THE CONTRACTUALISATION OF THE LAW OF LEASEHOLD: PITFALLS AND OPPORTUNITIES

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Common lawyers have treated the lease as an interest in land since the late middle ages[1] recalling earlier Roman precedent.[2] Thus, the lease has been construed as a grant by English and Australian courts.[3] As grantor, the landlord could put conditions subsequent[4] on the grant which would determine the grant and allow the land to revert to the landlord on breach of such conditions.[5] On determination of the grant, the lessor, subject to any statutory restriction, might have ejected the lessee personally or by legal process and the lessee ceased to have any rights to the land. On the other hand, once the lessor had recovered possession of the demised premises, the lessor had no right to damages for lost rent.[6] All of these aspects of the traditional common law of tenancy follow from the construction of the lease as a grant of an interest in land.[7]

Yet the lease has always been a strange sort of grant, with many aspects more consistent with contract than land law. Although the concept of the lease as a grant necessarily implied a landlord's covenant of 'quiet enjoyment', landlords really never intended to surrender all rights and obligations to the demised premises in the same way that the grantor of a life estate or a conditional fee did. Landlords wanted to surrender a right to occupancy in return for income but were still concerned about the maintenance of the premises and the uses to which the tenant put the premises, for example. Tenants expected more from landlords than merely time on the land.[8] They expected a certain standard of maintenance and amenities, as well as the payment of

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[1] *See Halsbury's Laws of England* (London, 4th ed. Butterworths 1982, Vol. 39) pp.280-281.

[2] Pollock and Maitland, *The History of English Law* (2nd ed., Vol. II, Cambridge University Press, 1968) pp.114-115.

[3] *See e.g. Mestros* v. *Blackwell* (1974) 8 S.A.S.R. 323 (S.A.S.Ct.).

[4] On the use of this concept generally in land law *see* Sackville and Neave, *Property Law: Cases and Materials* (3rd ed. Butterworths, Sydney, 1981) p.160.

[5] *See e.g. Rosa Investments Pty. Ltd.* v. *Spencer Shier Pty. Ltd.* [1965] V.R.97 (Vic.S.Ct.). *But cf. Progressive Mailing Pty. Ltd.*v. *Tabali Pty Ltd.,* (1985) 59 A.L.J.R. 373, 378 and see the discussion at p.38 infra.

[6] *See* infra fn. 68 *cf. Shevill* v. *The Builders' Licensing Board* (1982) 56 A.L.J.R. 793 (H.C.). If the lessee remained in possession after forfeiture, he was liable to pay not rent but 'mesne profits', essentially damages for trespass. Sackville and Neave, op.cit. pp.703-704.

[7] Although the legal theory supporting the decision in *Shevill, id.* was deliberately left unclear (*see p.5.* infra) the decision is consistent with the concept of forfeiture of the lease as a vesting of the landlord's reversionary interest, which terminates his rights as lessor under the doctrine of merger.

[8] *Cf. e.g.* Megarry and Wade, *The Law of Real Property* (5th ed., London, Stevens & Sons Ltd., 1984) p.13 (Definition of 'Estates').

costs attaching to the land like rates and taxes. Thus, the basic 'grant' in the lease is insignificant today compared to the multiplicity of 'covenants' therein: express and implied, statutory and common law. The very idea of a 'covenant' is contractual in nature[9] and courts have shown the liberality in implying and construing covenants in a lease, which they are wary of doing with the terms of a grant by deed or devise[10] but regularly do with the terms of a contract.[11] The difference between the interest in land called a 'lease' and the contractual right to be on land called a 'licence' has become increasingly muddled,[12] and seems directed mostly toward whether landlord-tenant statutes apply,[13] revocability at will[14] and application to successors in title.[15] Indeed, in Australia's regime of land registration, where most vested interests in land less than the fee simple have been abolished, leasehold, as a vested right to possession without title seems an anachronism.[16] Thus, most writers seem to accept that a lease, while continuing to grant an interest in land, *is also, in some way, a contract.*[17]

Perhaps in reaction to the greater concern for tenants' needs in the past decade[18] and to increasing legislative activity in this area,[19] Australian courts have now begun to construe leases according to the law of contract rather than under the law relating to interests in land.[20] This paper explores the potential impact of this change in the legal concept of a lease for landlords and tenants.

