

VICTORIAN CIVIL AND ADMINISTRATIVE TRIBUNAL

CIVIL DIVISION

BUILDING AND PROPERTY LIST

VCAT REFERENCE NO. R200/2012

CATCHWORDS

Retail Tenancies List; Retail lease of premises for gymnasium and fitness academy; Whether Landlord gave Tenant written offer of first right of refusal to lease Shop 1 pursuant to clause 22.1 of Lease. Whether Tenant refused or deemed to have refused offer. Declaration granted in favour of Landlord.

APPLICANT	24 Hour Fitness Pty Ltd (ACN 080 352 334)
RESPONDENT	W & B Investment Group Pty Ltd (ACN 127 810 691)
WHERE HELD	Melbourne
BEFORE	Judge Jenkins, Vice President
HEARING TYPE	Preliminary Hearing
DATE OF HEARING	27 November 2014
DATE OF ORDERS	27 November 2014
DATE OF WRITTEN REASONS	16 December 2014
CITATION	24 Hour Fitness Pty Ltd v W & B Investment Group Pty Ltd (Building and Property) [2014] VCAT 1616

ORDER

- 1 Declaration: The Tribunal declares that the Respondent made a written offer to the Applicant for the lease of that part of the premises known as Shop 1 on the Ground Floor of the building known as 276 Russell Street, Melbourne, in accordance with Clause 22.1 of the Lease.

Note

On 27 November 2014, the Tribunal made Orders including the above Declaration with oral reasons.

The Applicant subsequently sought written reasons which are now provided.

Judge Jenkins
Vice President

APPEARANCES:

For Applicant

Mr C. Northrop of Counsel, instructed by
Goldsmiths Lawyers

For Respondent

Mr J. Searle of Counsel, instructed by
Macpherson and Kelley Lawyers

TABLE OF CONTENTS

ORDER.....	1
APPEARANCES:.....	2
TABLE OF CONTENTS	3
REASONS	4
NATURE OF APPLICATION.....	4
BACKGROUND	4
Initial Re Leasing of Shop 1 and the First Floor	7
Additional Provision Clause 22.1 of the Lease	7
CURRENT DISPUTE.....	7
Respondent’s offer to Applicant to lease Shop 1.	7
ANALYSIS AND FINDINGS	13
Applicant’s Objections to affidavit of Andy Ng	13
Applicant’s Objections to Respondent’s Letter of Offer.....	13
Respondent’s Position	14
Clause 22.1	14
What comprises a valid offer?.....	14
What is the effect of the Respondent specifying the rental in the letter of offer?.....	15
What is the effect of the Respondent specifying terms and conditions in the letter of offer?	16
Circumstances in which Offer is made.....	16
Relevance of Different Terms and Conditions available to a third party tenant.	16
Sequence of Events.....	17
Did the Applicant Refuse the Offer.....	18
CONCLUSION	19

REASONS

NATURE OF APPLICATION

- 2 The Applicant is the tenant and the Respondent is the landlord of premises situated at 276 Russell Street, Melbourne.
- 3 The proceeding is listed for hearing on 2 March 2015 for five days, limited to a damages claim by the Applicant, with the Respondent's counterclaim for possession to be heard on a date to be fixed.
- 4 On 22 October 2013, the Tribunal made Orders, which included the following:

The Respondent is restrained from offering to enter into or entering into a lease with any prospective tenant for either Shop 1 on the Ground Floor and/or the First Floor of the building known as 276 Russell Street Melbourne, without first giving the Applicant a right of refusal by making a written offer to the Applicant for the lease of that part of the premises, in accordance with Clause 22.1 of the Lease.
- 5 The Respondent makes an interim application for a declaration to the effect that it has now made such a written offer to the Applicant, in accordance with Clause 22.1 of the Lease, in relation to Shop 1. The ramifications of such declaration is that the Respondent is at liberty to enter into a lease with a third party.

BACKGROUND

- 6 It is instructive to briefly set out the existing commercial relationship between the parties.
- 7 By a lease date 27 September 2007 (the 'Lease'), Rido (Australia) Pty Ltd (the 'Previous Landlord') leased to the Applicant, the Basement, Shop 2 on Ground Level, Second Floor and Third Floor of 276 Russell Street, Melbourne (the 'Premises').
- 8 The Lease was for a term of five years, commencing on 1 October 2007 and contained two options for renewal of five years each.
- 9 The permitted use is the retail provision of physical training and education; and the business operates under the name Australian Institute of Fitness.
- 10 The Premises was vacant at the start of the Lease. The Applicant renovated part of the premises to make them suitable for a training business by, amongst other things, plastering walls and replacing carpet, paid for by the previous Landlord. Work included modifications in two bathrooms on the Third Floor, which took place before the business started in early 2008.
- 11 At the commencement of the Lease, there was a tenant in Shop 1 on the Ground Floor; and a tenant on the First Floor. The Applicant wanted to have the opportunity to take a lease of those parts of the building if they became vacant. Accordingly, a special condition was negotiated between

the Applicant and the Previous Landlord, which became incorporated into the Lease as Additional Provision 22.1.

