/china-is-not-just-shackling-hong-kong-it-is-remaking-it?itm_source=parsely-api).

<sup>134</sup> Wu Da Dichan Shang Qi Cheng Tang Chuzhan (5 大地產商 齊撐唐出戰) [Five Major Real Estate Developers Support Tang's Running in Election], H.K. ECON. TIMES (Feb. 21, 2021), <https://paper.hket.com/article/767077/5%E5%A4%A7%E5%9C%B0%E7%94%A2%E5%95%86%20%E9%BD%8A%E6%92%91%E5%94%90%E5%87%BA%E6%88%B0>.

<sup>135</sup> Xuanwei Baitai Xian Yanliang (選委百態顯炎涼) [Election Committee at a Glance], Dongfang Ribao – Xiri (東方日報 - 昔日) [Oriental News], ORIENTAL ENTER. (Mar. 26, 2012), [https://orientaldaily.on.cc/cnt/news/20120326/00176\\_023.html](https://orientaldaily.on.cc/cnt/news/20120326/00176_023.html).

<sup>136</sup> *Chief Executive Election Result*, H.K. PRESS RELEASES (Mar. 25, 2012, 11:40 PM), <https://www.info.gov.hk/gia/general/201203/25/P201203250290.htm>.

sale of their small house entitlement. As for rhetoric, they invoke a quasi-promise made by the British to respect their traditional rights under Qing law. Like the sense of entitlement felt by Old Age insurance beneficiaries, this sense that their small house property is backed by a promise mobilizes villagers to act with moral unity and purpose. That motivation is backed by a powerfully ensconced position in Hong Kong politics. Indigenous villagers and their representatives are an important base of the pro-Beijing governing coalition in Hong Kong.<sup>137</sup> The Heung Yee Kuk, a statutory advisory body representing villagers' interests in the New Territories under Article 40 of the Basic Law, is a powerful organization comprising heads of rural committees. The "Kuk" contributes one functional constituency seat in the Hong Kong Legislative Council, one member in Executive Council, 27 votes in Election Committee (2022), and 27 ex officio members in district council. In addition, Heung Yee Kuk also has a good network with the largest political parties in Hong Kong, Democratic Alliance for the Betterment and Progress (DAB) of Hong Kong and Business and Professional Alliance for Hong Kong, two bodies with powerful blocs in LegCo.<sup>138</sup> The interconnection between the "Kuk," the DAB, and the New Territories Association of Societies (NTAS), a pro-Beijing umbrella political group which consists of hundreds of the New Territories community organizations, insures that the government will not lightly ignore indigenous interests.<sup>139</sup>

The power of existing law to create constituencies by defining a single stable focal point for political activism can be seen in the activism on behalf of the status quo. The Land Justice League has successfully rallied Hong Kong residents to defend existing landscapes and the

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<sup>137</sup> Isabella Steger & Jacky Wong, *Why Did Pro-Beijing Lawmakers Walk Out of the Hong Kong Vote?*, WALL ST. J. (June 18, 2015), <https://www.wsj.com/articles/BL-CJB-27136> .

<sup>138</sup> Currently, Business and Professionals Alliance for Hong Kong has 8 seats in legislative council, and DAB has 13 seats in the legislative council.

<sup>139</sup> *Annual Declaration of Registrable Interests of Members of the Executive Council*, HKSAR CHIEF EXEC. (2021), [https://www.ceo.gov.hk/exco/pdf/Kenneth\\_Lau\\_e.pdf](https://www.ceo.gov.hk/exco/pdf/Kenneth_Lau_e.pdf) .



current possessions of non-indigenous farmers, but the League has not focused much effort on fighting for the construction of new residential buildings. One reason might be that the existing historic buildings, scenic landscapes, or non-indigenous possessions all define a clear focal point around which activists can organize. By contrast, prospective buildings, precisely because they do not yet exist, cannot constitute a stable focal point defining a unified constituency. People who currently pay too much for rent to live in an over-crowded apartment unit have no reason to support one possible residential building over another. Unsurprisingly, because they lack any stake in a particular building, they do not make the effort to march in support of a proposed development in which they might never have any chance of living. By contrast, Hong Kong residents rally in defense of existing county parks' boundaries, because those residents know precisely how such parks benefit their particular neighborhoods. Thus, Tseung Kwan O residents will fight fiercely to defeat a small reduction in the size of the nearby Clear Water Bay Country Park, because this park's boundaries form a focal point that can coordinate their resistance to change.

Frontal assaults on existing property rights through novel liability rules, therefore, are politically dead on arrival. However academically clever such systems of forced sales might be for promoting efficient transactions, they all ignore the political influence created by those property rights in need of reform. They assume the ladder – that is, the political will radically to transform property -- necessary to escape from the hole.

#### IV. Using Land Use Options to Break Monopoly by Creating Effective Constituencies

Ending bilateral monopolies that are entrenched by constituency effects is no easy task. We are mindful of what Eric Posner and Adrian Vermeule call the “inside/outside fallacy.”<sup>140</sup> We have diagnosed constituency effects as the problem “outside the system” that is blocking the legislature’s enacting creative liability rules as a solution to Hong Kong’s housing crisis. We cannot then turn around to endorse some clever legislative solution that is likely to be blocked by those selfsame constituency effects. Instead, we must somehow devise a mechanism by which new constituencies can be created to fight for new housing without encroaching on existing constituencies’ defense of their existing entitlements. These new constituencies also must somehow break the bilateral monopoly that currently exists between lessee-owners and the government when they bargain, parcel by parcel, over the lease modifications and zoning of specific properties.

In what follows, we will suggest that “land options for housing” (“LOHs”) could meet these exacting standards as a practically feasible reform. LOHs could sidestep the resistance of existing constituencies, because they allocate the vertical dimension of development, an asset that is currently unallocated by the law and, therefore, is (to use a basketball metaphor) a “jump ball” – an asset that is (literally) up for grabs. Moreover, because LOHs allocate this dimension to a broad swathe of Hong Kong residents who are currently sitting on the sidelines of the fights over housing, LOHs have the potential to mobilize a new constituency. Finally, our proposal ends bilateral monopoly by requiring existing parcel owners to bid against each other to purchase LOHs from multiple and competing LOH holders. Fostering such inter-parcel competition requires the government to identify multiple parcels as equally eligible for development, letting

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<sup>140</sup> Eric A. Posner & Adrian Vermeule, *Inside or Outside the System?*, 80 U. CHI. L. REV. 1743, 1743 (2003).

the bids to purchase LOHs determine where actual housing is ultimately built. In such a regime, LOH holders rather than the government itself would sell these LOHs to developers and indigenous villagers who would compete with each other to pay LOH holders in return for the right to build high-density housing.

Critically, our proposal leaves intact existing property rights of lessee-owners: Unlike Posner's and Weyl's COST<sup>141</sup> or Ayres' higher-order liability rules,<sup>142</sup> such competition does not take anything away from existing stakeholders like developers or indigenous villagers: These constituencies retain their brownfields or fallow farmland untouched – but they gain an extra option that they never before enjoyed –the option of buying air rights from LOH holders for vertical residential construction. By avoiding such a frontal assault on existing entitlements and instead allocating new rights to new constituents, LOHs thereby avoid the constituency effects that have foiled more direct efforts to change the current uses of property.

#### **A. The Mechanics of Land Options for Housing**

Before defending LOHs, we will outline their mechanics to anchor that defense. In barebones summary, LOHs require lessee-owners of Crown Lands to purchase LOHs from LOH holders as a necessary condition for building residential projects. The LOH holders would bargain for either in-kind or monetary compensation from the landowner in return for agreeing to sell their rights. In-kind compensation would be units in the new project; monetary compensation would be money equal in value to the square footage that the LOH holder transfers to the landowner. As elaborated below, these purchases of LOHs should be designed with a few characteristics in mind to help solve the twin problems of bilateral monopoly and constituency effects.

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<sup>141</sup> See *supra* note 5.

<sup>142</sup> See *supra* note 116 and accompanying text.

## **1. Creation and Distribution of LOHs**

The first step in any LOH program would be the government's definition of a total number of LOHs and distribution of these LOHs among a set of LOH holders. As a general matter, the government would create enough LOHs to meet the projected housing needs for Hong Kong's residents over some fixed planning period. This calculation would require an estimate of the number of new dwelling units required to meet that housing need. The total number of LOHs would be calculated as an overall percentage of this denominator, estimated as a uniform percentage of a development's floor area the purchase of which would entitle the developer of a project to build the development.

