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### **Lessors beware! A few loose words may land you with a five year obligation!**

Two recent decisions of the Administrative Decisions Tribunal Retail Leases Division have far reaching implications in declaring when a statutory lease or sub-lease exists. These cases establish that, even if a contract for a formal lease has not been entered into and only verbal or implied agreements exist, the combined effect of sections 3 and 8 of the *Retail Leases Act* 1994 (the Act) may mean that a statutory lease is nonetheless created. Section 16 of the Act then provides that this lease is for a minimum term of five years.

Accordingly it is critical that, in negotiating potential leases, lessors conduct themselves very carefully to avoid creating a statutory lease which would bind them for the next five years when this is not their true intention.

Section 8(1) of the Act states that a retail shop lease is created when a person enters into possession of the retail shop as lessee under the lease or begins to pay rent as lessee under the lease (whichever happens first).

In *Helou & Ors v Bong Bong Pty Limited & Anor trading as Regional Retail Properties* [2006] NSWADT 2006 (1 May 2006) the Tribunal stated that the requirements of section 8(1) may be met even though no formal deed or agreement to lease is ever executed, so long as the parties have reached a 'consensus' as to the terms of the lease when the lessee enters into possession.

The Tribunal further held that in order to reach a 'consensus' it was not necessary for agreement to be reached on all of the terms of the right of occupation. This was because section 3 of the Act gives a broad definition of the term 'lease' to be 'any agreement', express or implied, and whether oral, in writing, or partly oral or partly in writing, 'under which a person grants or agrees to grant to another person for value a right of occupation of premises for the purposes of the use of the premises as a retail shop'.

In *Helou* the Tribunal found that the combined effect of sections 3 and 8 of the Act meant that a statutory lease for a minimum period of 5 years had been created. This was despite the fact that the 'consensus' reached came in the form of a letter setting out the proposed terms of a lease, but **expressly** stating that no binding lease would come into existence until a formal document of lease had been prepared and executed.

The lessee in *Helou* had taken possession of the premises after purchasing the business at a time when the previous owners of the business had been in possession only on a monthly

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tenancy following the expiry of their lease. The lessee took over this monthly tenancy which fell outside the Act. The Tribunal held that this was sufficient to 'enter into possession' under s8(1) and it was not necessary for the lessee to vacate and re-enter the premises for a new lease under the Act to be concluded.

In *Thai Star Video Pty Limited v Walpole* [2007] NSWADT 193 (27 August 2007), the Tribunal found that a statutory sub-lease for a potential period of ten years was created by way of an oral agreement between the lessee and the sub-lessee.

In that case there was a verbal agreement that a sub-lease for the same term as the head lease was created when the lessee said to the sub-lessee (who was in possession at the time) "You stay as long as I stay". The only agreed terms of this occupation were the space to be occupied within the lessee's shop (a counter running down the side of the lessee's shop), the rent to be paid and that the sub-lessee would pay its own electricity.

The Tribunal stated that "This is, obviously, from a commercial view point, a most unsatisfactory situation but follows inevitably from the width of the definition of retail shop lease". The Tribunal found that the combined operation of sections 3 and 8 of the Act compelled it to declare that a statutory sub-lease existed for the same term as the lessee's lease.

As noted in *Helou*, the general purpose of the Act is the protection of lessees and the Act operates to create a statutory contract, despite the fact that under traditional contract law a binding contract may not yet have been concluded. Accordingly, the negotiation of potential leases can be very dangerous territory for lessors. Lessors must be careful not to reach any 'consensus' on lease terms or make any statements which could be construed as expressing an agreement until they are certain that those terms are as they should be. Even more critically, a lessor should not allow a lessee into possession or accept rental payments until they are confident that satisfactory terms for the lease have been agreed to. A failure to be absolutely meticulous in this regard may saddle a lessor with a five year obligation on most unsatisfactory terms!

## **For more information please contact:**

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