[9] *Cf. Id.* 739.

[10] *Cf. e.g.* The treatment by the courts of the implied covenants in the New South Wales *Conveyancing Act,* in *Coronet Homes Pty. Ltd.* v. *Bankstown Finance and Investment Co. Pty. Ltd.* (1966) 85 W.N. (N.S.W.) (pt. I) 69 (N.S.W.S.Ct.).

[11] *See,* for example, the increasing willingness to import the 'business efficacy' doctrine of interpretation from contract law into lease law, in *Karagianis & Another* v. *Malltown Pty. Ltd.* (1979) 21 S.A.S.R. 381, 392 (S.A.S.Ct.) and *Hayes* v. *Seymour-Johns* (1981) 2 B.P.R. 9366, 9370-71 (N.S.W.S.Ct.) after an earlier reluctance in *Mestros* v. *Blackwell* (1974) 8 S.A.S.R. 323 (S.A.S.Ct.).

[12] *See Hayes v Seymour-Johns* (1981) 2 B.P.R. 9366 and *Lewis* v. *Bell* [1985] 1 N.S.W.L.R. 731 (N.S.W.C.A.).

[13] *e.g. Radaich* v. *Smith* (1959) 101 C.L.R. 209 (H.C.).

[14] *Graham H. Roberts Pty. Ltd.* v. *Maurbeth Investments Pty. Ltd.* [1974] 1 N.S.W.L.R. 93 (N.S.W.S.Ct.), *Sibson* v. *Ball* [1974] Qld.R. 282 (Qld. F.C.).

[15] *Hayes* v. *Seymour-Johns* (1981) 2 B.P.R. 9366.

[16] As is demonstrated by the fact that every state exempts leases from the necessity of registration. *See* Sackville and Neave, op.cit. pp.655-656.

[17] The confusion over this issue is illustrated by Redfern and Cassidy, *Australian Tenancy Practice and Precedents* (Sydney, Butterworths, 1987), who state, on the same page (p.1551) "A lease is a contract" and "A lease, though created by contract, is a conveyance". *See also* Sackville and Neave, *Id.*147 ('leasehold estates') and p.638 ('contractual arrangement'); Megarry and Wade, op.cit. p.628 ('interest in land') and p.632 ('bilateral contract'); Halsbury's Laws of England, op.cit., Vol.27, p.9 ('grant or demise') and p.10 ('contract of tenancy').

[18] Beginning with the Australian Royal Commission on Poverty, *Poverty In Australia and Law and Poverty in Australia* (1975). *See also* Community Committee on Tenancy Law Reform, *Reforming Victoria's Tenancy Laws* (Victorian Council of Social Service, Melbourne, 1978); Cabramatta Tenancy Working Party, *Reforming a Feudal Law* (Australian Consumers' Association, Sydney, 1982) and Nunan, N. *Tenancy Law In Queensland* (Caxton Street Legal Services, Brisbane, 1983).

[19] *See* Bradbrook, A., "The New Era of Tenancy Protection" (1987) 61 (10) A.L.J. 593.

[20] *Progressive Mailing Pty. Ltd.* v *Tabali Pty. Ltd.* (1985) 59 A.L.J.R. 373 (H.C.). *See* also the discussion at pp.11-14 infra.

THE FIRST CHANGES

In 1906, the High Court decided [in the case of *Buchanan* v. *Byrnes*][21] that a landlord had a right to damages for lost rent, maintenance costs and rates and taxes payable by the tenant under the lease, after the tenant had abandoned the demised premises and the landlord had re-entered. In that decision, all three judges treated the lease as a contract and nothing more, deciding the issues on contract principles of repudiation.[22] The tenant's defence of surrender of the interest, based as it was on a land law theory, was rejected.[23]

