DEPARTMENT OF JUSTICE LIBRARY

1999 CACV Nos. 4, 5 & 6

IN THE HIGH COURT OF THE HONG KONG SPECIAL ADMINISTRATIVE REGION COURT OF APPEAL

BETWEEN

STANDARD CHARTERED BANK	Plaintiff
and	
(1) GROW UP TRADING LIMITED (2) SOUNDTOP INDUSTRIES LIMITED (3) VIA HONG KONG READY-TO-WEAR COMPANY LIMITED (now known as CHEONG TAI INTERNATIONAL HOLDINGS LIMITED)	Defendants

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Before: Nazareth V.-P., Leong J.A. and Keith J. in Court
Date of Hearing: 18th May 1999
Date of Handing Down of Judgment: 3rd June 1999

JUDGMENT

Keith J.:

Introduction

In September 1998, warrants of distress were issued for arrears of rent in respect of various premises in an industrial building in Kwai Chung. The warrants had been sought by the Plaintiff, Standard Chartered

Bank ("the Bank"). The Defendants ("the lessees"), who were the lessees of the three sets of premises to which the warrants related ("the premises"), applied to the District Court for the discharge or suspension of the warrants. On 3rd November 1998, in a concise and well-argued judgment, the judge held that the Bank was entitled to distrain for arrears of rent, and he refused to discharge or suspend the warrants. From that judgment, the lessees now appeal.

The facts

The facts are not in dispute. In 1994, Regal Grace Ltd. ("Regal") granted the Bank a mortgage over the building in which the premises are in return for the Bank granting banking facilities to Regal. In due course, Regal let the premises to the lessees. Towards the end of 1997, Regal got into financial difficulties. Accordingly, at Regal's request, one of the lessees issued a number of post-dated cheques in favour of Regal to cover rent payable in the future by the lessees. All dates from now on in this judgment are dates in 1998.

On 9th April, Regal assigned to the Bank its right to the rent payable to it by the lessees. The lessees were informed of that, and the following month they were told that in future they had to pay the rent to the Bank. At that stage, the lessees took legal advice. No doubt they were worried about what they should do about the post-dated cheques if rent for the same period had to be paid to the Bank. They were advised that they should countermand payment on those of the post-dated cheques which had not yet been presented for payment, so that they could pay the rent to the Bank without having to worry about the payments for rent which had already been made to Regal. Those were the cheques dated 1st June, 1st

July, 1st August and 1st September, which covered the rent for the months of June-September inclusive.

The problem for the lessees was that a finance company, Edward Wong Finance Co. Ltd. ("Edward Wong"), had by then acquired an interest in the proceeds of the cheques. It is unclear what that precise interest was. Either the cheques had been discounted to Edward Wong, or they were being held by Edward Wong as security for a loan to Regal. Either way, though, the lessees were told that Edward Wong would sue them if they stopped payment on the cheques. The lessees must have taken the view that discretion was the better part of valour, because the bank statements of the lessee on whose account the cheques were drawn show that the cheques were not stopped. The Bank did not in fact receive from the lessees the rent due for June-September.

In the meantime, Regal had defaulted under its mortgage with the Bank. On 1st June, the Bank exercised its power to take possession of the building, which included the lessees' premises. Its solicitors informed the lessees a few days later that property agents had been appointed to manage the building on the Bank's behalf, and they repeated what the lessees had been told the previous month, namely that in future they had to pay the rent to the Bank. It was because that rent had not been paid that the Bank applied for warrants of distress to be issued for the arrears of rent. Those warrants were issued on 12th and 14th September. The arrears of rent to which the warrants related covered not only the arrears for June-September, but the arrears for April and May as well. On 18th and 21st September, the lessees applied for the discharge or suspension of the warrants.

Relationship of landlord and tenant

One of the arguments which the judge had to consider was whether the relationship of landlord and tenant existed between the Bank and the lessees. It was not immediately apparent to me why that would be relevant. Could it not be said that because the Bank was entitled to the rent in respect of the premises by virtue of the assignment, it was entitled to distrain for any arrears? After all, section 81 of the Landlord and Tenant (Consolidation) Ordinance (Cap. 7) ("the Ordinance") provides:

> "Any person claiming to be entitled to arrears of rent, or his duly constituted attorney or agent, may apply for a warrant [of distress]."

Even if the Bank was not the lessees' landlord, it was by virtue of the assignment entitled to the rent.

