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Case Note: *N R Reid & Co Pty Ltd v Pencarl Pty Ltd and Santosa Realty Co Pty Ltd* [2011] VCAT 2241

Introduction

Quite often in commercial leases, landlords are given the right to terminate the lease as a consequence of an act of insolvency or the insolvency of the tenant, and in some cases of the guarantor. In relation to the administration or liquidation of a tenant company, the landlord's ability to obtain possession of the premises is restricted by statute.

(Please **click here** for an article written by Jarrod Munro – Senior Associate and member of our Commercial Litigation and Reconstruction & Insolvency teams – on a recent decision of the Supreme Court of Victoria regarding a landlord succeeding against the liquidator of a tenant in obtaining possession of the premises in a shopping centre.)

In a recent decision before the Victorian Civil and Administrative Tribunal (**VCAT**), VCAT found that the landlord was entitled to terminate the lease upon the bankruptcy of the tenant's guarantor.

Summary of the decision

The tenant argued that the landlord should have served a notice under section 146 of the *Property Law Act 1958* (**PLA**), and submitted that the landlord's termination of the lease was on the basis of the tenant's 'repudiation'. VCAT held that the lease had been terminated pursuant to a contractual right and therefore a notice that complied with section 146 did not have to be served. His Honour Judge O'Neill also stated in his reasons that *'if the bankruptcy of the guarantor was a breach, then it was a breach that could not be remedied'*.

Issues raised

VCAT's decision raises two very important issues:

1. the ability of a landlord to terminate a lease pursuant to a contractual right (and not a breach or repudiation by the tenant); and
2. service or giving of notices.

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Facts

The applicant, N R Reid & Co Pty Ltd (**N R Reid**), was the tenant of the first respondent (Pencarl Pty Ltd (**Pencarl**)) and the franchisor of real estate agencies running under the name 'N R Reid'.

The second respondent, Santosa Realty Co Pty Ltd (**Santosa**), was the sub lessee of the premises from N R Reid and was previously a franchisee of N R Reid. The applicable franchise agreement had expired, and N R Reid and Santosa were in negotiations regarding a new franchise agreement.

The director of N R Reid, Mr Ernst Shadbolt (**Mr Shadbolt**), was made bankrupt on 10 March 2010. He was the guarantor of N R Reid as lessee under the lease with Pencarl.

Mr Shadbolt considered his bankruptcy as a private and confidential matter, and did not advise either Pencarl or Santosa.

Pencarl claimed that by letter dated 27 October 2010, it gave notice to Mr Shadbolt purporting to terminate the lease on the basis of his bankruptcy.

The letter was sent to Mr Shadbolt's address contained in the lease. Mr Shadbolt gave evidence that he had not lived at that address for approximately 4 years. His evidence was that he had lived at a number of addresses and more recently had moved into premises at Rosebud. It was the Rosebud address that was contained in the records of the Insolvency Trustees Service of Australia (**ITSA**).

The submissions

N R Reid submitted that the landlord had conducted a search of the ITSA database, and was therefore aware of Mr Shadbolt's address – accordingly, no proper notice of termination was given.

N R Reid also submitted that the lease was being terminated by the landlord 'for repudiation'.

Clause 7.1 of the lease provides:

> *'The Landlord may re-enter the Premises and end this Lease if –*
>
> *7.1.5 A guarantor is a natural person and –*
>
> *(a) becomes bankrupt or…'*

N R Reid submitted that either pursuant to clause 7 of the lease or section 146 of the PLA, a notice was required to be given before the lease could be terminated.

The decision

His Honour Judge O'Neill, Vice President of VCAT, rejected those submissions and found as follows:

1. On the issue of service of the notice

Clause 14 of the lease provides that a notice given under the lease may be given by post to the recipient party's *'last known address'*.

His Honour found that, given the address referred to in the lease, it was reasonable for the landlord to rely on it as the last known address because there was no advice to the contrary.

2. Notice pursuant to section 146

His Honour found that the landlord was not required to serve a notice pursuant to section 146 of the PLA.

Section 146 provides: *'a right of re-entry or forfeiture under any proviso or stipulation in the Lease or otherwise arising by operation of law for a breach of covenant or condition in the Lease, including a breach amounting to repudiation, shall not be enforceable, by action or otherwise, unless until the Lessor serves on the Lessee a notice…'*

The tenant argued that the bankruptcy of the guarantor was a repudiation of the lease by the tenant, and accordingly the landlord was required to serve a notice pursuant to section 146.

The argument put forward by the landlord, which was accepted by VCAT, was that it was not a repudiation of the

lease, but the landlord was entitled to terminate the lease pursuant to a contractual right.

The landlord's re-entry of the premises was evidenced by the execution of the lease that it entered into with Santosa.

His Honour also found that if he was wrong in relation to section 146, and it was a breach by the tenant, then the breach was incapable of remedy.

The tenant made an application for relief from forfeiture; however this was refused.

Conclusion

This case highlights how important it is for tenants to fully understand the provisions of their leases, and the ability of landlords to terminate in certain circumstances. Further, although this was not a case of breach, it is also important for tenants to understand the consequences of any breaches of their lease and the rights available to landlords in relation to them.

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