Despite the clear treatment of the lease as a contract in *Buchanan's Case*, over the following seventy-five years the decision was restricted to its facts, as only addressing the narrow question of whether abandonment was sufficient *per se* to constitute a surrender of a leasehold.[24] In 1926, the High Court let a decision of the Court of Appeal of New South Wales stand which decided that the contractual law of frustration did not apply to leases, neither court mentioning *Buchanan* v. *Byrnes.*[25] In 1945, Herring C.J. of the Victorian Supreme Court cited *Buchanan's Case* for the land law principle that re-entry by the landlord after abandonment was sufficient to constitute a surrender of the lease: the very argument rejected by the High Court in *Buchanan's Case.*[26] It was left to the Canadian courts to recognise the implications of this 1906 decision of the High Court of Australia.[27]

A major turn of events was signalled by the House of Lords in the 1981 decision of *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.*[28] A lease for a warehouse included a restrictive covenant that the building might not

[21] (1906) 3 C.L.R. 704.

[22] *Id.* 713 (Griffith C.J. – "contract"), 718 (Barton J. – "personal covenants"), and 720 (O'Connor J. – "contract").

[23] Proceeding on a strictly contractual theory, Griffith C.J. held that there could be no surrender of the lease without the consent of both parties thereto (*Id.* 713). Barton J. used a mixed approach: while the tenant might surrender an interest in the land and be excused payment of rent, the covenants to maintain the premises, carry on a licenced premises and pay rates and taxes were personal promises in contract enforceable notwithstanding a surrender of the leasehold and re-entry (*Id.* 718, 719). O'Connor J. followed a more curious mixture of contract and land law, suggesting that the tenant might have surrendered his interest at any time before breaching the lease but, upon the breach, surrender was no longer an option and damages began to accrue (*Id.* 720-721). Where Barton J. suggested that those parts of the lease concerning rent and quiet enjoyment were to be dealt with as a real interest and other covenants were to be dealt with as contracts, O'Connor J. seemed to suggest that the whole lease was a grant of an interest in land until it was breached, whereupon it instantly became a contract and no longer merely granted an interest in the land.

[24] *Re Stewart ex p. Overells' Ltd.* [1941] Q.S.R. 175, 177 (Qld. Bank. Ct.). *N.R.M.A. Insurance Ltd.* v. *B & B Shipping & Marine Salvage Co. Ltd.* (1947) 47 S.R. (N.S.W.) 273, 281 (N.S.W.F.C.). *Union Trustee Co. of Australia Ltd.* v. *Baker* (1948) W.N. (N.S.W.) 247, 249 (N.S.W.S.Ct.). *Thompson* v. *McIntosh* (1953) 53 S.R. (N.S.W.) 212, 215 (N.S.W.F.C.). *Australian Safeway Stores Pty. Ltd.* v. *Toorak Village Development Pty. Ltd.* [1974] V.R. 268, 274 (Vic.S.Ct.). *Shevill* v. *The Builders' Licencing Board, supra fn.6 at 798.*

[25] *Firth* v. *Halloran* (1926) 38 C.L.R. 261 (Isaacs J. dissenting).

[26] *Parsons* v. *Payne* [1945] V.R. 34, 39.

[27] *Highway Properties Ltd.* v. *Kelly, Douglas & Co. Ltd.* (1971) 17 D.L.R. (3d) 710, 720-721 (S.C.C.).

[28] [1981] A.C. 675.

be used for any other purpose than as a warehouse without the consent of the lessor. Due to the closure of the access road to the warehouse by the local authority, the warehouse was rendered commercially worthless. The lessees 'ceased use' of the building and defaulted in payment of rent. When the lessor brought an action to recover rent, the lessees pleaded frustration of the lease. Four of their Lordships[29] held that, in spite of precedents to the contrary, the law of frustration applied to leases, but rejected its application on the facts.

