VICTORIAN CIVIL AND ADMINISTRATIVE TRIBUNAL

CIVIL DIVISION

BUILDING AND PROPERTY LIST VCAT REFERENCE NO BP863/2016

CATCHWORDS

RETAIL TENANCY DISPUTE – Whether landlord failed to supply an air-conditioning system to service the premises; repair of air-conditioning; whether failure to repair air-conditioning system constitutes a repudiation of the Lease – Repudiation – reasonable person test – Damages – whether accrued rights survive termination of the lease. Costs – whether costs otherwise recoverable under the lease are prohibited under s 92 of the *Retail Leases Act 2003.*

APPLICANT	S 3 Sth Melb Pty Ltd (ACN 609 947 408)
RESPONDENT	Red Pepper Property Group Pty Ltd (ACN 167 218 662)
SECOND RESPONDENT BY COUNTERCLAIM	Paul Anthony Norris-Ongso
WHERE HELD	Melbourne
BEFORE	Deputy President E. Riegler
HEARING TYPE	Hearing
DATE OF HEARING	6 and 7 December 2017, 30 and 31 May 2018, 27 June 2018
DATE OF ORDER	25 October 2018
CITATION	S 3 Sth Melb Pty Ltd v Red Pepper Property Group Pty Ltd (Building and Property) [2018] VCAT 1684

ORDER

1. The Applicant and the Second Respondent by Counterclaim must pay the Respondent $506.30.
2. Liberty to apply on the question of costs, subject to such liberty being exercised within 14 days of the date of this order.

DEPUTY PRESIDENT E. RIEGLER

APPEARANCES:

For the Applicant	Mr A Flower, solicitor
For the Respondent	Mr Deller of counsel
For the Respondent by Counterclaim	Mr A Flower, solicitor

REASONS

INTRODUCTION

1. The Applicant (**'the Tenant'**) was the tenant of retail premises located in Bank Street, South Melbourne (**'the Premises'**). The Respondent is the registered owner of the Premises (**'the Landlord'**). The Tenant occupied the Premises pursuant to a written lease executed on 26 February 2016 (**'the Lease'**). Under the terms of the Lease, the Tenant was permitted to use the Premises to conduct its *Pilates and Barre Studio* business.

2. Prior to the Tenant commencing its business, the Landlord was to undertake certain preliminary works, following which the Tenant would undertake its fit-out works. Save for the matters in dispute, the Landlord's and Tenant's preliminary works were completed in or around May or June 2016. In June 2016, the Tenant commenced operation of its *Pilates and Barre Studio*.

3. Disputes arose between the parties, which ultimately led to the Tenant commencing this proceeding on 26 October 2016. Those disputes were unable to be resolved, with the result that the Tenant purported to terminate the Lease by letter dated 1 August 2017.

4. The Tenant contends that it was entitled to terminate the Lease because the Landlord had failed to *install air-conditioning to service the Premises* in accordance with the terms of the Lease. The Tenant claims return of the security deposit in the amount of $22,000, which was provided to the Landlord under the terms of the Lease.

5. The Landlord contends that the Tenant's action in purporting to terminate the Lease and subsequently vacating the Premises amounted to a repudiation on its part, entitling the Landlord to terminate the Lease, which it sought to do by letter dated 8 August 2016.

6. The Landlord contends that it is entitled to retain the security deposit and set off that amount against further losses which it counter-claims against the Tenant and the guarantor under the Lease (the Respondent by Counterclaim), which amount to $194,733.

7. It is common ground that the determination of the competing claims depends upon which of the parties lawfully terminated the Lease. That question lies at the very heart of the matters to be considered by the Tribunal in this proceeding.

BACKGROUND

8. The Tenant first inspected the Premises in February 2016. Shortly thereafter an offer was made to lease the Premises. Negotiations between the parties ensued, with the result that heads of agreement were executed by the parties on 15 February 2016 (**'the Heads of**

Agreement'). The Heads of Agreement set out the core terms that had been agreed between the parties, which included:

(a) the area to be let;

(b) the lease term of five years;

(c) the commencement date of 1 March 2016, with a rent-free period of three months;

(d) the rent of $80,000 per annum plus GST;

(e) the tenant's liability for outgoings;

(f) the payment of a security deposit representing three months rental, in the amount of $20,000, plus GST;

(g) provisions requiring the Tenant to make good upon vacating the Premises; and

(h) a description of the works to be carried out by the Landlord and those to be carried out by the Tenant.

9. As part of the works to be carried out by the Landlord, the Heads of Agreement provided, in part:

> Install split unit air-conditioning units to service the ground and first floor tenancy… the Tenant to take out a maintenance contract with a reputable air-conditioning service contractor to service the units on a 6 monthly basis at the cost of the Tenant.

10. According to the Landlord, the Heads of Agreement were altered by verbal agreement on a date between 15 and 23 February 2016 to delete the requirement to provide split unit air-conditioning units and in lieu thereof, the existing roof mounted air conditioning unit would be re-commissioned to service the Premises. The Landlord says that this variation to the Heads of Agreement arose after the Landlord pointed out that the installation of multiple split system air-conditioning units would result in unsightly exposed conduits and piping.

11. The Tenant concedes that the obligation to provide split unit air-conditioning units was ultimately dispensed with. However, it contends that the removal of that requirement did not in any way diminish the obligation for the Landlord to install air-conditioning to service the Premises. It says that the existing roof mounted air-conditioning system failed to provide adequate air-conditioning to the Premises. The Tenant further contends that this requirement was a fundamental term or condition of the Lease and the failure on the part of the Landlord to comply with this term or condition constituted a repudiation on the Landlord's part, entitling the Tenant to terminate the Lease, which it purported to do by letter dated 1 August 2017.

12. The Landlord disputes that it breached the terms of the Lease. It contends that it complied with its obligation to install air-conditioning

to service the Premises by utilising the existing roof mounted air conditioning system. The Landlord contends that the Tenant had no lawful right to terminate the Lease and that its conduct in purporting to do so, coupled with it vacating the Premises on or about 1 August 2017, constitutes a repudiation on its part, which the Landlord accepted by correspondence dated 8 August 2017.

THE CLAIMS

13. It is uncontested that the Tenant vacated the Premises on or after 1 August 2017. It contends that if it is successful in proving that the Landlord repudiated its obligations under the lease, it is entitled to reimbursement of the security deposit in the amount of $22,000, which it claims in this proceeding, plus interest.

14. By contrast, the Landlord claims that it has suffered loss as a result of the Tenant vacating the Premises. That loss is set out in a spreadsheet prepared by the Landlord, which sets out its claim (excluding interest) as follows:

    (a) Monies owed under the Lease as at termination:..... $4,163.80

    (b) Enforcement costs:..... $3,082.75

    (c) Make good: $21,0699

    (d) New Lease: $5,103.70

    (e) Rent and outgoings foregone $73,093.38

    (f) Difference in rent to new lease: $108,460.14

    (g) Repainting of façade:..... $1,760

    (h) LESS SECURITY DEPOSIT:..... ($22,000)

    (i) TOTAL: $194,733

15. The Tenant concedes that if the Tribunal finds that the as-installed air-conditioning unit satisfies the relevant term of the Lease, then its purported termination of the Lease was unlawful. In its *Amended Points of Claim*, the Tenant details what acts or omission on the part of the Landlord support its contention that the Landlord failed to install air-conditioning to service the Premises. It states:

    (a) there is no air-conditioning at the Premises;

    (b) the Landlord has sought to rely on the existing air-conditioning system;

    (c) the existing air-conditioning system has no ductwork installed;

    (d) the existing air-conditioning system is in poor repair and requires replacement;

    (e) the existing air-conditioning system cannot work because the supply and return air are adjacent to each other; and

(f) the existing air-conditioning system does not and cannot *service the Premises*.

16. These allegations raise several issues for determination; namely:

(a) Did the Landlord *install* air-conditioning if it merely re-commissioned the existing air-conditioning unit?

(b) Was the existing air-conditioning adequate, in terms of its capacity and installation, to *service* the Premises?

(c) Was the existing air-conditioning in disrepair and if so:

(i) who was responsible for its repair; and

(ii) did that mean that the Landlord did not provide air-conditioning to *service* the Premises?

(d) Does the failure to *install* air-conditioning or provide air-conditioning that *services* the Premises constitute a repudiation of the Lease?

DID THE LANDLORD INSTALL AIR-CONDITIONING TO THE PREMISES?

17. Annexure A – Special Conditions of the Lease states, in part:

> 1. Landlord works
>
> (a) the Landlord must carry out and complete the following works to the Premises:
>
> …
>
> (xiii) install air-conditioning to service the Premises.

