# SUPREME COURT OF QUEENSLAND

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| CITATION: | *Grepo & Anor v Jam-Cal Bundaberg Pty Ltd* [2015] QCA 131 |
| PARTIES: | **FRANK GREPO & BERYL DOROTHY GREPO**<br>(appellants)<br>**v**<br>**JAM-CAL BUNDABERG PTY LTD**<br>ACN 089 493 550<br>(respondent) |
| FILE NO/S: | Appeal No 6131 of 2014<br>SC No 514 of 2013 |
| DIVISION: | Court of Appeal |
| PROCEEDING: | General Civil Appeal |
| ORIGINATING COURT: | Supreme Court at Cairns – [2014] QSC 119 |
| DELIVERED ON: | 17 July 2015 |
| DELIVERED AT: | Brisbane |
| HEARING DATE: | 24 February 2015 |
| JUDGES: | Holmes and Morrison JJA and Douglas J<br>Separate reasons for judgment of each member of the Court, Holmes JA and Douglas J concurring as to the orders made, Morrison JA dissenting in part |
| ORDERS: | **1. The appeal is allowed.**<br>**2. The judgment below is set aside, and it is ordered that there be judgment for the appellants for recovery of possession of premises at 1 Ray Road Mareeba described as Lot 874 on CP NR 4546, County of Nares, Parish of Tinaroo, Title Reference 20945056.**<br>**3. The respondent is to pay the appellants' costs of the appeal and the proceeding at first instance.** |
| CATCHWORDS: | LANDLORD AND TENANT – RENT – PROVISIONS AS TO RENT IN AGREEMENT FOR LEASE OR LEASE – RENT REVIEW CLAUSES – where the lease provided for rent review after the first year, either by way of market review or review based on the consumer price index – where the lessee paid rent at the base rate for the whole of the three year term – where the lessor argued that the lessee was required to calculate the rent payable in accordance with the consumer price index – where the lessee argued that the obligation to pay any increase was dependent on a determination being made by the lessors – whether the terms of the lease required a determination to be |

made – whether the trial judge erred in failing to find that the lessee was in breach of its obligation to pay rent

LANDLORD AND TENANT – COVENANTS – OTHER COVENANTS – where the lease prohibited the accumulation of rubbish on the premises – where the lessors argued that there was photographic evidence of an unacceptable accumulation of tyres – where there was no evidence as to when the photographs were taken – whether the trial judge erred in failing to find that the lessee was in breach of the lease

LANDLORD AND TENANT – COVENANTS – NOT TO ASSIGN OR SUBLET – LESSOR'S CONSENT – where the lease prohibited the lessee from underletting the premises without the lessors' prior consent – where the permitted use of the premises was as a wrecking business – where the lessee rented a granny flat which was part of the premises to an employee without the lessors' permission – where the lessee argued that the tenant was a caretaker and that his occupation of the flat was ancillary to the permitted use of the premises – whether the trial judge erred in failing to find that the lessee's underletting of the premises was in breach of the lease

LANDLORD AND TENANT – COVENANTS – OTHER COVENANTS – where the lease required the tenant to keep the premises free and clear of rodents, termites, cockroaches and vermin – where a pest inspector found active termites in parts of the premises – where the lessee had not undertaken any termite treatment during the term of the lease – where the trial judge construed the obligation under the lease as an obligation to address any evident termite problem – whether the trial judge erred in construing the obligation – whether the trial judge erred in failing to find that the lessee was in breach of the lease

LANDLORD AND TENANT – RENEWALS AND OPTIONS – EXERCISE OF OPTION – RELIEF AGAINST LOSS OF OPTION FOR RENEWAL – where the lessee gave notice of its intention to exercise an option to renew – where the lessor did not give notice of the lessee's breaches under s 128 of the *Property Law Act* 1974 (Qld) – where the lessee argued that the protective effect of the section endured for the entire term of the lease – where the lessor argued that the section did not apply after the lessee purported to exercise the option by giving notice – whether the purported exercise of the option to renew for the purposes of s 128 occurred at the time of the giving of notice, or at the expiration of the lease – whether s 128 applied to the lessee's breaches which occurred after the giving of notice but before the expiration of the term of the lease

LANDLORD AND TENANT – RENEWALS AND OPTIONS – NATURE OF OPTION – where the lessee argued that the giving of notice of intention to exercise the option to renew created an agreement for a lease, entitling it to seek relief from

forfeiture under s 124 of the *Property Law Act* 1974 (Qld) – where the lessor argued that the option to renew was an irrevocable offer with conditions precedent to its acceptance, namely the giving of notice and compliance with obligations under the lease – where the lessee argued that the conditions precedent were not met and there was no entitlement to a lease, and no entitlement to seek relief from forfeiture – where there were breaches of covenants up to and at the date of the lease's expiry – whether there was an agreement for a lease – whether the lessee could claim relief from forfeiture under s 124 of the *Property Law Act* 1974 (Qld)

*Conveyancing Act* 1919 (NSW), s 128, s 129, s 133E, s 133F, s 133G
*Property Law Act* 1974 (Qld), s 123, s 124, s 128

*Beca Developments Pty Ltd v Idameneo (No 92) Pty Ltd* (1989) 4 BPR 9575, not followed
*Bentley v Chang Holdings Pty Ltd* [2012] QSC 366, considered
*Brennan v Kinjella Pty Ltd* (1993) 6 BPR 13,168, cited
*David Deane & Associates Pty Ltd v Bonnyview Pty Ltd* (2005) ANZ ConvR 518; [2005] QCA 270, considered
*Eighteenth Ashlaw Nominees Pty Ltd v Vadelly Pty Ltd*, unreported, Williams J, Supreme Court of Queensland, No 4864 of 1986, 25 November 1987, considered
*Flagstaff Investments Pty Ltd v Cross Street Investments Pty Ltd* (1999) 9 BPR 17,067; [1999] NSWSC 999, applied
*Gilbert J McCaul (Aust) Pty Ltd v Pitt Club Ltd* (1957) 76 WN (NSW) 72, considered
*Jack Butler & Staff Pty Ltd v Black* (1991) ANZ ConvR 186, not followed
*Laybutt v Amoco Australia Pty Ltd* (1974) 132 CLR 57; [1974] HCA 49, considered
*Lolly Pops (Harbourside) Pty Ltd v Werncog Pty Ltd* (1998) NSW ConvR 55-861; [1998] NSWSC 304, not followed
*Nessmine Pty Ltd v Devuzo Pty Ltd* (1989) NSW ConvR 55-496, not followed
*Reilly v Liangis Investments Pty Ltd* (2000) 9 BPR 17,509; [2000] NSWSC 47, considered
*Rethmeier v Pioneer House Pty Ltd* (1990) 6 BPR 13,245, applied
*West Country Cleaners (Falmouth) Ltd v Saly* [1966] 1 WLR 1485; [1996] 3 All ER 210, distinguished

COUNSEL: M Jonsson for the appellant
T Arnold for the respondent

SOLICITORS: Girgenti Lawyers for the appellant
Dave McHenry & Associates for the respondent

[1] **HOLMES JA:** The appellant lessors, Mr and Mrs Grepo, appealed a judgment dismissing their claim for recovery of possession of premises leased to the respondent, Jam-Cal Bundaberg Pty Ltd. Their argument was, essentially, that the trial judge erred in failing to find that the lessee had breached clauses of the lease as to payment of rent, control of termites, accumulation of rubbish and sub-letting, those breaches disentitling it to exercise an option to renew the lease. The case was further complicated by questions as to whether and to what extent the protective effect of s 128 of the *Property Law Act* 1974 applied, so as to prevent the lessors from relying on any established breaches, and whether there was an agreement for a new lease in respect of which relief from forfeiture under s 124 of the Act was available to the lessee.

*The lease and the option to renew*

[2] The lease in question was of land adjacent to the lessors' own residence. They had previously used it in their business as scrap metal dealers, which they sold to the lessee; the contract of sale was subject to the execution of the lease. The use of premises for which the lease provided was "Wrecking Yard & Scrap Metal Merchant". The area leased contained a small caretaker's cottage with a granny flat attached. The lease was for a term of three years, commencing on 14 May 2010 and expiring on 13 May 2013. It contained provision in cl 17 for the lessee to exercise an option to renew:

> "17. OPTION
>
> 17.1 Option to Renew
>
> If the Tenant:
>
> 17.1.1 not less than six (6) months prior to the expiration of this Lease gives written notice to the Landlord that it wishes to renew this Lease; and
>
> 17.1.2 has at all times up to the date of expiration of the term of this Lease complied punctually with its obligations under this Lease,
>
> then the Landlord will grant to the Tenant a further lease of the Premises [on specified conditions]…"

[3] By letter dated 5 November 2012, the lessee gave notice of its desire to exercise the option to renew. On 30 May 2013, however, the lessors advised that the lease had expired and that rent remained outstanding. Notices to remedy breach had been served in October 2012 and December 2012; another was served in August 2013. On 2 October 2013, the lessors gave notice terminating the lease to the extent that it was not already terminated and requiring the lessee to give up possession. They followed with the claim for recovery of possession which was the subject of the judgment under appeal.

