

VICTORIAN CIVIL AND ADMINISTRATIVE TRIBUNAL

CIVIL DIVISION

BUILDING AND PROPERTY LIST

VCAT REFERENCE NO. BP863/2016

CATCHWORDS

Retail lease, assessment of damages, three categories of damages: costs associated with new lease, rent and outgoings forgone and difference between rent under termination lease and lease to new tenant.

APPLICANT	S3 Sth Melbourne Pty Ltd
RESPONDENT/APPLICANT BY COUNTERCLAIM	Red Pepper Property Group Pty Ltd t/as The Red Pepper Property Group Trust (ABN: 53 299 668 365)
RESPONDENT BY COUNTERCLAIM	Mr Paul Anthony Norris-Ongso
WHERE HELD	Melbourne
BEFORE	L Forde, Senior Member
HEARING TYPE	Hearing
DATE OF HEARING	24 October 2019
DATE OF ORDER	13 November 2019
CITATION	S3 Sth Melbourne Pty Ltd v Red Pepper Property Group Pty Ltd (Building and Property) [2019] VCAT 1794

ORDER

- 1 I declare the respondent's damages on its counterclaim are \$151,009.47.
- 2 The applicant and respondent by counterclaim must pay the respondent the sum of \$151,009.47.

L Forde
Senior Member

APPEARANCES:

For Applicant and Respondent by Counterclaim Mr DC Gration of counsel

For Respondent Mr JDS Barber of counsel

REASONS

- 1 Following a successful appeal by Red Pepper Property Group Pty Ltd (**landlord**) from Tribunal orders made on 25 October 2018, the proceeding was remitted to the Tribunal, differently constituted, for an assessment of damages on the landlord's counterclaim¹ against the tenant and its guarantors.
- 2 It is common ground that the landlord leased part of premises at 124 Bank Street, South Melbourne to S3 Sth Melbourne Pty Ltd (**tenant**) for a term of 5 years commencing 1 March 2016 at an annual rent of \$80,000 plus GST. The guarantors were the respondents. The lease terminated when the tenant wrongfully vacated the premises on 1 August 2017.
- 3 The landlord relet the premises effective 1 May 2018 to Longboat Holdings Group No 3 Pty Ltd (**new tenant**) for a lesser rent than payable under the tenant's lease.
- 4 The damages remitted for assessment on the landlord's counterclaim against the tenant Mr Norris-Ongso are:
 - a the costs associated with the new lease;
 - b rent and outgoings forgone after termination; and
 - c the difference between rent under the terminated lease and the rent expected from a new lease.
- 5 The landlord seeks damages of \$167,891.82.

Category 1 damages - Costs associated with the new lease

- 6 The landlord claims the following:

Re-Letting Costs (ex GST)

Teska Carson for advertising:	SCB 733	\$1,250.00
Realserve for floor plan:	SCB 734	\$600.00
McKean Park for new lease:	Partics of L&D attachmt 6	\$2,789.74
Total:		\$4,639.74

- 7 The tenant accepts liability to pay the Teska Carson advertising fee of \$1,250.
- 8 The tenant disputes the Realserve floor plan fee as a legitimate reletting cost on the basis that it was unnecessary.
- 9 The tenant also disputes the legal costs paid to McKean Park for the new lease. I find that the Realserve fee was a legitimate cost of reletting because:
 - a a prospective tenant disputed the lettable area;

¹ Red Pepper Property Group Pty Ltd v S3 STH Melb Pty Ltd and anor [2019] VSC 41

- b the advice from Tesca Carson, the landlord's agent, was that the survey was required for future market reviews and was necessary²; and
- c the fee was incurred in the mitigation of the landlord's loss.

- 10 The tenant disputes the fees McKean & Park charged for the preparation of the lease to the new tenant on the basis that the new lease was an uncommercial transaction and as such the costs associated with the transaction cannot be claimed. For the reasons given when addressing category 3 damages, I reject this position. The legal costs are a legitimate cost of reletting the premises.
- 11 I assess the landlord's damages for the reletting costs at \$4,639.74.