As Lord Russell of Killowen demonstrated in his speech, the result in *National Carriers Ltd.* v. *Panalpina (Northern) Ltd.* is equally consistent with the traditional land law principle that "the purchaser of land, whether for a freehold or a leasehold interest, takes the risk that it may . . . turn out to be less suitable or quite unsuitable for the purpose he has in mind, unless the vendor or lessor has taken upon himself . . . liability in that event".[30] What makes *National Carriers* notable is not the decision but the *dicta* of their Lordships on the applicability of the contract doctrine of frustration to the lease. Lord Hailsham rejected the argument that there ought to be a distinction between the legal treatment of a lease for real property (historically a land law concept) and a lease for chattels (a contractual relationship).[31] Lord Wilberforce rejected the argument which held that frustration could not apply to a lease because a "lease is more than a contract: it conveys an estate in land".[32] Although he did not directly refer to *Buchanan* v. *Byrnes,* Lord Wilberforce quoted the conclusion drawn by the Canadian Laskin J. from his analysis of *Buchanan's Case*, that "It is no longer sensible to pretend that a commercial lease . . . is simply a conveyance and not also a contract".[33] Lord Simon of Glaisdale saw "nothing about the fact of creation of an estate or interest in land which repels the [contractual] doctrine of frustration".[34] Lord Roskill noted the "narrow distinctions" between a [contractual] licence and a lease.[35] Therefore, although their Lordships were only discussing the application of the doctrine of frustration, (and that it was *obiter dicta*) there is no doubt about where they stood on the question of whether a lease was a contract or the grant of an interest in land.

The Australian version of *National Carriers* (in that the court accepted the application of contract law to leasehold in principle but not on the facts before them) was *Shevill & Another* v. *The Builders' Licencing Board.*[36] As in *National Carriers*, the lease in question was of a commercial nature but in *Shevill* the issue was repudiation not frustration. The lessee had failed to make timely payments of rent. The lessor had both re-entered and sued for

[29] Lord Hailsham of St. Marylebone L.C., Lord Wilberforce, Lord Simon of Glaisdale and Lord Roskill. Lord Russell of Killowen dissented.
[30] *National Carriers* v. *Panalpina Ltd.* [1981] A.C. 675, 708.
[31] *Id.* 690-691.
[32] *Id.* 694.
[33] *Id.* 696. Lord Simon of Glaisdale also cited this passage at 703.
[34] *Id.* 705.
[35] *Id.* 714.
[36] (1982) 56 A.L.J.R. 793.

the difference between rent collected on relet and rent under the lease. Counsel for the lessor submitted alternatively that the failure to pay rent under the terms of the lease constituted a repudiation of the lease or that it constituted breach of a fundamental term. Either of the theories would allow the lessor, as the 'innocent' party, to treat the contract as determined (i.e. re-enter) and sue for damages.[37]

The High Court in *Shevill's case* was sympathetic to Shevill's argument. The majority of the court made its decision on the basis that contract law applied to a lease[38]: however the decision was that the lease as worded did not provide for the lessee's liability for loss of rent after re-entry by the landlord. Wilson J. held that the issue of repudiation did not arise on the facts.[39]

As in *National Carriers*, the result in *Shevill's case* was consistent with traditional land law principles. On re-entry, the lease, including the covenant to pay rent, determines. The lessee's interest having been divested by the re-entry, the lessee is under no further obligation to pay rent required by the lease as a condition of holding that interest.[40] However, the significance of *Shevill's case* for the purpose of the present argument is that it was neither argued nor decided on this land law theory.

The Victorian Supreme Court took the next step in the contractualisation of lease law in the case of *Ripka Pty. Ltd.* v. *Maggiore Bakeries Pty. Ltd.*[41] *Ripka* was the first Australian case since *Buchanan* v. *Byrnes*, in 1906, to apply the law of contract to a lease both in principle and on the facts. The lessor had gone heavily into debt to construct a reception centre and rent from the centre was the lessor's sole income. Several defaults by the lessee in payment of rent had put the lessor into serious financial difficulties. The lessor notified the lessee that the lessee's defaults were being treated as a repudiation of the lease. The lessor brought an action for possession and damages for lost rent and mesne profits to the date of possession. Gray J. granted the relief demanded and, following the *dicta* in *National Carriers, Shevill's case* and other Australian and English cases, held that the doctrine of repudiation applied to the law of leases.[42]

In line with comments on the earlier cases, we may note here that the holding that repudiation applies to leases was not essential to the decision in *Ripka's case*. The decision in *Ripka's case*, like the decisions on *Shevill's case* and *National Carriers*, is equally consistent with the land law theory that, on breach of the condition subsequent for the timely payment of rent, the lessee's interest divested and reverted to the lessor. The lessor, under this theory, would have received the same judgment for rent in arrears under the