*The issues before the trial judge*

[4] The lessors' statement of claim alleged that the lessee had breached a number of its obligations under the lease so that it had not met a condition precedent for renewal of the lease under cl 17.1, and no further lease had been granted. In its defence and counter-claim, the lessee denied any breach, asserted that it had lawfully exercised the option and pleaded that in any event the lessors had lost any right to deny renewal of the lease when they failed to give notice pursuant to s 128 of the *Property Law Act*.

(That section, inter alia, precludes a lessor, where the lessee purports to exercise its option, from relying on a breach of covenant to refuse renewal unless it gives notice to that effect within 14 days of the purported exercise of the option.) It counter-claimed for relief from forfeiture if it were found liable to it, a declaration that it had validly exercised its option and an injunction requiring the lessors to do what was necessary to enable the execution of a new lease.

[5] At trial, counsel for the lessors conceded that s 128 did not permit a lessor who had not given the requisite notice to rely on breaches committed prior to the time of the purported exercise of an option, but maintained that the provision had no bearing on subsequent breaches. The trial judge accepted that argument, regarding the critical period for consideration as that between the date of the letter of 5 November 2012, expressing the lessees' desire to exercise the option, and 13 May 2013, when the lease expired. The learned judge referred to the parties as being "content that [he] focus on what happened after November 2012", but it appears in fact that the lessee did not abandon its initial position, which was that s 128 applied to the entire period up to the expiration of the lease; indeed, its counsel revisited that argument in reply.

[6] Counsel for the lessee in reply also asserted that if there were breaches between the giving of notice and the expiry of the lease, the trial judge had power to relieve against forfeiture; he relied for that proposition on statements by Philip McMurdo J in *Bentley v Chang Holdings Pty Ltd*,[1] referring in turn to *Nessmine Pty Ltd v Devuzo Pty Ltd*[2] and *Beca Developments Pty Ltd v Idameneo (No 92) Pty Ltd*.[3] The trial judge said that he was aware of the jurisprudence relating to the section, specifically mentioning *Bentley v Chang Holdings Pty Ltd*, but because he did not find the existence of any breach, the questions of whether s 128(4) applied for the entire term of the lease or whether there was any power to grant relief did not require resolution.

*The appeal grounds*

[7] The lessors' appeal grounds complained of the trial judge's findings that between 5 November 2012 and 13 May 2013 there was no breach of covenant in respect of the four matters already mentioned - payment of rent, control of termites, accumulation of rubbish and sub-letting - and of his failure to find that because of breach, the lessee had not met a condition precedent to the grant of a further lease.

*The finding that the lessee had not breached its obligation to pay rent*

[8] Clause 3.1 of the lease required the lessee, without demand, to pay rent in advance on the first day of the month. A figure was set for the first year, with provision made in cls 3.2 and 3.3 for review thereafter. Clause 3.2.1 provided for annual review based on the Consumer Price Index. Clauses 3.2.2 and 3.3 provided for market rent reviews, while cl 3.4 dealt with what was to occur in the interim before the rent for a given year was determined. The review clauses were in the following terms:

> "Rental Reviews
>
> 3.2.1 **Rent and Annual Reviews**
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> The expression "Rent" means an annual sum calculated as follows:

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1 [2012] QSC 366.
2 (1989) NSW ConvR 55-496.
3 (1989) 4 BPR 9575.

(a) for the first (1st) Lease Year:

the sum specified in **Item 4(b)(i)** of the **Reference Data**;

(b) for the second (2nd) and each subsequent Lease Year:

subject to **cl. 3.2.2** the higher of:

(i) that amount derived annually by multiplying the Rent for the Lease Year last concluded by a fraction obtained by dividing the Index Number for the last quarter immediately preceding the first day of the Lease Year under review by the Index Number for the last quarter immediately preceding the first day of the Lease Year last concluded; and

(ii) the Rent reserved and payable during the Lease Year last concluded.

(The "Reference Data" referred to in cl 3.2.1(a) formed a schedule to the lease, while "Index Number" was defined as meaning the Consumer Price Index (CPI) for Brisbane as published by the Australian Bureau of Statistics, or, if none were available, an index agreed or determined by the Australian Institute of Valuers & Land Economists.)

3.2.2 **Reviews to Market**

The Rent will be further reviewed so that the Rent for the Lease Years commencing on the Market Review Dates will be the greater of:

(a) the Rent reserved and payable during the Lease Year last concluded; and

(b) the market rent for that Lease Year calculated in accordance with **cl. 3.3**,

and the Rent so determined will be reviewed annually in accordance with cl. 3.2.1.

3.3 Market Rent Reviews

3.3.1 The Landlord may at any time prior to the date which is twelve (12) months after each sate [sic] stated in **Item 5** of the **Reference Data** ("the Market Review Date") give written notice to the Tenant of the amount of rent the Landlord believes is the market rent for the Premises as at that Market Review Date.

3.3.2 If the Landlord does not give written notice in accordance with **cl. 3.3.1** in respect of a Market Review Date the rent payable for the Lease Year commencing from that Market Review Date will be the same rent as was payable in the preceding Lease Year.

3.3.3 If the Landlord gives written notice in accordance with **cl. 3.3.1**, the Tenant may give written notice to the Landlord within twenty-one (21) days of receipt of the Landlord's notice disputing the Landlord's assessment of the market rent.

3.3.4 If the Tenant does not give notice in accordance with **cl. 3.3.1** the amount set out in the Landlord's notice will be the Rent payable from the Market Review Date.

> 3.3.5 If the Tenant gives notice in accordance with **cl. 3.3.3** the market rent will be determined as follows: [a procedure for an Arbitrator's determination of market rent was set out].
>
> 3.4 Obligation to Pay Pending Determination
>
> Pending determination of the Rent for any Lease Year, rent will be paid at the rate payable during the Lease Year last concluded and will be adjusted retrospectively to the beginning of the Lease Year under review."

[9] Clause 17.1.4 of the lease provided for another instance of market rent adjustment: where a further lease was granted pursuant to the exercise of an option to renew, the rent for the first year of the new term was to be determined in accordance with cl 3.2.2 as if the first year of the new term were a continuation of the existing lease and "the date of commencement of the further term were a Market Review Date". Clause 20.1.2 provided that "[a]s soon as the rent payable from each rent review [was] determined", the lessee was to supplement its cash bond accordingly so that it amounted to a year's rent at the rate currently payable.

[10] The lessee had paid rent at the base rate, but had made no adjustments by reference to the CPI as contemplated in cl 3.2.1. The amount involved was $3,893.43, which at the time of trial the lessee had paid to its solicitor's trust account. The lessors relied on its failure to pay that amount as a breach of cl 3.1 of the lease. The trial judge considered that it would be "inappropriate" to find the lessee in breach on the basis that no actual payment had been made, when the funds were "destined" for the lessors. He also concluded that an increase in the rent after the first year of the lease required a calculation leading to a determination. The "determination" to which cl 3.4 referred must, his Honour considered, be a determination made by the lessors or at least acceptable to the lessors. No determination under cl 3.2.1 had been conveyed to the lessee; instead, the lessors had received payment of rental at the base rate over the three year term without complaint.

[11] Here, the lessors argued that the CPI adjustment provided for in cl 3.2.1(b) was simply a matter of calculation and required no determination. Clause 3.4 was directed solely to the market rent review provided for by cls 3.22, 3.3 and 17.1.4. The obligation to pay the CPI component was not subject to cl 3.4, but came into existence automatically. It was not met by retention of the funds representing the CPI component in the solicitor's account.

[12] There are certainly arguments both ways. Clauses 3.2.2 and 3.3 make reference to "determination" of rent in the context of market rent reviews; in contrast, cl 3.2.1, dealing with CPI adjustment, speaks only of calculation. On the other hand, Item 5 of the Reference Data, which is to provide the dates by reference to which market reviews may take place, contains only the words "market review date/s: n/a"; which rather suggests that market rent reviews were not in fact to be a feature of the arrangement. That lends some support to the view that the "determination" in cl 3.4 contemplated the CPI adjustment, because there was not much else to be determined about the rent. However, cl 17.1.4 was capable of operating to require a determination in the event of renewal, despite Item 5's lack of content, because it deemed the date of the commencement of the new term to be a market review date.

[13] I have, however, concluded that the trial judge's construction of cl 3.4 as applying, in its reference to a "determination", to the CPI adjustment under cl 3.2.1(b) was correct, for three reasons. The first is the positioning of cl 3.4 as a separate clause following

cls 3.2 and 3.3. There is nothing in its placement to suggest that its application is limited to only part of cl 3.2, so as to distinguish cl 3.2.1(b). Secondly, cl 3.4 is broadly expressed, not imposing any limit on the bases on which a different rent rate may be arrived at so as to require later adjustment. Thirdly, cl 20.1.2 speaks of "the rent payable from each rent review", which must be determined for the purposes of increasing the bond, and does not distinguish in that context between an annual review (involving the CPI adjustment) and market rent reviews. It makes sense that it does not do so, because the intent is evidently to reflect any increase in the rent, however arrived at, in the amount of the bond held; but importantly, it contemplates that the rent payable on either type of review is to be "determined". It is consistent with the approach implicit in cl 20.1.2 - that both annual and market reviews entail a determination - to regard cl 3.4 as contemplating retrospective adjustment of the rent after an alteration, whichever type of review has produced it; that adjustment to await determination of the amount payable.