18. It is common ground that the roof mounted air-conditioning unit was, at the time of the commencement of the Lease, approximately six years old and described as a *Daikin Rooftop Packaged Air Conditioner*. Both supply and return air are distributed and fed through solid roof mounted ductwork connecting to a split plenum box mounted to the ceiling above the internal stairs within the Premises. One side of the plenum box supplies air, while the other side draws air.

19. All experts engaged by the parties accepted that this was an inefficient and problematic installation, in that supply air tends to be drawn into the return air vent, rather than being pushed into the area to be serviced. Ideally, ductwork should have been connected to the plenum box to distribute conditioned air throughout the Premises, while at the same time isolating and distancing the supply air from the return air.

20. The Tenant contends that utilising the existing roof mounted air conditioning unit to service the Premises did not satisfy the special condition 1(a)(xiii) of the Lease. Mr Flower, the solicitor representing the Tenant and the Respondent by Counterclaim (**'the Guarantor'**),

argued that the word *install* meant something had to be installed, rather than existing equipment utilised.

21. Mr Norris-Ongso, the director of the Tenant, gave evidence that when the Landlord commenced its works in February 2016, he asked the Landlord's leasing agent whether the existing air-conditioning unit would be removed. He said that the leasing agent told him that he would check with the Landlord and if it was not removed, then it would be covered up. Further, at some time prior to the Tenant commencing its business operations in June 2016, a dispute arose between the Tenant and Landlord over the works completed or not completed by the Landlord. The dispute ultimately led to this proceeding being issued by the Tenant. In its original *Points of Claim* dated 6 June 2016, the Tenant alleged that the Landlord had, amongst other things, breached Clause 1(a)(xiii) of the Lease:

> 14. Further, in breach of clause 1(a) (xiii) of Annexure A of the lease the Respondent has failed to carry out and complete the installation of air-conditioning to service the premises in that:
>
> (a) there is no air-conditioning of the premises;
>
> (b) the Respondent has sought to rely on the old system previously in place; and
>
> (c) there are no ducts installed and there are gaping holes where ducts have been.

22. Both Mr Deller, counsel for the Landlord and Mr Flower both agreed that the question as to whether the existing air-conditioning system satisfied special condition 1(a)(xiii) turned, in part, on an interpretation of that special condition. In particular, do the words *install air-conditioning* mean that an air-conditioning system has to be installed into the Premises, as opposed to utilising the existing roof mounted air conditioning system?

23. In my view, a plain reading of special condition 1(a)(xiii) indicates that the Landlord was required to do something to satisfy that term. Simply leaving the existing air-conditioning system for use by the Tenant does not, in my opinion, equate to the Landlord *installing* air-conditioning to the Premises.

24. However, the evidence before me indicates that the Landlord did something to make the existing air-conditioning unit operational. In particular, Mr Kerlidis, the director of the Landlord, gave evidence that at the time the parties entered into the Lease, the roof mounted air conditioning unit was not operational. He said that it was made operational as part of the *Landlord works*. The following extract from the transcript of Mr Kerlidis' evidence provides some background to what was done:

Do you recall the question I asked you before about any differences between the depiction in photo 502 as it was during the tenancy and prior to the tenancy? --- Yes.

Can I ask you the same question about photo 503. Was the controller that is shown in 503 there prior to the tenancy? --- No, it wasn't.

How did that controller get there? --- We commissioned a company called Comyfirst. They installed the controller, connecting it back into the air-conditioning at the top. I can't remember the exact time when that actually happened but that happened after signing off on the lease and in that period of the landlord work component.

In the period when there was no controller, was it possible to operate the air-conditioner? --- Okay. So the controller was - the original controller servicing the air-conditioning unit was removed by us. We were taking out all - We stripped the building of all the electrical components. The building needed to be made flexible leasing options. So the original building as we bought it was made up of a series of offices. I recall there was a display and a storage component to it. There was also a strong room in the premises as well. What we did is, before purchasing the building we checked out the condition of the building, we looked at ideas of how to make this building more appealing to more leasing options and its original format with room after room after room was really quite limiting in terms of its market appeal. So before the tenancy that was entered into with S3, there was a program of stripping out the previous tenancy fit-out and take it back to what you'd call a bear shell, and that included removing all the electrics right back to the switchboard so that there would be no potential for any contamination of circuits for safety…

You've said that the air-conditioner was connected to a switch in the switchboard in the tenancy itself? --- Correct.

Was that something that was done as part of the landlord work or was the pre-existing? --- That was done as part of the landlord work. So the entire electrics - if you imagine the entire electrics were taken right back to the switchboard. We really took it right back to the switchboard to ensure that the electrics were moving forward to suit - whatever fit-out was going to be the could be done in the most safest way.

The controller that you've given us - the one that shown on p.503, who decided the location of that controller? Who decided where it was put? --- I honestly can't recall why that position came down. At the time when it was being discussed it was concurrent with the tenant doing their fit-out works…

> You've given evidence about the way in which the three-phase power was supplied --- ? --- Yes.
>
> --- and the controller was put on. Was there any other work that the landlord did in relation to that air-conditioning system that you want to tell the tribunal about? --- Yes. So as part of putting in the controller, what Comfyfirst did is they commissioned the air-conditioning unit which meant running a service, cleaning the filters, checking pressures, basically commissioning it and signing off and saying that the unit is operational.[1]
>
> -

25. In addition, it is common ground that the Landlord installed three phase electricity to the roof mounted air conditioning unit after the Lease had been entered into.

26. Consequently, I find that the work of providing three-phase power to the existing roof mounted air-conditioning system, installing the *Smart Temp* wall mounted controller and then arranging for the air-conditioning unit to be serviced, commissioned and tested before or during handover constitutes the work of *installing air-conditioning to the Premises*. However, the question remains whether that air-conditioning *serviced* the Premises.

DID THE AIR-CONDITIONING INSTALLED BY THE LANDLORD *SERVICE* THE PREMISES?

27. The Tenant contends that notwithstanding the recommissioning of the existing roof mounted air-conditioning unit, what was undertaken by the Landlord still did not satisfy special condition 1(a)(xiii) of the Lease because more work was required to ensure that the air-conditioning unit *adequately* serviced the Premises.

28. Whether the air-conditioning system *serviced* the Premises raises several questions for determination:

    (a) Was the Landlord required to install internal ductwork?

    (b) Was the air-conditioning system of sufficient capacity?

    (c) Was the air-conditioning system in poor repair, rendering it incapable of *servicing* the Premises?

Was the Landlord required to install ductwork?

29. As indicated above, the installation of the air-conditioning unit was problematic because ductwork had not been installed to direct and balance conditioned air. According to the Tenant, the responsibility for installing ductwork lay with the Landlord. The Landlord disputes that it

[1] Transcript 30 May 2017, pages 43-45.

was responsible for installing ductwork, save for the solid ductwork installed on the roof.

30. Special condition 1(a)(xiii) of the Lease does not mention ductwork. Nevertheless, the Tenant contends that the requirement to install ductwork is implicit because the Premises cannot be properly air-conditioned without the installation of ductwork.

31. I do not accept that proposition. In my view, *servicing* the Premises means to supply an air-conditioning system of working order and of sufficient capacity to service the Premises over the life of the Lease. How conditioned air is to be distributed or balanced will depend upon the internal fit-out undertaken by the Tenant and the needs of the Tenant. For example, partitioning areas of the Premises might require air to be ducted into those partitioned areas. Clearly, that work could not be done until after the Tenant had undertaken its fit-out. Similarly, balancing the air-conditioning within the Premises may also require ductwork to direct more or less conditioned air to specific areas, depending on the needs of the Tenant. The express terms of the Lease do not indicate, nor is there any evidence suggesting, that the Landlord was to be responsible for that work.

32. In my view, it is unlikely that the parties intended that the responsibility for installing ductwork was to rest with the Landlord. This is because the precise scope of that work could not have been known at the time when the parties entered into the Lease.

33. Accordingly, I construe the words *air-conditioning to service the Premises* to mean providing air-conditioning of sufficient capacity to cool or heat the Premises over the life of the Lease. In my view, that clause does not require the Landlord to supply and install ductwork to better meet the needs of the Tenant.

34. I have formed this view notwithstanding that the parties have, in part, relied upon subsequent conduct to support their respective positions. In particular, on 8 March 2016, the Tenant wrote to the Landlord stating:

> Theo
>
> Another issue has arisen with respect to air-conditioners. Upstairs the class [sic] walls will go to the ceiling - can you put a duct in from unit to each room before the ceiling goes in?

35. Mr Flower submitted that this statement demonstrates that the Tenant was acting in a way consistent with the Landlord having an obligation to install ductwork. On the other hand, Mr Deller submitted that this statement indicates the opposite; namely, that the Tenant had not considered the need for ducts before 8 March 2016 – well after the Lease had been executed.

