SQUIRE PATTON BOGGS

Real Estate Roundup

September 2023

In This Issue

Options to Renew a Lease and Expansion Rights

The Court of Appeal in New South Wales has recently delivered judgment in a case dealing with the exercise of an option under a lease and the simultaneous exercise of an option to lease expansion space under the new lease.

In summary, the facts in *Willis Australia Ltd v AMP Capital Investors Ltd [2023] NSWCA 158* were as follows:

- In 2014, AMP as landlord and Willis as tenant entered into a lease of premises in the CBD of Sydney.
- The lease contained an option for Willis to renew for a further term of four years and also contained an option for Willis to take a lease of further space on one of the two floors that was subject to the lease ("expanded space").
- The lease provided that AMP must grant the new lease in respect of the expanded space if:
  1. Willis exercised the renewal option
  2. Willis exercised the expanded space option
  3. AMP received notice of exercise of both options nine months before the expiry date of the lease
  4. Willis was not in breach of the lease
  5. Willis delivered a bank guarantee for a specified amount by the expiry date of the lease
- Willis gave notice of exercise of the options within time and provided a bank guarantee calculated by reference to the current space (not the expanded space) under the lease.
- Willis subsequently purported to withdraw the notice exercising the expanded space option.
- Following receipt of the expanded space option notice, AMP advised the tenant occupying the expanded space (Perpetual Limited) that Willis had exercised its option to acquire the space and the tenant subsequently vacated the space.
- The primary judge found that Willis was bound to take a lease of the expanded premises and ordered specific performance.

The Court of Appeal overturned this decision and found that all five conditions referred to above had to be satisfied before Willis had validly exercised the options. Because Willis had only provided a bank guarantee that was calculated by reference to the current space under the lease, not including the expanded space, condition 5 had not been satisfied. The court found that AMP had no right to waive the timely provision of a bank guarantee under condition 5.

As the lease also contained a provision to the effect that any waiver had to be in writing and signed by the parties, this further supported the court's decision that AMP had no right to waive condition 5.

Takeaways

1. Always ensure that all conditions of exercise of an option in a lease, whether for renewal or expansion of space, have been satisfied before assuming a party is legally bound by a notice of exercise of the option.
2. Landlords should think carefully about taking any action, which may be to the landlord's detriment, until there is a legally binding commitment in place.

When Is a Real Estate Agent Entitled to Be Paid a Commission?

The latest case to consider a real estate agents' entitlement to be paid a commission on the sale of a property is *Freedom Development Group Pty Ltd v D'Ettorre Properties Pty Limited T/as D'Ettorre Real Estate (2003) NSWCA 81.*

In summary, the facts in *Freedom v D'Ettorre Properties* were as follows:

- Freedom held call options over two adjoining properties in Randwick and entered into a non-exclusive agency agreement with D'Ettorre Properties to sell the properties.
- Mr. D'Ettorre, the sole director of D'Ettorre Properties, introduced Mr. Ben Ingham to the properties, and Mr. Ben Ingham's company was nominated as the purchaser. A sale was negotiated but never formalised by execution of sale documents.
- A second agent, Mr. Ippolito, introduced Mr. John Ingham to the property, and formal sale documents were entered into with a nominated company, Wansey Road Randwick Pty Ltd, the directors of which were Mr. John Ingham and Mr. Ben Ingham.

D'Ettorre Properties commenced proceedings in the District Court, asserting that it was entitled to commission because it had effectively introduced the actual purchaser, on the basis that the ultimate sale to Wansey Road Randwick Pty Ltd was due to Mr. D'Ettorre's introduction of Mr. Ben Ingham to the vendor. Damages were also sought for alleged misleading and deceptive conduct under the Australian Consumer Law on the part of a director of Freedom.

The agency agreement in *Freedom v D'Ettorre Properties* relevantly provided that "the agent was entitled to commission if during the agency period … the purchaser is effectively introduced by the agent, regardless of whether the sale occurs after the termination of the agency agreement."

The primary judge in the District Court found that D'Ettorre Properties was entitled to commission, as it had effectively introduced the actual purchaser.

The Court of Appeal, in allowing the appeal from the District Court and finding that D'Ettorre Properties was not entitled to commission, held that there must be sufficient causal nexus between the "introduction" of the purchaser and the ultimate sale of the property to the purchaser, which is a question of fact in each case.

Mr. Justice Gleeson summarised the position as follows:

> "Contrary to (D'Ettorre Properties) submission, an inference of causal continuity cannot be drawn between (D'Ettorre Properties) introduction of Ben Ingham to the properties in November 2019 and the ultimate sale in February 2020 to a corporate purchaser nominated by John Ingham merely because Ben Ingham was a common director of the actual purchaser … ."

And later:

> "(In this case) the prospective purchaser introduced by (D'Ettorre Properties) was not the actual purchaser. Nor was there any continuing effect of the initial introduction by (D'Ettorre Properties) because the ultimate sale was a new and independent transaction following Mr. Ippolito's introduction of John Ingham to the properties."

Takeaways

1. As a vendor, always ensure that the key words "effectively introduced" or "effective cause" are included as the qualifying condition entitling a real estate agent to commission.
2. Remember, a standard agency agreement can always be amended, including introduction of parameters clarifying what constitutes an effective introduction by an agent.
3. When changing agents, the original agent should be required to provide details of any parties it claims to have effectively introduced to the principal or the property so that appropriate provisions may be incorporated in the new agency agreement to cover the risk of double commission being payable. The requirement to provide these details can be covered in the agency agreement.
4. Remember that exclusive agency agreements provide that the agent will be entitled to a commission if a property is sold during the fixed term of the agreement, even if sold by the vendor or another agent.
5. Under a sale contract, the purchaser should be required to give a warranty that it was introduced to the property by the named agent and indemnify the vendor for any commission payable to another agent as a result of a breach of that warranty. If there is a breach, the vendor is then entitled to recover damages from the agent if double commission is payable.