[14] Consequently, the CPI adjustment provided for by cl 3.2.1(b) required determination before it became payable through a retrospective adjustment; although the lease did not identify on whom the burden of making the calculation was cast. Wherever it lay, neither party purported to have reached any determination of rent payable under that provision, so that cl 3.4 provided for payment of rent in the interim at the existing rate. The lessee's continued payment of rent at that rate was not in breach of the relevant covenant.

*The failure to find that the lessee was in breach by accumulating tyres on the premises*

[15] Clause 6.7.2 of the lease prohibited the "accumulation of useless property or rubbish", while cl 6.8 required the lessee to maintain the grounds "in good order and condition" and "neat and free from rubbish". An environmental health officer had inspected the premises a number of times. He deposed to seeing perhaps 100 tyres contained in a single bin, with a tarpaulin over the top. The trial judge noted his evidence and other evidence to the effect that it was normal in the wrecking trade to accumulate tyres until there were sufficient numbers to contract for their removal. In light of the health officer's evidence and the type of business to be conducted on the land, his Honour concluded that any accumulation of tyres over the period between November 2012 and May 2013 had not breached the lease.

[16] Here, the lessors submitted that photographic evidence showed an unacceptable accumulation of tyres on the premises. They pointed out that the environmental health officer had conceded in cross-examination that what was depicted in the photographs was a very large number of tyres, some of them uncovered, which was not consistent with what he had seen on his inspections.

[17] The difficulty with the reliance on the photographs, at trial and here, is the absence of evidence as to when they were taken. At trial, the lessors' counsel stated, without objection, that Mr Grepo had taken the photographs, but nothing was said as to when. The photographs themselves bear some writing on them which at best would be documentary hearsay, but in any event, does not establish that they were taken between November 2012 and May 2013. One sheet of photographs is headed "tyres after November 2012"; the other two sheets are headed "tyres May 2014". Other photographs were taken by a former employee of the lessee, Mr Hutchinson, but his affidavit made it clear that they dated from October 2013, outside the time period the trial judge was considering.

[18] There is nothing to show that the environmental health inspector's assessment of affairs within the relevant time period was inaccurate or that the trial judge was wrong in relying on it. Accordingly, I do not consider that any error has been shown in his Honour's finding that there was no breach of the lease in this regard.

*The failure to find that the lessee was in breach by permitting underletting*

[19] Clauses 9.1.2 and 9.1.3 of the lease respectively prohibited underletting the premises and sharing occupancy with any person without first obtaining the lessors' written consent. Clause 5.1 prohibited the use of the premises for any purpose other than that of "wrecking yard & scrap metal merchant". Clause 5.2 required compliance with statutes, which would include the *Residential Tenancies and Rooming Accommodation Act* 2008.

[20] When the lessee took the lease, the man it employed to manage its business, Mr Hutchinson, already occupied the cottage on the property. He had been paying rent of $200 per week to the lessors for the cottage and granny flat, although on two occasions when he was short of funds he assisted in their business in lieu of paying rent. After the lessee commenced business, Hutchinson remained in the cottage for about six months, paying rent to the lessee, before he was dismissed and two other employees of the lessee moved in. One lived in the cottage itself, while the other, a Mr Graham, occupied the granny flat attached to it. According to the affidavit of Mr Goldsmith, the sole director of the lessee company, the two employees acted as caretakers of the premises.

[21] In an affidavit sworn in May 2014, Mr Goldsmith deposed that he and his wife now lived in the cottage, while Mr Graham "boarded" with them, still living in the granny flat. Mr Graham contributed $100 per week, which Mr Goldsmith in evidence at trial explained went to outgoings such as electricity and water. Cross-examined, Mr Goldsmith agreed Mr Graham lived alone in the flat, cooked his own meals and had separate facilities. He accepted that Mr Graham was not a boarder but a tenant, and the permission of the lessors had not been sought for either Mr Hutchinson or Mr Graham to occupy the cottage or the granny flat. However, Hutchinson had rented the cottage from the lessors and continued to rent it from the lessee without any complaint from the lessors about his living there as caretaker. Mr Grepo, Mr Goldsmith said, knew the lessee would put tenants in the cottage and had said nothing about it. If the cottage were not used to house the lessee's employees, anyone could enter the property and ransack it.

[22] The lessors asserted that the lessee had underlet the granny flat to Mr Graham without consent. Permitting its workers to live in the granny flat was a residential use, not one which fell within the permitted use of the premises as a wrecking yard and for dealing in scrap metal. The lessee had also breached various provisions of the *Residential Tenancies and Rooming Accommodation Act* 2008, by failing to put the tenancy agreement in writing, failing to obtain a condition report at the end of the tenancy and failing to provide an information statement to the tenants.

[23] The trial judge noted in his judgment that the lessee was a company and was entitled to occupy the premises through its employees. The covenant in cl 9.1.3 against shared occupancy was directed to natural persons. Section 32 of the *Residential Tenancies and Rooming Accommodation Act* excluded the Act's application to residential agreements where the tenant was a boarder or lodger. The Act did not apply because there was a shared occupancy rather than a tenancy; Mr Graham contributed to outgoings rather than paying rent, and appeared to be a lodger.

[24] The lessor here did not seek to rely on any breach of cl 5.2 of the lease but confined itself to arguing that the trial judge should have found breaches of cl 5.1, as to the permitted use, and cl 9.1 and cl 9.2, as to underletting and sharing occupancy. But it was not, in fact, a part of the lessor's pleaded case that there was any breach of cl 5.1, nor does it appear to have been argued at trial. The relevance of cl 5.1 there was that the lessee argued that the permitted use under the lease encompassed occupation of the granny flat by an employee working in the business, so that no consent was necessary. It made the same argument here, contending that the nature of the business, the rural location of the premises, the lack of complaint about Mr Graham's presence, and the fact that Mr Hutchinson had previously occupied the premises while working for the lessors all indicated that Mr Graham's occupation of the flat as an employee of the lessee should be regarded as at least ancillary to the conduct of the permitted use. Alternatively, consent was implicit in Mr Hutchinson's continued occupation of the flat after he became the lessee's employee.

[25] Mr Goldsmith deposed that Mr Graham and another employee had acted as caretakers of the premises, although he did not elaborate on what activities they performed in that regard. Given the nature of a wrecking yard with the attendant problems of keeping various items lying about secure, one could conceivably characterise the employment of a caretaker as ancillary to the permitted use of the leased premises. But the position of an employee who was also a tenant, not merely an occupant of the premises for the purposes of caretaking, requires further consideration. The express requirement in cl 9.1 for consent to be obtained for underletting and shared occupancy does not suggest that cl 5.1 should be read liberally as contemplating a combined purpose of housing a caretaker and receiving income from the same individual as a tenant.

[26] Mr Graham had the exclusive possession and use of the flat, for which he paid $100 per week. From the fact that it was half of what Mr Hutchinson had paid for both cottage and flat, it may be assumed it reflected a commercial rent. However that payment was allocated, he was, as Mr Goldsmith conceded, a tenant. I do not think that the circumstance of Mr Hutchinson's having previously occupied the premises assisted at all. He plainly had been a tenant; he was not a regular employee of the lessors, although he twice worked for them in lieu of paying rent. His continued occupation was consistent with a continuing tenancy subsequently taken over by Mr Graham and another.

[27] In my view, the arrangement with Mr Graham could not properly be regarded as anything but an underletting which went beyond the permitted use of the premises, regardless of whether the lessee was a company. The failure to seek written consent for the underletting amounted to a breach of the covenant in cl 9.

*The failure to find a breach of the covenant to keep the premises clear of termites*

[28] Clause 5.10 of the lease required the tenant "at its own cost and expense [to] keep the Premises free and clear of rodents, termites, cockroaches, and other vermin". A pest inspector who conducted an inspection of the premises on 7 May 2013 reported that there were active termites in the wall framing timbers of the granny flat, while live termites were found in a tree stump, in trees, and in a stored timber pallet. He said that it was difficult to assess the age of the termite damage in the tree stump. It was likely that termites had been present in the buildings for years, but they were live and active on inspection. A builder had also inspected the property on behalf of the lessee in May 2010 and again at a later date; it was unclear whether it was June 2013 or early

2014. In his first report, he identified termite damage in a workshop and in pine trees and stumps around the yard. In the later report, he reported the same damage but added that there were possible termite penetrations between the ground and subfloor of the cottage, while trees and stumps in the yard were damaged by termite activity. He was not qualified, he agreed, to undertake testing for the presence of live termites.