However, it was conceded by Mr. Joseph Fok S.C. for the Bank that the common law vests the right to distrain only in the landlord of the tenant who is in arrears of rent, and that the Ordinance cannot be construed as modifying or abrogating such a well-established common law principle. He therefore accepted that a mere assignee of the rent is not entitled to distrain. Similar considerations apply to section 106(f) of the Ordinance, which gives mortgagees in possession the right to apply for warrants of distress. It was conceded that mortgagees in possession only enjoy such a right when the relationship of landlord and tenant exists between them and the person from whom the rent is due. Subject to a jurisdictional point to which I shall return later, it was therefore accepted that the judge's order can only be sustained if the relationship of landlord and tenant can be said to have existed between the Bank and the lessees when the warrants were

issued, or if the lessees had by then lost the right to assert that they had not become the tenants of the Bank.

The law on the topic is summarised in Halsbury's Laws of England, Vol. 13, 4th ed., para. 218 as follows:

> "A lease by a mortgagor subsequent to the mortgage, unless made under an express power given by the mortgage or under the statutory power, is void as against the mortgagee, who cannot distrain, as there is no relation of landlord and tenant between him and the lessee."

The mortgage between the Bank and Regal prohibited the granting of a lease in respect of any of the premises in the building without the Bank's written consent. The Bank does not contend that it ever gave such consent. Moreover, the statutory power referred to is the power conferred by section 99 of the Law of Property Act 1925 on the mortgagor to lease the mortgaged property if certain provisions as to the contents of the lease are fulfiled. Mr. Fok accepted that the corresponding provision in the Conveyancing and Property Ordinance (Cap. 219) would not have conferred on Regal the power to grant these leases to the lessees. The relationship of landlord and tenant between the Bank and the lessees could not therefore have arisen by virtue merely of the leases granted to the lessees by Regal.

However, para. 218 continues as follows:

> "Such a relationship, however, may arise by express agreement or by conduct, but it does not relate back to notice of the mortgage."

This principle was encapsulated by Cross J. (as he then was) in *Stroud Building Society v. Delamont* [1960] 1 WLR 431 at p. 434:

> "When a mortgagor has granted a tenancy which is not binding on the mortgagee, since he has not given his consent, the mortgagee can, instead of treating the tenant as a trespasser, consent to treat him as his tenant or, at all events, act in such a way as precludes him from saying that he has not consented to take him as his tenant. Such an acceptance by the mortgagee of the mortgagor's tenant, whether express or implied, or operating by way of estoppel, must, I think, amount to a creation of a new tenancy between the parties. The tenancy between a mortgagor and a tenant is not one which is merely voidable by the mortgagee if he chooses not to accept it, but which he can confirm by waiving his right to avoid it. It is a nullity asagainst the mortgagee; and so, if the mortgagee is to lose his right to treat the mortgagor's tenant as a trespasser, it must be because the tenant has become the mortgagee's tenant under a new tenancy."

The critical question, therefore, is whether it is possible to infer from the conduct of the parties that the relationship of landlord and tenant had arisen between the Bank and the lessees. On that question, para. 218 goes on:

> "The question whether a new tenancy between the mortgagee and the tenant has been created is one of fact; mere failure by the mortgagee to evict the tenant is insufficient; mere notice of the mortgage deed and of the interest being in arrear accompanied by a demand for rent is not sufficient, but the fact that rent is paid in accordance with such notice is evidence of a tenancy. The notice is the offer, and evidence of acceptance of or assent to the offer is necessary."

There are a number of authorities in which the courts have had to address the issue whether, on the facts, such a relationship had been created. The authorities are useful to illustrate those features which make the creation of the relationship easier or more difficult to infer, but it should not be forgotten that each case depends on its own facts. It is also to be noted that, more often than not in these cases, it is the mortgagee who is seeking to assert that the lessee has not become its tenant, and the cases have to be viewed in that light.

In the present case, the judge held that a new tenancy had been created between the Bank and the lessees because "the [Bank] has at all material times accepted the [lessees] as tenants, and vice versa" (emphasis added). In my view, the judge was plainly right to conclude that the Bank had accepted the lessees as its tenants. The Bank had not taken any steps to evict the lessees. On the contrary: it had required the lessees to pay it the rent in future, and it had appointed property management agents to collect that rent on its behalf. Mr. Benjamin Chain for the lessees did not contend otherwise.