The distribution of LOHs among Hong Kong's residents would also reflect the government's assessment of Hong Kong households' housing needs. Top priority, for instance, could be given to households who have been on the waiting list for public housing for the longest time or are the most "under-housed," in the sense of occupying the most over-crowded or over-priced housing. The LOH program could, however, also be designed to give influential Hong Kongers a stake in future housing development, by giving away some share of LOHs to middle-class as well as indigent Hong Kong residents. The point would be to give to as many Hong Kong residents as possible a stake in the future housing stock of Hong Kong so as to create a constituency for housing.

## **2. LOHs as A Necessary and (Almost) Sufficient Condition for New Residential Construction**

LOHs serve as a certificate of pre-approval for residential development. By "pre-approval," we mean that the purchase of LOHs would presumptively entitle the purchasers to build residential housing in proportion to the LOHs that they purchased. This presumption would be slightly qualified by a very few ex ante and ex post constraints. – specifically, that (1) the land

would be part of Hong Kong's total inventory of buildable residential land, (2) the purchaser would pay a per-unit fee, defined uniformly in advance for every transaction, to cover the cost of necessary infrastructure, and (3) the government would retain a very limited power to block developments for urgent public necessity. We elaborate each of these three conditions briefly below.

First, in advance of any LOH purchase, the government would undertake a jurisdiction-wide planning process that would, in effect, define Hong Kong's total inventory of land suitable for high-density residential housing. This inventory could be constrained by a few obvious prohibitions knocking some parcels out of eligibility to purchase LOHs. For example, the government could prohibit construction in environmentally fragile areas and ban tall buildings near the airport. We are confident, however, that these *ex ante* constraints on residential construction would leave ample sites available for new residential construction: As explained above in Part II(A), Hong Kong has ample supplies of fallow farmland and brownfields already occupied by warehouses, parking lots, and the like. Such sites are obviously not ecologically sensitive enough to preclude crops or gas stations: There is no reason, therefore, why their location or current use should preclude housing.

Second, again as part of the process for setting up the LOH system, the government would define a uniform per-unit fee to be charged to every new residential development to cover the average cost of infrastructure required by new housing. This fee would not be negotiated parcel-by-parcel or tailored to specific buildings but instead would be based only on the government's best estimate of the total quantity of housing expected to be built using LOHs and the total budget for infrastructure required by all new housing. These projections would, like any

other sort of budgeting, would necessarily be rough estimates. Shortfalls in fee-based revenue would be covered from Hong Kong's general revenues.

Finally, the government would retain a limited power to block developments after the lessee-owner purchases sufficient LOHs for urgent public necessity. The reasons justifying such ex post prohibitions would be stringent, resembling the sort of public purpose needed under current doctrine to resume leases and subject, as lease resumption currently is, to robust judicial review.<sup>143</sup> Our LOH proposal thus reverses the burden of inertia now favoring retention of brownfields and fallow farmland: Such inertia would now favor the construction of new housing.

Once a developer presents a document establishing a proposed project's satisfaction of these minimum ex ante criteria, the proposed development would be placed on an internet platform as an eligible buyer of LOHs. Such listings would include an offer price for LOHs. The price of the LOH would be required to be identical to the price at which dwelling units in the proposed development would be offered. Thus, LOH holders would receive exactly what housing purchasers pay – either a dwelling unit or its equivalent price. Assuming an ample supply of eligible land, lessee-owners would thus bid against each other to purchase LOHs from the total supply conferred by the government on LOH holders. The offering price would reflect the ratio of eligible land to total available LOHs: Too many LOHs chasing too few parcels would cause LOH prices to fall, while an abundance of parcels chasing a limited number of LOHs would cause the price to increase.

Once a developer had acquired a sufficient number of LOHs to build a particular project, then the trading platform would automatically generate a certificate of pre-approval. The government would be given a tight deadline — say, sixty days — by which to approve or reject

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<sup>143</sup> See *supra* note 34 and accompanying text.

the pre-approved project. This review would not involve any consideration of the purchase price paid for the LOHs. As noted above, the criteria for disapproval would be urgent health and safety considerations unforeseen through the general planning process that defined the inventory of LOH-eligible land. The question of how the premium from conversion should be divided between lessee-owner and the public would be determined exclusively through the process by which LOH purchases were negotiated. In effect, that bargaining process between lessee-owner and LOH holder would be the substitute for the public participation provided by governmental negotiations.

### **3. Contingent (and therefore Risky) Compensation for LOH holders**

The lessee-owners' obligation to pay LOH holders would be triggered by the completion of a residential project. The amount of compensation likewise could be keyed to the success of that project. LOH holders, therefore, would bear some of the project's risk. Those who sell LOHs to unreliable developers, for instance, would bear the risk that the project might go bankrupt because of cost overruns or lack of market demand. In such a case, the LOH seller would not be paid until the project is eventually built by the foreclosing bank. Likewise, if the initial project turns out to be less profitable than anticipated, then the LOH holders, like any other unsecured creditors, would receive less compensation (smaller units or less money) than they initially expected. LOH holders' sales of their LOHs should, therefore, reflect an assessment of the project's viability. Once the sale is made, then the fortune of LOH holders and the developer who purchased those holders' LOHs are bound together by the ties of economic self-interest.

### **4. Limited Alienability**

LOHs would not be alienable prior to being sold to the lessee-owner of a particular parcel of land. Third-party speculators, therefore, could not purchase “unattached” LOHs to re-sell to lessee-owners. After LOH holders sell their LOHs to a landowner for a particular project, however, anyone can acquire the prospective project (including the LOHs attached to that project) along with the contingent obligation to pay the LOH holders. For instance, a bank might foreclose on the project, including the LOHs that were necessary for the project, if the initial developer ran out of money and could not pay the construction loan. In such a case, the bank would also acquire the obligation to pay the LOH holders if the project were ever completed.

## **5. LOH Trading Platform**

The government would be obliged to create an internet platform on which LOHs can be traded similar to the Hong Kong Futures Exchange. On this platform, everybody would be able see in real time all updates of supply, demand, and transactions, second by second. Developers seeking to purchase LOHs would submit a development proposal on the government’s LOH trading platform. The proposal would include the location of the parcel to be developed, its inclusion within the area of Hong Kong’s developable land, the total number of dwelling units in the proposal, and the total number of LOHs required to develop those units. The proposal would propose a per-square-foot purchase price for the LOHs as well as the dwelling units. To better inform prospective LOH sellers about the project’s likelihood of success, the proposal would include a quality report disclosing the project’s financial feasibility, estimated completion date, average duration of the last five projects of the developer making the proposal, any regulatory concerns and infrastructure fees and plans, and any social and environmental impact of a proposed project that might result in ex post governmental disapproval. (The trading platform, which will be an independent non-for-profit entity, can provide templates for developers to



prepare such quality reports). Both the estimated LOH and unit prices and the quality report would be uploaded to the trading platform and accessible to the public before any transaction starts. LOH holders would evaluate competing proposals on the platform, selling LOHs to those developers whose proposals seem most likely to succeed.

## **B. The Justifications for Land Options for Housing: A Solution to Bilateral Monopolies Entrenched by Constituency Effects**

The LOH mechanism described above is presented as a solution to bilateral monopolies and constituency effects that stymie housing production not only in Hong Kong but throughout the world. We have tried to set the bar high for success: As we argued in Part III, it is not enough to either assume or ignore the existence of a constituency capable of championing or thwarting a clever liability rule or auction. Judged according to this stringent standard, how does our proposal stack up?

As we explain in more detail below, LOHs not only break bilateral monopolies in land but also do so without stepping on the toes of existing entitlement holders. The key to breaking bilateral monopolies is that lessee-owners of different parcels compete to buy LOHs from LOH holders who are also competing for high-quality projects in which to invest. The result of such competition is that strategic holdouts lose opportunities to competitors who disclose their true valuation. Unlike the liability rules, taxes, or auctions urged by other scholars,<sup>144</sup> however, this competition leaves intact the property rights of the stakeholders, instead allocating an unallocated asset – air rights – to a new constituency who thereby gains not only property but also an incentive to lobby for more housing.

### **1. Fostering Inter-Parcel Competition to Break Bilateral Monopolies in Land**

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<sup>144</sup> See *supra* Part III.