[37] Greig and Davis, *The Law of Contract* (Sydney, Law Book Co. Ltd., 1987) p.1196. *et seq.*
[38] Gibbs C.J. (Brennan and Murphy JJ. concurring) (1982) 56 A.L.J.R. 793, 794 *et.seq.*
[39] *Id.* 798. *Cf. also* Murphy J. at 797 ("The appellants did not repudiate their obligations").
[40] *Cf.* Megarry and Wade, op.cit. p.684 on the effect of surrender of a lease: "surrender discharges the parties from all future obligations under the lease but not from liabilities already incurred". *Cf.* The comments by Samuels J.A. in the *Wood Factory* case, infra fn. 56, at 118, that a repudiation of the lease may be equivalent to a surrender.
[41] [1984] V.R. 629.
[42] *Id.* 634.

lease and mesne profits up to the date of possession by the lessor which *Ripka Pty. Ltd.* in fact received. Again, however, what is significant about *Ripka's case* is that it was argued and decided as a contract case and not as the divesting of an interest.

In 1985, the High Court removed any doubts that the lease was to be treated as a contract and not as a grant in *Progressive Mailing Co.* v. *Tabali Pty. Ltd.*[43] *Progressive Mailing* was the first Australian decision since 1906 in which the decision was not only justified by a contractual theory of the lease but actually differed from the result which a land law theory of the lease indicated.

In *Progressive Mailing*, the lease at issue was a five-year commercial letting, beset almost from the outset with a number of disputes over lease interpretation and alleged breaches by both sides. In response to the lessor's alleged breaches, the lessee, *inter alia*, ceased to pay rent.[44] The lessor sued both for possession and for damages in the form of:

(a) rent in arrears,
(b) mesne profits and
(c) the cost and delay of reletting the premises,

submitting that the lessee had either repudiated or fundamentally breached the lease. The High Court unanimously agreed to let stand a decision granting this relief.

The majority of the High Court held, in *Progressive Mailing*, that "the ordinary principles of contract law, including that of termination for repudiation or fundamental breach, apply to leases."[45] The court based its decision on three points:

(a) The decision in *Buchanan's Case,*
(b) The *dicta* in *National Carriers, Shevill's Case* and other decisions throughout the common law world and
(c) the change in the socio-economic context of a lease since its medieval conception as an interest in land.

While the judges conceded that the lease conveyed an interest in land,[46] the concession did not seem to have any impact on the decision and may be taken as *obiter dicta.*[47] Brennan J.'s concurring opinion also agreed that

[43] Supra fn.20.

[44] The lessor had alleged various forms of damage to the premises, such as damage to the roof, rendering the electrical system faulty and dangerous and failing to repair broken windows and pipes, as well as subletting in violation of the lease and violating the local planning scheme. However, the majority of the court gave no weight to these other alleged violations of the lease and focussed expressly upon the failure to pay rent. *Id.* 381.

[45] Mason J., *Id.* 378. See also Wilson J. *Id.* 382; Deane J. *Id.* 387, 388 and Dawson J. *Id.* 390.

[46] Mason J. *Id.* 380, Brennan J. *Id.* 383, Deane J. *Id.* 388.

[47] Mason J. *Ibid.* used the reference to land law only to illustrate the truism in contract law that "mere" (insignificant?) breaches of contract are not fundamental and do not constitute repudiation. Brennan J. *Ibid.* was referring to the "consequences" of the application of the law being different in a lease compared to other contracts, not the law itself being different. Deane J. *Ibid.* was mostly referring to the historical basis of leases in land law except for a vague hypothetical case where the tenant's rights might be "more properly to be viewed" as an estate in land, *Id.* 388, 389.

"ordinary contractual principles do apply to a lease".[48] Using these contractual principles, the court held that, in failing to pay rent persistently, the lessee had either repudiated or fundamentally breached the lease, allowing the lessor to terminate the contract and sue for damages.