- 12 At the commencement of the Lease, the Applicant did not require all of the areas within the Premises for training purposes. As the business grew, parts of the Premises were made suitable for students and classes. Initially the Basement was not used for classes.
- 13 The Respondent became the registered proprietor of the Premises on 3 June 2008.
- 14 The Applicant alleges that, as a consequence of the Respondent's failure or refusal to repair pipes and drains, the Basement flooded with sewerage, causing damage to all flooring and walls and rendering the Basement entirely unusable.
- 15 Repairs to the plumbing were undertaken by the Applicant so as to make the Premises usable and also to fit out the Basement to enable it to be used for its training purposes. The Applicant alleges that no work of a structural nature was undertaken and, on the advice of its architect, a permit was not required to do the repair work.
- 16 Pursuant to an order dated 30 October 2012 made in this proceeding by His Honour Judge Macnamara, the Lease was renewed for a further period of five years commencing 1 October 2012, on the same terms and conditions as the original Lease.
- 17 Following an application for an injunction before the Tribunal on 19 December 2012, orders by consent were made which included the following order:
 1. Upon the Applicant giving the usual undertaking as to damages, until the hearing and determination of this proceeding or further order, the Respondent is restrained from offering to enter into or entering into a lease with any prospective tenant for either Shop one on the Ground Floor and/or the First Floor of the building known as 276 Russell Street Melbourne without first offering to the Applicant the lease of that part of the premises.
- 18 By Notice of Breach of the Lease dated 15 April 2013, served pursuant to s 146 of the *Property Law Act 1958*, the Respondent alleged that the Applicant was in breach of clause 22.8 of the Lease, for failing to submit to the Respondent, for review and approval, all plans and permits and designs in respect of any proposed fit out to be undertaken on the Premises.
- 19 On 24 April 2013, the Applicant applied to the Tribunal for an interim injunction to restrain the Respondent from relying or acting upon its Notice of Breach of Lease, following which orders were made by consent to set aside and declare void the Notice; with costs ordered in favour of the Applicant.
- 20 By further Notice of Breach of the Lease dated 21 May 2013, served pursuant to s 146 of the *Property Law Act*, the Respondent alleged breaches

of the Lease, principally by the Applicant undertaking building works in the Basement without the knowledge or consent of the Respondent and without requisite Council permits.

- 21 Between the date of the latest Notice and the date of hearing which commenced on 12 August 2013, there was a further exchange of correspondence between the parties; urgent Directions Hearings convened by the Tribunal on 2 and 9 August; filing of expert reports by the Respondent;¹ but no filing of an expert report for the Applicant, which was intended to address the damages allegedly sustained by the Applicant.
- 22 The proceeding was set down for hearing on 12 August 2013. At the commencement of the hearing, it became apparent that the expert report filed by the Respondent included an email from the Melbourne City Council dated 25 June 2013, which had not been previously discovered by the Respondent. The email refers to an inspection on 6 June 2013 at the Premises in response to a complaint made by the Respondent, in relation to alleged unauthorised building works. The email documents certain observations made at such inspection and notes that an annual Essential Safety Measures report was not provided during the inspection, as required pursuant to the *Building Regulations 2006*. The email further advises that:
- A building notice will be issued and it is your responsibility as the owner to respond within the designated time period stated in the building notice.
- 23 Counsel for the Respondent confirmed that a Building Notice had not yet been received. Subsequent enquiries by the Respondent's solicitor elicited advice from the Council to the effect that such Notice 'was imminent'. In view of the fact that a Building Notice issued by the City of Melbourne may reflect directly upon matters in dispute between the parties, the Tribunal determined that all matters in dispute between the parties relating to the building works be deferred until such Notice had been issued and after the parties had time to consider their response to it.²
- 24 Accordingly, the hearing was limited to determining two issues:
- (a) The apparent impasse over the mechanism for rent review, which eventually resolved by consent; and
 - (b) The interpretation and application of the Additional Provision Clause 22.1, which gives a right of first refusal to the Applicant in respect of Shop 1 and the First Floor, upon becoming vacant and available for lease.

¹ Building Inspection Report of TGVK Pty Ltd dated 15 July 2013; and report dated 7 August 2013 of the Lorenzini Group.

² It is noted that during the course of the hearing the Respondent did not produce any electrical services maintenance report beyond the one appearing at TB 1021-1024.

