

## **Part 7: Leasing and Tenancy Matters**

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## TENANCIES AND LEASES

1. A tenancy or a lease is an arrangement whereby the owner of land, the landlord or the lessor, agrees to grant the right to possession of his land to the tenant or the lessee, for a fixed period, on the payment of rent. Where the term granted is long, the arrangement is usually referred to as a 'lease'. Where the term is short, the arrangement is referred to as a "tenancy". However, if the arrangement only gives a person a non-exclusive right to occupy another's land, it is a licence.
2. The main difference between a tenancy/lease and a licence is that a tenancy/lease creates an interest in land, whereas a licence does not. A licensee has only a personal interest and this interest can be revoked by the landowner at any time.
3. Differences between a lease and a tenancy:
  - A lease is commonly created for a term exceeding three years and executed as a deed. A deed is a document which both the lessor and the lessee will "sign, seal and deliver". The lessee has a legal interest in the land.
  - A tenancy agreement is commonly created for a term not exceeding three years. It needs not to be executed as a deed but can be signed underhand (i.e. by affixing a signature). Notwithstanding that a tenancy agreement is executed underhand, the tenant has a legal interest in the land if the tenancy does not exceed three years and the tenant remains in possession, pays market rent, and does not have to pay an extra payment to the landlord to obtain the tenancy.
  - The rights of a lessee under a lease which exceeds three years are protected against third parties, who deal with the lessor to create an interest in the land, if the lease has been registered in the Land Registry under the terms of the LRO. So if the lessor sells the property, the lessee will be able to enforce the lease against the new owner.
  - The interest of a tenant under a tenancy agreement/lease which does not exceed three years is protected against third parties even without registration so long as the tenancy is bona fide and the rent is at market rate.
  - If the lease/tenancy agreement contains an option to renew or to purchase, registration of the lease/tenancy agreement causes the option to bind a third party.
  - The option creates an interest in land which needs registration to allow it to be enforced against the third party. The lessee/tenant must ensure the lease/tenancy agreement which contains the option is registered otherwise he cannot enforce it against a third party. That is, if the lessor/landlord sells the land, and if the lease/tenancy agreement containing the option has not been registered before the sale, the new owner does not have to honour the option.

## TENANCIES BY CONTRACT AND BY OPERATION OF LAW

4. In most cases, a tenancy/lease will be created by a contract made between the parties. This tenancy/lease is often referred to as a “fixed term tenancy”. In other cases, the circumstances of occupation of land are treated as creating a tenancy by operation of common law principles. Examples of these tenancies by operation of law include periodic tenancies, and tenancies by estoppel.
5. A fixed term tenancy is a lease/tenancy for a fixed period of any length. The lease/tenancy comes to an end at the end of the last day of that period. The tenant must then vacate the premises.
6. Tenancies created by common law

A periodic tenancy is a tenancy whose term is classified by reference to the period for payment of rent. It is not a fixed term tenancy. Instead it continues indefinitely until it is terminated by the service of a notice to quit, giving the appropriate amount of time based on the period for payment of rent. Either party can give notice. So if the tenant pays rent each week he is a weekly tenant, and either the landlord or the tenant only needs to give the other party a week’s notice to quit. The most common periodic tenancy in Hong Kong is monthly tenancy, for which the landlord would need to give the tenant one month’s notice to quit. A periodic tenancy does not need to be in writing and the majority of its terms will be implied by common law.

7. A tenancy at will is created by operation of law. The essential element of a tenancy at will is that the tenant occupies the premises with the consent, express or implied, of the landlord. Usually it occurs where a tenant has a fixed term tenancy which comes to an end, and the tenant remains on the land. If the landlord does not object to the tenant “holding over”, but they have not agreed on a new fixed term tenancy, the tenant can remain until the landlord determines the tenancy by asking the tenant to leave. This is usually taken to mean that the landlord has consented to the tenant remaining until a new tenancy is agreed upon, or the tenant becomes a periodic tenant, or he is asked to leave by the landlord.

This tenancy is referred to as a tenancy at will because it is determinable immediately at the will of either party by simply informing the other party that the tenancy is at an end. No notice is required.