The most obvious benefit of a LOH program is its elimination of the bilateral monopoly now afflicting negotiations between the government and lessee-owners. The LOH program pits multiple parcel lessee-owners against multiple LOH holders, forcing each side to moderate their demands to avoid being over- or under-bid by competing buyers and sellers. The lessee-owner who insists on offering a low price for LOHs will risk having rival lessee-owners outbid them, thereby losing the opportunity to build new and profitable housing. In the extreme case, all available LOHs might be sold to competing parcels if a lessee-owner stalls too long. LOH holders also have an incentive to moderate their demands: Their insistence on a top price for their LOHs could lead them to be under-bid by competing LOH holders willing to take a lower price in return for the chance to invest in high-quality development proposals from reliable developers. Because the LOH holders are bidding against each other, they lack the monopolistic position that allows the government to hold out indefinitely for ever-greater amounts of goodies (revenue, housing, plazas, parks, subway improvements, etc.), exhausting developers' patience and revenue.<sup>145</sup>

Such valuation-disclosing competition is a product of the simple, comprehensive planning required by our LOH Program outlined in Part IV(A). By simultaneously classifying as many parcels as possible as eligible for high-density residential uses, the government avoids getting locked into negotiations with a single developer over a single parcel. As one of us has argued elsewhere, although such standardized rules have disadvantages, they avoid the thin market that results from choosing a parcel first and only afterwards bargaining over development rights.<sup>146</sup> LOHs instead begin by defining a general inventory of land and needed residential

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<sup>145</sup> For an example of such failed negotiations between the government and a New York City developer, consider the case of the Kingsbridge Armory. See Sam Dolnick, *Voting 45-1, Council Rejects \$310 Million Plan for Mall at Bronx Armory*, N.Y. TIMES, Dec. 14, 2009, <https://www.nytimes.com/2009/12/15/nyregion/15armory.html> .

<sup>146</sup> Hills & Schleicher, *supra* note 4, at 120, 129–34.

development and then use competition between parcel owners and LOH holders to determine the ultimate location of development. By simplifying development approvals to create a thicker market, LOHs are a species of property emphasizing standardization of rights to reduce information costs and thereby enlarge the market for real estate.<sup>147</sup>

LOHs do not merely avert a bilateral monopoly but do so through a kind of descending-price (or “Dutch”) auction that maximizes speed.<sup>148</sup> Landowners who have a more pessimistic estimation of Hong Kong’s future housing market can always hold back to observe what LOH transaction reveal about other landowners’ estimation of housing’s future. Because a LOH sale never requires more than one bid, the LOH program also emphasizes transactional speed. By requiring developers to propose identical prices of housing units and LOHs prices in their quality reports, the LOH program allows developers with a more optimistic estimation of the future housing market to participate soonest, creating a “rush effect” that pressures others to follow.

Hong Kong’s poor track record in moving parcels from patently inappropriate uses to housing<sup>149</sup> suggests that these benefits of speedy allocation of residential uses across parcels outweighs the benefits of expert planners trying to determine impartially the ideal location of housing. Hong Kong has tried that expert planning approach for decades with nothing more to

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<sup>147</sup> See Henry E. Smith & Thomas W. Merrill, *The Property/Contract Interface*, 110 COLUM. L. REV. 773, 777 (2001) (“[F]ree customization of property forms would create an information-cost externality; mandatory standardization is the legal system’s way of reducing these external costs to an acceptable level.”); Bell & Parchomovsky, *A Theory of Property*, 90 CORNELL L. REV. 531, 551 (2005) (“[T]he creation of idiosyncratic property rights increases the information costs property imposes on third parties. Standardization, on the other hand, reduces them.”).

<sup>148</sup> On the theoretical advantages of auctions over individualized negotiations, see generally Jeremy Bulow & Paul Klemperer, *Auctions Versus Negotiations*, 86 AM. ECON. REV. 180 (1996). On the different properties of “English” (ascending) and “Dutch” (descending) auctions, see generally Paul Milgrom & Robert J. Weber, *A Theory of Auctions and Competitive Bidding*, 50 ECONOMETRICA 180 (1982). For experimental evidence on how the Dutch auctions maximize the speed of transactions and efficiency, see generally Elena Katok & Anthony M. Kwasnica, *Time is money: The Effect of Clock Speed on Seller’s Revenue in Dutch Auctions*, 11 EXPERIMENTAL ECON. 344 (2018).

<sup>149</sup> See, e.g., Alexandra Stevenson & Jin Wu, *Tiny Apartments and Punishing Work Hours: The Economic Roots of Hong Kong’s Protests*, N.Y. TIMES (July 22, 2019), <https://www.nytimes.com/interactive/2019/07/22/world/asia/hong-kong-housing-inequality.html>.

show than acres of fallow farmland, small houses, and brownfields.<sup>150</sup> LOHs, by contrast, allow LOH holders and lessee-owners to work out quickly the details of how gains from conversion should be divided and where new housing should be located. By evading the gridlock of bilateral monopoly, that competitive process has promise of out-performing the Hong Kong government's past practice of parcel-by-parcel negotiations.

## 2. Creating A New Pro-Housing Constituency

Our proposed LOH program would be worth little if current entitlement holders would likely block it from ever being enacted. LOHs, however, hold the promise of harnessing, rather than being defeated by the constituency effects of property law. In particular, LOHs (1) respect existing entitlements and thereby avoid being defeated by current owners' opposition and (2) create a new constituency of LOH holders with the clout to lobby for new housing.

First, consider how a LOH program sidesteps opposition from existing entitlement holders that rival proposals invite. As explained in Part III(A), the innovative proposed by Ian Ayres and Jack Balkin,<sup>151</sup> Lee Anne Fennell,<sup>152</sup> and Posner & Weyl<sup>153</sup> all re-arrange property in ways that directly assault current owners' sense of entitlement. LOHs, however, change no lessee-owners' current entitlements: Their rights to maintain and use small houses, farmland, and brownfields do not include any right to build residential high-rises. To the extent that villagers rest their entitlement to small houses on Qing Dynasty property customs,<sup>154</sup> for instance, that sense of entitlement does not include any expectation to build higher than three stories. Turning

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<sup>150</sup> See *supra* Part II.

<sup>151</sup> See *supra* note 116 and accompanying text.

<sup>152</sup> See *supra* note 118.

<sup>153</sup> See *supra* note 5.

<sup>154</sup> See Shirley Zhao, *Controversial Small-House Policy Was Never Traditional Right of Indigenous Male Villagers in Hong Kong, Landmark Hearing Told*, S. CHINA MORNING POST (DEC. 3, 2018), <https://www.scmp.com/news/hong-kong/law-and-crime/article/2176204/controversial-small-house-policy-was-never-traditional>.

this right to the vertical dimension of land over to the permanent residents of Hong Kong, therefore, should not trigger any sense of injustice that would mobilize incumbent owner-lessees to resist the innovation. It is revealing that innovative auctions have been used mostly to allocate forms of property like radio spectrum, offshore wind rights, or mineral rights on public land, where the property rights are initially defined and held by the government free from incumbent owners who might be motivated by a strong sense of entitlement to block the auction process.<sup>155</sup> LOHs likewise allocate an asset, air rights, that is undefined by any law and that no one currently is entitled to exploit.

Second, consider how a LOH program can create new expectations that will lead LOH holders to defend the development of new housing. The idea that unallocated interests in land belongs to the state – the “Crown” in colonial terms – is deeply embedded in Hong Kong’s history.<sup>156</sup> This idea overlaps with the Communist idea that land is the common property of the people.<sup>157</sup> Hong Kong’s commitment to capitalism qualifies this idea to the extent that Crown lands have already been leased out. But air rights that have not yet been allocated seem to belong to everyone equally under the logic of Hong Kong’s pre-existing system of property. Beijing has long sought to create a constituency in Hong Kong that has a stake in maintaining the system rather than challenging the regime.<sup>158</sup> There is no better way to accomplish this goal than making the majority of the residents holders of entitlement that will not be fulfilled without stability or

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<sup>155</sup> For a simple summary of Nobel Laureates Robert Wilson’s and Paul Milgrom’s role in designing auctions for mineral rights and radio spectrum, see generally Leandro Arozamena, Andrés Fioriti & Federico Weinschelbaum, *From Auction Theory to Market Design: Paul Milgrom and Robert Wilson’s Contributions to Economics*, 38 ESTUDIOS ECONOMICOS 279 (2021).

<sup>156</sup> See *supra* notes 32–33 and accompanying text.

<sup>157</sup> See generally Shitong Qiao, *The Evolution of Chinese Property Law: Sticky by Stick?*, in PRIVATE LAW IN CHINA AND TAIWAN 182 (Cambridge Univ. Press, 2016) (reviewing Chinese property laws and policies over the past three decades as well as the meaning of public land ownership under the current system).

<sup>158</sup> See, e.g., Greg Torode & Marius Zaharia, *What Is Love? Beijing Desires Unconditional Loyalty from Hong Kong*, REUTERS (Feb. 26, 2021, 11:50 PM), <https://www.reuters.com/article/us-hongkong-security-politics-explainer/what-is-love-beijing-desires-unconditional-loyalty-from-hong-kong-idUSKBN2AR05L>.

development. Although Beijing has long relied on business groups, particularly developers, to govern Hong Kong, Beijing elites have started reexamining this approach.<sup>159</sup> Relying on the majority of permanent residents, rather than a handful of tycoons, seems consistent with this new strategy.