Initial Re Leasing of Shop 1 and the First Floor

- 25 By Commercial Lease dated 5 October 2009,³ the Respondent as lessor leased Shop 1 Ground Floor at 276 Russell Street, Melbourne to Peuta World Pty Ltd for five years commencing 2 November 2009. This premises is currently vacant.
- 26 By Commercial Lease dated 21 January 2009,⁴ the Respondent as lessor leased the First Floor at 276 Russell Street, Melbourne to Mr Ting Liang for two years commencing 15 March 2009.
- 27 The issue before the Tribunal at the previous hearing on 12 August 2013 was the interpretation and application of the Additional Provision Clause 22.1 and whether the Respondent had indeed given the Applicant a written right of first refusal in respect of either Shop 1 or the First Floor, upon each becoming vacant and available for lease and prior to entering into leases of those premises to third parties.
- 28 On the previous occasions the Tribunal found that the Respondent had indeed failed to comply with clause 22.1 on either of the previous occasions when Shop 1 and the First Floor became vacant and were again offered for lease.
- 29 The question of compliance with Clause 22.1 now arises upon application by the Respondent.

Additional Provision Clause 22.1 of the Lease

- 30 Clause 22.1 of the Lease states as follows:⁵

Subject to those areas becoming vacant, the Tenant shall have the right of first refusal to lease the premises known as Shop 1 on the Ground Floor of the building in which the premises are situated (“the said building”), as well as the first floor of the said building, should they become available at any time after the commencement date of this lease, subject to satisfactory terms and conditions being agreed upon between the landlord and the tenant and a rental to be determined which shall be the market rental for such premises. The landlord will not offer the above-mentioned premises to anyone else without first of all making an offer in writing to the Tenant.

CURRENT DISPUTE

Respondent’s offer to Applicant to lease Shop 1.

- 31 By letter dated 26 August 2014, addressed to the Directors of the Applicant, the Respondents solicitors advised the Applicant as follows:

We act for W&B Investment Group Pty Ltd ... The registered proprietor of Shop 1, 276 Russell Street, Melbourne (“Premises”).

³ Exhibit F, TB 902 and following.

⁴ Exhibit E, TB 876 and following.

⁵ TB 194.

We refer to a lease between our client (“Landlord”) and 24 Hour Fitness Pty Ltd dated 27 September 2007 and renewed 1 October 2012 for the Basement, Shop 2 on Ground Level, second floor and third floor, 276 Russell Street Melbourne (“ Current Lease”).

Pursuant to Additional Provision 22.1 of the Current Lease, we are instructed to offer to lease the Premises to 24 Hour Fitness Pty Ltd on the following terms (“ Offer to Lease”).

Rent: \$138,000 plus GST plus outgoings for the Term

Term: one (1) year less one (1) day.

Option to renew: Nil

Security Deposit: the equivalent to six (6) rent plus GST)

Guarantee: Guarantee provided by the Lessees Directors

Rent Free Period: not applicable

Make Good: Reinstatement to same condition as at commencement date. Painting and recarpeting if required by the Landlord

In respect of the offer above, we are instructed that:

1. the offer of Rent above is in accordance with the estimated rental offer that our client would accept from a prospective tenant;
2. the length of the term is a result of, inter-alia, the Landlord preserving the right to develop the Premises Or Utilise the Premises for its own use following the expiration of the Term; and
3. in accordance with a recent review of the Landlords existing leases, the Landlord currently requires security deposits equivalent to six (6) months rental in addition to directors guarantees on its leases moving forward.

We advise that our clients Offer to Lease, in accordance with Additional Provision 22.1 of the Current Lease is open for acceptance for a period of seven (7) days from the date of this letter.

Accordingly, should 24 Hour Fitness Pty Ltd fail to accept our client’s Offer to Lease on the terms specified above by 5 pm on 2 September 2014 (or earlier if refused in writing by 24 Hour Fitness Pty Ltd) the Landlord will have deemed that 24 Hour Fitness Pty Ltd has forfeited its rights contained in Additional Provision 22.1 of the Current Lease.

Should you have any queries in respect of the above, please do not hesitate in contacting the undersigned.

- 32 No response was made by the Applicant to the above letter.
- 33 By letter dated 3 October 2014, the Respondent’s solicitors advised the Applicant’s solicitors as follows:

We confirm an offer to lease Shop one was made to your client by a letter dated 26 August 2014 in accordance with Additional Provision 22.1 of the Lease. Enclosed is a copy of the letter of offer dated 26 August 2014.

We are instructed your client has to date not responded to the offer and in the absence of a response to the offer, your client is now deemed to have rejected the offer. In the circumstances, we consider our client is entitled to lease Shop 1 to another party.

We have advised our client accordingly and expect it will now proceed to lease Shop 1. Please confirm within seven days that you will take no steps to allege our client is in breach of the lease or the orders made on 22 August 2013 as a result of it leasing shop 1.