If the tenant pays rent to the landlord, which the landlord accepts, the tenant then becomes a periodic tenant.

Often during the time of holding over, the landlord and tenant will negotiate the terms of a new fixed term tenancy. So instead of becoming a periodic tenant, the holding over tenant will become a tenant under a new tenancy agreement.

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8. A tenancy at sufferance is another form of tenancy created by operation of law. This occurs where a tenant at the end of a fixed term tenancy holds over and the landlord does not indicate that he consents or objects to the tenant remaining on the premises. A tenancy at sufferance is terminated when the tenant moves out. If the tenant at sufferance pays rent which the landlord accepts, the tenant becomes a periodic tenant.

Alternatively, the landlord and the tenant may agree on a new fixed term tenancy.

As the landlord has not consented to the tenant's possession, there is no tenancy. If the landlord does not accept rent, does not negotiate with the tenant, but instead asks him to leave, the tenant would then become a trespasser. If the landlord does not then take action to have him removed, the trespasser will be able to start building up the required time to gain a possessory title over the land.

9. A tenant cannot deny the title of his landlord.

Tenancy by estoppel occurs where the landlord has no power to deal with possession of the land, and so cannot grant a tenancy. The usual situation is where a mortgage prohibits the mortgagor from granting a tenancy without the mortgagee's consent. Where the mortgagor, who has not sought the necessary permission from the mortgagee to grant a tenancy, the tenant cannot deny title of his landlord and must acknowledge the mortgagor as his landlord. When the mortgagee discovers that the tenant is there and takes action, the tenancy by estoppel becomes void. The mortgagee is considered to have "title paramount" to deal with possession during the currency of the mortgage. When the mortgagee exerts his rights, the tenant by estoppel becomes a trespasser.

In *Typhoon 8 Research Ltd v Seapower Resources International Ltd* [2001], the owner of land mortgaged it, and then leased the premises to the plaintiff in breach of a term of the mortgage which required the mortgagor to have the prior written consent of the mortgagee to lease.

In the above case, the tenant was a tenant by estoppel because, between himself and the mortgagor, he could not deny the mortgagor's right to lease the land and so the tenant had to pay rent to the mortgagor. When the mortgagee found out about the lease, the mortgagee demanded the tenant to pay mesne profits from the time it learnt of the lease until the tenant vacated the premises. "Mesne profits" is the term used to refer to damages payable by a trespasser.

### DOMESTIC AND COMMERCIAL TENANCIES

10. Tenancies can be classified by reference to the purpose for which the premises is to be used. The two major purposes are domestic and commercial.

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11. Under Part IV of the LT(C)O, a domestic tenancy means a tenancy of certain premises “let as a dwelling”. The premises are usually those in post-war buildings. Whether or not a tenancy is a domestic tenancy is a question of fact, and generally speaking, if the actual principal use to which the premises are put is domestic, then the tenancy is a domestic tenancy.
12. Commercial tenancies are provided for in Part V of the LT(C)O and relate to tenancies used for commercial purposes such as shops, offices, factories and warehouses, etc.
13. Until 9 July 2004, a Part IV tenancy had the protection of security of tenure and rent control, whilst a Part V tenancy had limited security of tenure protection.

With a Part IV tenancy, a tenant, having observed the statutory requirements for adequate notice to be served on the landlord, could apply to the Lands Tribunal to order the landlord to grant a new lease. In most cases, the Lands Tribunal would decide that the tenant should get a new term at the market rent. If the tenant would not accept that rent, he had to surrender possession.

With a Part V tenancy, the LT(C)O provided that six months’ notice had to be given by the landlord to terminate the tenancy.

14. The LT(C)O was amended substantially on 9 July 2004. A tenant of a Part IV tenancy could no longer seek the assistance of the Lands Tribunal for a new tenancy, and a Part V tenant lost his right to six months’ notice.

All tenancies, which previously were under Part IV and Part V, created on or after 9 July 2004 are now governed by common law and by the terms and conditions contained in the leases/tenancy agreements. On expiry of the periodic tenancy or the fixed term, the tenant should deliver up possession of the premises to the landlord.