36. Further, Mr Kerlidis gave evidence that the issue of ductwork was discussed with the Tenant's fit-out contractor after the Lease had been entered into. He stated:

> Can you please proceed on and tell Senior Member Riegler what the discussion was? --- Yes. So on 8 March, I – I – I got an email from Paul. I – but at that stage, it was very early on in the piece. And it was virtually daily conversations with the guys on-site, and ---
>
> With who on-site? --- With various people, so it would have been either with Paul or - Matthew, but predominantly at this early stage it seemed to me that it was being handed over to Matthew to lead the project management style work.
>
> Okay. Then there's the conversation you are about to start on with Matthew? --- Yes. So Matthew comes over to me and asks, "What do we do with the ducting?" And I explained to Matthew, "it's not in my lease to do the ducting. I'm providing the base building work. It is for you guys to do the ducting." He then replied to me, "I guess you're right," and then proceeded to walk away.
>
> Do you recall the date of that meeting? --- It would have been after the 8th.

37. In my view, the subsequent conduct of the parties does not assist in interpreting the words of the Lease or in discerning the intention of the parties. Indeed, the predominant view of superior courts in Australian is that it is not legitimate to use as an aid in construction of a contract anything which the party said or did after the contract was made.[2]

38. Similarly, accepting statements made after the Lease was executed offends the parole evidence rule. In *Goss v Lord Nugent*, Lord Denman CJ explained the rule as follows:

> … if there be a contract which has been reduced to writing, verbal evidence is not allowed to be given of what has passed between the parties, into or before the written instrument was made, or during the time it was in a state of preparation, so as to add to, subtract from, or in any manner to vary or qualify the written contract.[3]

39. Similarly, in *Hope v RCA Photophone of Australia Pty Ltd*, Latham CJ said:

> When parties express their agreement in writing they do so for the purpose of securing certainty and preventing disputes. They may choose to leave their arrangements to the risks and chances of verbal evidence. But if they have recourse to writing for the purpose of recording their agreement they cannot afterwards change their attitude and, by seeking to give parole evidence, introduce the very

[2] *Agricultural & Rural Finance Pty Ltd v Gardiner* (2008) 238 CLR 570, [35].
[3] (1833) 110 dear 713, 716.

> element of uncertainty which the adoption of writing was intended by both parties to exclude.[4]

40. In the present case, construing the agreement to impose an obligation on the Landlord to install ductwork during or after the Tenant's fit-out work has been undertaken would require words to be imported into the Lease that simply are not there. I do not accept that such a course is open on the evidence or at law.

41. Moreover, I am not persuaded that the absence of ductwork prevents the air-conditioning system from *servicing* the Premises. There is no evidence that the air-conditioning, when it was operational, did not cool or heat the Premises, notwithstanding the concession made by the Landlord and the expert opinion of all expert witnesses that the air-conditioning system would have performed better if ducting had been installed to meet the needs of the Tenant, having regard to its fit-out and use of the Premises.

Was the air-conditioning system of sufficient capacity?

42. Despite Mr Norris-Ongso's evidence that the air-conditioning unit was old and undersized, all experts, including Mr Gattellaro, the mechanical plumber engaged to give evidence on behalf of the Tenant, conceded that the unit itself is correctly sized for the Premises. The problem lay in the distribution of conditioned air, rather than the capacity or type of air-conditioning unit installed.

43. Mr Hislop, the mechanical engineer engaged by the Landlord, provided an expert report on the air-conditioning system installed in the Premises. He stated, in part:

> Cooling and heating load calculations have been carried out on the building using the latest version of the CAMEL computerised load calculation program.
>
> The calculated cooling and heating loads from the output data are included below
>
> …
>
> A copy of the more detailed CAMEL output data is included in Appendix B for information at the rear of this report.
>
> From the data the calculated maximum cooling capacity required is 18.5 kWR. The calculated supply air flow rate total for the system is 1,299 1/sec.
>
> This load calculation is based on office use and includes 10 watts/m^2 for internal heat gain from equipment such as computers. For the building, which had a computation of Net Lettable Area carried out on it of 218 m^2, this represents 2.18 kW. If, as we are advised, the

[4] (1937) 59 CLR 348, 357.

> tenant did not use the building for office use but some form of fitness or training use than the calculated load would be 18.5 - 2.18 = 16.32 kWR. That is almost exactly the capacity of the unit at 16 kWR.[5]

44. It is common ground that the Premises were used predominantly for fitness training but also partly office use. With that in mind, I find that the air-conditioning unit carries adequate load capacity to service the Premises. My finding is reinforced by a statement made by the mechanical plumber engaged by the Tenant that:

> The unit is correctly sized for the building…[6]

45. Further and notwithstanding Mr Norris-Ongso's evidence that the air-conditioning system constantly broke down, Jasmine Turner, the Barre and Pilates instructor of the business recounted her experience working at the Premises during the period June 2016 to April or May 2017. Ms Turner said that she helped set up the business, which included finding the site and assisting with the fit-out. She then conducted Barre and Pilates lessons as well as performing administrative duties such as overseeing client memberships, paying bills, banking money, et cetera. She said that she conducted classes approximately six or seven days each week, with the number of classes ranging from between two to six per day. She said that if she started in the morning it was either at 6 AM or 9:30 AM and she would be there until approximately 2 PM. She said she would come back sometimes at 5:30 PM or 6:00 PM.

46. In my view, her regular attendance at the Premises placed her in a good position to gauge the effectiveness of the air-conditioning system. The following extract of the transcript of Ms Turner's evidence provides, in my view, first-hand and compelling insight as to the operation of the air-conditioning system:

> Was there air conditioning provided at the premises? --- Yes.
>
> How did the air-conditioning operate? --- How did it operate?
>
> Yes. Did you operate the air-conditioning? --- Yes.
>
> How did you operate it? --- I used to use the keypad and then that stop working so I'd use the switchboard.
>
> You used the switchboard. What did you do there? --- Just turned it on and off.
>
> Which switchboard is that? --- The main switchboard near the front door.
>
> To turn it on, what did you do? --- Just flick the switch up.
>
> And to turn it off what did you do? --- Turned the switch down.

[5] Report prepared by Geoff Hislop, of *MechAir Pty Ltd* dated 21 October 2017, pp 6-7.
[6] Report prepared by Glenn Gattellaro of *ServiceToday* dated 22 November 2017, p 3.

Did it operate when you did that? --- Yes.

In terms of the operation of the air-conditioning, who turned it on during the day or was it already on? --- The instructor or whoever was in the building first would turn it on if they wanted it on. I didn't always use it.

Who would then turn it off? --- The last person. Before you left, you turned it off.

…

When you did that, did the air-conditioning function? --- Yes.

And in the wintertime did the air-conditioning provide warm air? --- Yes.

And in the summertime when it was hot did it provide cold air? --- Yes.

Were you able to adjust the temperature settings --- ? --- Yes.

--- Or was it just on and off? --- You can adjust the temperature settings most of the - it was temperamental but it worked, yes.

When you were there and conducting the classes downstairs, that's what you are using the air-conditioning for? --- Yes, or if I was doing paperwork I'd have it on as well.

Were there any times when you were there and you sought to use the air-conditioning when it operate? --- Yes.

What happened?--- It didn't turn on.

When was this? --- I recall one time in particular, it must've been over the January sort of period, it was a 39 degree day and it didn't work.

And what happened? --- I remember that one.

What did you do? --- Called or emailed Theo and then couldn't get in contact with Theo so I contacted my husband to see if any of their - he works for a company that has air-conditioning and see if any of the tradesmen were on the road.

And what happened? --- One of them call past and turned it on.

Where did they turn it on at? --- I don't know. I think they went up to the machine at the top, on the roof.

…

After that, did the air-conditioning continue to work? --- Yes, I believe so.

> Any other instances where you sought to operate the air-conditioning and it didn't work? --- Yes, but I can't recall exactly when or where.
>
> Can you tell the tribunal approximately how many times that may have happened over the course of the months that you were there? --- I'd be guessing.
>
> I won't ask you to guess. Can I put the question this way: with the number of times at the air-conditioning didn't work when you would there be more or less than five times? --- Maybe more.
>
> More than 10? --- No, I don't think so.
>
> So between five and 10? --- I would - yes.
>
> On the times when the air-conditioning didn't work when you were there, was that air-conditioning fixed so that it then after point was able to be operated and worked? --- Yes, by using the switchboard.
>
> …
>
> So what would you do when that happened, go back down to the meter box? --- Yes, and turn it off.
>
> On the circuit breaker? --- Yes.
>
> And then back on again? --- Yes.
>
> And then it would work? --- Yes, most of the time.
>
> For how long? --- I don't know exactly. Enough for me to - yes, for the day.
>
> …
>
> … Other than the times that you've given evidence about where there were specific issues with the air-conditioning that were either fixed by your husband or someone on his behalf or were referred to the landlord Theo for rectification just so I understand further to Senior Member Riegler's question, in each of those instances the air-conditioning was fixed and then continued to operate thereafter? --- I believe so.
>
> Other than those times, did the air-conditioning generally operate? --- Yes.[7]

47. Ms Turner presented as a credible witness, willing to make concessions when pressed on certain issues and accepting that her memory of certain events may have diminished with time. I consider her evidence to be material for several reasons. First, it did not appear that she had any interest in the outcome of this proceeding as she had no on-going role within the business that had been conducted from the Premises.