Furthermore, please confirm within 7 days that you will provide any necessary consent to vary Order 1 of the further orders made 22 August 2013 to release our client from any injunction in so far as it relates to Shop 1.

- 34 No response was made by the Applicant to the above letter. In the meantime Mr Andy Ng, the Respondent's estate agent, who on instructions from the Respondent had advertised Shop 1 for lease, received a commercial lease application from a prospective tenant dated 14 October 2014. This application proposed an annual rental of \$138,000 plus GST⁶ to operate a Japanese restaurant for an initial five-year term with two further terms of five years each; subject to council approval and a request for three months rent free for renovation.⁷
- 35 By email dated 15 October 2014, Mr Ng advised the Respondent of the offer made by the prospective tenant together with further recommendations as to additional terms.⁸
- 36 By letter dated 22 October 2014, so far as it is relevant to the current application, the Respondent's solicitors advised the Applicant's solicitors as follows:

Offer to Lease

We refer to our letter dated 3 October 2014.

Having received no response, we confirm our client will be proceeding to lease Shop 1.

- 37 By letter dated 27 October 2014 the Applicant's solicitors advised the Respondent's solicitors as follows:

We refer to your letter dated 3 October 2014 and do not agree that your client is entitled to lease Shop 1. The relevant lease terms is set out in paragraph 22.1 of the Lease and reproduced conveniently on paragraph 25 of the Judgement you forwarded to our office. At no time has your client offered to lease the shop to our client at the

⁶ Being the rent level which had been advertised.

⁷ Exhibit AN2 to affidavit of Andy Ng sworn 26 November 2014.

⁸ Exhibit AN24 to affidavit of Andy Ng sworn 26 November 2014.

market rental. It is pointed out that our client offered to have the market rental independently determined by the same value appointed to fix the rental of the premises, upon the rental review. Until market rental is determined, our client is not in a position to respond. Our client would expect the term of the offer to lease to be five years as provided by the Act.

Our client therefore declines to consent to the variation of the Order.

- 38 By letter dated 28 October 2014, Mr Ng advised the prospective tenant that his offer had been approved as to the following terms and sought certain specified information and payment of a deposit:⁹

Rent: \$138,000 first year plus GST

Bond: \$23,000 (2 months)

Outgoings: all paid by the tenant approx. \$12,500 a year

Use of premises: Restaurant

Annual adjustment: 4%

Initial term: five (5) years

Optional terms: One (1) further term of five years (5+5 in total)

Commencing date: access to the property once all documents are finalised or on 28.11.2014

Rental commencing: 1 March 2015

Other Issues: 1. Three (3) months free rental from 01.12.2014 to 28.02.2015 are for the tenant to apply permits and renovation

2. The landlord and tenant covenanted one with the other that if the planning permit rejected by the council within the rent free period, the tenant will compensate the landlord with one month in rental equal to \$12,650 for landlord's costs and to put the property back on the market for lease.

- 39 By letter dated 31 October 2014, the Respondent's solicitors advised the Applicant's solicitors as follows:

We refer to your letter dated 27 October 2014.

We are instructed the offer to lease was based on market rental.

Given your client has not engaged a valuer to independently assess the rental, we do not consider there is a proper basis for your assertion that our client has not offered to lease Shop 1 at market rental.

Further we are instructed your client has neither offered to have the market rental independently determined as suggested in your letter nor has your client responded to the offer made within the time stipulated.

⁹⁹ The prospective tenant paid the deposit on 21 November 2014: Para 13 of Mr Ng's affidavit and Exhibit AN-7.

Despite several correspondences to you, the first response our client has received in relation to the offer is your letter dated 27 October 2014, being two months after the offer was made.

If your client was genuinely keen in leasing Shop 1, it would have commenced negotiations with our client within the stipulated time frame. We consider the latest correspondence to be nothing more than a delay tactic.

We reiterate your client is now deemed to have rejected the offer and our client is entitled to lease Shop 1 to another party.

We are instructed our client is in negotiations with a potential tenant. We put you on notice if your client delays the signing of a new lease, our client will be seeking approximately 11,000 to 12,000 per month in rental opportunity costs against your client and a copy of this letter will be produced on the question of costs.