Category 2 damages - Rent and outgoings forgone

- 12 The landlord claims \$66,796.44 for lost rent and outgoings for the period between the date the tenant vacated the premises and when the new lease commenced. The figure is calculated as follows:

Rent and Outgoings Forgone (ex GST)

2 Aug -31 Aug 17 @ \$83,200 pa or \$6,933.33 pcm	\$6,709.67
September 17	\$6,933.33
October 17	\$6,933.33
November 17	\$6,933.33
December 17	\$6,933.33
January 2018	\$6,933.33
February 2018	\$6,933.33
March 2018 (4% increase as per lease to \$86,528 pa)	\$7,210.66
April 2018	\$7,210.66
Outgoings – South East Water 28 July 17 SCB 762 (no GST)	\$161.22
Outgoings – South East Water 27 Oct 17 SCB 762 (no GST)	\$144.42
Outgoings – City of Port Phillip 28 Jul 17 SCB 753 (no GST)	\$3,193.62
Building Insurance - IMC Insurance Brokers - 13 Aug 17 SCB 747-52	
\$2119.25 - \$176.64 (GST) = \$1,942.61 @ 29.147%	\$566.21
Total:	<u>\$66,796.44</u>

- 13 The tenant accepts liability to pay the rent and outgoings claimed except for the March 2018 rent and part of the April 2018 rent. Liability for rent for these two periods is disputed on the basis that the landlord knew by 19

² Landlord's tender bundle (LTB) 825, 864

March 2018 that an agreement had been struck with the new tenant and as such cannot claim any rent and outgoings after this date.

- 14 The landlord submits that if I accept that the new lease was legitimate, then the tenant must be liable to pay forgone rent and outgoings until the new lease commenced.
- 15 For the reasons set out when addressing the third category of damages, I reject the tenant's submissions. The landlord is entitled to all forgone rent and outgoings for the period between the termination of the lease and the commencement date of the new lease. The liability does not cease when the landlord knew it had secured a new tenant. It only ceased once the new lease commenced which was about 6 weeks later.
- 16 I assess the landlord's damages for lost rent and outgoings at \$66,796.44.

Category 3 damages- Difference between rent under the terminated lease and the new lease

- 17 The landlord claims damages for the difference between the terminated lease rent and the new lease rent of \$96,455.64 assessed as follows:

Difference between rent payable under terminated lease and rent expected over balance of term (ex GST)

Old lease: rent between 1 May 2018 and 28 February 2021:

10 months @ \$7,210.66 (\$86,528 pa)	\$72,106.60
1 year @ \$89,989.12	\$89,989.12
1 year @ \$93,588.68	<u>\$93,588.68</u>
Sub-total:	\$255,683.96

New Lease: rent between 1 May 2018 and 28 February 2021:

1 year @ \$65,000 less 5 months rent-free	\$37,916.66
1 year @ \$66,170 (1.8% CPI increase)	\$66,170.00
10 months @ \$5,514.16	<u>\$55,141.66</u>
Sub-total:	<u>\$159,228.32</u>

The claim is for the difference between the new rent: \$96,455.64

- 18 The total of the category 1, 2 and 3 damages is accordingly \$167,891.82.
- 19 It is common ground that the landlord took reasonable steps to relet the premises for at least 7 months without success. The lack of carparking in a heavily congested area was cited by the letting agent as the main reason for the premises remaining unlet.

- 20 The landlord's position is that it then made a commercial decision to let the premises to a related company at a reduced rent and on terms more favourable to the tenant than in the tenant's lease.
- 21 The tenant submits that by leasing to a related company on less commercial terms, the landlord entered into an uncommercial or sham transaction which severed the causal connection between its loss and the tenant vacating the premises. It says the new lease is an intervening cause, and the landlord by its own conduct lost the opportunity to relet on more commercial terms. As such no loss or damage was suffered after 19 March 2018 being the date the landlord knew it had a new tenant in place.
- 22 The landlord relied upon the decision in *Sharrment Pty Ltd v Official Trustee in Bankruptcy*³ to determine whether the transaction was a sham. Megarry J was quoted in that case as saying
- Mere circumstances of suspicion do not by themselves establish a transaction as a sham; it must be shown that the outward and visible form does not coincide with the inward and substantial truth.
- 23 In support of its position, the tenant relied on the following matters: -
- a Mr Theodore Kerlidis is a director of both the tenant and the new tenant, Longboat. He is the sole shareholder of Longboat; Longboat is the trustee of a unit trust. Mr Kerlidis has a 7% interest in the unit trust and two family members also have a joint 7% interest⁴;
 - b in November 2017, Mr Kerlidis discussed the possibility of Longboat leasing the premises with another Longboat director Mr Nick Makridi. The proposed use was as display units for another project;
 - c the rent under the new lease is for \$65,000 per annum, a significant reduction from the previous lease's \$83,000 per annum. The new lease gave a 5 month rent free period when the industry standard is 3 months, the new lease allowed CPI increase whereas the original lease required 4% fixed rent increases. The new lease had no directors' guarantees whereas the old lease required them. Previously the landlord had said it would only waive guarantees if an 8 or 9 month bank guarantee was in place, and this requirement was omitted.
 - d the new lease rent of \$65,000 per annum was well below the letting agent's recommendation of the market rent;⁵
 - e the landlord had been largely inflexible with its rent figure and security terms before letting the premises to Longboat. It had only agreed to reduce the rent to \$80,000 to a prospective tenant⁶ and