[7] Transcript of hearing 31 May 2018, pp 150-155.

Second, she was at the Premises for most of the time that the business was being conducted. She clearly had first-hand knowledge of how well the air-conditioning system operated during the period June 2016 until April/May 2017.[8]

48. Accordingly, I find that notwithstanding some problems in the operation of the air-conditioning system, the system was of sufficient capacity to service the Premises, even without installation of ductwork to distribute or balance conditioned air. Clearly, installation of ductwork would have improved the performance of the air-conditioning system. However, I do not accept that its absence rendered the air-conditioning system, as installed, as not being able to service the Premises.

Was the air-conditioning system in poor repair?

49. A further ground relied upon by the Tenant in support of its contention that the Landlord failed to install air-conditioning to *service* the Premises was that the air-conditioning system was in poor repair. This ground is supported by Mr Norris-Ongso's evidence that the air-conditioning unit only ever operated for 20 minutes at a time before it would switch off.

50. Ms Turner gave some account of problems experienced with the air-conditioning system over the period that she worked in the Premises. However, she did not say that the air-conditioning unit only ever operated for 20 minutes at a time. Moreover, that allegation is not mentioned in either the original *Points of Claim* or the *Amended Points of Claim*. Therefore, I do not accept that the fault which caused the air-conditioning system to switch off after 20 minutes running existed at the time when the system was first commissioned.

51. During his evidence in chief, Mr Norris-Ongso detailed instances where the air-conditioning system did not operate or operate properly. The first instance occurred nearing the end of the Landlord completing its works in May 2016. Mr Norris-Ongso recounted:

> Right. So when were the works eventually – well, when weather works completed to such a standard that you - that the - tenancy could be occupied? --- At the beginning of June. But, at that stage, there was still no air-conditioning.
>
> Right? --- And – but – but not – not the issue that we're complaining about. On 23 May [2016], I sent a letter to Theo and said, "As of today, there is no power for the air-conditioning because it required three phase power which you had removed previously. So although the air-conditioning is - you say the air-conditioning is there and it

[8] Transcript of 31 May 2018, pp150-151.

> may work, we don't know because there is no power for it to turn it on."
>
> Right? … So that came - I can't remember when. It was some days a week later the power was finally installed, because the electrician was working there still, into June.

52. Mr Norris-Ongso recounted other occasions where the air-conditioning system was unable to be turned on. In particular, on one occasion, the power of Main Switchboard had been turned off, on another occasion the controller malfunctioned but was eventually replaced by the Landlord under warranty. Critically, however, it appears that the most significant issue with the air-conditioning system occurred after Ms Turner had left the business in April or May 2017. After that time, the preponderance of evidence indicates that the air-conditioning system would only run for 20 minutes before it inexplicably turned off.

53. It appears from correspondence produced during the hearing that the Landlord was first informed of this problem by email correspondence dated 15 May 2017. Despite several email exchanges between the parties, that problem persisted for the remainder of the period that the Tenant occupied the Premises.

54. Clearly, this fault resulted in the air-conditioning system not being able to *service* the Premises from at least May 2017.

55. It is regrettable that this malfunction was not properly diagnosed at that time. In particular, Mr Kerlidis gave evidence of what work was undertaken after the Tenant had vacated the Premises and in order to make the air-conditioning unit operational again. He recounted:

> On top of p.164 Mr Gattellaro says there, "I found that after having the unit running for 20 minutes the unit cut out and is not running. This was in the presence of Theo." Were you there when Mr Gattellaro did the work that subject of this report? --- I was there.
>
> What do you recall happened during the course of this attendance by Mr Gattellaro? --- There were three gentlemen, three technicians. They turned the air conditioning on and it ran. They then went up on the roof and whilst on the roof it stopped to work and then came down and the air-conditioning wouldn't turn back on.
>
> Do you know what the cause of that was on that day, why the air-conditioning didn't work on that day? --- I didn't know why it didn't work on that day.
>
> What did you do, if anything, after that to make the air-conditioning work again? --- I then contacted Daikin Air-conditioning. So Daikin have got a service component to them. Actually, sorry I must go back. I contacted a ComfyFirst originally, who came out after this and then wanted me to call Daikin because identified it to be the fan

> unit but weren't entirely sure. So it was a little bit more expertise was required than what they could offer at that stage. I then called Daikin. They ran some diagnostics and identified that the fan unit that had stopped to work.
>
> Was a fan unit subsequently fixed? --- Yes, it was.
>
> Is that the fan unit that you gave evidence to Senior Member Regular about earlier today. I think there was a discussion about whether that was a fan in the condensing unit? --- It's the same.
>
> Is it the same fan we're talking about? --- It's the same. Yes, it was just basically bolted out and put a new one in. It was a half an hour exercise.

Who was responsible to repair the air-conditioning unit?

56. Special Condition 1(e) of the Lease states:

> In relation to the air conditioning units installed as part of the Landlord's Works (pursuant to special condition 1(a)(xiii)):
>
> (i) the Tenant will, at its sole cost, take out and maintain a maintenance contract for the Term (and any further term) with a reputable air conditioning service contractor to service those air conditioning units on a 6 monthly basis; and
>
> (ii) subject to the Tenant's compliance with special condition 1(e)(i), the Landlord is responsible for any capital repairs associated with those air conditioning units.

57. The reference to air-conditioning units (plural) appears to be a mistake, given that the original draft of the special conditions, as found in the first draft of the Heads of Agreement contemplated that there would be multiple split system air-conditioning units. However, it is common ground that during the negotiation process, the parties agreed not to proceed with the installation of multiple split system air-conditioning units.

58. It is unclear what is meant by the words *capital repairs*. On one hand, it may mean any substantial or serious repairs, while the other hand it may mean any repairs which are of a capital nature, namely, that have the effect of increasing the value of the air-conditioning units.

59. The lease was drafted by the Landlord's previous solicitors. As such, any ambiguity in its terms should be construed *contra proferentum*; namely, against the party that drafted the document.[9] Moreover, read in context, the subclause purports to make the Tenant responsible for servicing the air-conditioning units on a six-monthly basis and the

[9] *CE Heath Underwriting Insurance (Australia) Pty Ltd Edwards Dunlop & Co Ltd* (1992) 176 CLR 535, 541-2.

Landlord responsible for any substantial or serious repairs. This would not include repairs of a minor nature associated with the maintenance of the air-conditioning units. For example, replacing filter pads or other consumables.

60. Therefore, I find that special condition 1(e)(ii) obliged the Landlord to carry out the repairs to the air-conditioning unit, which included repairs such as replacing the condenser fan. This is consistent with s 52 of the *Retail Leases Act 2003* which requires a landlord to maintain the plant and equipment in a condition commensurate with its condition at the commencement of the Lease. The provision states, in part:

> (1) A retail premises lease is taken to provide as set out in this section.
>
> (2) The landlord is responsible for maintaining in a condition consistent with the condition of the premises when the retail premises lease was entered into -
>
> …
>
> (b) plant and equipment at the premises; and.

61. Having regard to Ms Turner's evidence that the air-conditioning system operated for most of the period leading up until May 2017, I find that the problem with the condenser fan manifested sometime in May 2017, when first raised by the Tenant. It was a fault that occurred almost a year after the Tenant started using the air-conditioning system. This leads to the inference that the condenser fan was operational at the time the Lease was entered into, even though other aspects of the air-conditioning system were not. Moreover, Mr Kerlidis confirmed that the only *capital* works that the Landlord carried out from the commencement of the Lease comprised the installation of the controller, connecting three phase electricity and commissioning the air conditioner unit. After that work was completed, the air-conditioning system operated. This means that the condenser fan must have functioned at that time. If it had not, then the problem with the air-conditioner cutting out after 20 minutes running would have occurred from the date when it was first commissioned in June 2016. This was not the case. As I have found, that problem first arose in May 2017 and was attributable to the condenser fan malfunctioning, requiring its replacement.

