

re:lease

law news for commercial landlords, tenants
and property managers

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Rent reviews: mind your step

How closely do the precise requirements of a rent review procedure in a lease need to be followed? A recent case before the High Court shows that strict adherence may be required; and exposed a risk for tenants and, possibly, an opportunity for landlords.

Background

In *Freehold Properties (Investments) LLP v Bridgeway Projects Ltd*, the landlord leased premises in Hamilton to the tenant under an Auckland District Law Society (4th Edition) form of lease. The lease provided for a market rent review on 1 July 2007.

The landlord gave notice on 10 October 2007 of its proposed new rent of \$104,780 (plus GST) (**Landlord's Notice**).

The tenant gave the landlord written notice, within the required 28 day dispute period, stating "the rental you propose is utterly preposterous and will be vigorously disputed" (**Tenant's Notice**).

On 29 November 2007, the landlord sent the tenant a rent valuation and offered a lower rent of \$96,720 plus GST (**Lower Rent Offer**). Almost a year later, on 17 November 2008, the landlord issued the tenant an invoice for rent arrears. Its rent calculations

were based on the Lower Rent Offer.

The tenant did not pay the increased rent (neither the rent set out in the Landlord's Notice or based on the Lower Rent Offer). The landlord accordingly sued the tenant for rent arrears. Its calculation of these arrears was based on the figure in the Landlord's Notice, being \$104,780 plus GST.

The tenant argued (amongst other things) that the rent had not been effectively increased to \$104,780 plus GST because:

- a it had, by the Tenant's Notice, disputed the rent; and
- b the landlord's subsequent actions (particularly the Lower Rent Offer) amounted to a "waiver" of the landlord's right to rely on the Landlord's Notice.

Major question – was the Tenant's Notice sufficient to dispute?

The major question before the Court, therefore, was whether the Tenant's Notice was sufficient notice of rent dispute for the purposes of the rent review procedure in the lease.

The rent review procedure in the lease allowed the tenant to dispute the Landlord's Notice by giving

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“...without specifying a proposed alternative rent, the rent determination provision... is thwarted.”

written notice “disputing the annual rent proposed and specifying the annual rent proposed by the [tenant] as the current market rent...”. If such notice was given, the new rent was then to be determined in accordance with the procedure in clause 2.2 of the lease (that is, by arbitration).

It is settled law that, if a tenant wants to dispute a landlord’s rent review notice and instead have the rent determined by a third party, their notice must make this clear: it may not be sufficient for the tenant to simply express mere disagreement. The test is whether the terms of the notice are sufficiently clear to show “to the ordinary landlord” that the tenant is purporting to exercise the tenant’s right to have the rent determined by a third party.

The language used in this case (“the rental you propose is utterly preposterous and will be vigorously disputed”) would surely pass this test? However, the landlord argued that it was not proper notice under clause 2.1(b) of the lease because the tenant had not “specified the annual rent proposed by the [tenant] as the current market rent”.

The Court accepted the landlord’s argument with the result that the tenant had failed to dispute the Landlord’s Notice and was therefore deemed to have accepted it. It reached the conclusion that, without specifying a proposed alternative rent, the rent determination provision in clause 2.2 is “thwarted”. The landlord was accordingly able to claim the rent arrears, with accrued interest, at the level set out in the Landlord’s Notice.

Waiver argument

The tenant’s argument that the landlord had waived its right to rely on the Landlord’s Notice (for example by making the Lower Rent Offer) was not accepted. Waiver is generally the abandonment of a right and will often occur when the party who is entitled to it does some act which is inconsistent with the continued insistence on compliance with the relevant stipulation. The Court did not consider that anything the landlord had done indicated that it formally dispensed with the requirement in clause 2.1(b) that the tenant give notice of an alternative market rent. Instead, the Court regarded the fact that no formal steps had been taken to proceed with arbitration (which should have followed if the Tenant’s Notice was effective notice of dispute) supported the view that the Landlord’s Notice had not been properly disputed.

Points to note

The points to note from this case are:

- **Follow procedure:** There may sometimes be room to operate the rent review machinery outside the strict written requirements. This is because a stipulation may not necessarily be regarded as of the essence (for example, outside stipulated timeframes if these are not expressed to be of the essence). Whether the stipulation is essential (and failure to adhere to it therefore fatal to the process) depends on whether this is a

“...[you] may not need to be quick to accept that a notice given by the other party is effective...”

necessary implication from the terms of the clause as a whole. However, as *Freehold Properties v Bridgeway* shows, the risk is that a step taken may be regarded as invalid if it does not fully comply with the requirements set out in the rent review clause.

- **Preserve rent review procedure:** If you want to move outside the rent review procedure (for example, if you want to try and resolve the dispute by negotiation) but do not want to lose your right to insist on compliance with that procedure, make it clear that your actions (such as negotiations) are on a without prejudice basis. Note also that any agreement (outside the rent review procedure) settling a rent review dispute would need to satisfy the requirements of a contractually binding agreement to be enforceable.
- **Accept dispute?** The party initiating the rent review may not need to be quick to accept that a notice given by the other party is effective to dispute the proposed rent.
- **Act consistently with your position:** In this case, the tenant’s position was weakened by the fact that the parties had not proceeded to arbitration (which they should have done following a

successful dispute of the Landlord’s Notice).

In short, tread carefully when involved in a rent review that comes under dispute. Mind your step!

ADLS lease: up for review

The Documents and Precedents Committee of the Auckland District Law Society has formed a subcommittee to review the ADLS deed of lease form. The law profession will shortly be invited to submit comments. We would be interested to hear any concerns you have with the form of lease which should be communicated to the Committee.

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If you want to discuss the issues raised here, or have any other leasing queries, please contact Shieff England’s leasing team:

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This paper gives a general overview of the topics covered and is not intended to be relied upon as legal advice.