Once the LOH program is up and running, LOH holders' effectiveness as a property-defending constituency is likely strengthened by their focused interests in specific development projects. Homeowners with undiversified interests in a particular building have greater incentives to defend that building's value through the political process than prospective buyers and renters have in potential buildings. Because the value of LOHs is tied to particular buildings in which LOH holders have invested their LOHs, LOH holders have a similarly focused incentive to lobby on behalf of development. If a proposed development fails, then those LOH holders lose their entire investment. The political clout of the LOH holders will help, therefore, with those necessary permissions that remain even after a parcel is pre-approved for construction because it has acquired sufficient LOHs.

LOH holders' incentives to defend housing development authorized by LOHs are further enhanced by the implicit promise contained in a LOH program. As Paul Romer has noted, "people . . . will be willing to incur a cost to punish someone who has made and broken a promise."<sup>160</sup> The LOH program, once enacted, contains an implicit promise to LOH holders that their selling LOHs to otherwise eligible developers will result in the completion of a building from which LOH holders will receive compensation in the form of housing or money. For the government to renege on this implicit promise "induces a taste for punishing the offender" from

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<sup>159</sup> See Claire Jim & Farah Master, *With Tighter Grip, Beijing Sends Message to Hong Kong Tycoons: Fall in Line*, REUTERS (Sept. 17, 2021, 4:25 AM), <https://www.reuters.com/world/china/with-tighter-grip-beijing-sends-message-hong-kong-tycoons-fall-line-2021-09-17>.

<sup>160</sup> Romer, *supra* note 121, at 199.

the LOH holders.<sup>161</sup> The ad hoc negotiations between the government and current lessee-owners, by contrast, do not create any such sense of implicit promise, because the specific terms under which development will be permitted have not been defined in advance. Although the government issues requests for proposals (RFPs) to develop leased Crown lands to which tycoons respond by offering some mix of amenities, revenue, and housing, the government reserves the right not to accept any of the bids or even to add conditions after a bid is accepted. By contrast, the Government's turning over the decision to accept a bid to LOH holders makes it hard for the Government to renege approval of the housing project on which landowner and LOH holder agree, because the existence of the program creates an implicit promise that pre-approved projects will not be lightly blocked.

### **3. What About Government Officials as An Interest Group?**

The description of constituency effects above leaves out one potentially enormous interest group: The Hong Kong or Chinese governments themselves. Do governmental officials themselves constitute a constituency that would fight to retain the land status quo? As we shall explain in more detail below, LOHs have a feature likely to be attractive to the Chinese Communist Party, which is the practical ruling decision-maker in Hong Kong: LOHs supply information to the rulers about what Hong Kong's residents want without risking resistance to the Party's rule that might emerge from democratic elections.

Hong Kong's semi-authoritarian system presents a special challenge to land use scholarship that has typically assumed the existence of a liberal democratic system in which politicians are simply transmission belts for interest groups. Even Neil Komesar's account of land-use "dictators," for instance, imagined that such "dictators" would have no interests of their

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<sup>161</sup> *See id.*

own but instead either disinterestedly maximize the value of all real estate or, alternatively, become the captive of the most influential interest groups.<sup>162</sup> Likewise, the “growth machine” and “homevoter” models, the two leading depictions of land-use politics in American land-use scholarship, both take as their starting point elected politicians who cater to interest groups: The “growth machine” model assumes interests favoring construction like real estate brokers and building trades unions, while the “homevoter hypothesis” imagines that homeowners favoring maximization of home values rule the roost, but both imagine that the interests of the politicians themselves merely reflect whichever group can best mobilize at the polls.<sup>163</sup>

Hong Kong’s semi-authoritarian system defies traditional land use models that assume a liberal democracy. Unlike those models, Hong Kong’s government answers ultimately to the leadership of the Chinese Communist Party (CCP). The CCP is undoubtedly an authoritarian system capable of ignoring the interests of Hong Kong residents. The CCP, however, still needs a mechanism to solve the “dictator’s dilemma” of obtaining information about citizen’s preferences without creating electoral threats to the dictator’s rule.<sup>164</sup> Without such information, the CCP leadership could lose citizens’ willing cooperation, incur productivity losses from quiet slowdowns, and even suffer sudden flare-ups of rebellion from smouldering but undetected resentments. The overwhelming defeat of CCP-backed candidates in the 2019 district council elections made it clear to the CCP’s leaders that their unaided guesses about public opinion were

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<sup>162</sup> Neil K. Komisar, *Housing, Zoning, and the Public Interest*, in PUBLIC INTEREST LAW: AN ECONOMIC AND INSTITUTIONAL ANALYSIS 218, 219–21 (Burton A. Weisbrod et al., eds. 1978).

<sup>163</sup> For overviews of the “growth machine” and “homevoter” models as rival accounts of land-use politics, see *Note on Planning, Deal-Making, and Zoning Politics*, in ELLICKSON ET AL. at 361–66.

<sup>164</sup> For an overview of dictators’ need for information-sharing from their subjects and the dilemma that poses for rulers fearful of rebellion sparked by citizens’ negative judgments of the regime, see BRUCE J. DICKSON, *THE DICTATOR’S DILEMMA: THE CHINESE COMMUNIST PARTY’S STRATEGY FOR SURVIVAL* (Oxford Univ. Press 2016); RONALD WINTROBE, *THE POLITICAL ECONOMY OF DICTATORSHIP* (Cambridge Univ. Press 1998).



not equal to the task of inferring what Hong Kong citizens really wanted.<sup>165</sup> Eliminating “unpatriotic” candidates from contention in local elections might eliminate open resistance to the CCP, but such crackdowns do not remedy the CCP’s lack of information about local preferences or the potential embarrassment from popular hostility manifested by low voter turnout.<sup>166</sup>

LOHs provide such a mechanism. Like housing purchases by homebuyers in Mainland China, LOHs enable LOH holders to express their housing preferences with their sales of LOHs to the developers of prospective projects.<sup>167</sup> In both cases, those purchases or sales are akin to “votes” insofar as they express the purchasers’ or sellers’ desire to live in, and they bear the default risk associated with a particular structure. Unlike votes for candidates, however, those sales do not produce officeholders who might resist the CCP. LOHs, therefore, can be expected to win CCP support insofar as they provide information about citizens’ preferences at low political risk to the CCP.

LOHs also serve the expressed interest of CCP leaders in building more housing in Hong Kong as a means of building more widespread popular support for the CCP.<sup>168</sup> CCP leaders have

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<sup>165</sup> See Keith Bradsher, Austin Ramzy & Tiffany May, *Hong Kong Election Results Give Democracy Backers Big Win*, N.Y. TIMES (Sept. 24, 2021), <https://www.nytimes.com/2019/11/24/world/asia/hong-kong-election-results.html>.

<sup>166</sup> On the exclusion of “unpatriotic” candidates from the 2021 elections, see Kelly Ho, *Beijing Approves Resolution to Overhaul Hong Kong’s Elections – Candidates to Be Vetted*, H.K. FREE PRESS (Mar. 11, 2021, 7:16 PM), <https://hongkongfp.com/2021/03/11/breaking-beijing-approves-resolution-to-impose-electoral-overhaul-on-hong-kong>. On the CCP leaders’ worries about loss of prestige resulting from low voter turnout, see Shibani Mahtani, *The Opposition Is in Jail. Hong Kong Wants Its ‘Patriots’-Only Vote to Look Legitimate*, WASH. POST (Dec. 17, 2021, 12:13 AM); Edmond Ng & Sara Cheng, *Pro-Beijing ‘Patriots’ Sweep Hong Kong Election with Record Low Turnout*, <https://www.reuters.com/world/china/hong-kong-patriots-only-election-draws-record-low-turnout-2021-12-19>.

<sup>167</sup> On the ways in which a land market reveals the preferences of homebuyers not only for structures but also local amenities and reliability of local government, see generally Roderick M. Hills, Jr. & Qiao Shitong, *Voice and Exit as Accountability Mechanisms: Can Foot-Voting Be Made Safe for the Chinese Communist Party?*, 48 COLUM. HUM. RTS. L. REV. 158 (2017)

<sup>168</sup> As Han Zheng, vice premier and a standing member of the politburo in charge of Hong Kong affairs, has stated, the “Hong Kong housing problem must be solved.” 韩正：香港的住房问题要解决 [Han Zheng: Hong Kong’s Housing Problem Must Be Solved.], <https://topics.caixin.com/2021-03-08/101672514.html>. The director of the Central Government Liaison Office in Hong Kong expressed the urgency of the CCP’s commitment to increasing housing supply by visiting a poor public housing unit to show Beijing’s concern about the Hong Kong housing

acknowledged that the massive 2019 public protests triggered by the Hong Kong government's proposal of an extradition law were manifestations of deep discontent with the Hong Kong government, but they have attributed such discontent to material rather than political deprivations – in particular, the high cost and scarcity of housing.<sup>169</sup> Whatever the balance of economic and political factors, there is little doubt about the widespread dissatisfaction with housing in Hong Kong.<sup>170</sup> The CCP's own account of the legitimate sources of public anger, therefore, commits it to solving the housing crisis. By unlocking land from the paralysis of gridlock, LOHs allow the CCP to meet this commitment without embracing electoral democracy that it deems threatening to the CCP's rule.