However, with respect to the judge, I cannot go along with his conclusion that the lessees had accepted the Bank as their landlord. The lessees never paid any rent to the Bank, and I have not discerned any unequivocal act on their part from which their acceptance of the Bank as their landlord can be inferred. If a new tenancy is to be regarded as having been created, there must have been acts constituting the offer of a new tenancy and its acceptance. The Bank's requirement that the lessees pay the rent to it in future amounted to an offer by the Bank to the lessees of a new tenancy, but there was nothing which the lessees did from which the acceptance by them of that offer can be inferred. As was held in *Towerson v. Jackson* [1891] 2 QB 484, the mere fact that the lessee remained in possession after being served with a notice to pay the rent to the mortgagee was not evidence of an agreement that the lessee should become the tenant of the mortgagee.

In reaching this conclusion, I have not overlooked two particular features of the evidence relied on by Mr. Fok:

(i) When the lessees heard that the Bank was requiring them to pay the rent in future to it, they thought of stopping the post-dated cheques which they had issued to Regal so that they could pay the rent to the Bank. They only refrained from doing so because of the threat from Edward Wong of being sued if they did that.

(ii) On a number of occasions between May and September, the Bank was told by the lessees' accountant that the lessees were not liable to pay the Bank rent up to the end of September "as rent had been paid to Regal".

These features of the evidence show that the lessees may well have been prepared to accept the Bank as their landlord if they had been able to get the post-dated cheques back from Regal or if they had been able to stop payment on them with impunity. But since they were not able to do either, the fact that they might have been prepared to accept the Bank as their landlord in other circumstances cannot mean that they accepted the Bank as their landlord in the prevailing circumstances. It follows that, in my view, the relationship of landlord and tenant between the Bank and the lessees had not come into existence by the time the warrants were issued.

Mr. Fok also contended that the lessees had lost their right to assert that they had not become the tenants of the Bank. This argument is based on the fact that prior to 1st June when the Bank went into possession of the building, the Bank was treating the lessees as its tenants. The lessees would have known that from the Bank's requirement that in future all rent be paid to it. For my part, I do not think that that helps the Bank.

I do not see how the lessees' lack of response to the treatment of them by the Bank as the Bank's tenants prevented the lessees from subsequently asserting that the relationship of landlord and tenant had not arisen between them. It follows from all this that in my judgment the Bank was not entitled to distrain for the arrears of rent.

The jurisdictional bar

Having concluded that the Bank was not entitled to distrain for the arrears of the rent, it is necessary to consider the Bank's alternative argument that the judge did not have power to entertain the lessees' application to discharge or suspend the warrants. The argument is as follows. The statutory rules regulating distress for rent are contained in Part III of the Ordinance. Section 93(1), which is in Part III, provides:

> "The debtor, or any other person alleging himself to be the owner of any property seized under this Part, may, at any time within 5 days from such seizure, apply to the court to discharge or suspend the warrant or to release a restrained article; and the court may discharge or suspend the warrant or release the article, on such terms as it may think just."

The "court" is the District Court. Since Part III of the Ordinance is intended to be a complete and comprehensive code governing distress for rent, an application for the discharge or suspension of a warrant for distress has to be made in accordance with the terms of section 93(1). The Bank's argument is that section 93(1) is only triggered once goods have been seized under the warrant, in which case the debtor has 5 days from the seizure to make the application. No goods were ever seized under these warrants, and section 93(1) had therefore not been triggered.

I cannot accept this argument. In my view, section 93(1) merely prevents an application for the discharge or suspension of a warrant

from being made after 5 days have elapsed since the seizure. It does not prevent an application for discharge or suspension being made before the seizure. I do not regard that view as in any way inconsistent with the language of section 93(1). The words "at any time within 5 days from such seizure" could be construed as meaning "at any time up to 5 days after any seizure of the property" just as it can be construed as meaning "at any time during the 5 days immediately following the seizure of the property".

This view also accords with common sense. I appreciate that someone other than the debtor who claims "to be the owner of any property seized under this Part" can only apply for the discharge or suspension of the warrant after the property has been seized. But that does not apply to the debtor. Why would the legislature have wanted to require debtors — on those admittedly rare occasions when they happen to discover that warrants for distress have been issued against them and wish to have the warrants discharged or suspended — to wait until the goods have been seized and then to allow them only a few days to make their application to the court? In my opinion, the judge was entirely correct to reject the Bank's argument on this issue.