³ 18 FCR 449

⁴ Oral evidence of Mr Kerlidis given at hearing

⁵ LTB 779

⁶ LTB 825-840 & 899

rejected letting without director's guarantees unless extended bank guarantees were provided;⁷

- f the market rent was \$80,000. Tesca Carson provided a report to the landlord's lawyers on 30 November 2017 in which it was asked 'At what rental do you expect the property to be leased?'"⁸ The response was

We are seeking \$82K pa Net with outgoings and another \$7,500 pa approx. If we lower the rental to \$80K pa Gross (including outgoings) parties may forego the car parking requirement as a major priority and compensate for this based on a lower rent. The question of rent has not been a blocking factor in discussions with parties. It's more been a suitability of premises for use and availability of parking for directors and clients within the vicinity.

- g in March 2018 the landlord dropped the rent to \$67,000 in the new lease notwithstanding Tesca Carson's advice of \$80,000 pa rent being fair;

- h the landlord was confident on 19 March 2018 that the Longboat lease was going to be signed;⁹

- i Mr Makridi's use of the nomenclature "Mr Kerlides" in emails on 21 March 2018 was artificial¹⁰ given he usually referred to him on a first name basis;

- j the landlord was advised it was leasing on uncommercial terms by its lawyers. The landlord's lawyers in addressing the new lease wrote to the landlords saying:

Ignoring the relationship of the Landlord and Tenant for a moment, a lease without guarantees and only one month security deposit is well below current commercial terms.¹¹

- k the landlord was in the middle of the VCAT proceedings when it agreed to the new rent and it entered into the new lease so that it could amend its counterclaim to increase the damages claim to allow for rent shortfall over the life of the lease; and

- l the landlord acknowledged that the new lease was not on commercial terms¹²

24 Counsel for the tenant relied upon the decision of *Golden Strait Corporation v Nippon Yusen Kubishka Kaisha*¹³ in support of the tenant's position that the premises should have been relet on a more commercial

⁷ LTB 853

⁸ LTB 1030 - 1032

⁹ Above 3

¹⁰ LTB 1055

¹¹ LTB 1095

¹² Above 3

¹³ [2007] UKHL 12

basis. That case is premised on there being an available market for the chartering of vessels or, to correlate it to this case, the availability of tenants for the premises on more commercial terms than given to Longboat. There is no evidence of an available market in the present case.

- 25 Reliance was also placed by the tenant on the decision of *Gumland Property Holdings Pty Limited v Duffy Bros Fruit Market (Campbelltown) Pty Limited*¹⁴ as authority for the proposition that the landlord can only recover loss of bargain damage if they tried unsuccessfully to obtain a new tenant at the rent stipulated in the terminated lease. There is nothing contentious in this position. The tenant submits that the landlord should have told the agent to market the premises at \$75,000 pa and test the market then drop it again if necessary and test the market. It claims there was no attempt to test the market.
- 26 The landlord's position can be briefly summarised as follows:
- a nowhere in the pleadings does the tenant raise a sham transaction;
 - b the advice given to the landlord from McKean & Park about terms not being commercial was not related to the rent.¹⁵ The absence of a bank guarantee or director's guarantee does not impact the claim against the tenant. It is unconnected to loss;
 - c the transaction is not a sham because of artificial formality in communication between Mr Kerlidis and Mr Makridi. The emails show the relationship was strained as explained by Mr Kerlidis because of the hard-bargaining position adopted by Mr Makridi;
 - d the property was vigorously marketed. After trying to relet the premises for more than 7 months it made the best decision it could to secure a tenant and mitigate its loss;
 - e it had offered reduced rent and was advised by its agent that the rent was not the issue but rather the lack of parking¹⁶;
 - f the rent under the new lease is not uncommercially low in the context of previous attempts to let the premises and the agent's advice of offering \$80,000 inclusive of outgoings.¹⁷ Outgoings are \$7500 so the rent for an all up rent of \$80,000 inclusive is really \$72,500 plus outgoings of \$7500. The current rent is \$67,000 which is about 10% lower;
 - g rather than being a sham the new lease is the only lease that the landlord was able to arrange;