Given the CCP's likely posture, it is unlikely that Hong Kong officials would have any self-interested reason to impede the expansion of housing. Under the terms of the Basic Law, the Hong Kong Chief Executive must negotiate among rival Hong Kong groups represented among the various interests in the Election Committee and Legislative Council. By creating a new constituency of LOH holders to press for development, LOHs give the Hong Kong officials the political cover necessary to accept development proposals that might otherwise inspire popular resentment as corrupt giveaways to established interests.

Apart from acting as the broker for local Hong Kong interests, the Hong Kong leadership has an incentive to meet the CCP's expectations, because the CCP leadership ultimately controls appointment to Hong Kong's political offices. There is little doubt that Hong Kong's chief

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problem. 骆惠宁访香港笼屋住户：亲眼见到这么挤迫的居住条件，心情十分沉重 [Luo Huining Visited Cage-House Residents], [https://www.sohu.com/a/493109234\\_115479](https://www.sohu.com/a/493109234_115479).

<sup>169</sup> See e.g., China Targets Hong Kong Wealth Gap, Housing Woes After Political Purge, <https://www.wsj.com/articles/china-targets-hong-kong-wealth-gap-housing-woes-after-political-purge-11615813651>

<sup>170</sup> Alexandra Stevenson & Jin Wu, *Tiny Apartments and Punishing Work Hours: The Economic Roots of Hong Kong's Protests*, N.Y. TIMES (July 22, 2019), <https://www.nytimes.com/interactive/2019/07/22/world/asia/hong-kong-housing-inequality.html>.

executives have all struggled to satisfy the CCP leadership’s call for more housing with measures ranging from revision of Hong Kong’s tenant protection law<sup>171</sup> to the unveiling of the 2021 North Metropolis plan’s proposed 350,000 additional residential units.<sup>172</sup> As explained in Part IIC3 above, however, these initiatives have yielded little fruit in the past and are unlikely to break the land gridlock in the future.

One might understandably suspect that some ulterior motive explains such persistent failure to follow through on proclaimed commitments to create more housing. One such possible motive is commonly termed “fiscal illusion” – the illusion allegedly suffered by governmental officials that only programs beneficial to the public are worthy of official effort.<sup>173</sup> Fiscal illusion, however, is not a law of nature: Assuming that it exists, it is contingent on specific facts that would give governmental officials an incentive to maximize revenue of the organization that employs them.<sup>174</sup> The Hong Kong government might have such an incentive from the revenues that they derive from lease modifications, revenues that it would have to surrender to LOH holders under our proposal. That revenue, however, is purely theoretical if gridlock prevents rezoning and lease modification. Precisely because gridlock freezes up the process of lease modification, the amount of revenue derived from land premiums is surprisingly small: Based on numbers provided on the Hong Kong government’s website, land premiums contributes to 13.5%

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<sup>171</sup> Gigi Choy & Jack Tsang, *Hong Kong Lawmakers Pass Tenancy Control Bill to Protect Poorest from Landlord Exploitation*, S. CHINA MORNING POST (Oct. 20, 2021, 7:29 PM), <https://www.scmp.com/news/hong-kong/hong-kong-economy/article/3153049/hong-kong-lawmakers-pass-tenancy-control-bill>

<sup>172</sup> *CE Unveils Visionary Northern Metropolis Plan in Policy Address*, GOV’T H.K. PRESS RELEASES (OCT. 6, 2021, 12:45 AM), <https://www.info.gov.hk/gia/general/202110/06/P2021100600466.htm>.

<sup>173</sup> Lawrence Blume & Daniel L. Rubinfeld, *Compensation for Takings: An Economic Analysis*, 72 CALIF. L. REV. 569, 572–73, 621 (1984) (explaining theory of “fiscal illusion” and proffered solution of cost-internalization through compensation).

<sup>174</sup> Daryl Levinson, *Making Government Pay: Markets, Politics, and the Allocation of Constitutional Costs*, 67 U. CHI. L. REV. 345, 353–56, 364–6, 373–75 (2000).

(2015-2016) to 26.6% (2017-2018) of Hong Kong government revenue in the last 10 years.<sup>175</sup>

Given that the Hong Kong government has been repeatedly running budget surpluses and keeping a significant amount of fiscal reserve,<sup>176</sup> it would be surprising that governmental officials would reject a solution to the salient political crisis of housing for the sake of such paltry cash, especially since they have publicly committed to spending many times more to reclaim land from the ocean to solve that crisis.

The more likely explanation is not an obsession with revenue but rather an inability to figure out an acceptable price. Hong Kong's leadership is vulnerable to accusations of "government-business collusion" if they allow lease modification for an insufficiently high price, but the prices that they demand are too high to win over reluctant owner-lessees. Trapped without a price-revealing market, everyone sits on their existing rights, maintaining a status quo unsatisfactory to everyone. By using a market mechanism to set prices of lease modification, LOHs remove this paralyzing blame about "government-business collusion," unlocking land for housing that everyone wants.

Aside from the CCP leadership in Beijing and the Hong Kong leadership in the Admiralty, the last set of officials who might oppose LOHs is the Hong Kong planning bureaucracy. They might argue that our trading mechanism jeopardizes the integrity of urban planning, where "urban planning" is understood as a science that urban planning bureaucrats

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<sup>175</sup> *Annex 2, LCQ8: Collection of Stamp Duties and Land Premium* (Mar. 18, 2015), LEGIS. COUNCIL, [https://gia.info.gov.hk/general/201503/18/P201503180592\\_0592\\_143561.pdf](https://gia.info.gov.hk/general/201503/18/P201503180592_0592_143561.pdf); *LCQ3: Revenues from Stamp Duties and Land Premiums* (Apr. 28, 2021, 11:45 PM), GOV'T H.K. PRESS RELEASES, <https://www.info.gov.hk/gia/general/202104/28/P2021042700613.htm?fontSize=1>; *Major Sources of Government Revenue*, LEGIS. COUNCIL SECRETARIAT (Aug. 10, 2016), <https://www.legco.gov.hk/research-publications/english/1516fs04-major-sources-of-government-revenue-20160810-e.pdf>.

<sup>176</sup> Twinnie Siu & Clare Jim, *Hong Kong Plans Lower Budget Deficit as Economy Expected to Recover*, Reuters (Feb. 24, 2021, 12:45 AM), <https://www.reuters.com/article/us-hongkong-economy-budget/hong-kong-plans-lower-budget-deficit-as-economy-expected-to-recover-idUSKBN2AO0GB> ("Hong Kong usually runs balanced budgets or surpluses, since its pegged currency system commits it to fiscal prudence. Its fiscal reserves are expected at HK\$902.7 billion at the end of March 2021 and fall to HK\$775.8 billion by end-March 2026.").

apply to decide where to build and what should be allowed. If city planning is understood as the expert specification of where structures ought to be built, then we plead guilty. We share the skepticism of critics ranging from Jane Jacobs to Kenneth Kolson about the capacity of expert planners to meet the informational demands required for the micromanagement of complex systems like cities.<sup>177</sup> Hong Kong's track record illustrates the inadequacies of expert planning: Despite voluminous plans, nothing gets built, and land sits idle as fallow farmland, warehouses, and parking lots – uses that are obviously inappropriate by any planning criteria.