- 40 By email dated 17 November 2014 1.31 am Andy Ng licensed estate agent advised the prospective tenant, on behalf of the Respondent, as follows:

We would like to confirm your lease application for the above captioned property has been approved. In order to secure the property, please bank in a deposit of \$12,650 (one month) to our trust account, details provided in the Application Form and below. We would like to confirm the terms below and at the same time we would like you to provide us with further information as follows:

Rent: \$138,000 first year plus GST

Bond: \$23,000 (2 months)

Outgoings: all paid by the tenant approx. \$12,500 a year

Use of premises: Restaurant

Annual adjustment: 4%

Initial term: five (5) years

Optional terms: One (1) further term of five years (5+5 in total)

Commencing date: access to the property once all documents are finalised or on 01.12.2014

Other Issues: 1. Three (3) months free rental from 01.12.2014 to 28.02.2015 are for the tenant to apply permits and renovation

2. The landlord and tenant covenanted one with the other that if the planning permit rejected by the council within the rent free period, the tenant will compensate the landlord with one month in rental equal to \$12,650 for landlord's costs and to put the property back on the market for lease.

You also need to confirm you want me to prepare the lease.

- 41 By letter dated 24 November 2014 to the Respondent's Solicitors, the Applicant's Solicitors advised as follows:

We refer to the offer your client has received to rent Shop 1. It is our client's contention that Shop 1 has to be offered to our client at the market rental. To that end, our client has always been willing to pay what they believe to be the market rental for the property. For the sake of clarity, our client believes that upon a proper assessment of value, by an independent valuer, he would value rental consistent with the rental currently being paid for Shop 2 (as adjusted for size).

Notwithstanding our clients lease, our client is prepared to vary the existing lease to include Shop 1, with the rental to increase by \$100,000 per annum plus GST.

Alternatively our client would be prepared to enter a new lease of Shop 1 in the email dated 17 November 2014 @ 1.31 am (including the rent free period) for a rent of \$100,000 per annum plus GST.

42 By affidavit of Andy Ng sworn 26 November 2014, Mr Ng attests in part to the following:

- (a) He is the principal licensed estate agent of Exceland Camberwell which is involved exclusively in the leasing of commercial real estate in and around Melbourne;
- (b) Approximately 4 to 5 months ago the Respondent instructed him to ascertain the availability of prospective tenants and the likely market rental which could be obtained for Shop 1;
- (c) He already had one prospective tenant interested in leasing Shop 1 for \$128,000 per annum plus outgoings, however he considered that a prospective tenant may well pay more;
- (d) He placed advertising signs inside the window of Shop 1 and also placed advertisements in a real estate newspaper and online in which Shop 1 was offered for lease at \$138,000 per annum excluding GST; and
- (e) By email dated 15 October 2014, Mr Ng advised the Respondent of proposed rental terms which a prospective tenant had agreed, including an annual rental of \$138,000 plus GST.

43 In the affidavit of Robert Hornsey, Solicitor for the Applicant, dated 18 November 2014, he attests in part as follows:

- (a) The rental determination dated 1 October 2012 in respect of those parts of the building occupied by the Applicant was done to fix the rent for the renewed lease;
- (b) Prior to such rental determination the Applicant's solicitor requested of the Respondent's solicitor that a market rental also be determined for Shop 1 as part of the rental determination. However, such request was declined; and
- (c) If the rental for Shop 1 was calculated on a pro rata basis by reference to the rental determination and the area of Shop 1, the rental would be

\$65,770.63 exclusive of outgoings and on this basis the rent which the Respondent seeks of \$138,000 is well above market rent.

ANALYSIS AND FINDINGS

Applicant's Objections to Affidavit of Andy Ng

- 44 The Tribunal acknowledges the objections made by Applicant's Counsel to the affidavit of Andy Ng, in particular, paragraphs 16, 17 and 18, on the basis that:
- (a) Mr Ng has not disclosed his qualifications or the basis of his expertise to give valuations of market rental;
 - (b) Mr Ng asserts that the proposed tenant is independent; and
 - (c) Mr Ng asserts that the Respondent would be liable to legal proceedings by the proposed tenant if it were prevented from renting Shop 1 to such party.
- 45 During the hearing I indicated that these objections were either well founded or would properly be the subject of cross-examination. However, I am now satisfied that for the purpose of this interim application, the impugned paragraphs have no bearing upon my determination. The value of Mr Ng's affidavit otherwise lies in the recitation of the historical sequence of events and the circumstances and timing in which a third party prospective tenant made an offer to lease Shop 1.

Applicant's Objections to Respondent's Letter of Offer

- 46 In summary, Applicant's Counsel raised the following objections to the Respondent's written offer:
- (a) The Respondent did not make any reference to the proposed rent being market rental, let alone market rental as determined;
 - (b) The Respondent purported to prescribe terms and conditions without any indication that it would negotiate;
 - (c) The offer was expressed in 'take it or leave it' terms which is contrary to Clause 22.1;
 - (d) It was not incumbent upon the Applicant to indicate a rejection or acceptance of the offer until it knew what was the market rental, as determined;
 - (e) Clause 22.1 contemplated that the Applicant would be offered terms and conditions commensurate with the existing lease of the premises between the parties. Accordingly, the option of first right of refusal was to enable the Applicant the opportunity to extend its existing operations if the additional space became available;
 - (f) Within the terms of the Respondent's initial offer, when the Applicant did not respond, the offer lapsed. It was then incumbent upon the

Respondent to first offer to the Applicant the lease on the terms and conditions which it has in fact now offered to a third party, before it had made such offer to the third party; and

- (g) The offer was not genuine as evidenced by the significantly different offer subsequently made and accepted by a third party.