62. Accordingly, either special condition 1(e)(ii) or s 52 of the *Retail Leases Act 2003* required the Landlord to carry out the repair and/or replacement of the condenser fan. In reaching that conclusion, I note that s 52 of the *Retail Leases Act 2003* was not relied upon by the Tenant. However, the Landlord did not, correctly in my view, submit that special condition 1(e)(ii) of the Lease did not operate to bind the

Landlord. In those circumstances, it was unnecessary for the Tenant to raise s 52 of the *Retail Leases Act 2003*.

DID THE LANDLORD REPUDIATE THE LEASE?

63. In *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*,[10] Dean and Dawson JJ summarised the concept of repudiation as follows:

> … repudiation turns upon objective acts and omissions, not on uncommunicated intention, and it is sufficient that, viewed objectively, the conduct of the relevant party has been such as to convey to a reasonable person, in the situation of the other party, repudiation or disavowal either of the contract as a whole or of a fundamental obligation under it.[11]

64. Similarly, in *Kane Constructions Pty Ltd v Sopov*,[12] Warren CJ stated:

> Gibbs CJ in *Sheville & Anor v The Builders Licensing Board* likewise observed that a contract may be repudiated where one party renounces their liabilities under it, evincing any intention to no longer be bound by the contract. His Honour further observed that repudiation may also occur when one party demonstrates an intention to fulfil the contract, but in a manner "substantially inconsistent with his [or her] obligations and not in any other way…"[13]

65. The Tenant contends that the disrepair of the air-conditioner, coupled with other factors, constitute a breach of the obligation to *install air-conditioning to service the Premises.*

66. I do not accept that the malfunction of a part or parts of the existing air-conditioning system necessarily mean that there has been a failure to provide air-conditioning to *service* the Premises, especially when the component is easily replaced or repaired, rendering the air-conditioning system once again fully functional. As I have already found, the as-installed air-conditioning system, when working, satisfied the requirements of special condition 1(a)(xiiii).

67. Indeed, when special condition 1(a)(xiii) is read in context with special conditions 1(e)(i) and (ii), which allocate responsibility for maintenance to the Tenant and *capital* repairs to the Landlord, it is clear that the parties envisaged that repairs may be required from time to time. This reinforces my view that special condition 1(a)(xiii) is not to be construed to mean that a single breakdown, of itself, leads to a failure to install air-conditioning *to service* the Premises.

[10] (1989) 166 CLR 623.
[11] Ibid at at 658.
[12] [2005] VSC 237. See also Supreme Court of Appeal judgment in *Sopov and Anor v Kane* [2007] VSCA 257, which upheld Warren CJ's findings on the question of termination.
[13] Ibid at [795].

68. However, that scenario is to be distinguished from one where there is an obligation to repair and a landlord refuses, either expressly or implicitly, to perform that obligation. In that situation, it may be that the failure to repair a critical component of an air-conditioning system, necessary to enable that air-conditioning system to function properly, constitutes a breach of an obligation to install air-conditioning *to service the premises*.

69. In that sense, I find that special condition 1(a)(xiii) of the Lease is not subject to any temporal limitation. It does not mean that once the air-conditioning system has been installed and is servicing the Premises, the special condition has no further work to do. If that were the case, removing the air-conditioning system after it had been installed would satisfy the special condition, which would be an absurd interpretation of that special condition. In my view, the obligation to install air-conditioning *to service the premises* means to *service* the Premises on an ongoing basis during the currency of the Lease. If the air-conditioning system stops working due to a malfunction of one of its critical components, and the Landlord refuses to repair that component, then the air-conditioning is no longer *servicing* the Premises.

70. In the present case, I accept Mr Norris-Ongso's evidence that air-conditioning was critical for the financial success of the Tenant's business. He said that clients were moving to other premises because the Premises could not be properly warmed during the colder months of the year. Although no data was provided evidencing the migration of clients from one fitness centre to another, I accept that it is likely that customers of a fitness centre require and expect a comfortable ambient temperature in which to work out. Consequently, I find that the obligation to provide air-conditioning to *service* the Premises is a fundamental term of the Lease.

71. With that in mind, I further find that the refusal or failure to repair the air-conditioning system, if fallen into disrepair so that it cannot service the Premises, may constitute a repudiation of the Lease.

72. In this case, the Landlord received written notice that the air-conditioning was not working on 15 May 2017 by email correspondence, stating:

> Theo
>
> The air-conditioning has not been working for the past couple of weeks. I've only just been informed. Could you please arrange for a technician to come in service it.

73. The Landlord responded with the following email from Mr Kerlidis on the same day:

> Hi Paul,

> Thanks for the email and sorry to hear that the a/c unit has stopped working.
>
> In terms of maintenance, in accordance with the lease, S3 is meant to be maintaining the unit every 6 months. The last I heard, see attached email, you were had a maintenance plan in place. Best to check with Jasmine.

74. By email dated 21 June 2017, Mr Norris-Ongso responded:

> Dear Theo
>
> The situation with the air-conditioning unit in the Premises has become intolerable. I am not going to argue the point in this email that are the subject of our dispute at VCAT but merely highlight your obligations under the Lease.
>
> All you are required to "INSTALL AN AIR-CONDITIONING UNIT" suitable for the Premises. You have never done that and the unit that is there is beyond repair and has never functioned properly for more than a couple of days. It is not functioned at all for the past 6 months.
>
> … I attach a quote from technicians we had inspect the unit for the purpose of repairing it. They reported that it was beyond economical repair…
>
> I urge you to see sense and meet your obligations under the lease with respect to the air-conditioning unit.

75. The quotation referred to in Mr Norris-Ongso's email was from a plumbing company; namely, *Servicetoday*, which was to remove the existing unit and replace it and all roof ductwork with another 16 kw Daikin package. The total cost of that work was quoted at $32,276.20. A brief report accompanied that quotation, which stated:

> Arrived on site fault find on unit motherboard is needing to be replaced as is compressor fan and all sheet metal ductwork and flashings. This being said unit is beyond worthy of repair as more faults will occur due to units age, also the general install is incorrect as return and supply air are the same outlet…

76. The comments in the site report suggested the unit is beyond repair because of its age. However, its manufacture date was April 2010, which meant that the air-conditioning unit was approximately six to seven years old at the time of the inspection. The expert opinion evidence of Mr Hislop, the mechanical engineer who gave evidence on behalf of the Landlord, was that the unit should have a lifespan of 20 years. That being the case, I do not accept that the air-conditioning unit was past its lifespan.

77. The Landlord responded on the same day with the following email:

> Hi Paul, …
>
> In terms of the A/C you are meant to maintain it have you been doing so?
>
> Please confirm ASAP.

78. Mr Norris-Ongso responded on the same day:

> Theo
>
> We are supposed to maintain the air-conditioner you were supposed to instal. You never met that obligation so there is nothing for us to maintain.
>
> Effectively you are trying to force us to make your run-down air-conditioner serviceable to meet your obligations. It doesn't work that way.

79. No further correspondence passed between the parties other than the Tenant's correspondence dated 1 August 2018, wherein it gave notice that the Lease had come to an end.

80. In its *Amended Points of Claim* the Tenant alleges that special condition 1(a)(xiii) was breached because, *inter alia*, that:

> (d) the old system was in such poor repair that it requires replacement, which the Respondent has repeatedly refused to do despite repeated requests by the Applicant;

81. There is no evidence of the Landlord arranging for its technician to inspect the air-conditioning system in response to the complaints raised by the Tenant from 15 May 2017 to when the Lease came to an end. Similarly, there is no evidence as to why the Landlord did not do so, which is curious given that the Landlord had, on previous occasions, arranged for its technician to inspect the air-conditioning system following complaints raised by the Tenant.

82. On 1 August 2017, the Tenant sought to terminate the Lease agreement on the ground that the Landlord failed to install an air-conditioning system to service the Premises. By that stage, approximately 10 weeks had passed since the Landlord was given notice that the air-conditioning system had effectively stopped working.

83. Although I accept that some time should be afforded to allow the Landlord to engage its technicians to inspect the air-conditioning system and carry out repairs, 10 weeks is an unreasonably excessive period, especially so when compared to other occasions when the Landlord arranged for its technicians to inspect air-conditioning system after complaints were raised by the Tenant.

84. As I have already indicated, the Tenant contends that that this failure to repair, amongst other things, amounts to repudiation on the part of the Landlord.

