

LEASES

Registration of Leases for 3 Years or Less (Risks of Under-Value Rents)

Option Invalid for Uncertainty

Registration of Options to Renew and Exercise Notices

Tse Siu Hoi v Lee Dick Gold and Jewellery Ltd

Lands Tribunal [2015] HKCU 2007

Summary

An unclear “option to renew” in a tenancy agreement was held to be invalid. Further, neither the option nor its exercise had been registered and the rent was at less than the market rent. A purchaser from the original landlord was not bound by it and acceptance of rent after the end of the term did not change this.

The case highlights:

- The risk for a tenant in not registering a short term lease if there is any question that the reserved rent is at less than the market value.
- The need to register a lease of any length that contains an option to renew.
- The need to register a notice exercising an option to renew.
- The risk of accepting rent after a lease has ended as it may evidence an agreement for a new lease.
- The perils of deficient drafting and the difficulties of implying terms to remedy it.

Facts

- Between 2004 and 2012 Silver Joyce Investment Limited (Original Landlord) granted to Lee Dick Gold and Jewellery Ltd (Tenant) various tenancy agreements of a shop in Sheung Shui (Premises).
- The last Tenancy Agreement was prepared in Chinese in a standard form by an estate agent. It provided:

- The term was to be 2 years from 1 July 2012 to 30 June 2014 and, separately, “for 2 fixed years and 2 years open”.
- The Tenant was to “inform (the Landlord) by 1-month prior written notice of its intention to renew or surrender the Lease on expiry”.

In particular, the Tenancy Agreement contained no provisions as to how to determine the terms of any renewal. There were also several other inconsistencies which impeded clear interpretation.

- On 5 February 2014, the Original Landlord served notice on the Tenant to bring the tenancy to an end on 30 June 2014.
- The Tenant rebutted the notice stating that the Tenancy Agreement contained an option to renew for a further 2 years. It also purported to exercise the option.
- Between February 2014 and September 2014 the Tenant continued to insist the Tenancy Agreement contained an option to renew that had been validly exercised whilst the Original Landlord continued to insist it did not and to demand vacant possession. No new agreement was entered into but the Tenant remained in occupation and continued to pay rent to the Original Landlord at a higher rate alleging that this was the amount that had been agreed for the renewal term.
- On 11 September 2014, the Premises were sold to Tse Siu Hoi (New

Landlord) who sought vacant possession.

- The issues before the Lands Tribunal were:
 - Should the Tenancy Agreement be construed as containing an option to renew?
 - Did the acceptance of rent create a tenancy (this is referred to as a waiver of the New Landlord's right to possession)?
 - If there was an option that had been exercised, was the New Landlord bound by it given that neither the option nor its exercise had been registered and the rent which had allegedly been agreed was at an under-market value?

Legal Principles

- An implied term is not an addition to a contract. It will only be added if it spells out what the parties clearly meant, that is, if it spells out in express words what the instrument, read against the background, would reasonably be understood to mean. The implied term must be "so obvious it goes without saying".
- Tenancies for 3 years or less do not need to be registered at the Land Registry in order to bind successors in title to the Landlord (Section 3(2) Land Registration Ordinance). However, to qualify for this exemption, the tenancy must be granted at a rack rent (that is a market rent). If not, then the tenancy will be invalid against the landlord's successors in title (although it will remain valid against the original landlord).
- The exercise of an option creates an agreement for lease which must be in writing (Section 5(1)(a) Conveyancing and Property Ordinance) and must be registered to bind successors in title to the Landlord (Section 3(2) Land Registration Ordinance).

Decision

The Tribunal held that the Tenant was a trespasser from 30 June 2014 and was ordered to pay the New Landlord mesne profits and deliver up vacant possession.

Did the Tenancy Agreement contain an option to renew?

- The Tribunal held that it did not. The Tenancy Agreement contained conflicting language – one clause said 2 years, and the other 2 years fixed and another 2 years open. The reference to the "open" term could mean two things: first, either party could bring the tenancy to an end at the expiry of the contractual term or secondly, the Tenant had the right to renew. The Tribunal considered that the "open" term provision, read a whole, merely stated the obligation of the Tenant to inform the Landlord and that this was, at most, equivalent to an invitation to treat rather than a renewal right.
- The Tribunal declined to imply an option on the basis that it was neither reasonable nor obvious to a reasonable bystander that the Tenancy Agreement was intended to contain one. "Having agreed to a contract through its own lack of prudence or failure in exercising due diligence, the respondent cannot turn around and argue that the 2012 agreement is not complete because there should be another term to be added."
- Further, the Tenancy Agreement did not contain a mechanism for determining the terms of the new tenancy or rent or how to deal with any disputes and so the option was unenforceable for being uncertain.
- There was therefore no option to renew for the Tenant to exercise.

Did the acceptance of rent create a tenancy?

- The Tribunal found no evidence of mutual intention to create a tenancy. The unilateral act of depositing money into the Original Landlord's bank account did not amount to unequivocal evidence of a new tenancy.

If there had been an option, would the New Landlord have been bound by it?

- The Tribunal found that the New Landlord would have taken free of the option on several grounds.
- First, the option would have had to have been registered to bind a purchaser from the Landlord under Section 3(2) Land Registration Ordinance. The proviso to Section 3(2) states that "leases at a rack rent for a term not exceeding 3 years" do not have to be

registered, but this does not extend to options of renewal which extend the tenancy beyond 3 years (PC Fortune Company Limited v Mastermind Asset Management limited, CACV 89/2014). The option would therefore have been void for non-registration.

- Second, if there was a new option and it had been exercised, it became an agreement for lease, that is, an equitable interest in land. That interest also had not been registered. The fact the New Landlord had actual or constructive notice was irrelevant.
- Third, if there had been an option or agreement for lease, under Section 5(1)(a) Conveyancing and Property Ordinance it should have been in writing: "no equitable interest in land can be created or disposed of except by writing signed by the person creating or disposing of the same, or his agent...". This had not happened. Neither would the exercise of the option have fallen within the caveat in Section 6(2) Conveyancing and Property Ordinance that "nothing in Section 2 or 5..... shall affect the creation by parol of leases taking effect in possession for a term not exceeding 3 years (whether or not the lessee is given power to extend the term) at the best rent which can be reasonably obtained without a premium." The evidence was that the actual rent was not the best rent that could be obtained as required by Section 6(2) Conveyancing and Property Ordinance and for the proviso to Section 3(2) Land Registration Ordinance to apply.

lease if other evidence shows that this was the intention. If this is not the intention, then the parties should very clearly express the fact in writing.

Comments

- Short term leases should be registered if there is any question that the reserved rent is at less than the market value
- The best practice is that leases of any length that contain an option to renew should be registered.
- The best practice is that notices exercising an option to renew should be registered.
- Tenants should consider the effect of confidentiality provisions commonly imposed by landlords in relation to the above.
- Where rent is paid and accepted after a lease has ended it may constitute a new

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