[29] The trial judge noted that the pest control expert had not conducted his examination until 7 May 2013, close to the end of the first term of the lease. His Honour said that he was not prepared to infer from the expert's findings that the lessee should have known of the termite problem between November 2012 and May 2013 and that it had done nothing to address it. The obligation under cl 5.10, he said, should be construed "in a commercially realistic way" as an obligation to "address any evident termite problem"; it had not been breached. His Honour said he was conscious that a decision to which he had been referred, *Healy v Southern Milk Transport Pty Ltd*,[4] made it clear that breaches of covenant "however trivial" precluded an extension of a lease. The issue was, however, one of construction of a contractual obligation.

[30] Here, the lessee submitted that the clause could only be construed as meaning that the lessee was obliged to keep the premises "reasonably free" of termites and vermin. It was suggested that any different construction would lead to the result that if a single insect were found, the lessee would lose its right to a further term. The trial judge had referred to the dire consequence for the lessee of a trivial breach in this regard. To cast the obligation imposed by cl 5.10 as requiring a preventive program went beyond the language of the clause. His Honour had found as a matter of fact that the tenant had not acted unreasonably and this Court should not interfere with that finding.

[31] The lessors contended that whether the result of finding a breach might be harsh could not determine the construction of the provision:

> "The court has no power to remake or amend a contract for the purpose of avoiding a result which is considered to be inconvenient or unjust."[5]

I do not think, however, that the trial judge at any stage regarded the proportions or consequences of a suggested breach as having any bearing on the construction of the lessee's obligations under the lease. But with all respect to the primary judge I do not think cl 5.10 can properly be construed as limited to an obligation to deal with evident termite problems. To do so is neither consistent with the wording of the clause nor the obvious intent of keeping the property in good order. To wait until the damage was manifest could hardly promote the latter. In my view, the clause in order to have any effect must at least be read as requiring the lessee to take reasonable steps to keep the premises free of the various vermin identified, including termites. The lessee had admitted that it had undertaken no termite treatment or maintenance at all. The only available conclusion was that it had breached this covenant of the lease.

*The contentions as to the consequences of breach*

[32] The lessee here repeated arguments which it had made below in the event that any breach of covenant was found. The first was that the protective effect of s 128(4) endured for the entire term of the original lease, so that the lessors, not having given notice pursuant to the provision, could not rely on the lessee's breaches, whether before or after the date on which it gave notice of its desire to exercise the option.

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4 [1954] VLR 448.

5 *Australian Broadcasting Commission v Australasian Performing Right Association Limited* (1973) 129 CLR 99 at 109.

[33] Section 128(4) provides:

> "Where an act or omission that constituted a breach by a lessee of the lessee's obligations under a lease containing an option would, but for this section, have had the effect of precluding the lessee from exercising the option, the act or omission shall be deemed not to have had that effect where the lessee purports to exercise the option unless, during the period of 14 days next succeeding the purported exercise of the option, the lessor serves on the lessee prescribed notice of the act or omission and–
>
> (a) an order for relief against the effect of the breach in relation to the purported exercise of the option is not sought from the court before the expiration of the period of 1 month next succeeding service of the notice; or
>
> (b) where such relief is so sought–
>
> (i) the proceedings in which the relief is sought are disposed of, in so far as they relate to that relief, otherwise than by granting relief; or
>
> (ii) where relief is granted upon terms to be complied with by the lessee before compliance by the lessor with the order granting relief, the lessee fails to comply with those terms within the time stipulated by the court for the purpose."

[34] It may be seen that to attract the protective deeming effect of the section, the lessee must "purport to exercise the option" and to defeat that protection, the lessor must serve the prescribed notice within 14 days of "the purported exercise of the option". The lessee argued that the "purported exercise of the option" should be regarded as having occurred, not when notice of exercise was given, but at the expiration of the term of the lease, i.e. as at 13 May 2013. Thus s 128(4) would apply to any breaches found to have been committed before and during the period 5 November 2012 and 13 May 2013. No notice under that provision having been given by the lessors, the lessee should be regarded as having effectively exercised its option. Any breaches were relevant only to whether specific performance should be granted.

[35] Alternatively, the lessee argued, it was entitled to seek relief from forfeiture under s 124 of the *Property Law Act*, which renders any right of forfeiture for a breach of covenant unenforceable unless the lessor serves the prescribed notice, and gives the court a discretion to grant relief against forfeiture. The provision applies to leases, but s 123 of the *Property Law Act* defines "lease" as including "an agreement for a lease where the lessee has become entitled to have the lease granted". The lessee's argument was that at the point it gave notice of exercise of the option, an agreement for lease came into existence and, by definition, a lease. Strictly speaking, both arguments, which involve grounds not relied on for the decision below, should have been the subject of a notice of contention, but they were addressed by the lessors in their submissions and are, in my view, properly dealt with by this Court.

[36] The lessors' position was, firstly, that s 128 did not apply after the purported exercise of an option by the giving of notice. Secondly, there was no scope for the operation of s 124 in providing an avenue for relief against forfeiture in relation to the loss of an option to renew through failure to fulfil conditions precedent. The relevant option to renew was an irrevocable offer with conditions precedent to its acceptance: the giving of notice and compliance with obligations under the lease. Until they were met there was no entitlement to a lease so as to meet the definition in s 123.

[37] Both parties' submissions as to the consequences of breach turned on a series of New South Wales cases as to the effect of that State's equivalent of s 128(4) and whether on a lessee's giving of notice of exercise of an option, a lease arose capable of protection against forfeiture. The lessee relied on decisions of Young J in *Beca Developments Pty Ltd v Idameneo (No 92) Pty Ltd*[6] and *Lolly Pops (Harbourside) Pty Ltd v Werncog Pty Ltd*[7] and Hodgson J in *Nessmine Pty Ltd v Devuzo Pty Ltd*[8] as supporting its arguments. The lessors urged acceptance of the New South Wales Full Court's characterisation in *Gilbert J McCaul (Aust) Pty Ltd v Pitt Club Ltd*[9] of an option to renew as an irrevocable offer and relied on the reasoning of Windeyer J in *Flagstaff Investments Pty Ltd v Cross Street Investments Pty Ltd*[10] and Bryson J in *Rethmeier v Pioneer House Pty Ltd*.[11]

*The New South Wales decisions*

[38] Section 128(4) is the equivalent of an earlier form of s 133E of the *Conveyancing Act* 1919 (NSW), which was enacted in order to ameliorate the effects of the decision in *Gilbert J McCaul (Aust) Pty Ltd v Pitt Club Ltd*. In that case, the failure to comply with the conditions specified for exercise of an option to renew was held to have prevented its exercise. The option was exercisable on giving notice, punctual payment of rent and observance of covenants up until the expiration of the term. The court characterised it as an irrevocable offer which could only be accepted by performance of the prescribed conditions. A purported acceptance without their performance would not be an acceptance of the offer, but a counter-offer by the lessee requiring acceptance by the lessor before any agreement could result.[12]

[39] In *Beca Developments Pty Ltd v Idameneo (No 92) Pty Ltd*, relied on by the lessee, the salient parts of the option to renew were as follows:

> "If the Lessee shall desire to take a new lease of the premises for a further term … and prior to the expiration of the old term shall give to the Lessor not less than six (6) months notice of such desire and provided that at the time of expiration of the old term the Lessee shall not be in breach of … any covenant … the Lessor will … grant the Lessee a lease of the premises for a further term …"

There were breaches as at the expiry of the lease. Young J observed that one possible construction of the clause was that the date of exercise of the option (for the purposes of s 133E) was not when notice was of exercise was given, but the date when the new lease was to take effect. Support for that view was to be found, he said, in the English case of *West Country Cleaners (Falmouth) Ltd v Saly*.[13] On that view, there was a condition precedent at that date which was unfulfilled, but the protection of s 133E was then available.

[40] However, Young J did not consider that the option clause did contain a condition precedent. Instead, equitable rights came into existence when the notice of exercise of option was given, so that the lessee was entitled to a new lease with a condition that

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6 (1989) 4 BPR 9575.
7 (1998) NSW ConvR 55-861.
8 (1989) NSW ConvR 55-496.
9 (1957) 76 WN (NSW) 72.
10 (1999) 9 BPR 1700, and 17,067.
11 (1990) 6 BPR 13, 245.
12 At p. 123-4.
13 (1966) 1 WLR 1485; [1966] 3 All ER 210.

the right to it would be forfeited if there were breaches at the date of expiry of the existing term. That was an agreement for a lease which section 128 of the *Conveyancing Act* (the equivalent of the definition section in s 123 of the *Property Law Act*) deemed to be a lease, so that to seek forfeiture for breach, the landlord had to give notice under s 129 (the equivalent of s 124 of the *Property Law Act*).

[41] Young J rejected the lessors' argument that because of the breach of the relevant covenant, no entitlement to grant of the lease, and hence nothing which fell within the definition of a lease, had come into being. He referred to his earlier decision in *Hayes v Gunbola*,[14] in which he regarded two previously-taken approaches to construction of the definition section as commending themselves. The first was to read the word "entitled" in the definition provision as if the words "had there been no forfeiture" appeared immediately after it. The second was to regard a tenant who had at any time had a right to have a lease granted, but had lost it by later breach, as meeting the definition. On either view, the proper approach was to ask whether the lease, apart from the breach, would have been specifically enforceable, and, if so, apply s 129, the relief against forfeiture provision. No notice under that section having been given by the lessor, Young J granted the lessee specific performance.