85. In *Versus (Aus) Pty Ltd v A.N.H. Nominees Pty Ltd*, Croft J reviewed several authorities when considering whether the landlord's failure to undertake remedial work constituted a repudiation of the lease agreement under consideration in that case. After re-stating the well-established principle that repudiation is a serious matter which is not likely to be inferred, his Honour continued:

> 121 … It was often said in the oft-cited decision in *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* that what must be present to support a finding of repudiation is conduct, verbal or otherwise, which conveys to the innocent party the defaulting party's inability, or unwillingness, to perform the contract, or, an intention to perform it only in a manner substantially inconsistent with that party's obligations.[14]
>
> In that case, Brennan J expressed the test as follows:[15]
>
> > The question whether an inference of repudiation should be drawn merely from continued failure to perform requires an evaluation of the delay from the standpoint of the innocent party. Would a reasonable person in the shoes of the innocent party clearly infer that the other party would not be bound by the contract or would fulfil it only in a manner substantially inconsistent with that party's obligations and in no other way? Different minds may easily arrive at different answers.
>
> …
>
> 130 In *Laurinda*, Mason CJ spoke of the fine line which exists between a reluctance to perform one's obligations in a timely manner, as opposed to a reluctance to ever those perform those obligations. The Chief Justice said:
>
> > There is a difference between evincing an intention to carry out a contract only if and when it suits the party to do so and in evincing an intention to carry out a contract as and when it suits the party to do so. In the first case the party intends not to carry out the contract at all in the event that it does not suit him. In the second case the party intends to carry out the contract, but only to carry it out as and when it suits him. It is much easier to say the first than of the second case that the party has evinced an intention no longer to be bound by the contract or to fulfil it only in a manner substantially inconsistent with his obligations and not in any other

[14] (1989) 166 CLR 623.
[15] (1989) 166 CLR 623, 648.

way. But the outcome in the second case will depend upon its particular circumstances, including the terms of the contract. In some situations the intention to carry out the contract as and when it suits the party may be taken to such lengths that it amounts to an intention to fulfil the contract only in a manner substantially inconsistent with the party's obligations and not in any other way.[16]

131 In the same case, Deane and Dawson JJ examined a number of English authorities which discussed the circumstances where non-performance may constitute repudiation, again emphasising the importance of viewing the non-performance through the eyes of a reasonable person in the position of the innocent party. Their Honours said:[17]

> An issue of repudiation turns upon objective acts and omissions and not upon uncommunicated intention. The question is what effect the lessor's conduct 'would be reasonably calculated to have upon a reasonable person.'[18] It suffices that, viewed objectively, the conduct of the relevant party has been such as to convey to a reasonable person, in the situation of the other party, repudiation or disavowal either of the contract as a whole or of a fundamental obligation under it.
>
> …
>
> It is not necessary for repudiation of a contract that the repudiator make plain that he will never perform his contractual obligations at all. What Lord Dunedin described[19] as the assumption of 'a shilly-shallying attitude in regard to the contract' and what Lord Shaw of Dunfermline[20] called 'procrastination ... persistently practised' can, in some circumstances, reach the stage of repudiation even though accompanied by assurances of ultimate performance at some future time. In that regard, the law was correctly stated by Lord Shaw in the following extract from his judgment in *Forslind*[21] which is directly in point to the circumstances of the present case:
>
> > If, in short, A, a party to a contract, acts in such a fashion of ignoring or not complying with his obligations under it, B, the other party, is entitled to say: 'My rights under this contract are being completely ignored and my interests may

[16] (1989) 166 CLR 623, 634.
[17] (1989) 166 CLR 623 at 658.
[18] *Carswell v Collard* (1893) 20 R (HL) 47 at 48; *Forslind v Bechely-Crundall* (1922) SC (HL) 173 at 190 ("*Forslind*").
[19] *Forslind* (1922) SC (HL) 173 at 190.
[20] *Forslind* (1922) SC (HL) 173 at 192.
[21] *Forslind* (1922) SC (HL) 173 at 191–2.

> suffer by non-performance by A of his obligations, and that to such a fundamental and essential extent that I declare he is treating me as if no contract existed which bound him.' ... In business over and over again it occurs—as, in my opinion, it occurred in the present case—that procrastination is so persistently practised as to make a most serious inroad into the rights of the other party to a contract. There must be a stage when the person suffering from that is entitled to say: 'This must be brought to an end. My efforts have been unavailing, and I declare that you have broken your contract relations with me.'
>
> Lord Shaw[22] went on to point out that 'the question whether the stage has been reached when procrastination or non-performance' constitutes repudiation is essentially one of fact. That question will, as has been said, only be properly answered in the affirmative when procrastination or non-performance has marked the stage of conveying to a reasonable person, in the situation of the other party, repudiation or disavowal either of the contract as a whole or of a fundamental obligation under it.

86. In my view, the failure on the part of the Landlord to do anything to make the air-conditioning system function, so that it *serviced* the Premises, after receiving written notice on 15 May 2017 until the Lease was eventually terminated on 1 August 2017, is a fundamental breach of the Lease. It meant that the Tenant was effectively left without air-conditioning to service the Premises for more than two and a half months, before eventually terminating the Lease. This was an intolerable situation and, according to Mr Norris-Ongso, led to customers migrating to other fitness centres.

87. In my view, the Landlord's *procrastination or non-performance* would convey to a *reasonable person* in the shoes of the Tenant that the Landlord had disavowed itself of its obligation to repair the air-conditioning system, notwithstanding repeated requests being made by the Tenant for the Landlord to honour its obligations under the Lease.

88. Therefore, I find that the Landlord repudiated its obligations under the Lease and that the Tenant was entitled to accept that repudiation, which it did by correspondence dated 1 August 2017. I find that the Lease came to an end on that day.

THE LANDLORD'S CLAIM

89. My finding that the Landlord repudiated its obligations under the Lease and that the Lease came to an end on 1 August 2017, does not extinguish rights which may have crystallised prior to termination.

[22] *Forslind* (1922) SC (HL) 173 at 192.

That proposition is made clear in the majority judgment in *Westralian Farmers Limited v Commonwealth Agricultural Service Engineers Ltd*.[23] In that case, Dixon and Evatt JJ stated:

> In general the termination of an executory agreement out of the performance of which pecuniary demands may arise imports that, just as on the one side no further acts of performance can be required, so, on the other side, no liability can be brought into existence if it depends upon a further act of performance. If the title to rights consists of vestitive facts which would result from the further execution of a contract but which have not been brought about before the agreement terminates, the rights cannot arise. But if all the facts have occurred which entitle one party to such a right as a debt, a distinct chose in action which for many purposes is conceived as possessing proprietary characteristics, the fact that the right to payment is future or contingent upon some event, not involving further performance of the contract, does not prevent it maturing into an immediately enforceable obligation. [24]

90. Accordingly, any arrears of rent or outgoings up until 1 August 2017 remain payable by the Tenant to the Landlord. Similarly, any other amounts which were due and payable under the Lease prior to termination also remain payable. In addition, the obligation to reinstate the Premises following termination of the Lease survives termination. Therefore, even though the Tenant ended the Lease consequent upon the Landlord's repudiation, the Tenant is not absolved of its obligation to make good upon vacating the Premises.

91. Details of the Landlord's counterclaim are set out in a document filed on 30 May 2018. There are eight categories of loss claimed; namely:

Category	Description	Amount claimed
1	Money owing under lease at time of termination	$4,163.80
2	Enforcement costs	$3,082.75
3	Make good/reinstatement costs	$21,069.99
4	Costs of securing new lease	$5,103.70
5	Rent and outgoings forgone after termination	$73,093.38
6	Difference between Lease rental and rent expected over balance of term	$108,460.14

[23] (1936) 54 CLR 361
[24] Ibid at pages 379-380

Subtotal	$214,973.76
Less bank guarantee retained by landlord	($22,000)
Total	$192,973.76

92. In addition, the Landlord claims interest pursuant to Clause 27 of the Lease, or alternatively under s 3 of the *Penalty Interest Rates Act 1983.* What follows are my observations and findings concerning the Landlord's counterclaim.

Money owning under Lease at time of termination

93. There are five subcategories of loss and damage claimed under this head.

Major service of air-conditioner ($698.50)

94. The Landlord claims the cost of servicing the air-conditioner during the currency of the Lease. It relies upon an invoice from *Plumbfirst* dated 4 November 2016, which describes the following work undertaken by that contractor:

> Major service on 16 Kw Daikin Package Reverse Cycle A/C $635 + GST

95. Referring to the above invoice, Mr Kerlidis gave the following evidence:

> "Major Service": the tenant was at that stage obviously in the first sixth months in the tenancy. They weren't undertaking the maintenance as set up by the lease so I had to maintain the air-conditioning system. Their expensive systems. Its commercial grade. So we undertook that with notice. We told them we going to do it and they refused to do it.