47 In my view, the construction of Clause 22.1 given on behalf of the Applicant is unnecessarily and unreasonably narrow and not consistent with an existing commercial relationship where parties are seeking certainty in a timely manner. I will address these issues in more detail below.

Respondent's Position

48 Respondent's Counsel submitted that the Applicant must be taken to have refused an offer made pursuant to Clause 22.1.

49 The Respondent made a written offer giving the Applicant a first right of refusal to lease Shop 1, which the Applicant elected not to respond to at all for eight weeks. Significantly, the Applicant continued such failure to respond, despite the Respondent giving a clear indication in its second and third letters as to what it proposed to do. When the Applicant did respond it effectively stated that it was not in a position to respond. In the context of a continuing commercial relationship, and where the Applicant is clearly upon notice that the Respondent proposes to lease to a third party, the Applicant must be deemed to have refused an offer made to it. Clause 22.1 cannot be interpreted so as to allow the Applicant to remain silent for two months and then complain about the form of the offer. For reasons more fully set out below, I agree.

Clause 22.1

50 It is common ground that Clause 22.1 is an additional provision inserted into the Lease for the benefit of the Applicant, in anticipation of it requiring more space for its existing business as a fitness and training centre. That is, it was not contemplated that the Applicant would be seeking a lease of either Shop 1 or the First Floor to operate an entirely different business. Accordingly, the term for a lease of Shop 1 would necessarily have to coincide with the term for the remainder of the building occupied by the Applicant.

51 If either Shop 1 on the ground floor or the First Floor became available for lease then the Applicant must be given in writing a first right of refusal before the Respondent is at liberty to offer to lease either of these areas to a third party.

What comprises a valid offer?

52 In my view, the obligation placed upon the Respondent would be satisfied in the first instance by simply making an offer in writing to the Applicant to lease Shop 1. There is only one term prescribed by Clause 22.1, namely that

the rent shall be market rental as determined or implicitly as otherwise agreed between the parties. Hence the parties may always agree upon a rental without further action being taken. If either party requires market rental to be determined then Clause 11 of the Lease provides for the appropriate procedure. Clause 22.1 provides further that the lease will be subject to satisfactory terms and conditions being agreed upon between the landlord and the tenant.

- 53 Clause 22.1 may be contrasted with Clause 22.2, which deals with a proposed sale of the building by the landlord. In the latter case, the Respondent must give the Applicant a notice in writing giving the Applicant the right of first refusal to purchase the building at the price and upon the conditions which the Respondent is prepared to sell the building to any purchaser. That is, there is no mechanism to determine the sale price for the purpose of Clause 22.2 as there is for determining market rental for the purpose of Clause 22.1.
- 54 Applicant's Counsel relied upon the distinction between Clauses 22.1 and 22.2 in submitting that, for the purpose of Clause 22.1, the Respondent was not at liberty to prescribe a rental in the offer to lease which was not the market rental as determined. In my view, this is not quite correct as indicated below.

What is the effect of the Respondent specifying the rental in the letter of offer?

- 55 The offer made by the Respondent was expressed to be made 'pursuant to Clause 22.1.' In my view this was sufficient to invoke the operation of that Clause, which carried with it further obligations on the part of both parties.
- 56 There is no prohibition upon the Respondent proposing either a rental at the outset and/or other lease terms and conditions. Indeed, there is no logical reason why this should be the case. In this particular instance, surrounding events as subsequently disclosed to the Applicant provides the evidence upon which the Respondent relied to advance the proposed rental as the current market rental. However, the Applicant was not bound to accept any figure proposed by the Respondent, although it was entitled to do so. Furthermore, the Respondent was not bound to accept a counterproposal by the Applicant, although it was also entitled to do so.
- 57 Having proposed a rental figure, the Applicant could merely accept such figure or require that the market rental be determined in accordance with the Lease. If the Applicant proposed another figure, the Respondent could accept that figure or require the market rental to be determined in accordance with the Lease.
- 58 In this instance, if indeed the Respondent had acted upon its 'take it or leave it' rental offer then it would not have been acting in accordance with the terms of Clause 22.1. However, the Respondent was never placed in this position and we shall never know whether that was the Respondent's real intention.

What is the effect of the Respondent specifying terms and conditions in the letter of offer?