[42] In *Nessmine Pty Ltd v Devuzo Pty Ltd*, Hodgson J considered whether the "purported exercise" of an option under s 133E(2) of the *Conveyancing Act* referred to the giving of the notice of exercise or the expiry date of the original lease. The lease (like the lease in the present case) referred to compliance with obligations up until the end of the term, which Hodgson J regarded as creating a condition precedent, unlike the option in *Beca*. However, he concluded that the purported exercise of the option should be regarded as occurring at the end of the term, when the condition precedent was met, so that if the lessor wished to rely on any breach, he would have to give notice within 14 days of the term's end, as s 133E(2) required. Hodgson J went on to say that if his construction of the clause were wrong (presumably, if it did not contain a condition precedent) he would take the approach of Young J in *Beca*, of regarding it as necessary that a notice under s 129 be given before the equitable right to a new lease could be forfeited.

[43] In a later decision, *Lolly Pops (Harbourside) Pty Ltd v Werncog Pty Ltd*, Young J seems to have regarded as conditions precedent requirements that the lessee, in order to exercise an option, not be in default in performance of covenants as at the date of the exercise of the option or at the expiry of the term. He did not suggest relief from forfeiture was available, but reiterated his view in *Beca* that if an option clause contained a condition precedent, the notice of exercise of option was to be regarded as operating at the end of the existing lease term, and it was then that the lessor must give a notice under s 133E. He observed that in an earlier case, *Brennan v Kinjella Pty Ltd*,[15] he had held that s 133E only applied to breaches up to the date of the lessee's notice. However, he may have overlooked the fact that in *Brennan v Kinjella*, the option clause specified the relevant time for disentitling breach as at the giving of the lessee's notice of exercise of the option, not, as in the case before him, both then and on the expiry of the lease.

[44] At any rate, his Honour expressed the view that the legislature's purpose in enacting s 133E was to end the consequences of the *Gilbert J McCaul* case, enabling justice to be done in each situation. His construction in *Beca*, and that in *Nessmine*, accorded with that intention, whereas the different approach of Bryson J in *Rethmeier v Pioneer House Pty Ltd* effectively permitted the remedial effect of the provision to be thwarted.

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14 (1988) NSW ConvR 55-375.

15 (1993) 6 BPR 13,168.

The lessor in the case before him not having given a s 133E notice, the breaches did not preclude the lessee from exercising its option; they merely went to whether specific performance should be granted.

[45] In *Rethmeier*, the option clause provided that a further lease would be given if the lessee gave the requisite notice three months before the end of the term, paid the rent and observed the covenants up to the expiration of the existing term. Those were, Bryson J considered, conditions precedent. No question of relief against forfeiture arose, and Young J's approach to the availability of that remedy was not relevant, because the relevant disentitling conduct was a failure to pay rent. The argument was whether the option could be said to be exercised before the conditions precedent had been met (i.e. before the end of the term); or whether the giving of the notice of exercise itself amounted to a purported exercise of the option within the meaning of s 133E. Bryson J preferred the latter approach, observing that it was almost invariably the practice that leases required the giving of a written notice as a condition of the exercise of an option for renewal, and the legislation recognised that practice in speaking of the "purported exercise" of an option. Consequently, s 133E(2) was relevant only to breaches up to the date of giving of the notice.

[46] The option clause in *Flagstaff Investments Pty Ltd v Cross Street Investments Pty Ltd* was identical in its form to that in *Rethmeier*. Windeyer J followed the decision in *Gilbert J McCaul*, regarding the option to renew as an irrevocable offer, with a condition precedent to its exercise being observance of the lease covenants. In the course of his judgment, Windeyer J reviewed the New South Wales Supreme Court decisions to which I have referred. He disagreed with Young J's view of the lease in *Beca*: on his construction, what came into existence in that case was an agreement to lease with, as a condition precedent to any right to a lease under the agreement, fulfilment of the covenants of the existing lease. If the condition precedent were not fulfilled, there was no lease within the meaning of s 129 (the relief against forfeiture provision), because the lessee became entitled to nothing, and there was nothing to be forfeited. The two approaches to the words "entitled to have his lease granted" which Young J had relied on were referable only to situations where the term of a lease had actually begun. Section 129 could not assist: it was directed to circumstances where a term which had commenced was determined by forfeiture and had nothing to say about breach of a condition precedent to entitlement to a lease.

[47] On the question of whether s133E applied after the giving of notice of exercise of the option, Windeyer J noted that in *Gilbert J McCaul*, the effects of which the provision was designed to correct, the breaches relied on had occurred prior to the giving of the notice. The Court had referred twice in its discussion to the "purported exercise of the option" by the giving of notice. His Honour mentioned a number of other decisions in which the expression "purported exercise of the option" referred to service of notice of intended exercise.

[48] Windeyer J agreed with Bryson J that in ordinary legal practice, sending a notice of desire for a new lease would be regarded as purporting to exercise an option. He considered it "a strange view of language"[16] to speak of a lessee purporting to exercise an option by observing the covenants of an existing lease. His view, he said, was supported by the language of s 133G of the *Conveyancing Act*, which deems the lease to continue in force after its expiry date for periods necessary to allow for the lessor to give notice and the lessee to seek relief. Yet on the reasoning in *Nessmine*, the lessor could give notice up to 14 days after the term ended, something not contemplated by

16 At 17,076.

s 133G, which did not permit renewal of a term already ended before notice was given. And if "purported exercise of the option" referred to both the giving of notice and performance of the covenants to the end of the term, since covenants usually included one to deliver up the premises in good repair, no tenant or landlord would know his or her position at the end of the existing lease term.

[49] Windeyer J concluded that s 133E did not apply to breaches of covenant after notice was given; a condition precedent to the entitlement to a new lease had not been fulfilled; and relief against forfeiture would not be granted in respect of the loss of a new term through non-fulfilment of a condition precedent.

[50] Young J had what appears to have been the last word in *Reilly v Liangis Investments Pty Ltd*.[17] In that case, his Honour found that there had been a breach during the term of the lease of the covenant to repair. Once again he referred to *Brennan v Kinjella*, saying that in that case he had decided that, where there was a notice to be given a set period before the end of the lease and there was an obligation to keep the premises in repair until the end of the term, s 133E applied only until the giving of the notice. (Again, that may overlook the fact that in *Brennan v Kinjella*, the relevant time for disentitlement was the giving of notice, not the end of the lease.) Young J noted the divergence in views between him and Hodgson J, on the one hand, and Windeyer J and Bryson J, on the other, as to the construction of s 133E, and endorsed Windeyer J's remark that the attention of the legislature was required. His own approach and that of Hodgson J, he considered, was more in accordance with both the remedial nature of the provision and an earlier observation of the Court of the Appeal[18] as to the provision's intent to remove the hiatus left by *Gilbert J McCaul*. However, even if the *Flagstaff* decision were correct, it was necessary to consider the particular option clause. In the case before him, renewal was subject to the lessee not being in breach at the expiration of the term (rather than up to it); at that date there was no obligation to repair, because the landlord had prevented access to the property; consequently, there was no breach, and the exercise of the option to renew was effective.

[51] The debate went no further: the New South Wales legislation was amended in 2001[19] to apply the protection of s 133E to breaches both before and after the giving of any notice exercising an option to renew.

*The proper construction of s 128*

[52] Section 128 has not been similarly amended. Its construction, however, does not seem to have attracted the same level of attention. In *Bentley v Chang Holdings Pty Ltd*, Philip McMurdo J noted that most of the cases (he mentioned the exception of *Nessmine*) had held that the exercise of an option for the purpose of s 128 occurred on the giving of notice of its exercise, so that s 128 had no effect thereafter. Because he did not find any post-notice breach, it was unnecessary for him to reach any conclusion on the point.

[53] In construing s 128, I would not adopt the approach of Young J and Hodgson J. Their reasoning seems, with respect, to entail a disregard of the actual words of the section; particularly the significance of the word "purported" in the phrase "purported exercise of the option". There is a distinction between the respective references in s 128 to "exercising the option", that is to say, exercising the entitlement which the section is

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17 (2000) 9 BPR 17,509.

18 In *Stellar Mining NL v Evanel Pty Ltd* (1983) NSW Conv R 55-118 at 56,867.

19 *Land Titles Legislation Amendment Act* 2001 (NSW) Schedule 1.

designed to preserve, and the "purported exercise" of an option: the expression of an intent to take up the entitlement which may or may not ultimately occur, depending on whether the preconditions are met. The latter is the event triggering both the protection of s 128 and the need for the lessor to give notice if he or she wishes to rely on a breach of covenant as precluding the first-identified event, the exercising of the option.