¹⁴ [2008] 234 CLR 237

¹⁵ Above 10

¹⁶ *ibid*

¹⁷ LTB 1032

- h given his 7% interest in the unit trust of which Longboat is a trustee, there was no commercial incentive for Mr Kerlidis to act in a sham way; and
 - i securing a tenant at a reduced rent was better than having the property sit vacant for an unpredictable amount of time. The lower rent was accepted because there had been no other offer and the premises had been on the market for more than seven months. Furthermore, the leasing agent outlined a consistent problem with letting the premises with a lack of car parking and was unable to give any indication as to when the premises might be let;¹⁸
- 27 I accept on the basis of the advice from the letting agent that the main reason the property remained vacant was due to a lack of on-site car parking which was a consistent issue for prospective tenants. It was accepted by the parties that parking around the premises was extremely limited.
- 28 The history shows that the original recommendation from Teska Carson that the rental rate of \$83,000 per annum for the premises was in line with current market expectations¹⁹ was not correct. Active marketing for 7 months did not produce a tenant.
- 29 This recommendation was varied on 30 November 2017 when a suggestion of an all-inclusive rent of \$80,000 was made by Teska Carson. In this regard I reject the interpretation of the recommendation adopted by the tenant, as the plain words clearly show that the suggestion was a rent of \$80,000 which included outgoings. To suggest otherwise is to ignore the words. Furthermore, the alternative implies that the agent believed that a mere \$2,000 pa rent reduction would produce a tenant. This cannot be the meaning.
- 30 While the property was not actively marketed at a lower rate, the letting to Longboat was not at such a reduced rent compared with the Teska Carson suggestion of \$80,000 “all up” that it can be viewed as uncommercial.

Findings

- 31 The new lease is not intended to be mistaken for anything other than a new lease at a reduced rate and on different terms. This does not make it a sham.
- 32 Mr Kerlidis has a connection and interest in both the landlord and Longboat. This does not of itself make the new lease a sham transaction. However, it does explain why the landlord did not require guarantees. It knew the risk.
- 33 I am satisfied on the evidence that the market had not produced a tenant willing to pay at or near the previous rent of \$83,000 by March 2018. There is no evidence to show when a tenant might otherwise have been secured to

¹⁸ Above 3

¹⁹ LTB779

pay that rent. The only evidence is that the letting agent was unable to provide any indication other than “how long is a piece of string”.²⁰

- 34 In the circumstances it was reasonable for the landlord to proceed with the new lease at the reduced rent.

Rent-free period

- 35 I am not satisfied that the landlord attempted to get a better commercial deal on the rent-free period. Unlike the rent amount, no evidence of negotiation on this issue was provided. A three-month rent-free period is the usual period for such a lease. Given the lower rent, I think it more likely than not that Longboat would have agreed to a three-month rent free in lieu of the five-month period it secured. Accordingly, I will deduct two months of the rent claimed from the amount the landlord seeks. The rent was \$7,210.66 in March and April 2018 making a total to be deducted of \$14,421.32. The amount of rent differential I will allow is \$82,034.32.
- 36 The landlord is being compensated for rent it would not have received until a later point in time. On this basis it is appropriate to discount the figure to bring it to present day values. In the absence of specific figures being suggested by the parties I will discount the amount by 3%.
- 37 On the rent differential claim I assess the landlord’s damages at \$79,573.29.
- 38 For the reasons provided, I assess the damages on the landlord’s counterclaim at \$151,009.47.

L. Forde
Senior Member

²⁰ Above 3