As explained in Part IV(A)(1) and (5) above, the LOH system requires both a comprehensive inventory of all parcels suitable for residential development and a trading platform through which LOH are traded. Both of these tasks require planning expertise provided by Hong Kong's urban planning officials. These officials not only would work closely with the Hong Kong Futures Exchange to create and administer a new LOH trading platform but also would provide guidance to developers preparing the quality reports for individual development proposals. Urban planning officials would also determine which parts of Hong Kong should be included or excluded from the inventory of potentially buildable residential land. This task of creating an inventory would indeed become more expert-based insofar as it would be rooted in hard-edged baseline rules about safety and environment rather than endless dickering between different groups. To the extent that planners have an open mind, both their skills and self-interest suggest that they could support LOHs not only as a better mechanism for creating housing but

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<sup>177</sup> See JANE JACOBS, *THE DEATH AND LIFE OF THE GREAT AMERICAN CITIES* 3 (1961) (“This book is an attack on current city planning and building”); KENNETH L. KOLSON, *BIG PLANS: THE ALLURE AND FOLLY OF URBAN DESIGN* 187 (2002) (summarizing history of planning disasters by noting that, “our conception of city planning, a vestige of baroque regimentation and display, has been destructive of urban order”); MELVILLE C. BRANCH, *CONTINUOUS CITY PLANNING: INTEGRATING MUNICIPAL MANAGEMENT AND CITY PLANNING* (1981); John Rahenkamp, *Land Use Management: An Alternative to Controls*, in *FUTURE LAND USE* 191–92 (Robert W. Burchell & David Listokin eds., 1975) (“the best master planners we have in the country inevitably are failures when it comes to prognosticating over a long period of time”).

also a guarantee of job security in which their skills will still be valued even as they play a different type of planning role.<sup>178</sup>

## **V. Beyond Hong Kong: Land Options as Motivations for Pro-Housing Constituencies Across the Globe**

Housing shortages afflict cities across the globe. Can land options like the LOH program help with such shortages in places other than Hong Kong? As we explain in this final section, customized land options do not have any magical power to break bilateral monopolies or promoting pro-housing constituencies. In fact, land options superficially similar to our proposed LOH program can actually exacerbate these problems or, at least, do little to solve them. Hong Kong's colonial land exchange entitlement, for instance, did little beyond making Hong Kong's real estate tycoons even richer, because it did not break their land monopoly. Likewise, Israel's TAMA 38 program, while initially promising as a way to increase housing supply, was foiled by its failure to create a sufficiently powerful constituency to protect the program from repeal.

Land options cannot break bilateral monopolies and create new pro-housing constituencies unless they address three simple propositions: (1) Bargaining frameworks in which a single (usually local) government negotiates with a single land developer invite the gridlock of bilateral monopoly in which each side conceals their actual valuation of the land conversion, and (2) changing this bargaining framework can be impeded by the constituency effects of existing property entitlements, but (3) allocating new property rights to third parties – in our proposal, LOH holders – can break the gridlock by allowing new constituencies to bargain competitively over the gains from land conversion. To illustrate these principles, we will take a

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<sup>178</sup> Hong Kong's planners can learn a lesson from officials across the border in the career benefits of such a change in roles. In the 1980s and 1990s, Chinese local officials were competing with each other to sell locally controlled state-owned enterprises (SoEs). See Yutao Huang, *Solve the Problem or Escape the Responsibility? The Politics of Chinese Privatization Reform*, 4 CHINESE POL. SCI. REV. 1, 13 (2019).

brief look at below some land option failures as well some experiments with land options that hold more promise for success.

## **A. Two Failed Land Option Systems in Colonial Hong Kong and Israel**

Colonial Hong Kong and Israel have both created new forms of property to stimulate housing production or renovation. Colonial Hong Kong's land-exchange entitlements, however, promoted housing at an exorbitant cost by turning over enormous land rents to the real estate tycoons who ended up purchasing those entitlements. Viewed more abstractly, Colonial Hong Kong's land-exchange entitlements failed to solve the information-blocking problem of bilateral monopoly. Israel's TAMA 38 program, by contrast, stimulated housing production without such a maldistribution of land wealth, but it never created a constituency effective enough to protect the program from the hostility of mayors and neighbors.

### **1. How Colonial Hong Kong's Land-Exchange Entitlements were thwarted by bilateral monopoly**

Between the Communist takeover of Mainland China in 1949 and the early 1960s, Hong Kong was deluged with over a million refugees, driven to the colony by famine and fear of persecution and in need of housing.<sup>179</sup> To meet this new demand, the colonial government of Hong Kong needed housing, and the natural location for hundreds of thousands of necessary units was the mostly agricultural New Territories. Lacking cash to compensate the villagers who occupied this land, the government instead issued New Territories land exchange entitlements, commonly known as Letters A/B, between 1960 and 1983.<sup>180</sup> Those Letters A/B were land options, entitling their holders to exchange their old land for new land on which new residential structures could be built. Accordingly, the exchange ratios for the letters varied depending on

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<sup>179</sup> *Million Refugees from China Crowd Housing in Hong Kong*, N.Y. TIMES (May 3, 1964), <https://www.nytimes.com/1964/05/03/archives/million-refugees-from-china-crowd-housing-in-hong-kong.html>

<sup>180</sup> Liu, *supra* note 47.

whether the land taken by the government had been used for residential as opposed to farming purposes: Letters A were issued for residential land that could be exchanged for new land at a ratio of 1:1, while Letters B were issued for farmland that could be redeemed at a ratio of 2:5, reflecting its much lower value.<sup>181</sup> The lower value of agricultural land was reflected as well in the obligation of Letter B holders to pay a lease premium equal to the difference, at the time that the land was surrendered to the government, between the value of the agricultural land that they surrendered compared to the residential land that they received.<sup>182</sup>

This formula contained within it the seeds of an extraordinary windfall for the compensated owner, because the land premium was calculated based on the year that the old land was surrendered, not the year in which the new land was acquired. If the new land appreciated significantly between the time of surrender and the time that the new land was acquired, then the owner would receive 100% of this appreciation.<sup>183</sup> Letters A/B thus became profitable investment tools for those who could afford to wait to acquire new land until the latter appreciated far higher than the land premium charged by the government. For independent landowners or small developers, the need for immediate cash led them either to sell their Letters A/B on the secondary market or develop their new land prematurely.<sup>184</sup> Developers with larger cash reserves developers, by contrast, purchased the letters as investments, holding them until the land appreciated far higher than the land premium demanded by the government.<sup>185</sup> By 1980 the government had issued land-exchange entitlements valued at more than 36 million sq. feet of

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<sup>181</sup> Zhaoping Zheng, 吸取換地經驗邁向四贏 [Learning from Land Exchange Entitlements], 信報財經新聞 (Aug. 17, 2012), <http://www.sdahk.com/symposium/120817.pdf>.

<sup>182</sup> *Id.*

<sup>183</sup> 低價買地魔法 — 換地權益書 [Land Exchange Entitlements: The Magic of Purchasing Land at Low Prices], 經濟一週 (June 14, 2013), <https://www.edigest.hk/投資/低價買地魔法-換地權益書-9978>.

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*



land.<sup>186</sup> Lacking sufficient land with which to redeem these letters, the government ended the policy in 1983, requiring in a 1984 ordinance that outstanding Letters A/B be redeemed with either cash or land at 1984 market rates.<sup>187</sup>

Letters A/B thus contributed to the land oligopoly from which Hong Kong still suffers. The value of those land-exchange entitlements was far in excess of the loss incurred by the New Territories' lessee-owners,<sup>188</sup> and the form of this compensation insured that most of those landowners would transfer the greater share of this value to developers with the cash reserves to hold on to the letters as an investment. In effect, the Hong Kong government arbitrarily turned over an enormous appreciation in real estate value to speculators for no better reason than inability more accurately to calculate compensation. While this exchange had the advantage of eventually producing housing in the New Territories' new towns, the policy did so at an exorbitant cost that deprived the mass of Hong Kong citizens of any share of the wealth created by real estate appreciation. In recent years, developers and scholars have suggested re-adopting the land-exchange model to promote development<sup>189</sup> All such proposals, however, either allow developers to monopolize future land rents as the old policy had done, or they do not provide a clear mechanism for pricing land bonds.<sup>190</sup>

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<sup>186</sup> Zheng, *supra* note 181.

<sup>187</sup>New Territories Land Exchange Entitlements (Redemption) Ordinance, (June. 26, 1997) Cap. 495 (H.K.), [https://www.elegislation.gov.hk/hk/cap495!zh-Hant-HK?xid=ID\\_1438403271676\\_001&INDEX\\_CS=N](https://www.elegislation.gov.hk/hk/cap495!zh-Hant-HK?xid=ID_1438403271676_001&INDEX_CS=N); Zheng, *supra* note 181.

<sup>188</sup> The New Territories was leased to Britain for 99 years from 1 July 1898, block Crown leases were granted for 99 years to owners of land in each block with titles derived from the Qing Emperor.