[54] And I am unable to see, also with respect, that *West Country Cleaners (Falmouth) Ltd v Saly*, relied on by Young J in *Beca*, does in fact support the proposition that an option is to be regarded as exercised when the new lease is to take effect. The case involved an option to renew which required giving notice 12 months before the lease's end, when the lessor would, if all covenants had been observed, grant a further term. The English Court of Appeal held that the material time for compliance with the covenants was the date of expiration of the lease. Because there were breaches at that point, the lessor was entitled to refuse a further lease. The case seems to me to say nothing about when a lessee exercises an option, let alone when a lessee "purports" to exercise an option.

[55] I regard the reasoning of Windeyer J and Bryson J as compelling. The Queensland provision is based on the New South Wales section; so Windeyer J's observations about the significance of the use of the expression "purported exercise" in *Gilbert J McCaul*, and the fact that the problem thrown up by that case related to pre-notice breaches, are apposite. And as in New South Wales, it seems probable that most practitioners in this State would regard the lessee's purported exercise of an option as the act of giving notice, not the combination of that act and the passage of the rest of the term without breach.

[56] Section 128(9) points away from the view that the purported exercise of an option conditional on an absence of breach at the end of the existing term takes place when the term ends. It deals with instances in which the lease expires shortly after the exercise of the option or soon after the serving of the lessor's notice under s128(4), and is clearly designed to cater for any hiatus:

> "(9) Subject to any order of the court and to subsections (10) and (11)–
>
> (a) where –
>
> (i) an option is contained in a lease; and
>
> (ii) the lessee exercises, or purports to exercise, the option; and
>
> (iii) the lease would, but for this paragraph, expire within the period of 14 days after the exercise, or purported exercise, of the option;
>
> the lease shall be deemed to continue in force until the expiration of that period; and
>
> (b) where –
>
> (i) a prescribed notice is duly served on a lessee; and
>
> (ii) the lease in respect of which the notice is served would, but for this paragraph, expire within the period of 1 month referred to in subsection (4)(a);
>
> the lease shall be deemed to continue in force until the expiration of that period; …"

Section 128(9)(a) does not appear to contemplate what would commonly be the case on the *Beca/Nessmine* approach, that the expiry of the lease and the exercise of the option would be precisely contemporaneous. In relation to s 128(9)(b), the anomaly which Windeyer J identified appears. On the *Beca/Nessmine* approach, the prescribed notice could be served up to 14 days after the existing lease had ended; but the sub-section does not provide for the revival of a lease which has already expired.

[57] The trial judge was, I consider, correct in his approach of regarding s 128 as inapplicable to breaches between the date of giving of notice and the expiry of the term.

*When does an option to renew become an agreement for lease?*

[58] There is a divergence in views as to the correct legal characterisation of an option. The first of the possible approaches is that taken in *Gilbert J McCaul*: an option is an irrevocable offer only capable of acceptance by fulfilling the conditions specified in it. The reasoning in *Gilbert J McCaul* was accepted as correct by the Appeal Division of the Supreme Court of Victoria in *B S Stillwell & Co Pty Ltd v Budget Rent-A-Car System Pty Ltd*[20] and by Stephen J in *Bowman v Durham Holdings Pty Ltd*[21], although that conclusion was not necessary to his judgment.

[59] In *Laybutt v Amoco Australia Pty Ltd*,[22] Gibbs J took a different tack, characterising an option to purchase exercisable upon giving notice and providing a deposit as a conditional contract giving the grantee the right, if he performed those conditions, to become the purchaser.[23] He took a similar view in *Quadling v Robinson*.[24] The different approaches were canvassed by the Full Court in this State in *Traywinds Pty Ltd v Cooper*.[25] Its preferred view seems to have been that an option to renew amounted to a conditional agreement to grant a lease for a further term, although it was not necessary to decide the point: the conclusion that the option had been effectively exercised would still have been reached on an acceptance of the *Gilbert J McCaul* approach.

[60] In *David Deane & Associates Pty Ltd v Bonnyview Pty Ltd*,[26] this Court adopted the Gibbs J approach in *Laybutt*. It held that a put option which obliged a prospective purchaser to acquire such lots as the owners might elect to put to it for purchase was a contract of sale, notwithstanding that the obligation to purchase was conditional on the put option's exercise. The put option gave the owners the right to become the vendors of the property upon fulfilment of that condition. Reference was made to Wilson J's observation in *Perri v Coolangatta Investments Pty Ltd*,[27] that where an obligation to complete a contract was conditioned upon the fulfilment of a condition, there was, in the meantime, a conditional contract from which neither party was at liberty to withdraw at will, having undertaken interim obligations.

[61] In *Beca*, Young J effectively found that a conditional contract was created, not on the giving of the option, but on the giving of notice of its exercise. He did so by construing the option clause in that case as creating, not a condition precedent, but a condition subsequent (that the right to a new lease would be forfeited if there were a breach of covenant as at the date of the existing term's expiry), so that *Gilbert J McCaul* was distinguishable.

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20 (1990) VR 589.
21 (1973) 131 CLR 8.
22 (1974) 132 CLR 57.
23 At 76.
24 (1976) 137 CLR 192 at 200.
25 (1989) 1 Qd R 222.
26 [2005] QCA 270.
27 (1982) 149 CLR 537 at 556-557.

[62] In *Bentley v Chang*, Philip McMurdo J referred to the argument that once notice was given, an agreement for lease protected by s 124 was created, mentioning Young J's decisions and also two single judge decisions in this State: *Eighteenth Ashlaw Nominees Pty Ltd v Vadelly Pty Ltd*[28] and *Jack Butler & Staff Pty Ltd v Black*.[29] (Again, because he found no breach, it was unnecessary for him to reach any conclusion.) In *Ashlaw*, the breach was a continuing one which both pre-dated and post-dated the giving of notice of desire for a new lease (which Williams J described as a "purported exercise" of the option to renew). Counsel for the lessor expressed himself prepared to proceed on the basis that as at the date of giving of the notice there was a valid exercise of the option and thereafter an agreement between the parties for a lease for the further term. His argument was that the lessee was in breach of an essential covenant of the renewed agreement, in respect of which notice to remedy had been given. Williams J proceeded to consider the matter on that basis, concluding that the breach had not been remedied and the lessee should not be granted specific performance of the agreement for lease. I do not think that much can be drawn from that case, given the agreed premise on which it proceeded.

[63] *Ashlaw* was referred to in *Jack Butler & Staff Pty Ltd*, in which the applicant lessee was seeking a declaration that he had validly exercised an option to renew and an injunction requiring the lessor to provide a lease. Unfortunately, it is not clear from the available report what the terms of the option were, although it is plain that the lessor was relying on breaches before and after the exercise of the option to resist renewal. The lessee submitted, wrongly in my view, that Williams J's judgment supported the proposition that the lessor had to give notice under s 124 in order to forfeit the lease. Mackenzie J expressed the view that the lessor could not rely on a breach of a condition precedent if he had failed to give notice under s 128 and would have to proceed under s 124. Because the application was one for summary judgement and there were some evidentiary issues as to whether a s 128 notice had in fact been given by the lessor, judgment was not granted. Given the circumstances in which the (ex tempore) judgment was given, and the fact that it pre-dated Windeyer J's decision in *Flagstaff*, I do not think the dicta concerning s 124 and s 128 are persuasive.

[64] For the purposes of this case, it is unnecessary for me to decide between the irrevocable offer and conditional contract approaches. I have concluded that, whatever view one takes of the character of an option to renew, in the present case the terms of cl 17, and the fact that there were breaches of covenants in this lease up to and at the date of its expiry, meant that the lessor was not obliged to grant a new lease. On the Gibbs J approach, the cl 17 option was an agreement to grant a further lease conditional on the lessee's performance of the conditions set out in the clause. Absent the performance of those conditions, no entitlement to a further term arose. The option could be called an agreement for a lease but it could not be characterized as an agreement for a lease with the lessee then being entitled to the lease so as to meet the definition in s 123, and make available relief from forfeiture under s 124.

[65] Applying the irrevocable offer analysis, I do not think that cl 17 lends itself to a similar construction to that of the clause in *Beca*. Clause 17 contained conditions precedent to acceptance of the offer: that notice be given at least six months before the existing lease's end, which was met, and that it comply with the lease's covenants up until that time, which was not met, so that the offer was not accepted. I note that in *Tenstat*

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28 Unreported, Williams J, Supreme Court of Queensland, No 4864 of 1986, 25 November 1987.

29 (1991) ANZ ConvR 186 per Mackenzie J.

*Pty Ltd v Permanent Trustee Aust Ltd*,[30] McLelland J similarly construed an option with the same conditions as those in cl 17.

[66] Even if that were not so, and the offer were accepted on the lessee's giving notice of exercise of the option, with the requirement to fulfil the obligations in the lease as a condition subsequent, I would not regard s 124 as having any application. The next step in Young J's reasoning in *Beca* was to say that the conditional contract was an agreement to grant a lease to which the lessee was entitled, triggering the relief from forfeiture provision. That was the step too far, in Windeyer J's view. I agree with his analysis for the purposes of this case. If there were a conditional contract at the point when notice of exercise of the option was given, it was an agreement which gave the lessee the right if it performed the stipulated conditions to enter a new lease. It was not an agreement for a lease which the lessee was entitled to have granted while the requirement that it not be in breach of covenant at the end of the lease remained unfulfilled. There was, consequently, no agreement for lease within the terms of the definition in s 123, and s 124 was not enlivened.

