SQUIRE PATTON BOGGS

Real Estate Roundup

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Evicting a Difficult Tenant

Evicting a difficult tenant from commercial premises is sometimes a difficult task, and a recent case in the Supreme Court of New South Wales, *West Asset v Sara Investments*,[1] highlights the potential problems.

A landlord can terminate a commercial lease for breach of covenant by the tenant in one of two ways, either physical re-entry of the premises, which is not prohibited in most jurisdictions in Australia, or commencing proceedings for possession of the premises in the Supreme Court.

Before a landlord can terminate a lease, the tenant must have breached a term or covenant of the lease and, subject to the comments below, failed to remedy the breach within the time specified in a notice of breach of covenant. Legislation in each jurisdiction in Australia specifies the terms to be included in the notice.

It is important to note that, except in Queensland and the Northern Territory, the legislation does not require service of a notice of breach of covenant for non-payment of rent. However, as is often the case, a lease itself may require notice to be given to the tenant, and the legislation will not override this requirement.

When a landlord becomes entitled to re-enter or forfeit a lease, the tenant effectively becomes a trespasser. Except in the Northern Territory, legislation does not prohibit a landlord from recovering possession of premises by re-entry; however, the landlord must not use more force than is necessary to re-enter the premises. Physical re-entry usually involves employing commercial agents to obtain possession and to prevent the tenant re-entering and to change the locks of the premises.

Commencing and prosecuting court proceedings for possession involves both cost and delay, which hampers the landlord's ability to relet the premises. For this reason, most landlords choose the lock-out alternative rather than commencing proceedings.

The facts in *West Asset v Sara Investments* are complicated but, in summary, West Asset contracted to buy a warehouse from Sara Investments, which had granted a lease to a related company, Bulolo Investments. After protracted legal proceedings, the sale of the property was completed after the court made an order for specific performance of the sale contract. The sale was subject to Bulolo Investments monthly tenancy under its lease. The relationship between West Asset and Sara Investments/ Bulolo Investments was acrimonious prior to completion of the sale and appears to have further deteriorated after completion.

West Asset gave 30 days' notice to Bulolo Investments, terminating its monthly tenancy of its premises. Shortly after the notice expired, West Asset, together with four security guards and a locksmith, attended the property and sought to re-enter the premises. A confrontation then took place with the principal of Bulolo Investments and his daughter, who were evicted that day, leaving perishable goods and plant and equipment in the property. Further court proceedings were commenced in relation to these goods and plant and equipment.

Mr Justice Slattery commented that "Commercial landlords seeking to evict hostile tenants can avoid the risk of breaches of the peace by obtaining a judgment for possession and proceeding to eviction in an orderly way under the supervision of the [Court Sheriff]. The perceived attraction of direct eviction action is often illusory, as this case illustrates."

Takeaway

If properly arranged, a lock out should be the easiest, quickest and most cost-effective way of ejecting a defaulting tenant from premises.

However, in situations like those that existed in *West Asset v Sara Investments*, a landlord with a difficult or hostile tenant would be advised to remember the comments of Mr Justice Slattery and carefully consider whether a lock out was a preferable alternative to commencing proceedings for possession in the Supreme Court.

In such a situation, as the Romans said, "*festina lente*", or "make haste slowly" in deciding how to evict the difficult or hostile tenant.

1 *West Asset Holdings Pty Limited & Anor v Sara Investments (NSW) Pty Ltd & Anor* [2023] NSWCS 136.

What Are Your Rights if There is a Problem With the Title to Your Land?

Now that electronic conveyancing is a fact of life in Australia, it may be the case that the chances of errors or omissions occurring on the register of Torrens title land have increased.

At the time Torrens title was introduced, it was generally accepted that the state should compensate anybody who suffered a loss by relying on the register where it proved to be inaccurate.

All Australian jurisdictions provide for compensation to be paid on an indemnity basis to compensate a party for losses suffered. Compensation for loss may be claimed in different circumstances, one of which is error, misdescription or omission in the register.

In a recent New South Wales case, *Ausbao v The Registrar General*,[1] the purchaser contracted to buy 286 Sussex Street in Sydney for redevelopment. The property consisted of four separate lots in different deposited plans, which described the area of each of the four lots as having a total site area of 1,337.4 square metres. After completion, the purchaser discovered that the total site area was only 1,255.9 square metres.

In fact, the site area of one of the four lots (Lot 1) was 502.3 square metres rather than 588 square metres, as shown in the registered deposited plan – a difference in area of 85.7 square metres, which is significant in the CBD of Sydney.

What had happened was that 85.7 square metres of Lot 1 had been resumed by the commissioner for main roads in 1975 for road widening. Due to an error in the registrar general's office, a new certificate of title for Lot 1, issued in 1978, still (incorrectly) showed the site area as 588 square metres.

The purchaser consequently commenced proceedings against the registrar general for compensation under the Torrens Assurance Fund established under the Real Property Act 1900 (NSW) (Act).

However, to the detriment of the purchaser, under the Act, compensation is not payable in relation to any loss or damage suffered by a party "to the extent which the loss or damage is a consequence of any act or omission…" of that party.

