

Variation of a Lease - risks and issues to consider during Covid-19 rent relief negotiations

September 2020

A variation of a lease may operate to surrender the existing lease and become a new lease incorporating the variation due to a common law principle.

This derives from the common law principle of “estoppel” that is, that two leases cannot co-exist. Therefore, subject to the degree of variation (irrespective of the parties intentions) the existing lease must be surrendered, for the new variation to take effect.

What variations may cause this to occur?

Increasing or even reducing the lease term or adding further options although not conclusive may cause this to occur. There are cases that determined either will affect a surrender of the original lease and the re-grant of a new lease.

Halsbury states, “where the term of the lease is altered it is difficult to satisfy the court that there has been a mere variation.”

A change to the premises by adding or reducing them or relocating in a shopping centre may also surrender the lease and create a new lease.

A change of use of the premises could trigger the principle or variations about removal of fixtures, internal alterations of works, adding a guarantor or bank guarantee, or altering these terms on a transfer of the lease may also trigger the principle.

Varying the lease to make the tenant liable for Essential safety measures may also trigger the principle.

What is the risk if the principle applies?

The variation may bring a non-retail lease under the Retail Lease Act if it becomes a term less than 15-years.

This means the Landlord cannot recover Land tax, must provide disclosure and cannot have any underpinning or ratchet rent review clause.

The tenant can access mediation and the Landlord has section 52 obligations to maintain the premises plant and equipment and meet Essential safety measures.

A recent case on point:

Richmond Football Club Limited v Verraty Pty Ltd [2011] VCAT 2014

RFC entered into pre-Retail Leases Act in 2003 and in 2004 significant variations were agreed to, reducing the rent, amending rent reviews, varying bank guarantee provisions, introducing an obligation to pay GST, and extending the term of the lease by 10 years to 18 May 2018.

VCAT determined the substantial changes to the original lease operated at law to affect a **surrender and a re-grant** of the lease on substantially the same terms as the original lease amended by the 2004 variation.

This meant the Lease then fell under the **RLA and RFC** could then recover land tax that it had paid under a mistake and contrary to section 50 and section 94 of the Retail Leases Act.

The Landlords Counsel raised a number of defences which did not succeed:

- a. promissory estoppel (RFC had not sought to enforce new rights arising under the RLA until December 2009 more than six years after the 2004 variation).
- b. Unconscionable conduct reliant on the Dog Depot decision that the landlord was entitled to compensation for lost land tax under a counter-restitution claim for use and occupation.

The Member said that RFC was not unjustly enriched by not having to pay the landlord's land tax where it never had an obligation to do so. Fortunately for the Club the "re-granted lease" was for a term of less than 15 years for the Tenant.

The Landlord did succeed arguing the statute barred by the Limitation of Actions Act 1958 and the Landlord was ordered to repay RFC \$125,320 for land tax mistakenly paid after 29 October 2004.

Covid -19 Lease variations

At this point there are no cases as to whether Covid -19 lease variations to reduce the rent and extend the term of the lease by the period of the deferral period cause a surrender of the existing lease?

However, where the rent reduction includes other variations extending the lease term or adding a further option it is more likely to trigger the principle.

Variation's that do **NOT** trigger this risk are rent review clauses, correcting an error or omission in the lease provided there is no material change to the remaining parts of the lease or reduction of the premises or assignment of a Lease.

Where the tenant is locked out and then let back in under terms which restore and vary the lease term and require the tenant to provide a greater bank guarantee the Tribunal determined there was **no surrender** of the Lease.

So, beware variations of a lease if they are significant, that is a red flag that it may surrender the lease!

Check your lease terms and include a statement in your deed of variation

The lease may state that any variation does not constitute a surrender of the lease and regrant of a new lease?

Any Deed even dealing with Covid 19 rent relief should include a clause as follows:

“the tenant warrants and covenants that any variation of the lease will not be a surrender of the lease and a regrant of a new lease”.

The above statement is not conclusive, and a Court may still find there was a surrender at common law.

Mortgagees consent

Landlords should obtain a mortgagee's consent to any lease or variation of a lease, whether or not registered otherwise the landlord will be in breach of its mortgage and the variation will then not bind the registered mortgagee.

A subsequent mortgage of the freehold or refinance after lease was entered still requires the mortgagees consent otherwise the mortgagee will not be bound by that new lease and the new lease will only be enforceable by the parties to it in equity.

Sale of a business – transfer of lease with variations

In this case the vendor / transferor bears the cost of obtaining the mortgagees consent (GC 7.6(b) LIV May 2014 copyright contract of sale).

But if the sale of business is subject to surrender of the existing lease and grant of a **new lease Retail Lease** the landlord cannot claim costs and rely on the 'assignment' exemption and they cannot claim consent costs from the outgoing tenant. Sect 23 also prevents a landlord placing a premium on providing its consent.

Guarantors and Variations

Despite a clause in a deed of guarantee that the guarantor of a lease will be bound by any variation to the lease it is important to ensure the guarantor acknowledge their continuing guarantee of the obligations of the tenant as varied.

Assignments of a Lease with a variation that may trigger the surrender principle

The landlord may lose its rights to sue the former tenant unless the former tenant has **consented to the variation** under the Assignment of the lease therefore on a transfer of lease with variations, consider if the variation trigger the surrender principle? If so, include a provision that the Assignor consents to the lease **as varied**.

Note: The LIV form of Transfer of Lease does not cater for variations of a lease at the same time as a transfer of it.

The form of variation of a lease

A lease made by deed can be varied by an agreement not by Deed) but it should be by Deed as should the mortgagee's consent and include a provision that states the deed **binds and benefits the Landlord and tenants successors and assigns due to** the protection under **section 42(2)(e)** of the *Transfer of Land Act and the variation should also be expressed as supplemental to the lease,(section 58 of the Property Law Act 1958).*

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