For Part IV tenancies entered into before 9 July 2004, a Transitional Termination Notice (TTN) must be served by the landlord on the tenant if the landlord wishes to terminate this tenancy. The landlord must serve a TTN giving the tenant 12 months’ notice, without a change in the terms of the old tenancy. A tenant who wishes to terminate the tenancy must serve a TTN giving the landlord one month’s notice of termination. The TTN cannot be served earlier than the expiration of the existing tenancy.

### **STAMP DUTY**

15. Under the SDO, appropriate stamp duty is payable on a lease/tenancy agreement within 30 days of execution of the lease/tenancy agreement. If the stamp duty is not paid, the

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document cannot be registered in the Land Registry, nor can it be received in evidence in any court proceedings (except criminal proceedings and civil proceedings taken by the Collector of Stamp Revenue to recover stamp duty). There is late payment penalty for failing to pay the stamp duty on the due date.

### **FORM CR 109**

16. The landlord of a domestic tenancy is required to lodge a Form CR 109 (Notice of New Letting or Renewal Agreement) with the Commissioner of the Rating and Valuation within one month of the execution of the tenancy agreement for his endorsement. The form requires the landlord to supply such information as the term of the tenancy, the monthly rental, whether any rent-free period has been given, who will pay the rates, government rent, and management fees of the property, etc. After endorsement by the Commissioner of Rating and Valuation, one copy of the form will be returned to the landlord and the tenant. If it is submitted after one month, a penalty of \$310 will be payable by the landlord. Without a Form CR 109 endorsed by the Commissioner of Rating and Valuation, a landlord is not entitled to maintain an action to recover rent from the tenant. It is therefore important for the landlord that a Form CR 109 is lodged with the Commissioner of the Rating and Valuation within one month of the execution of a tenancy agreement.

### **COVENANTS AND CONDITIONS**

17. Some terms of the lease/tenancy are referred to as “covenants” and some as “conditions”. The term “covenant” means a term of the contract imposing an obligation or burden on one party for the benefit of the other. A “condition”, however, refers to the occurrence or non-occurrence of an event the breach of which by the tenant will entitle the landlord to forfeit the lease/tenancy automatically. The difference between a condition and a covenant relates to the remedies available on its breach. For example, breach of a covenant will not automatically entitle the landlord to re-enter and forfeit the lease/tenancy; for that to happen there has to be an express or implied “re-entry” term in the lease/tenancy. On the other hand, on breach of a condition, the landlord will have an automatic right to re-enter.
18. Some covenants in a lease/tenancy are referred to as “usual covenants”. These are obligations implied into a tenancy where they have not been expressly provided for. The covenant for quiet enjoyment is such a covenant implied on the part of the landlord.

19. Section 117(3) of the LT(C)O implies certain covenants and right of re-entry in domestic tenancies for breach of such covenants.

## RIGHTS OF THE TENANT

### *Exclusive Possession*

20. Unless a person, who is in possession for a time certain and paying rent, is given exclusive possession by the landlord, he is not a tenant, even if the document describes him as a tenant. On the other hand, if he is described as a licensee, but he has exclusive possession then he is to be treated as a tenant not as a licensee. Exclusive possession gives the tenant a right to exclude all persons from the land whilst the lease/tenancy remains valid. Those excluded include the landlord and his agents except in accordance with any terms in the lease/tenancy such as allowing the landlord or his agents to enter and inspect the state of repair of the premises. Once exclusive possession is granted to a person paying rent, for a term certain, he becomes a tenant.

### *Quiet Enjoyment*

21. The purpose of this covenant is to protect the tenant against eviction or dispossession from the premises either by the landlord or by someone claiming to have derived title from the landlord. The covenant also protects the tenant against interference with normal and lawful use and enjoyment of the property. A landlord who disconnects the supply of water or electricity to the premises or changes the locks would be in breach of this implied covenant. If the landlord breaches this covenant in a serious manner, the tenant may be entitled to terminate the lease/tenancy and seek damages. In other cases he will have a right to damages only.
22. Sections 119V (Part IV premises) of the LT(C)O provides that any person who does any act calculated to interfere with the place or comfort of the tenant and knows that that conduct is likely to cause the tenant to give up occupation of the premises commits an offence and the court may order the person convicted of the offence to pay to the tenant damages by way of compensation.