<sup>189</sup>假如我是特首(3) - 什麼是乙種換地權益書? [*Suppose I Am the Chief Executive (3) – What Is Letter B Land Exchange Entitlement Document?*], H.K. LUXURY PORTAL (Mar. 28, 2012), [http://www.mls.hk/writing\\_manage/phk\\_tml/baab990e.html](http://www.mls.hk/writing_manage/phk_tml/baab990e.html); 有地主等升值「換地證」更吸引 [*Some Landowners Wait for Land Exchange Documents to Increase in Value*], WEN WEI PO (Oct. 6, 2021), <http://paper.wenweipo.com/2019/10/06/HK1910060035.htm>. One such proposal is the land bond solution proposed by the Ronald Coase Centre for Property Rights Research at the University of Hong Kong. Univ. H.K. Ronald Coase Ctr. for Prop. Rts. Rsch., *Land Bonds – a Tool for Large Scale Land Readjustment*, UNIV. H.K. (2018), [https://www.hku.hk/f/upload/18177/Land\\_Bond\\_Eng.pdf](https://www.hku.hk/f/upload/18177/Land_Bond_Eng.pdf).

<sup>190</sup> Univ. H.K Ronald Coase Ctr. for Prop. Rts. Rsch., *supra* note 189.

## 2. How Israel's TAMA 38 Program Failed to Create A Pro-Housing Constituency

By contrast with colonial Hong Kong's land-exchange entitlements, Israel's "TAMA 38" program was not initially aimed at producing new housing. The program was instead an effort to harness land values to renovate and strengthen buildings against risk of earthquakes. Enacted in 2005 as "National Outline Plan Number 38" ("TAMA" being the Hebrew acronym), TAMA 38 gave a new land option to the owners old buildings defined as buildings constructed before 1980.<sup>191</sup> On agreement by a super-majority of such buildings' owners, the owners could collectively sell air rights over their building to developers in return for the developers' strengthening the building's earthquake resilience. The quantity of air rights eligible for such sale varied during the life of the program, ranging from a single story in 2005 to up to 3.5 stories by 2016.<sup>192</sup> Likewise, the required super-majority of apartment owners within a building required to authorize reconstruction or even total demolition and re-building a a structure ranged from 66-80%. Abstracting away from such details, however, the general character of TAMA 38 was a definition of a new property entitlement that was given to existing apartment owners for sale to developers in exchange for building improvement and enlargement.<sup>193</sup>

Because it distributed the new land option to a broad set of stakeholders, TAMA 38 was vastly superior to colonial Hong Kong's land-exchange entitlement as a mechanism for producing housing and distributing land wealth. Rather than having the government arbitrarily concoct a price for land options like the ratios in Hong Kong's Letters A/B, TAMA 38 simply

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<sup>191</sup> For an overview of TAMA 38, see, e.g., Zev Stub, *As Israel Looks to Solve Housing Crisis, Future of Tama 38 in Question*, JERUSALEM POST (July 12, 2021), <https://www.jpost.com/israel-news/as-israel-looks-to-solve-housing-crisis-future-of-tama-38-in-question-673607>.

<sup>192</sup> Moshe Shamai & Ravit Hananel, *Urban Renewal or Earthquake Preparedness: Lessons from Israel's National Master Plan for Earthquake Preparedness (TAMA 38)*, 23 CITYSCAPE 381, 388–90 (2021).

<sup>193</sup> For an analysis of TAMA 38 as a value recapture mechanism, see generally Nir Mualam, Eyal Salinger & Sarah Goldberg, *Implementing Value Capture in Israel: An Examination of Recent Tools and Policies for Urban Renewal and Earthquake Preparedness* (Lincoln Inst. Land Pol'y, Working Paper WP20NM1, 2021).

handed over the new entitlement to a broad group of competing landowners, allowing the land market to work out a distribution of the gains from development between buyers and sellers. TAMA 38 also discouraged speculative purchases by requiring the developers to improve buildings and enlarge existing units by up to 25 square meters each as a condition of their purchase. To cover the cost of these improvements, developers immediately began adding stories of housing rather than sit on their entitlement as a speculative investment, as the Hong Kong developers did after acquiring land-exchange entitlements. TAMA 38, in short, eliminated bilateral monopoly between individual owners and the government by turning over the land option to a competitive market for development rights.

An unforeseen but beneficial side-effect of the TAMA 38 program was the creation of significant new housing in high-demand areas of Israel like Tel Aviv. Since at least 2011, Israel has suffered from an acute housing shortage that has only intensified in recent years.<sup>194</sup> This shortage has been exacerbated by Israel's public ownership of land. As in Hong Kong, the government (in the form of the Israeli Land Authority (ILA)) owns 93% of Israel's land, leasing it out for long terms to private "owners" who technically are merely lessees with leases up to 98 years. As in Hong Kong, the process by which the ILA issues and administers public tenders of land is time-consuming and expensive.<sup>195</sup> On top of the ILA's public tender process, municipalities also have regulatory authority to block new development. By opening up between one to 3.5 extra stories above older buildings to residential development, TAMA 38 promoted infill development in the areas where such development had the greatest value. The number of

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<sup>194</sup> On Israel's housing shortage, see, e.g., Ricky Ben-David, *Israeli Housing Prices Have Nearly Doubled in a Decade, with No Signs of Slowing*, TIMES OF ISR. (Oct. 6, 2021, 6:30 AM), <https://www.timesofisrael.com/israeli-housing-prices-have-nearly-doubled-in-a-decade-with-no-signs-of-slowing>.

<sup>195</sup> Ziv Rubin, *Supply Side Constraints in the Israeli Housing Market—The Impact of State Owned Land*, 65 LAND USE POL'Y 266 (2017).

units thus created was significant: Roughly a third of all new housing produced in Tel Aviv between 2018 and 2020 was produced through TAMA 38.<sup>196</sup>

Despite these benefits, however, TAMA 38 has attracted widespread opposition. Those extra stories of housing have provoked complaints about excessive density and uncompensated burdens on local services, especially from Israeli mayors who resented TAMA 38's bypassing their regulatory authority.<sup>197</sup> Because new housing created through TAMA 38 units is generally built in high-demand areas, it tends to be expensive, leading to complaints that such units drive up the price of other housing in the same neighborhood.<sup>198</sup> Set to expire in October of 2021, it is widely expected that TAMA 38 will be replaced by some alternative program giving local governments more authority to control new projects.<sup>199</sup>

Why is TAMA 38's existence in peril despite its successes? The complaints about density and gentrification seem weak. While extra stories obviously increase density, there was nothing magically appropriate about the status quo density before those stories were added. The claim that increasing the supply of market-rate housing raises housing prices contradict the overwhelming evidence that, far from raising rents, extra market-rate housing absorbs demand that would otherwise cause rents to rise even faster.<sup>200</sup>

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<sup>196</sup> John Myers, *How Tel Aviv Boosted New Homes by Half – and What It Tells Us About Fixing Housing*, CAPX (June 25, 2021), <https://capx.co/how-tel-aviv-boosted-new-homes-by-half-and-what-it-tells-us-about-fixing-housing>.

<sup>197</sup> Sara Toth Stub, *A Controversial Urban Development Program Divides Israelis*, U.S. NEWS (July 16, 2019), <https://www.usnews.com/news/cities/articles/2019-07-16/israel-considers-ending-a-controversial-urban-development-program>.

<sup>198</sup> Shamai & Hananel, *supra* note 192.

<sup>199</sup> Ofer Petersburg, *National Plan for Seismic Strengthening of Buildings Gets New Lease on Life*, ISRAEL HAYOM (July 22 2021), <https://www.israelhayom.com/2021/07/22/national-plan-for-seismic-strengthening-of-buildings-gets-new-lease-on-life>.

<sup>200</sup> Shane Phillips, Michael Manville & Michael Lens, *Research Roundup: The Effect of Market-Rate Development on Neighborhood Rents*, UCLA LEWIS CTR REG'L POL'Y STUD. (Feb. 2021), <https://escholarship.org/uc/item/5d00z61m> (summarizing empirical research).

Whatever the merits of TAMA 38's pro-housing policies, however, the program failed to create a constituency capable of sustaining the program. Because it relies on the value of extra stories to subsidize building renovation, TAMA 38 practically operates only in areas where demand for housing is high. In such areas, however, the share of pre-1980 housing stock is relatively low, compared to other parts of Israel. TAMA 38, therefore, benefits a small share of buildings in wealthy neighborhoods. It was entirely predictable that the neighbors living in such areas would be likely to resent the noise and density accompanying redevelopment of buildings eligible for enlarged air rights under TAMA 38. TAMA 38 also limited the betterment tax that municipalities could impose on new construction, thereby depriving the program of support from municipal officials. Small wonder, then, that this land option is vulnerable to political repeal.

## **B. Two Land Option Systems with Promise of Success**

The lesson to be drawn from colonial Hong Kong and modern Israel, then, is that land options help build housing only when they substitute competitive market mechanisms for bilateral monopoly while simultaneously creating a constituency that can protect the land options from repeal. In designing land options, therefore, it is prudent to keep both of these goals in mind.