96. There is no evidence contradicting the evidence of Mr Kerlidis on this point. In fact, email correspondence dated 21 June 2017 from Mr Norris-Ongso and referred to above is consistent with Mr Kelridis' evidence that no maintenance contract was entered into by the Tenant. That being the case, I find that this expense arises as a result of the Tenant breaching its obligations under special condition 1(e)(i) of the Lease. Consequently, this aspect of the Landlord's claim is accepted.

Legal fees for default notices dated 6 December 2016 ($2,200) and 20 April 2017 ($825)

97. Clause 31.1 of the Lease states, in part, that the Tenant must pay promptly on demand by the Landlord:

> (c) the Landlord's costs, charges and expenses including those:
>
> …

(iv) in connection with the Tenant's default; and

98. In my view, the Landlord is entitled to be reimbursed for the cost of engaging solicitors to prepare and serve a default notice, subject to the amount charged being reasonable and there being substance to the default notice.

99. A copy of a default notice dated 6 December 2016 was produced by the Landlord. The default notice alleges that a part of the Premises had been used for a use other than the permitted use as described under the Lease. In particular, the default notice alleged that part of the Premises was used as a law office by Mr Norris-Ongso when conducting his legal practice known as *IPT Law*.

100. Evidence was given by both Mr Kerlidis and Mr Norris-Ongso on this issue. In addition, photographs were produced which showed signwriting affixed to the upstairs offices advertising *IPT Law*. Having regard to that evidence and the photographs, I find that a small part of the Premises was being used as an office for running the business *IPT Law*. This is contrary to Item 18 of the Schedule to the Lease, which provides that the *Permitted Use* is:

> Pilates and barre studio and associated uses

101. Although I accept that the term *associated uses* may encompass office space, I do not accept that the term would include office space used for a separate and distinct business unconnected with the Pilates and Barre studio business.

102. Mr Norris-Ongso gave evidence that he ceased using the Premises for his law office on 23 November 2016. However, the photographs produced by the Landlord show his legal firm's signage still affixed to the glass partition walls as at the date when the Lease came to an end. Moreover, correspondence from Mr Norris-Ongso under the letterhead *IP Law* and dated 27 April 2017 to the City of Port Phillip states, in part:

> I am a director of S3 Sth Melb Pty Ltd which is a tenant under the lease and the owner/operator of the Pilates studio business at 124 Bank Street;
>
> I am also a lawyer;
>
> I am also a director of 4 other companies;
>
> I use the upstairs office on a part-time basis for all of my businesses.
>
> On occasion, on average once per month, I meet clients in my office….
>
> …

> I would appreciate your opinion on whether or not a planning permit is required or whether the current use complies with the existing planning permit.

103. I do not accept that Mr Norris-Ongso ceased using the Premises to conduct his law practice from 23 November 2016. That evidence is inconsistent with the photographs produced by the Landlord and the email correspondence referred to above.

104. Consequently, I find that the Tenant was in breach of the Lease by conducting a law practice from the Premises. Accordingly, I find that the Landlord was entitled to instruct solicitors to issue a default notice in respect of that breach and be reimbursed for the reasonable costs of issuing the default notice.

105. In support of this expense, the Landlord produced an invoice from *Hall & Wilcox Lawyers* in the amount of $2,200. The invoice describes the work as: *Fixed fee per agreement.*

106. However, there is little or no evidence linking the charge of $2,200 to the cost of issuing the default notice. The only evidence given by Mr Kerlidis is:

> … *they're the legal costs Hall & Wilcox default notice number 1*.

107. I do not accept the $2,200 represents a reasonable cost to prepare and serve a default notice. My view is supported by the fact that the Landlord only claims $825 in respect of a second default notice which is served on or about 20 April 2017.

108. The second default notice was prepared by a different law firm; namely, *McKean Park*. That notice also alleges that the Tenant failed to use the Premises exclusively for a Pilates and Barre studio and associated use, in addition to raising other complaints. Given my finding that the Tenant was conducting a business other than what was permitted under the Lease until at least until 27 April 2017, I find that the Landlord was within its rights to serve the Tenant with that second default notice

109. There is no invoice from *McKean Park* in the amount of $825. However, the notice itself states that the costs of and incidental to the preparation and service of the notice is $825. In my view, that amount best represents the reasonable costs of preparing and serving a default notice. Accordingly, I will allow that that amount in respect of both default notices served on the Tenant.

Outgoings to 1 August 2017

110. The Landlord claims arrears of outgoings up until 1 August 2017. The outgoings relate to water and municipal rates and usage charges, as follows:

Outgoing	Amount
South East Water pro rata to 1 August 2017	113.56
City of Port Phillip pro rata to 1 August 2017	326.74
TOTAL	**$440.30**

111. It is common ground that the Tenant was responsible for the payment of outgoings which included water and council rates together with usage charges. Invoices in respect of the two amounts claimed were produced which confirm the charges. Accordingly, I find this aspect of the Landlord's claim proven in the amount of $440.30.

Enforcement costs ($3,082.75)

112. The Landlord claims legal fees in the amount of $3,082.75, representing legal work undertaken by *McKean Park* and described in its invoice dated 10 July 2017. That amount represents legal work over the period 9 May to 16 June 2017. That legal work covers the period that this proceeding was on foot and appears, at least in part, to deal with the *party and own client costs* of and associated with this proceeding.

113. Section 92 of the *Retail Leases Act 2003* provides, in part:

> (1) Despite anything to the contrary in Division 8 of Part 4 of the **Victorian Civil and Administrative Tribunal Act 1998**, each party to a proceeding before the Tribunal under this Part is to bear its own costs in the proceeding.
>
> (2) However, at any time the Tribunal may make an order that a party pay all or a specified part of the costs of another party in the proceeding but only if the Tribunal is satisfied that it is fair to do so because –
>
> (a) the party conducted the proceeding in a vexatious way that unnecessarily disadvantaged the other party to the proceeding; or
>
> (b) the party refuses to take part in or withdrew from mediation or other form of alternative dispute resolution under this Part.
>
> (3) In this section, "costs" includes fees, charges and disbursements.

114. The Landlord contends that it is entitled to reimbursement of its legal costs because the Lease requires the Tenant to reimburse the Landlord for the costs *in connection with the Tenant's default*.

115. There is insufficient evidence that the legal costs claimed under this head of damage can be identified as costs in connection with the Tenant's default. The period over which the legal costs are claimed coincide with the running of this proceeding and in all likelihood, simply represent costs of the proceeding.

116. Even if some of the costs incurred over the relevant accounting period relate to costs *in connection with the Tenant's default*, I consider that those costs do not, thereby, lose their character as costs of the proceeding. That being the case, s 92 of this *Retail Leases Act 2003* prohibits recovery of those costs unless the two exceptions referred to above are satisfied. There is no evidence before me that the Tenant has conducted the proceeding vexatiously or that it has refused to take part in or withdrew from mediation.

117. Section 94 of the *Retail Leases Act 2003* provides:

> (1) A provision of a retail premises lease or of an agreement (whether or not the agreement is between the parties to a retail premises lease) is void to the extent that it is contrary to or inconsistent with anything in this Act (including anything that the lease is taken to include or provide because of a provision of this Act).

118. Consequently, I find that the amount claimed under the heading *Enforcement costs* is not recoverable and that aspect of the Landlord's claim is therefore dismissed.

Make good ($21,069.99)

119. There are five categories of expense or loss that the Landlord claims under the head of damage representing the cost to make good or reinstate the Premises.

120. Clause 19.1 of the Lease provides:

> The tenant must vacate the Premises on the earlier of the Expiry Date and the date this lease is terminated and, subject to clause 14.2(b)(ii), before vacating in the Premises, unless otherwise agreed by the Landlord, the Tenant must:
>
> (a) Make Good the premises back to base building configuration as per the attached base building plan attached under an annexure B; and
>
> (b) …

Replace glass, install handle ($499.99)

121. The Landlord produced an invoice from *MRI Aluminium Windows* dated 24 August 2017 in the amount of $499.99. The invoice described the work undertaken as:

> 100% for the replacement of glass 6.38 clear laminate (600 mm x 900 mm) and installation of stainless steel handle (600 mm)

122. There is no evidence as to what this expense related to, apart from the description of the work as set out in the invoice itself. Mr Kerlidis' evidence simply made reference to the invoice but failed to explain how that work was tied to making good or reinstating the Premises.

123. In the absence of any clear evidence explaining how this work relates to making good or reinstating the Premises, I find the claim unproven.

Painting ($10,450)

124. The Landlord produced an invoice dated 25 August 2017 from *Colour Splash Painting Decorating Pty Ltd* in the amount of $10,450. The invoice describes the work as:

> Repainting 124 bank Street South Melbourne
>
> Repainting all interior - includes paint and labour

125. The evidence in support of this expense is limited. Mr Kerlidis said that there was some damage to the internal walls. During cross examination, Mr Kerlidis was asked why the whole of the Premises had to be painted. He answered:

> There were components that weren't painted. So I can categorically state that the black ceiling and the soffit of the concrete didn't get painted…
>
> So the bits that got painted were those components of the fit-out of which necessitated to be repainted.