In *Yeung Wah, James v Alfa Sea Ltd.* [1993] 1 HKC 440, the landlord had on several occasions unsuccessfully tried to persuade the tenant of a flat to surrender his tenancy. When the tenant was overseas, the landlord entered the premises without notice to the tenant and carried out renovation work. The tenant was then locked out of the premises. The court held that the landlord was in breach of the covenant for quiet enjoyment and awarded damages to the tenant.

## OBLIGATIONS OF THE TENANT

### *Payment of Rent*

23. This is one of the most important terms of a lease/tenancy. In usual cases the lease/tenancy will mention the amount of rent and will have a clause under which the tenant expressly covenants to pay the rent.

Section 117 (3) of the LT(C)O now implies this covenant into a Part IV tenancy.

Section 126 provides in a limited manner similarly in respect of a Part V tenancy.

24. Section 117(3) gives the tenant 15 days to pay the rent. On default, the landlord can take action to forfeit the tenancy. Section 126 provides similarly for a Part V tenancy.

25. In addition, section 117(3) provides for certain other covenants and conditions to be implied into a Part IV tenancy. These include:

- a covenant that the tenant shall not use, or suffer or permit the use of, the premises or any part thereof for an immoral or illegal purpose; with
  - a condition for forfeiture if that implied covenant is broken;
- a covenant that the tenant shall not cause unnecessary annoyance, inconvenience or disturbance to the landlord or to any other person; with
  - a condition for forfeiture if that implied covenant is broken;
- a covenant that the tenant shall not make any structural alteration to, or suffer or permit any structural alteration to, the premises without the prior written consent of the landlord; with
  - a condition for forfeiture if that implied covenant is broken.

## RIGHTS OF THE LANDLORD

### *Receipt of Rent*

26. It is a contractual obligation on the part of the tenant to pay rent. Failure to pay the agreed rent gives the landlord a right to sue the tenant and to forfeit the tenancy resulting in the tenant having to vacate the premises.

### *Re-possession*

27. A landlord has various remedies on breach by a tenant. These remedies on breach by a tenant include:
- forfeiture of tenancy: the landlord can apply to the Lands Tribunal, the District Court or the Court of First Instance to recover possession;
  - distress where the tenant has not paid the rent: the landlord can apply to the District Court for a distress warrant to recover the arrears of rent by means of seizing and selling the tenant's goods and assets; or
  - depending on the amount owing, the landlord can apply to the Court of First Instance, the District Court, or the Lands Tribunal, to recover arrears of rent.
28. The landlord can claim possession of the premises under his right to re-enter and forfeit the tenancy. If the tenant remains on the premises, the landlord is entitled to mesne profits because the tenant is now a trespasser.
29. Forfeiture is available on:
- the breach of a condition; or
  - the breach of a covenant where
    - there is a forfeiture clause in the lease/tenancy agreement; or
    - (where the tenancy is one to which Section 117 or Section 126 of the LT(C)O applies) a condition for forfeiture is implied.

30. A typical forfeiture clause in a tenancy agreement is as follows:

“If the rent or any part thereof shall be unpaid for 15 days after the same shall become payable (whether legally or formally demanded or not) or if the Tenant shall fail or neglect to observe or perform any of the agreements, stipulations or conditions herein contained and on the Tenant’s part to be observed and performed or if the Tenant shall become bankrupt, or being a corporation shall go into liquidation (save for the purposes of amalgamation or reconstruction) or if any petition shall be filed for the winding-up of the Tenant, or if the Tenant shall otherwise become insolvent or make any composition or arrangement with creditors or shall suffer any execution to be levied on the Premises or otherwise on the Tenant’s goods, then and in any such case it shall be lawful for the Landlord at any time thereafter to re-enter the Premises or any part thereof in the name of the whole whereupon this Tenancy Agreement shall absolutely cease and determine but without prejudice to any right of action by the Landlord in respect of any outstanding breach or non-observance or non-performance of any of the agreements, stipulations and conditions contained in this Tenancy Agreement and on the Tenant’s part to be observed and performed.”