The order for possession, with the recovery of rent in arrears and mesne profits to the date of possession, in *Progressive Mailing* is equally consistent with the concept of a lease as an interest in land, for the reasons described in discussing *Ripka's case*. However, the recovery of damages for the cost and delay of reletting is consistent only with the lease being a contract and is inconsistent with the lease granting an interest in land. If the lease is a grant, once the lessee's interest has determined and the lessor is in possession, all legal relations between lessor and lessee end. There is no right of the lessor for the costs of reletting, or compensation for delay pending reletting, based upon the lease, because, on breach of the condition subsequent, the lease has no legal force. The lessor only gets mesne profits for the lessee's possession after the lease has determined as damages for trespass and not as rent or for any right under the lease.[49] Once the lease has determined the lessor has no right to rent, and once the lessee's possession has determined, the lessor has no right to anything else.

However, if the lease is viewed as a contract, as the High Court viewed it, there is no doubt about the ability of the lessor to recover the costs and delay of reletting as in *Progressive Mailing*. Had the lessee continued to perform his promise to pay rent under the lease, the lessor would not have had to incur the costs of reletting and would have suffered no loss of rent pending reletting. Thus, the costs and delay of reletting are added expenses directly and proximately flowing from the lessee's breach of the lease (assuming that, under the doctrine of fundamental breach, the lessor had no obligation to allow or expect the lessee to continue to perform and thus reletting was necessary). While, under land law theory, the determination of the lease *ends* the lessor's rights to claim money from the lessee (unless the lessee continues to illegally squat on the land, and creates a new right by this act), under contract theory, the determination of the lease due to fundamental breach or repudiation by the lessee *begins* the lessor's right to claim consequent damages. Thus, the award of any money to the lessor from the lessee for costs or losses accruing after the date on which the lessor is in lawful possession of the demised premises must be based on the lease being a contract, for there is no right to such an award in land law.

The first case to apply *Progressive Mailing* was *Wood Factory Pty. Ltd.* v. *Kiritos Pty. Ltd.*,[50] shortly after the High Court's decision in *Progressive Mailing*. The lessee had abandoned the premises with rent in arrears. The lessor had re-entered and relet the premises. The lessor sued, claiming that the lessee had fundamentally breached the lease and should pay the difference between the reserved rent and the relet rent for the whole term of the

[48] *Id.* 383.
[49] As Brennan J., points out *Ibid.*
[50] [1985] 2 N.S.W.L.R. 105 (N.S.W.C.A.).

original lease, as well as rent in arrears. The majority of the New South Wales Court of Appeal (Samuels J.A. dissenting) allowed a judgment granting the relief demanded to stand. The court accepted that the lessee had fundamentally breached the lease by failing to pay rent and found nothing in *Progressive Mailing* to the contrary.[51]

The *Wood Factory* case is another clear example of how the application of contractual principles has changed the law of leasehold. While the finding of repudiation for non-payment of rent over a significant period of time is similar to *Progressive Mailing*, the acceptance of the landlord's damages claim goes even beyond *Progressive Mailing* in two respects. First, the claim for net loss of rent on reletting is substantially the same as that rejected in *Shevill's Case* by the High Court, and is another step away from the land law view that, on determination of the lessee's interest and actual possession, reletting is the lessor's problem.[52] In *Progressive Mailing*, the lessor asked for and received only out-of-pocket expenses associated with termination: in the *Wood Factory* the lessor received expectation losses for the original term of the terminated lease. Second, the lessor in the *Wood Factory* case was under a far lighter duty to mitigate his damages. In *Progressive Mailing*, the lessor received lost rent only for that part of the unexpired term during which he was unable to relet the premises: once the lessor relet, he had the duty to do so at a rent sufficient to cover his losses on the first lease. In the *Wood Factory* case, however, the lessee was in effect made an involuntary guarantor of the rent under the terminated lease, whether the premises were relet or not. Thus, the lessor in the *Wood Factory* recovered rent as damages for a period during which he had allowed a third-party to occupy the premises rent-free.[53]

Nai Pty. Ltd. v. *Hassoun Nominees Pty. Ltd.*[54] was a case of repudiation by assignment of interest as well as by breach of covenant. The lessee had issued a debenture granting a third-party possession of a demised premises in violation of a covenant not to assign without the lessor's consent. The lessor then brought a successful action to recover the premises and eject the third-party. The lessee, now subject of a bankruptcy petition, applied to the court for temporary protection of its right to possession. The court denied the application, following *Progressive Mailing*, because the lessee had repudiated the lease:

(1) by granting possession to the third-party in violation of the lease,
(2) by failing to pay costs and taxes under the lease, and

[51] *Cf.* The discussion in the *Annual Survey of Australian Law,* 1985 pp.283-285.