126. It is difficult to ascertain from that limited evidence whether the area that was re-painted was required to be repainted in order to reinstate the Premises to a condition *back to base building configuration*. This is particularly the case in circumstances where Mr Kerlidis conceded that the repainting occurred approximately 18 months after the Premises had first been painted as part of the tenancy fit out.

127. Further evidence was given by Mr Kerlidis that there was damage to plasterboard walls when mirrors were removed. The cost of plastering represents a separate head of damage. Nevertheless, I accept that re-plastered walls would need to be repainted and that this expense can be attributed to removing the Tenants fit out. However, there is little or no evidence tying the balance of the internal painting to returning the Premises to a *condition back to base building configuration.*

128. In my view, it is likely that not all of the internal painting represents returning the Premises to a condition back to base building configuration. The balance of the internal painting was likely undertaken to rejuvenate the Premises in readiness for marketing the

Premises for re-lease. Accordingly, I will allow 75% of invoice, which I find attributable to the cost of returning the Premises to a condition *back to base building configuration*. That amounts to $7,837.50.

Plastering internal wall ($1,320)

129. As indicated above, Mr Kerlidis gave evidence that internal plasterboard walls were damaged when the Tenant's mirrors were removed. An invoice in the amount of $1,320 from *All Wall Plaster* dated 14 September 2017 was produced as evidence of that expense.

130. I accept Mr Kerlidis' evidence that this was an expense necessarily incurred to return the Premises to a *condition back to base building configuration*. Accordingly, I will order that the Tenant pay the Landlord $1,320 representing this head of damage.

Aluminium window and door frame ($8,800)

131. As already indicated, the Tenant had installed aluminium and glass partitions in the upper level of the Premises to create office space. It is common ground that the partitions were not removed when the Tenant vacated the Premises.

132. The Landlord claims $8,800, being the cost to remove the existing window and glass partitions. An invoice from *MRI Aluminium Windows* dated 7 May 2018 in that amount was produced as evidence of the expense.

133. Mr Kerlidis gave evidence that the petitions were removed, albeit at different times prior to reletting the Premises. He confirmed that the $8,800 has been paid.

134. I accept Mr Kerlidis' evidence that this was an expense necessarily incurred to return the Premises to a *condition back to base building configuration*. Accordingly, I will order that the Tenant pay the Landlord $8,800 representing this head of damage.

Repainting a facade ($1,760)

135. The Landlord claims $1,760, being the cost to repaint the facade consistent with its colour at the commencement of the Lease. Mr Kerlidis gave evidence that:

> The tenant had painted the exterior of the building without landlord consent and we, as I say, had to repainted and bring it back into uniform colour between both buildings.

136. Mr Norris-Ongso conceded that the Tenant had painted the facade of 124 Bank Street and that it differed from the adjoining premises. However, he said that the Tenant had repainted the facade back to its original colour. Mr Kerlidis acknowledged that some attempt been made to repaint the facade. However, he said that the colour did not

adequately match the facade of the adjoining property, which necessitated repainting the facade again.

137. I accept Mr Kerlidis' evidence on this point. In my view, it would not make sense for the Landlord repaint the façade if that work had already been done adequately by the Tenant. In all likelihood, the facade was repainted by the Landlord because it did not adequately match the adjoining facade. Therefore, I consider this was an expense necessarily incurred to return the Premises to a *condition back to base building configuration*. Accordingly, I will order that the Tenant pay the Landlord $1,760 representing this head of damage.

New Lease ($5,103.70)

138. The Landlord claims the costs of marketing, advertising and legal costs associated with entering into a new lease, after the tenancy came to an end. The total amount claimed is $5,103.70, made up as follows:

    (a) Marketing and advertising: $1,375

    (b) Marketing and advertising: $660

    (c) Legal fees: $3,068.70

139. In my view, given that the Tenant lawfully determined the Lease on 1 August 2017, there is no basis upon which to claim for the cost of marketing, advertising and legal costs associated with entering into a new lease. This aspect of the Landlord's claim will be dismissed.

Rent and outgoings foregone after termination

140. The Landlord claims damages representing rent and outgoings that would have been paid under the Lease, had the Lease continued. It claims damages under this head up until rental was received under a new lease entered into with a third party.

141. As is the case with the Landlord's claim for the costs associated with entering into a new lease, damages which accrue post termination are not recoverable. This aspect of the Landlord's claim is dismissed.

Difference between rent payable under terminated lease and rent expected over balance of term

142. Similarly, the difference between the rent payable under the Lease to the rent payable under the new lease cannot constitute damages in circumstances where the Lease was lawfully ended by the Tenant. This aspect of the Landlord's claim is also dismissed.

Conclusion on Landlord's claim

143. Having regard to my findings set out above, I assess the Landlord's loss and damage consequent upon the Lease coming to an end as follows:

Head of damage	Amount
Money owed at time of termination	
Major service of air conditioner	$698.50
Legal fees for default notices	$1,650
Outgoings to 1 August 2017	$440.30
Make good/reinstatement costs	
Internal painting	$7,837.50
Plastering internal walls	$1,320
Removal of internal partition walls	$8,800
Repainting the façade	$1,760
Cost of new lease	
Lettable Area Plan	$0
Legal costs to draft new lease	$0
Rent and outgoings foregone after termination	
Rent foregone	$0
Outgoings foregone	$0
Difference between old and new rent	$0
Subtotal	S22,506.30
LESS SECURITY DEPOSIT HELD	($22,000)
Total	**$506.30**

INTEREST

144. The Landlord also claims interest pursuant to clause 27 of the Lease alternatively under s 2 of the *Penalty Interest Rates Act 1983* or s 91(2) of the *Retail Leases Act 2003*.

145. Clause 27 of the lease states:

> **27.1 Default**
>
> If a party does not pay an amount due under this lease on time, that party is in default.
>
> **27.2 Interest**
>
> The party in default must pay interest on the amount in default.

146. Clause 27.1 entitled the Landlord to charge interest on amounts due under the Lease if not paid at the time specified under the Lease. It is

not clear what, if any of the amounts claimed by the Landlord were due under the Lease and if so, when they were due.

147. Accordingly, I do not accept that any interest is payable under clause 27 of the Lease.

148. Further, the Landlord made no submission as to why it would be appropriate for interest to be awarded under s 91(2) of the *Retail Leases Act 2003*. In the absence of any compelling argument that interest should be awarded, I decline to do so. This aspect of the Landlord's claim is also dismissed.

CLAIM AGAINST MR NORRIS-ONGSO

149. The Guarantor, Mr Norris-Ongso, is the Second Respondent to the Landlord's counterclaim. The claim against the Guarantor is pursuant to a guarantee and indemnity that he gave upon the Tenant entering into the Lease. Clause 25 of the Lease provides, in part:

> **25.1 Guarantee**
>
> The Guarantors, in consideration of the Landlord having entered into this lease:
>
> (a) unconditionally and irrevocably guarantee the punctual payment of Rent and all other money payable under this lease by the Tenant to the Landlord;
>
> …
>
> (c) must, on demand, immediately pay to the Landlord any amount of Rent or other money not paid by the Tenant on its due date that the Landlord is entitled to recover from the Tenant; and
>
> …
>
> **25.2 Indemnity**
>
> The Guarantors unconditionally and irrevocably indemnify the Landlord for any loss suffered by the Landlord, directly or indirectly if for any reason:
>
> (a) the Tenant does not promptly perform any of the Tenant's obligations under this lease
>
> …

150. It is not contested that the Guarantor is the sole guarantor named in the Lease; nor is it contested that the guarantee and indemnity operates to bind the Guarantor. Mr Deller submitted that in those circumstances, he is liable to pay the Landlord for any loss or damage or arrears in rent or outgoings if the Tenant fails to pay.

151. I accept that the guarantee and indemnity obliges the Guarantor to indemnify the Landlord for its loss and damage. Therefore, I find that the Guarantor is liable to pay the Landlord to the extent that the Tenant does not make payment to the Landlord of the amount ordered.

CONCLUSION

152. Having regard to my findings set out above, I determine that the Tenant is entitled to the return of the security deposit in the amount of $22,000 and the Landlord is entitled to damages in the amount of $22,506.30.

153. In my view, the most appropriate course is for the two amounts to be set off against each other, with the result that the Tenant and the Guarantor must pay the Landlord $506.30.

DEPUTY PRESIDENT E. RIEGLER