To illustrate how land options might be designed to achieve these twin goals, we turn to two land option programs that show promise of promoting housing in a politically sustainable way: transferable development rights and street- or block-level rezoning (sometimes dubbed "hyper-local zoning").

### **1. Transferable Development Rights: Building Coalitions with Air Rights**

Transferable development rights (TDRs) give owners of properties where vertical construction above some minimum level is barred by land-use restrictions the right to transfer

their unused air rights to other property owners. For instance, the owner of a historically landmarked building might have the right to transfer unused air rights to apartment buildings, located on another parcel allowing the owners of those buildings to build extra stories. In theory, TDRs provide compensation to owners of heavily regulated properties without requiring expenditure of public revenue. In practice, TDRs are neither necessary nor sufficient for such compensation and actually impose large hidden burdens on taxpayers. Judged by their conventional justifications, therefore, TDRs are failures.<sup>201</sup>

As one of us has argued elsewhere, however, TDRs nevertheless have political value, because they can be used to enlist politically influential constituencies to lobby on behalf of regulations that might otherwise be impossible to enact.<sup>202</sup> The effect of TDRs on politics can, therefore, be positive to the extent that TDRs strengthen constituencies or land use goals that local politics systematically undercounts.

Consider, for instance, how New York City increased residential uses by allowing landmarked theaters to sell air rights to the owners of apartment buildings. Ordinarily, neighboring residents have both incentives and political clout to defeat proposals to construct higher buildings to accommodate more new residents: Their long-term interests in residential real estate create a constituency sufficient to maintain existing zoning. Theaters, however, are a politically popular cause in New York City: Actors and production crews can be enlisted by TDRs to push successfully for higher buildings over the objections of neighbors.<sup>203</sup> TDRs thereby can build constituencies in favor of goals like housing that otherwise might be slighted by the rival constituency effects of residential zoning.

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<sup>201</sup> *Building Coalitions Out of Thin Air*, *supra* note 19 at 93–107.

<sup>202</sup> *Id.* at 112–17.

<sup>203</sup> Hills & Schleicher, *Planning an Affordable City* *supra* note 4 at 125–27.

TDRs do not, however, inevitably have the properties of creating effective pro-housing constituencies. China's practice of land tickets, which look similar to TDRs, demonstrates both that TDRs are appealing to any government concerned about equitable development and that, without empowering new constituencies, it is difficult to break the old monopolies and the so-called new entitlements can be a politically-convenient excuse. Chinese local governments monopolize the urban land market and the right to develop and transfer rural land (through expropriation), which has resulted in rapid urbanization but also increasing rural-urban inequality.<sup>204</sup> Granting Chinese farmers TDRs, or land tickets, are supposed to entitle them to a certain portion of the increased land rents brought by China's rapid urbanization. In reality, however, Chinese farmers are not granted such rights; instead, local governments use this proposal to reclaim farmers' land and generate land tickets which are then "sold" to the government-affiliated platforms by farmers who gets compensation rather than the market value of their lost development rights. The problem is that, without empowering farmers who are the theoretical primary beneficiaries of this policy, local governments have used this policy to expropriate extra land from farmers, resulting in a reality contradicting to the policy's original intention.<sup>205</sup>

## **2. Street- and Building-Level Zoning: Hyperlocal Rights to Waive Zoning**

Another way to promote a constituency friendly to housing is to delegate to current property owners themselves the power to waive zoning restrictions on their own property.

Dubbed "hyperlocal zoning" by John Myers,<sup>206</sup> such programs allow the residents of a small

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<sup>204</sup> Shitong Qiao, *The Politics of Chinese Land: Partial Reform, Vested Interests, and Small Property*, 29 COLUM. J. ASIAN L.J. 70 (2015); Shitong Qiao, *Rights-Weakening Federalism*, 102 MINN. L. REV. 1671 (2017).

<sup>205</sup> Shitong Qiao, *Expropriation in the Name of Rights: Transferable Development Rights (TDRs), the Bundle of Sticks and Chinese Politics*, 13 NYU J.L. & LIBERTY 1 (2019).

<sup>206</sup> John Myers, *Hyperlocal Zoning: Enabling Growth by Block and by Street*, MANHATTAN INST.: URB. POL'Y SERIES (Feb. 3, 2021), <https://www.manhattan-institute.org/hyperlocal-zoning-enabling-growth-block-and-street>.

area like a street or block to vote to allow all the properties included within that area to intensify their current use.<sup>207</sup> Such intensification might include, for instance, the neighbors' voting to permit accessory dwelling units or duplexes in a single-family zone. Because homeowners would share equally in the value created by such waivers, they would have incentives to support such a program to realize the extra rental opportunities provided by more residential options. TAMA 38 was indeed nothing more than such a waiver program applied to individual apartment buildings. TAMA 38, however, was limited to a small share of buildings in cities like Tel Aviv – those built before 1980. By contrast, city-wide hyperlocal zoning by street or block could build a city-wide constituency, because there are large numbers of politically influential homeowners who stand to benefit from such waivers throughout any city.

Hyper-local zoning could also theoretically break up bilateral monopolies between governments and developers to the extent that there are numerous roughly equivalent blocks within a single city or even neighborhood. To the extent that homebuyers regard city blocks or individual street frontages as roughly fungible, homeowners on those blocks or streets will have an incentive to take actions will enhance their area's comparative real estate values. If “granny flats” are popular among buyers, then one street's legalization of such flats will put pressure on competing streets to follow suit, to maximize the re-sale value of their home. Of course, such decisions will balance re-sale value against current consumption value: If neighbors really regard accessory dwelling units as a recipe for excessive traffic or crowded sidewalks, then they might decide to resist the market signals being issued by real estate buyers' brokers and their clients.

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<sup>207</sup> The idea of street-level “block improvement district” was explained and defended in Robert C. Ellickson, *New Institutions for Old Neighborhoods*, 48 DUKE L.J. 75 (1998), <https://scholarship.law.duke.edu/dlj/vol48/iss1/2>. George W. Liebmann, *Devolution of Power to Community and Block Associations*, 25 URB. LAW. 335 (1993) focused more directly on zoning waivers. Residents living on a particular street frontage have had the power to waive various regulatory restrictions under various states' laws since the late-19<sup>th</sup> century. *See, e.g.*, *City of Chi. v. Stratton*, 44 N.E. 533 (Ill. 1896).



Because tastes for more density might vary among households, hyperlocal zoning might require a super-majority to reduce risks of intra-street exploitation.

Hyperlocal zoning, however, provides only very limited incentives for large-scale increases in density. It is one thing to allow the space above a garage to be used as an accessory dwelling unit, because every house in the zoning district likely has a garage and can share in the value created by that granular change in density. Upzoning a street of detached single-family houses for multi-story apartment buildings, however, would provide immediate benefits only to a parcel that had some prospect of being redeveloped for an apartment building. Unless there was some mechanism for sharing the wealth generated by that redevelopment with the other owners on the street, those owners would likely look askance at a proposal for radically more dense zoning: What's in it, after all, for them? One could conceivably combine the powers to waive zoning rules with some power to consolidate parcels, selling off all the parcels on the entire block or street for a single project and distributing the gains among the parcels' owners.<sup>208</sup> Unlike the modest zoning waivers contemplated by scholars like Robert Ellickson, however, such a radical empowerment of a single street or block, however, has yet to be proposed, let alone attempted.

## **Conclusion**

Hong Kong's housing is uniquely unaffordable, but its predicament with land is anything but unique. Urban housing crises exist wherever property rights create bilateral monopolies that impede reallocation of land to housing. Those same rights also foster constituency effects that stymie efforts to break the gridlock by re-arranging property rights. One possible solution to both

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<sup>208</sup> For a proposal to replace eminent domain with Land Assembly Districts that would give neighbors the power to sell of an entire neighborhood, see Michael Heller & Rick Hills, *Land Assembly Districts*, 121 HARV. L. REV. 1465 (2008).

problems is to confer new types of property rights on new classes of owners. To the extent that those rights define entitlements in assets that current owners cannot exploit, they evade constituency effects, because they interfere with no current owners' expectations. To the extent that such rights can be embedded in a bargaining framework where many buyers and sellers compete with each other to purchase or sell that newly allocated asset, the rights also escape the gridlock of bilateral monopoly.

We suggest land options for housing in Hong Kong as one example of such a newly created right that can promote housing by breaking apart old monopolies in property. There are, however, many other types of land options that hold promise as ways to end gridlock between owners and governments bargaining to change current uses of land. Underlying all such ideas is a simple idea: Where property rights affect the political process, the solution to gridlock-inducing property rights might be more and different property that fosters economic and political competition.