[52] This is assuming, as in *Wood Factory*, that the lessor has accepted the repudiation and re-entered, extinguishing the lessee's interest. The lessor has always been able to relet the premises and sue for damages where the lessee abandons the premises and the lessor refuses to re-enter. *See e.g. Maridakis* v. *Kouvaris* (1975) 5 A.L.R. 197 (N.T.S.Ct.). The difference is that, in the latter case, the lessee is considered to be enjoying the premises *in absentia* and has the right to re-take possession at any time during the term of the lease. Under the repudiation doctrine, the lessee loses the right of possession but still must, as applied in *Wood Factory*, in effect, guarantee payment of rent by the new lessee.

[53] Supra fn. 50 at 137-138 and 146-147 (occupation by 'Insul Fluff').

[54] [1985-1986] Aust. & N.Z. Conv. Rep. 349 (S.A.S.Ct.).

(3) by failing to intervene in the lessor's action for possession against the third-party.

The court therefore found that the lessee had no protectable right to possession under the repudiated lease.

Nai has two implications. First, *Nai* demonstrates that not only failure to pay rent but an attempt to sublet in violation of the lease or a failure to pay other costs required by the lease (in *Nai*, rates, taxes, repairs and liquor licencing fees) or even a failure to intervene in proceedings affecting the lessee's interest, may be held to be a 'repudiation' of the lease. Second, the doctrine of repudiation may be used to evade landlord-tenant statutes. In *Nai*, the case might just as easily have been dealt with as a re-entry by the lessor extinguishing the lessee's interest: however, South Australia's *Landlord and Tenant Act* (1936) s.10 required that the landlord give notice before re-entry and such notice had not been given. The court, however, apparently held that, if the lease could be held repudiated, the notice requirement for re-entry under the statute did not apply (because a 'termination' for repudiation is not a 're-entry' under the statute?).

Finally, *Gallic Pty. Ltd.* v. *Cynayne Pty. Ltd.*[55] demonstrates an attempt by the parties (specifically the lessor) to make use of the new contractualisation of lease law. A clause in a commercial lease expressly stated that a breach of named covenants by the lessee which remained unremedied fourteen days after notice by the lessor in writing would constitute "a breach of an essential term of this lease amounting to a repudiation thereof . . .". The lessee failed to pay rent and the lessor sued on this clause. Paradoxically, the court decided this case, under a lease drafted as a contract, on land law principles. The court treated the 'essential breach' clause as a 'forfeiture' provision, allowing the lessor to use the summary ejectment provisions of the Northern Territory's *Real Property Act* s.192(IV) ("where . . . the lease become forfeited"). The court, as would any court interpreting a grant, construed the terms strictly: thus the court granted an order for possession for breach of the covenant to pay rent, because the lessor had given notice as required under the lease, but dismissed claims under other covenants as the landlord had not given the required notice.

The lessee in *Gallic* attempted to raise a classic defence under the law of contract: misrepresentation.[56] The court considered that provisions in the lease expressly excluding warranties and collateral agreements disposed of this defence. Echoing similar statements in *Progressive Mailing*,[57] Kearney J. criticised this defence as an attempt by the lessee "to take the law into its own hands",[58] by using the other party's misrepresentation as an excuse for the lessee's own failure to pay rent. The court stated that the lessee's proper course would be to bring an action for rescission or damages for misrepresentation, if these doctrines could be held to apply to leases.[59]

[55] (1986) 83 F.L.R. 31 (N.T.S.Ct.).
[56] *See e.g.* Greig and Davis, supra fn. 37 pp.473-517.
[57] Wilson J., supra fn. 20 at 382.
[58] *Cit.* supra fn. 55 at 37.
[59] *Id.* 38.