- 59 Having determined market rental or otherwise agreed upon a rental, the parties must then agree satisfactory terms and conditions.
- 60 In this instance, if indeed the Respondent had acted upon its 'take it or leave it' terms and conditions, without any attempt to negotiate satisfactory terms and conditions, then it would not have been acting in accordance with the terms of Clause 22.1. However, the Respondent was never placed in this position and we shall never know whether that was the Respondent's real intention.

Circumstances in which Offer is made

- 61 In the current proceeding the Respondent alleges it is entitled to possession of the leased premises. In particular, the Respondent alleges that the Lease has been terminated by reason of breaches by the Applicant. In this context, Respondent's Counsel submitted and I accept that the Respondent's offer of first right of refusal must have regard to the current litigation and the prospect of either the Respondent or the Applicant being successful.
- 62 Respondent's Counsel justified the term offered of one year less one day on the basis that if the Respondent were successful in the main proceeding, then it would not make sense for the lease of Shop 1 to be other than short term. Equally, if the Respondent were unsuccessful then both parties would wish to coincide the new term for the lease of Shop 1 with the balance of the term for the premises currently occupied by the Applicant. In this context, the term of any lease relating to Shop 1 would have to be the subject of negotiation between the parties, having regard to the current stage of the litigation between them.

Relevance of Different Terms and Conditions available to a third party tenant

- 63 Having offered a lease of Shop 1 to the Applicant, then it would be expected that the Respondent would be immediately negotiating with other parties if the Applicant refused the offer.
- 64 If the Applicant refuses an offer made by the Respondent, there is no obligation placed upon the Respondent under Clause 22.1 to only enter into a lease with a third party at the same rental and upon the same terms and conditions as initially offered to the Applicant. Furthermore, there is no obligation upon the Respondent to revisit its offer to the Applicant and give a further right of refusal to the Applicant upon the terms and conditions subsequently negotiated with a third party.
- 65 The only relevant question is whether the Respondent has discharged its obligation under Clause 22.1 and whether the Applicant has declined its offer either expressly or by its conduct. If the answer to both questions is yes, the Respondent is then at liberty to enter into a lease of Shop 1 on

terms and conditions relevant to the third party. Clearly there is no correlation between the Applicant and any other prospective tenant in terms of what may be acceptable terms and conditions between such third party and the Respondent.

Sequence of Events

- 66 The offer made by the Respondent was expressed to be ‘pursuant to Clause 22.1’ but was otherwise an offer to rent Shop 1 at \$138,000 per annum on specified terms and conditions which, if the Applicant did not accept within seven days, shall be deemed to have rejected the offer.
- 67 The rental for Shop 1 contained in the Respondent’s offer to the Applicant was based upon the rental which its estate agent had recommended as the applicable market rental, being the figure also used in advertisements offering Shop 1 for lease. This was the same figure which a third party subsequently offered to rent Shop 1. As already indicated, while the rental of \$138,000 per annum plus GST is not the market rental as determined in accordance with the Lease, there is at least a reasonable basis upon which the Respondent could advance such figure, in the first instance, as the current market rental.
- 68 Prior to the offer being made to the Applicant, the Respondent had not made any offer to a third party to lease Shop 1 and it had not accepted any proposal made by a third party. Clearly, it had made enquiries through its agent and publically advertised Shop 1 to the market, but in my view these preliminary steps are not inconsistent with its obligations under Clause 22.1.
- 69 The Applicant gave no response and therefore no indication that it was either interested or not in a lease, or if interested, whether it wished to negotiate upon terms and conditions. After a delay of about five weeks the second letter of the Respondent’s solicitors [initially sent by email] clearly outlined what action the Respondent proposed to take to lease Shop 1 to a third party. The letter further sought confirmation from the Applicant’s solicitors that they would not contest that the Respondent was no longer restrained from offering a lease to a third party.
- 70 The third letter of the Respondent’s solicitors, nearly two months after the first letter, confirms that the Respondent will be proceeding to lease Shop 1. The Applicant’s solicitor first responded by letter dated 27 October, purportedly in response to the Respondent’s solicitors letter of 3 October, disputing the Respondent’s entitlement to lease Shop 1 to a third party and disputing that the proposed rent was in fact market rent. Furthermore, the response indicates to the effect that the Applicant is not in a position to respond to the Respondent’s offer until such time as the market rental has been determined. However, there is still no indication as to whether the Applicant was interested to lease Shop 1 at market rental, upon terms and conditions to be negotiated.