In summarising the reasons for its decision that compensation was not payable, the Court of Appeal said that: "In the end result, a sophisticated investor embarked upon the multimillion-dollar purchase of a site for a proposed commercial development. As a result of its own internal analysis, the amount it offered was critically dependant on the accuracy of the statement of area in the Deposited Plans referred to in the Register. The [purchaser] wrongly assumed that those statements of area were infallible, whereas there was a real, albeit remote, risk that at least one of them was incorrect."

As was stated by the primary judge in the case, the material cause of any loss or damage suffered by the purchaser was its failure to "take any effective step to verify the site area" of the land it purchased.

While the purchaser carried out due diligence investigations in relation to the property, these did not include inspecting or obtaining a current survey of the property. The site area could easily have been verified if the purchaser had obtained an identification survey of the land to be purchased.

Takeaways

As was the case in *Ausbao v The Registrar General*, if land is being purchased for redevelopment or further development and floor space ratios are critical, an identification survey should be obtained as a matter of course.

As two of the High Court judges noted in *Svanosio v McNamara*,[2] "The making of a Survey is an ordinary precaution for a purchaser to take. Many purchasers, of course, decline to incur the expense involved in a Survey, and in many cases it may appear unnecessary, but, generally speaking, and in the absence of misrepresentation, a purchaser may fairly be regarded as omitting the precaution at his own risk."

There is no guarantee that the registered plan is accurate and free from errors, misdescriptions or omissions. If, in fact, the plan is inaccurate, *Ausbao v The Registrar General* highlights the fact that a party which suffers a loss because of an error, misdescription or omission may not be entitled to compensation from the state.

Whether you are a vendor or purchaser of land or a building, while obviously having regard to the physical configuration of the property, serious thought should be given to obtaining a survey before a contract for sale is entered into.

1 *Ausbao (286 Sussex Street) Pty Ltd v The Registrar General of New South Wales* [2023] NSWCA 18
2 *Svanosio v McNamara* (1956) 96 CLR 186

Enforcement of Incentive Clawback Clauses

In *BMG SP Pty Ltd v YFG Strathton Pty Ltd* [2023] QSC 52, the Supreme Court of Queensland held that a landlord's claim pursuant to an incentive repayment clause did not represent a genuine pre-estimate of loss and therefore amounted to an unenforceable penalty.

In this case, the incentive repayment clause was structured in the typical way – that is, if the lease was terminated, the tenant (BMG) would be required to repay a pro-rata amount of the incentive, based on the proportion of the lease term that had not expired. The landlord had paid BMG fit-out contributions totalling AU$1 million, and the lease was terminated due to BMG's repudiation within the first month of the term. The landlord's calculation of the incentive repayment amount was $993,607.29.

In determining that the incentive repayment clause was a penalty and was therefore unenforceable, the Court held that:

- The landlord would be entitled to claim loss of bargain damages for breach of contract, to compensate it for any period of lost rent and any shortfall between the rent it would have received from BMG and the rent it would be able to receive from the new tenant.
- The amount of rent payable by BMG had been agreed having regard to the amount of the fit-out contribution (the implication being that if no fit-out contribution was provided, a lower rent would have been agreed).
- The landlord would have effectively recouped the fit-out contribution through the payment of face rent by BMG over the term.
- The rent shortfall reflected in loss of bargain damages would notionally include the component of the rent the landlord expected to receive to recoup the fit-out contribution, and, in this way, the landlord would be compensated for the fit-out contribution paid.
- The landlord would be overcompensated if, in addition to the loss of bargain damages, it recovered an amount under the incentive repayment clause.

Key Takeaways

In circumstances where the term of a lease is not fully performed, most landlords require the ability to recover the pro-rata value of an upfront incentive (i.e. capital condition or upfront rent-free period).

1. Care needs to be taken to ensure that clawback clauses are appropriately structured and drafted. There is no "one size fits all".
2. The formula for recovery should be clear, unambiguous and fairly negotiated, noting that the party asserting that a clawback clause is a penalty bears both the evidentiary and the persuasive onus of proof.
3. The recoverable incentive should equate to a genuine pre-estimate of loss.
    a. If the sum is greater than the sum that the landlord would have been paid if the lease had been performed, it is likely to be held to be a penalty.
    b. The failure of a clawback formula to factor in the value of landlord's interest in items paid for from a capital contribution may result in an unintended double-dip, and it is likely to be held to be a penalty.

Market Insights

Delve into our selection of insights, news and hot topics from the property and construction industry across the globe to help you stay ahead of the market.

April Showers for UK Landlords of Substandard Non-domestic Private Rented Properties

If you are a UK landlord of non-domestic property with an EPC rating of F or G, then 1 April was a significant date for you. You will be in automatic breach of regulations that make it unlawful to continue to let a non-domestic property with an energy performance rating of F or G unless a valid exemption has been registered. Download our article to find out what compliance with the relevant regulations looks like, why it matters, and what the future may hold.

Hillside Parks Ltd and the Impact on "Drop-in" Permissions: A Lender's Perspective

In this article, we examine a recent England and Wales Supreme Court decision, confirming that a planning permission needs to be implemented in full for it to be lawful, was unwelcome news for developers. However, the ramifications are far wider than might, at first blush, be apparent. Lenders, too, will need to consider the impact of the decision on the value of their security.

Construction Matters – March 2023

Catch up on the latest edition of our quarterly *Construction Matters* newsletter, bringing you the information you need to know on the latest developments in the Australian building and construction industry.

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