*Conclusion*

[67] I conclude, then, that the lessee was not entitled to exercise the option because of its breaches of covenants after the giving of notice of exercise, to which s 128 did not apply. No agreement for a lease to which the lessee was entitled came into existence, so that s 124 did not apply to allow relief against forfeiture. The lease ended on 13 May 2013; thereafter the lessee remained, while the lessors consented, on a monthly tenancy under the holding over clause in the lease. The lessors are entitled to possession.

[68] I would allow the appeal, set aside the judgment below and order that there be judgment for the appellants for recovery of possession of premises at 1 Ray Road Mareeba described as Lot 874 on CP NR 4546, County of Nares, Parish of Tinaroo, Title Reference 20945056. The respondent should pay the appellants' costs of the appeal and the proceeding at first instance.

[69] **MORRISON JA:** I have had the advantage of reading the draft reasons of Holmes JA, with which I agree, except for one aspect, dealt with below. There is also one matter upon which I wish to add some observations of my own.

**The lessee's breach by failure to pay rent.**

[70] Clause 3.1 obliged the lessee to pay to the landlord "in each Lease Year the Rent without any formal or other demand...", in advance on the first day of each month. Item 4 of the Schedule:

- set the initial year's rent at $41,600, exclusive of GST;
- specified that was a calendar monthly amount of $3,466.67; and
- set the commencement date of the rent, 14 May 2010.

[71] Clause 3.2 provided a mechanism for calculating the rent for the second and third years of the lease.

> "The expression "Rent" means an annual sum calculated as follows:

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30 (1992) 28 NSWLR 625.

(a) for the first (1st) Lease Year:

the sum specified in **Item 4(b)(i)** of the **Reference Data**;

(b) for the second (2nd) and each subsequent Lease Year:

subject to **cl. 3.2.2** the higher of:

(i) that amount derived annually by multiplying the Rent for the Lease Year last concluded by a fraction obtained by dividing the Index Number for the last quarter immediately preceding the first day of the Lease Year under review by the Index Number for the last quarter immediately preceding the first day of the Lease Year last concluded; and

(ii) the Rent reserved and payable during the Lease Year last concluded."

[72] The term "Index Number" was defined in clause 2.1.7 as meaning the Consumer Price Index (All Groups) (**CPI**) for the city of Brisbane, as published by the Australian Bureau of Statistics (ABS). Clause 2.1.7 also provided for an alternative index to be nominated by the Bureau if the CPI was modified or discontinued. Further, if the Bureau did not nominate an alternative, then the term "Index Number" was defined to mean:

> "… an index or method of measuring increases in the cost of living agreed in writing by the parties and in default of agreement within a period of fourteen (14) days, an index or method determined … by the President or Acting President of the Australian Institute of Valuers & Land Economists…".

[73] When the lease was prepared for execution the parties omitted the requirement for market reviews. Thus Item 5 in the Schedule, "Market Review Date/s", had "N/A" inserted against it.

[74] The effect of deleting market reviews meant that the standard form clauses 3.2.2 (Reviews to Market) and 3.2.3 (Market Rent Reviews) became redundant, except for their operation in the event of the option being exercised and clause 17.1.4 applying. However the same could not necessarily be said of clause 3.4, which provided:

> "Pending determination of the Rent for any Lease Year, rent will be paid at the rate payable during the Lease Year last concluded and will be adjusted retrospectively to the beginning of the Lease Year under review."

[75] Clause 2.1.12 defined the term "Lease Year" to mean "each separate year of the term of this Lease". Thus because clause 3.4 was referrable to "any Lease Year" it applied to years beyond those that might be designated as market review years.

[76] The lessee paid the base rent but did not make any adjustments in accordance with the changes in the CPI. The difference was accepted to be $3,893.43. The lessee had paid that sum into its solicitor's trust account at the time of the trial, pending resolution of the issues between the parties.

[77] The lessee contended, and the trial judge accepted, that the reference to the "determination" in clause 3.4 required a determination of the rent to be made by the lessor, or a determination acceptable to the lessor. It was held that as no determination had been given to the lessee for its consideration, there could be no complaint about the failure to pay the true rent, and therefore no breach by failing to pay rent.

[78] The lessor's contention was that clause 3.4 was directed simply to market review provisions such as in clauses 3.2, 3.3 and 17.1.4 (dealing with the calculation of the initial rent on the lease option being exercised).

[79] In my view the trial judge's approach to the construction of clause 3.4 was in error. To that extent I am respectfully unable to agree with the reasons of Holmes JA in paragraphs [13] and [14] of her Honour's reasons. My reasons for reaching the different conclusion are below.

[80] Clause 3.2.1 defines the rent for each year to be a sum "calculated" in accordance with the formula in that clause. For the first year the rent is calculated as the amount in Item 4 of the Schedule. For the second and subsequent years, the rent is "calculated" by the formula in clause 3.2.1(b). That requires a simple application of three objectively known factors, namely:

- the rent for the year just concluded; that is the sum already agreed in Item 4;
- the Brisbane CPI for the quarter ended March 2011;[31] that is a figure published by the Bureau;
- the Brisbane CPI for the quarter ended March 2010;[32] that also is a figure published by the Bureau, and known well before the start of the second lease year, on 14 May 2011.

[81] Clause 3.2.1 requires that the last year's rent be multiplied by the fraction obtained by dividing the March 2010 CPI by the March 2011 CPI. Then the higher of that figure or the first year's rent is the new rent figure.

[82] No determination in the sense for which the lessee contends, and the trial judge found, is required for the first year or the second year. It is not a case where the lessor has to propose anything, as all the relevant factors are known or objectively set and ascertainable. There is nothing to debate if the correct CPI figures are used.

[83] It is true that clause 3.4 uses the term "determined" and not "calculated", but in my view that cannot be construed as creating a different regime for rent determination, when the parties agreed how the new rent was to be worked out in clause 3.2.1. There are three reasons for that.

[84] First, that gives to the term "determination" in clause 3.4 a meaning closely derived from clauses 3.2.2 and 3.3, when the operation of those clauses was limited to determining rent on the exercise of the option to renew, because market reviews were expressly excluded.

[85] Secondly, it could hardly be the presumed intention of two rational, commercially minded parties, that having agreed a precise formula for rent changes from year to year, and having excluded market reviews, they should be taken to have agreed to a different method, ill-defined and abandoning any objective criteria.

[86] Thirdly, clause 20.1.2 provides that the cash bond under the lease will be increased as soon as "the rent payable from each rent review is determined..". Given that the parties expressly excluded market reviews, that clause must be read as applying to

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31 Under clause 3.2.1(b)(i), the last quarter immediately preceding the first day of the lease year under review, i.e. the one commencing 14 May 2011.

32 Under clause 3.2.1(b)(i), the last quarter immediately preceding the first day of the lease year last concluded, i.e. 14 May 2010 to 14 May 2011.

the annual changes in the rent as a result of the recalculation under clause 3.2.1. Once that calculation has been done the new rent has been determined for the purposes of clause 20.1.2 and the bond will be modified accordingly.

[87] In my view clause 3.4 has rational work to do in the lease. First, there is no reason to conclude that when rent has been "calculated" under clause 3.2.1(b) it will not also have been "determined". The CPI figures for any quarter are not published in advance of that quarter ending, and often lag the end of a quarter by some weeks. Further, the definition of "Index Number" expressly contemplates the situation where the CPI figure will not be known, and must be determined by an arbitrator. If the figure for the end of the March quarter has not been published by 14 May (when one lease year ends and the next commences) then until the figure is known and the rent is "determined" because the calculation can finally be done, the old rent is payable.

[88] Secondly, it operates when clause 17.1.4 is triggered. However that does not compel a contrary view to the one I have expressed.

[89] Clause 17.1.4 provides:

> "17.1.4 the rent for the first year of the further term will be determined in accordance with **cl. 3.2.2** as if that year were a continuation of the term of this Lease and the date of commencement of the further term were a Market Review Date;"

[90] The reference to a "Market Review Date" means that the date of commencement of the new lease is deemed to be a "Market Review Date" for the purposes of clause 3.2.2. That then allows the rent for the first year of the new lease to be determined under clause 3.3. That applies only to the first year of the new lease on the exercise of the option.

[91] However clause 3.4 applies, on its face, to "any Lease Year", which under clause 2.1.12 means any separate year of the lease term.

[92] For the reasons set out above I have, with respect, reached a contrary conclusion to that of Holmes JA on this aspect. However the difference of opinion does not affect the outcome of the appeal. The true rent was not paid in accordance with clause 3.1, and the lessee was in breach of its obligations for that reason as well as those identified by Holmes JA.