Preliminary Agreements – When Are They Binding?

Preliminary agreements are variously described as heads of agreement, memoranda of understanding, term sheets and letters of intent.

The latest case relating to the enforceability of preliminary agreements is *Stellar Vision Operations Pty Ltd v Hills Health Solutions Pty Ltd [2023] NSWCA 102.* While this case involved a commercial transaction, the decision is still relevant to property transactions, which only differ because of the requirement for an executed memorandum in writing to exist before a binding contract is enforceable. This requirement, adopting the English Statute of Frauds 1677, is contained in legislation in all Australian jurisdictions.

The facts in *Stellar v Hills* were as follows:

- Stellar and Questek Australia Pty Ltd entered into an agreement under which Stellar agreed to provide software for patient entertainment systems to be installed at the Queensland Childrens Hospital.
- Stellar and Questek subsequently responded to a proposal to provide the software systems to the four western Sydney hospitals.
- Hills acquired Questek's business and entered into a letter of undertaking with Stellar under which the parties agreed that the prior arrangements between Questek and Stellar would be honoured, including those relating to the four western Sydney hospitals.
- Hills subsequently entered into a contract in relation to the four western Sydney hospitals to supply the software systems but excluded Stellar from these arrangements, instead selecting another software company (Lincor) to provide these systems.

Stellar subsequently sued Hills for breach of the contract constituted by the letter of undertaking and breach of fiduciary duties.

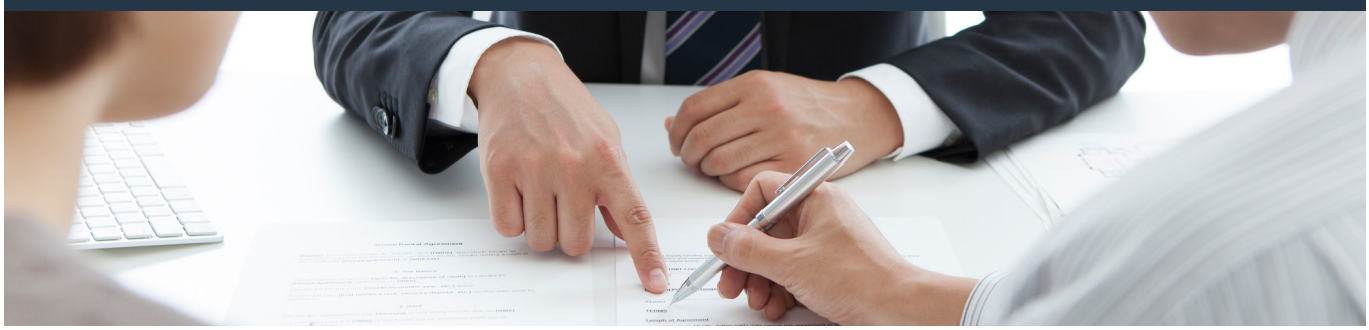
The primary judge found that the acknowledgement and agreement provisions of the letter of undertaking did not constitute a binding contract between Stellar and Hills. However, the Court of Appeal disagreed and found that these provisions, which used the language of contract, were an express agreement that Hills and Stellar would honour the intent of previous discussions.

The Court of Appeal stated the position as follows:

> "Whether parties intend to create binding legal relations is ascertained objectively, that is, by determining whether a reasonable person in the position of the parties would have taken them to have intended to contract."
>
> While the letter of undertaking in *Stellar v Hills* did not use the words "subject to contract" or similar expressions, even if it had used such words, there is authority to the effect that when a document recording the terms of the parties' agreement specifically refers to the execution of a formal contract, the parties may still be immediately bound.

Takeaways

1. Whether or not a preliminary agreement is binding on the parties comes down to an objective assessment by a reasonable person in the position of the parties to determine whether they would have taken them to have intended to contract.
2. Simply using words such as "subject to contract" does not automatically prevent a preliminary agreement being enforceable by the parties as a contract.
3. If the parties intend that the preliminary agreement is not to constitute an enforceable contract, clear words should be used to the effect that:
   a. Specified terms and further terms are yet to be negotiated and agreed
   b. Formal documents are to be prepared, approved, executed by the parties and exchanged
   c. Board and any other necessary approvals, for example finance, are to be obtained before the parties are contractually bound



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.

Why the Construction Industry Needs to Be Worried About "Greenwashing"

Growing environmental awareness and activism means it is likely that industries with a large carbon footprint and environmental impact, such as the construction industry, will face increasing scrutiny of their "green" claims. Managing the risk of greenwashing is challenging and complex. While at its core it is a matter of "doing what you say you are doing, or are going to do", in practice it is far from that simple, as our experts explain in this insightful article.

Construction Matters – July 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.

Update – Register of Foreign Ownership of Australian Assets

The Australian Taxation Office recently announced the introduction of a new Register of Foreign Ownership of Australian Assets, which is expected to come into effect from 1 July 2023. Our real estate experts explain the implications for businesses in this practical article.

Money Does Grow on Trees for Hotel Developers

The emergence of "green financing" in the hospitality and leisure sector stands to benefit not just the environment, but also hotel developers.

Environmental, social and governance investing has grown to prominence as the corporate sector seeks to positively contribute to reducing the impact of climate change. As a result, financing of corporate projects now includes mechanisms such as "sustainability-linked loans". Our insight examines the likely impact of this as part of the future of hotel development financing in Australia.

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