31. Section 117(5)(c) provides that persistent delay in the payment of rent is to be treated as “unnecessary annoyance, inconvenience or disturbance” making it a cause for forfeiture.

## **OBLIGATIONS OF THE LANDLORD**

### *Structural and Exterior Repairs*

32. There is no general obligation on a landlord to do any repairs to the premises, whether structural, external or otherwise. In some leases/tenancy agreements, the landlord undertakes an express obligation to do structural and external repairs. A common provision for this would read:

“At the Landlord’s own expense during the term to keep in good condition and proper repair the external parts of the premises (except the doors and windows thereof) and the walls and roofs thereof and to do all structural repair required to be done at any time by the Government.”

## TERMINATION OF TENANCY

### *By Effluxion of Time*

33. A fixed tenancy term automatically terminates on the expiry of the term, and upon such expiry the landlord is entitled to possession of the premises. Neither the landlord nor the tenant needs to serve any notice to terminate the tenancy. If the tenant holds over without a new tenancy, he becomes a tenant at will or at sufferance.

### *By Mutual Agreement*

34. A fixed term tenancy is terminated by surrender where, before expiry of the fixed term, the tenant surrenders his tenancy and the landlord accepts the surrender of tenancy by taking back possession. To avoid argument, the landlord and the tenant should execute a Surrender Agreement setting out the terms and conditions of such early termination. A tenant is not in breach of the tenancy agreement for the earlier termination if there is a valid surrender. However, he remains liable for past breaches unless the landlord excuses them.

### *Under a Break Clause*

35. A break clause is often inserted into a lease/tenancy agreement giving one or both parties the right to terminate the tenancy before the expiry of its term. The right may be exercised because of certain happenings, or merely to enable either party to terminate, without being in breach, before the end of the fixed term. It is now fairly common for both the landlord and the tenant to be given this right. The exercise of the right does not act as a breach of the agreement.

### *By Notice*

36. A periodic tenancy may be terminated by an appropriately timed notice to quit given by either the landlord or the tenant. Service of this notice does not amount to a breach because the tenancy is not for a fixed term.

### *Condition*

37. The continuation of a tenancy is conditional upon the occurrence of certain events or the tenant performing certain obligations, the non-occurrence of such events or the breach of such obligations will entitle the landlord to terminate the tenancy.

*Merge with Reversion*

38. If a tenant purchases the premises which he is holding under a tenancy agreement, he is said to have acquired “the reversion” (i.e. the right of the landlord during the currency of the lease including his title to the land and the right to recover possession). This means his term, or the right to possession, then merges with the reversion. It is then considered impossible for him to be both a tenant and landlord at the same time and the tenancy is extinguished.

*Forfeiture*

39. A landlord may forfeit the tenancy of the tenant if he is in breach of a condition of the tenancy. If he is in breach of a covenant of the tenancy, the landlord may also forfeit his tenancy if there is a “forfeiture clause” in the tenancy agreement for breach of the covenant.

*Frustration*

40. Frustration is a doctrine of the law of contract under which the parties to a contract are released from further obligations where a supervening event, over which the parties have no control and which was unexpected, radically changes the obligations in their agreement so that it would be unjust to hold them to the contract. For example, if a building is destroyed by earthquake, then in the absence of an express provision in the lease of the building for such occurrence, the performance of the lease would be frustrated, and the parties would be discharged from further obligations under the lease.

## **RENEWAL OF TENANCY**

*By Agreement*

41. With the repeal of security of tenure on 9 July 2004, the only means to renew a tenancy agreement, whether domestic or non-domestic, is by agreement of the parties.

*Option to Renew*

42. A tenancy agreement may contain an option to renew which gives the tenant a right to ask the landlord for a further term to commence at the expiry of the existing term. The option must be exercised strictly in accordance with its terms, otherwise it will not be effective. It is usual to add into the option a condition that the tenant may only exercise the option if he is not in breach of the tenancy agreement.