**Construction of s 128(4) *Property Law Act* 1974 (Qld).**

[93] I agree with the analysis of Holmes JA on this aspect, and wish to add the following.

[94] Section 128(4) applies in relation to past acts and omissions which constitute breaches. So much is signified by the words in the first few lines, engaging only "an act or omission **that constituted** a breach…", and one which "**would … have had** the effect of precluding" exercise of the option.[33]

[95] The only time the section is triggered is when the lessee "purports to exercise the option". It is only in respect of that event that the requirement is made for notice to be given if the lessor wishes to rely upon the past breach to deny "the purported exercise of the option".

[96] In the lease in question here, the lessee had two conditions to fulfil in order to be able to exercise the option. The first was to give notice at a certain time before the expiry of the term; the second was that it had to punctually comply with its obligations under the lease at all times up to the expiry of the term.

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[33] Emphasis added.

[97] At the time the notice was given the lessee was in breach of some of its obligations, at least in respect of its obligation to keep the property clear of termites, and underletting the premises. Those breaches continued after the notice and up to the expiry of the term. No notice was given by the lessor under s 128 consequent on the lessee's giving its notice of exercise of the option.

[98] As the decisions in *Beca Developments Pty Ltd v Idameneo (No 92) Pty Ltd*,[34] *Lolly Pops (Harbourside) Pty Ltd v Werncog Pty Ltd*,[35] *Reilly v Liangis Investments Pty Ltd*,[36] and *Nessmine Pty Ltd v Devuzo Pty Ltd*[37] show, there are many leases which contain variants of the requirements found in this lease, obliging the lessee to do more than merely give a notice in order to validly exercise an option.

[99] On the approach taken in those cases:

- the purported exercise of the option only occurs at the expiry of the lease term, when notice has been given and due observance of all the terms has occurred;
- the "purported exercise of the option" for the purposes of s 128 only occurs on the expiry of the term, notwithstanding that the lessee was obliged to take a particular step at an earlier time (giving notice), without which there could not be a valid exercise of option;
- the only time that a s 128 notice is called upon to be given is at the expiry of the term;
- where the extra conditions are conditions subsequent to the notice of exercise of option, the giving of the notice by the lessee creates equitable rights, entitling a new lease but subject to forfeiture;
- where the extra conditions are conditions precedent to the exercise of the option, the purported exercise of the option takes place on expiry of the term.

[100] I share the reservations of Holmes JA expressed in paragraphs [53]-[56] in respect of adopting that approach.

[101] Construing the text of the provision in context, and accepting that the origin of such provisions was to overcome the effect of the decision in *Gilbert J McCaul (Aust) Pty Ltd v Pitt Club Ltd*,[38] meaning must be given to the phrases "where the lessee purports to exercise the option" and "the purported exercise of the option".[39] On the approach in the *Beca* line of cases the section is treated as if the first use of that phrase was deleted, and the use of the word "purported" was deleted otherwise.

[102] Further, the fact that the legislation may be remedial does not lead to construing those words out of the section. In this respect I respectfully disagree with the conclusion of Young J in *Reilly*,[40] that a wide reading of the sections is warranted by the comments of the Court of Appeal in in *Stellar Mining NL v Evanel Pty Ltd*,[41] and by Wootten J at

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34 (1989) 4 BPR 9575; NSW Conv R 55-459. (***Beca***)

35 (1998) NSW Conv R 55-861.

36 [2000] NSWSC 47. (***Reilly***)

37 (1989) NSW Conv R 55-496.

38 (1957) 59 SR (NSW) 122; New South Wales Law Reform Commission, Report LRC 5; Queensland Law Reform Commission, Report 16, paragraph 128.

39 *Alphapharm Pty Ltd v H Lundbeck A/S* [2014] HCA 42; *Lacey v Attorney-General for the State of Queensland* (2011) 242 CLR 573, [2011] HCA 10 at [43]; *Project Blue Sky Inc v Australian Broadcasting Commission* (1998) 194 CLR 355 at [69]-[71].

40 *Reilly* at [40]-[41].

41 (1983) NSW Conv R 55-118 at 56,867. (***Stellar***)

first instance in the same case.[42] The comments there were directed at the breadth of the discretion under s 133F(3) of the *Conveyancing Act* 1919 (NSW), the equivalent of s 128(7) of the Queensland Act.[43]

[103] Further, in leases of the kind here, where there are two steps in the process of exercising the option, that approach has some results which seem unlikely to have been in contemplation when the section was enacted.

[104] First, it means that the very same acts will be relied upon by the lessee and lessor for opposite purposes; by the lessee to establish part of the purported exercise of option, and by the lessor to establish the breaches denying the exercise of the option.

[105] Secondly, where there is a relevant breach prior to the giving of the notice, notice in respect of that breach is not required to be given within 14 days under s 128, even though it may be a once only breach.

[106] Thirdly, in that event, since on that approach the time has not yet arrived for the purported exercise of option, the failure to give the s 128 notice could not be said to be any form of waiver or found an estoppel. The consequence is that the lessee would not be informed until sometime within 14 days after the expiry of the term if there is to be asserted a breach affecting the notice. Thus the chance to give a second, effectual, notice within time is denied.

[107] It may be accepted that certain equitable rights are created upon the giving of the notice by the lessee. However, the nature and scope of those rights depends on the proper construction of the clause under which they are said to arise. The extent to which equity might lend relief could be quite limited, and is likely to be so where the lessee still has obligations which must be precisely performed as a condition of exercising the option.

**Conclusion**

[108] I agree with the orders proposed by Holmes JA, except in that in addition I would order that the respondent pay the appellant $3,893.43 (including GST) for arrears of rent.

[109] **DOUGLAS J:** I agree with the reasons of Holmes JA and the orders proposed by her Honour. I also agree with Morrison JA's remarks on the construction of s 128(4) of the *Property Law Act* 1974 (Qld). These additional remarks are intended to explain why I agree with Holmes JA and not with Morrison JA in respect of whether the lessee had failed to pay rent in breach of the lease.

[110] The dictionary definitions of "determination" in this context contemplate an action leading to a result. For example, the online edition of the *Oxford English Dictionary* definitions include:

> "6a The action of definitely ascertaining the position, nature, amount, etc. (*of* anything). …
>
> b The result ascertained by this action; that which has been determined by investigation or calculation; a conclusion, a solution."

Similarly, the online edition of the *Macquarie Dictionary* refers to "a result ascertained; a solution … the fixing or settling of amount, limit, character, etc. …".

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42 *Evanel Pty Ltd v Stellar Mining NL* [1982] 1 NSWLR 380. (***Evanel***)

43 Wootten J in *Evanel* at 388-390; Court of Appeal in *Stellar* at 56,867.

[111] Those meanings are consistent with the derivation or calculation of the sum by the application of cl 3.2.1(b) of the lease to arrive at the result of a rental figure for the second and each subsequent lease year. The definition of "Index Number" in the lease, however, covers more possibilities than the comparison of one consumer price index figure for Brisbane with an earlier such figure. In the absence of such an index the definition provides eventually for the setting of an appropriate figure by a third party. The full definition is:

> "2.1.7 'Index Number' means the Consumer Price Index (All Groups) for the city of Brisbane as published by the Australian Bureau of Statistics. If that index is suspended, discontinued, or modified so that it does not reflect on a consistent basis changes which have occurred in the cost of living in the city of Brisbane during any Lease Year, the expression will mean an index which in the opinion of the Australian Statistician (whether published or advised at the request of either party) does reflect on a consistent basis changes which have occurred in the cost of living in the City of Brisbane during any Lease Year. If the Australian Statistician has not published and will not advise an appropriate index, the expression will mean an index or method of measuring increases in the cost of living agreed in writing by the parties and in default of agreement within a period of fourteen (14) days, an index or method determined at the request of either party by the President or Acting President of the Australian Institute of Valuers & Land Economists (Qld Division) or their nominee."

[112] In any case some person will need to calculate or derive a result from a mathematical process or the application of an appropriate index or method provided by a third party at some stage after the figures become available. The date that will happen is not one that can be derived with certainty from the terms of the lease.

[113] My view is, then, that some further action is required to identify to the parties the result of the determination that has been made pursuant to cl 3.4 to trigger the retrospective adjustment to the rental payable pursuant to that provision of the lease. One would expect, as the learned trial judge observed, that there must at least, in the end, "be a determination by the lessor, or a determination acceptable to the lessor, …".[44]

[114] While the calculation or derivation of the amount of the rental payable for the second and each subsequent lease year should be able to be ascertained with certainty once the relevant Index Numbers become available, the obligation to pay any increase retrospectively should not arise, and the sum of the retrospective payment not be made certain, until a determination is made pursuant to cl 3.4. The date of that determination will fix the amount of any retrospective payment that should then be made by the tenant.

[115] In the absence of such a determination made by either landlord or tenant, it is inappropriate to conclude that the tenant breached its obligation to pay the rental payable under the lease during its term, even though, by the time of the trial, the amount of the retrospective rental payable was known with certainty.

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[44] *Grepo & Anor v Jam-Cal Bundaberg Pty Ltd* [2014] QSC 119 at [22].