- 71 The Applicant's solicitor's letter of 27 October also makes reference to the Applicant's request to have the market value of the rental for Shop 1 determined at the time when the market rental was being assessed for the renewed lease. Respondent's Counsel submitted that this request was declined at the time because Shop 1 was not then being offered for lease and a market rental has to be assessed at the relevant time.
- 72 Finally, by letter dated 24 November, nearly three months after the Respondent's solicitors' letter of offer, the Applicant's solicitors state to the effect that... 'Shop 1 has to be offered to our client at the market rental. To that end, our client has always been willing to pay what they believe to be the market rental...' The letter then proposes that the Applicant would be prepared to lease Shop 1 for an additional \$100,000 per annum plus GST and otherwise on the terms and conditions set out in the email to the prospective tenant dated 17 November 2014.
- 73 Prior to its letter of 24 November 2014, being nearly three months after the Respondent's offer, the Applicant had not indicated whether or not it would rent Shop 1 at market rental to be determined or agreed, upon satisfactory terms and conditions, to be negotiated.
- 74 Although it is not entirely clear, Applicant's Counsel submitted that the rental figure of \$100,000 proposed by the Applicant is calculated by reference to the existing rent paid for the leased premises, adjusted for the area occupied by Shop 1 and with an added premium of about 50%. This figure of \$100,000 does not qualify as the market rental, as determined in accordance with the Lease, any more than the figure first proposed by the Respondent.

Did the Applicant Refuse the Offer

- 75 In my view, the position now apparently maintained by the Applicant is untenable.
- 76 Although it is not entirely clear, the Applicant appears to have taken the position that the Respondent's offer did not constitute a written offer of first refusal and therefore the Applicant was entitled to ignore the letter containing such purported offer at least until more information was forthcoming.
- 77 Accordingly, it is necessary to consider whether the Applicant was under any obligation to reply to the Respondent's offer in a timely manner by indicating either that:
- (a) It was not interested in leasing Shop 1; or
 - (b) It would be interested in leasing Shop 1, but only at market rental and upon terms and conditions to be negotiated, as provided for in clause 22.1.
- 78 As indicated above, I am satisfied that:

- (a) The Respondent did make a written offer pursuant to Clause 22.1, notwithstanding that it could not insist upon a rental other than a market rental as determined and it would have been obliged to negotiate in good faith other satisfactory terms and conditions with the Applicant;
- (b) It was not incumbent upon the Respondent to make any offer to the Applicant of terms and conditions that it may have been prepared to accept from a different party;
- (c) There is no obligation placed upon the Respondent to only enter into a lease with a third party on the same terms and conditions as an offer made to the Applicant. Clause 22.2 is irrelevant to the current circumstances; and
- (d) In light of the current proceeding in which the Respondent is seeking to repossess the premises currently occupied by the Applicant, any negotiations for the lease of Shop 1 to the Applicant would have had to take into account the possibility that the Respondent or the Applicant might be successful.

- 79 During the course of the hearing, Applicant's Counsel was asked on a number of occasions whether the Applicant treated the letter of 27 August as not an offer made pursuant to Clause 22.1 and therefore the Applicant was simply entitled to ignore it. I am not confident that Counsel gave a clear response to this question. In any event, having received an offer in purported compliance with Clause 22.1, it was incumbent upon the Applicant to respond within a timely manner. The Respondent also gave a clear and reasonable notice of its intention to lease to a third party.
- 80 The Respondent was entitled to treat the Applicant's failure or refusal to respond to the Respondent's offer within a reasonable time, as a deemed refusal by conduct.

CONCLUSION

- 81 The Respondent has made a written offer in compliance with Clause 22.1 which amounted to a first right of refusal, notwithstanding that upon the face of the offer it purports to propose a rental price and terms on a 'take it or leave it' basis. It was incumbent upon the Applicant, within a reasonable time, to either:
- (a) Object that the offer did not comply and therefore did not constitute a written offer of a first right of refusal; or
 - (b) Indicate it was not interested in renting Shop 1; or
 - (c) Indicate that it may be interested in renting Shop 1, subject to market rental being determined and satisfactory terms and conditions being negotiated.

- 82 The Applicant elected not to respond at all for two months, which in the context of parties in an existing commercial relationship, is not a response made within a reasonable time. In these circumstances, where the Respondent made further attempts to elicit a response, it was reasonable for the Respondent to treat the conduct of the Applicant as amounting to a rejection of its offer to lease.
- 83 It is not relevant that the Respondent may have been negotiating with other parties, as long as it had not made an offer to or accepted an offer from a third party, prior to making an offer to the Applicant, which offer had been refused. It is also not relevant that the terms and conditions ultimately negotiated with a third party were not first offered to the Applicant.
- 84 If the Respondent had insisted that the Applicant could only accept the terms as set out in the letter of 26 August, then the Respondent would not have complied with Clause 22.1 and the Applicant could have validly objected that it had not been given a valid first right of refusal. However, the Respondent was never given the opportunity to fulfil its obligations under Clause 22.1.
- 85 The Declaration sought by the Respondent is granted.

Judge Jenkins, Vice President