I should add that if section 93(1) is only triggered once goods have been seized under the warrant, and if Part III of the Ordinance is intended to be a complete and comprehensive code governing distress for rent, there is a gap in the legislation. I think it unlikely that the legislature intended debtors to be without a remedy before goods have been seized under the warrant, and that suggests that there must be another route by which the court has power to discharge or suspend a warrant before it has

been executed. However, that is not an issue which I need to address in view of my conclusion on the construction of section 93(1).

Conclusion

For the reasons I have given, I would allow the lessees' appeal, I would set aside the order of the judge, and I would substitute for it the following orders:

(i) an order that each of the warrants for distress be discharged, and

(ii) an order that the Bank do repay to each of the lessees the sums which they paid into court pursuant to the order of Judge Chow on 30th September, and which were paid out to the Bank pursuant to the order of Judge Whaley on 3rd December, together with interest thereon from the date of payment into court at the judgment rate.

At present, I see no reason why costs should not follow the event, and the order *nisi* as to costs which I would make is that the Bank should pay to the lessees their costs of the proceedings in the District Court and of the appeal, to be taxed if not agreed.

Finally, there are technically three separate appeals, because three separate warrants of distress were issued in respect of the three sets of premises, and that resulted in three separate applications for their discharge or suspension. The orders which I have said I would make apply to each of the appeals. In the interests of convenience, the heading which appears at the top of this judgment has been abbreviated. Strictly speaking, the

heading should have set out each of the cases individually. It just seemed easier to express it in the way I have.

Leong, J.A.:

I agree. There must have existed between the plaintiff (the mortgagee) and the defendant (the tenant) a landlord and tenant relationship before the plaintiff is entitled to distrain for the rent under the lease between the defendant and Regal Grace Ltd. (the mortgagor). This is so despite the express provisions in s. 81 and s. 106(f) of the Landlord and Tenant (Consolidation) Ordinance, Cap. 7. Whether such a relationship existed is a question of fact. The assignment by the mortgagor of the right to the rent payable under the lease to the plaintiff without more does not give rise to such a relationship nor the fact that the defendant remained in possession after notice of the plaintiff entering into possession. That the plaintiff did not treat the defendant as a trespasser after entering into possession may very well have estopped the plaintiff from denying the defendant as its tenant, but this is not sufficient to show a new tenancy with the defendant has been created. The defendant must also be shown to have accepted the plaintiff as landlord or that the defendant, by its own acts or omission, is estopped from denying that such a relationship existed.

To show the defendant had accepted the new tenancy, the plaintiff relies on the defendant's acceptance of the obligation to pay rent to the plaintiff and that between May and September 1998, the defendant's financial controller had told the representative of the plaintiff that the defendant was not liable to pay the rent to the plaintiff as it had been paid

to Regal Grace Ltd. In addition, the plaintiff relies on the defendant's attempt to stop payment of the cheques discounted to Edward Wong Finance Co. Ltd. and the defendant's notice of the plaintiff having taken over management of the premises.

All the above features of evidence, separately or cumulatively do not, in my opinion, amount to showing that in the circumstances of the present case, the defendant had accepted the plaintiff as the landlord. The conclusion of the District Judge that the plaintiff is entitled to distrain for rent cannot be upheld.

I also agree with the conclusion reached by my Lord, Keith, J. and the reasons therefor that the time limit of within 5 days from seizure to make an application to discharge a distress warrant under section 93(1) of the Ordinance does not apply where no seizure has been made pursuant to the warrant. That being so, the Judge's conclusion on jurisdiction is correct.

I would allow the appeal and I agree to the orders proposed by my Lord, Keith, J.

Nazareth V-P:

I agree with Keith J. and Leong J.A. In particular reference to what I regard as the central question for determination, I would add that I am also satisfied that there is nothing before this Court that would warrant

the judge's conclusion that the lessees had accepted the Bank as their landlord, including the matters Mr. Fok S.C. relied upon in that regard.

The appeals are accordingly dismissed with the orders proposed by Keith J.

(G.P.Nazareth)	(A. Leong)	(Brian Keith)
Vice-President	Justice of Appeal	Judge of the Court of First Instance

Mr. Joseph Fok S.C. and Miss June Wee, instructed by Messrs. Tsang, Chan & Wong, for the Plaintiff.

Mr. Benjamin Chain, instructed by Messrs. Y.S. Lau & Partners, for the Defendants.