IMPLICATIONS OF THE DECIDED CASES

1. The Narrow Interpretation

In principle, it is still possible that *Progressive Mailing, Shevill's case* and the others mentioned in the last section could go the way of *Buchanan* v. *Byrnes*. Earlier cases such as *Firth* v. *Halloran*,[60] denying the application of contract law principles to the law of leasehold, have not been expressly overruled and, as explained in the last section, many of the actual decisions can be justified by the application of traditional land law principles. For example, in *Gallic*, Kearney J. avoided application of *Progressive Mailing* by distinguishing the wording of the lease before him from the lease before the High Court in *Progressive Mailing*.[61a] Should the courts decide to recoil from the contractualisation of lease law, or consider that the application of contract principles in any given case yields an unacceptable result, it is always possible to view the cases in the preceding section of this paper as either dealing with peculiar sets of facts not relevant to most cases, or as addressing narrow legal issues other than the broad application of the law of contract to leases. However, the argument of this paper is that, while it is always possible to use legal tools to avoid the application of an undesired precedent, the statements of the judges on the High Court and below are clear, and their intent that leases are to be treated as any other contracts is unmistakable.

One likely means of avoiding the complete contractualisation of lease law may be for the courts to view the cases in the preceding section as wholly concerned with repudiation and fundamental breach.[61b] Since this was the issue with which each of the Australian cases since *Shevill's case* was concerned, the argument may be put that only if a lease is fundamentally breached or repudiated does contract law apply: otherwise the traditional view of tenancy as an interest in land applies. This hearks back to the approach of O'Connor J. in *Buchanan* v. *Byrnes*[62] to the effect that a lease is a grant until it is breached, whereupon it becomes a contract. We shall not know the fate of this argument until some aspect of contract law other than repudiation or fundamental breach is submitted in a leasehold case. Perhaps the treatment of misrepresentation as a defence to termination of a lease in *Gallic* is a signal: the argument did not succeed on the facts but it was not rejected out of hand. In any event, it would be unwise to limit the application of contract principles to repudiation and fundamental breach, especially given the facts that whether a given act constitutes 'repudiation' or a 'mere' breach and whether or not the breach is 'fundamental' are so much a matter of the court's impression of the case. With the strong financial incentive raised by the cases decided thus far for the 'innocent' party to argue on a contract basis rather than

[60] Supra fn. 25.
[61a] Supra fn. 55 at 40.
[61b] *cf* K. Mackie, "Repudiation of Leases" (1988) 62(1) Australian Law Journal 53.
[62] Supra fn. 23.

a land law theory,[63] there will be a great deal of manoeuvring of the meanings of 'repudiation' and 'fundamental-ness' of breaches of lease if contract principles are to be applied only in these circumstances, with the likely result that every breach will become 'fundamental' and result in termination. Should that be the result, the law will have come full circle, with every covenant in a lease liable to lead to forfeiture on breach, just as in land law, but now with the added effect that forfeiture yields a payment of damages to the lessor. The prospects for security of tenure if every lessor has a financial interest in his lessee's breach and forfeiture are not attractive.

Another possible way of avoiding the application of the principles laid down in the cases in the preceding section is to treat the cases as dealing only with commercial leases. Every case in the preceding section, from *Buchanan* v. *Byrnes* to the English case *National Carriers,* to all of the Australian cases in the 1980's, have had a commercial (as opposed to a residential) lease before the court. The judges actually did not comment on the fact that the leases were commercial, so it is not clear if they meant for residential leases to be treated as contracts too. Certainly there is less financial incentive for a lessor to sue a residential lessee in contract than a commercial lessee and less financial capacity for the average residential lessee to sue his landlord in contract for breach of a lease. Also, the residential tenancy is more likely to be regulated by statute than the commercial tenancy[64] which may, depending upon the wording of the statute, limit the ability to apply contract principles.[65] Still, while the residential lease is less likely to come to court for these reasons, the issue of whether contract principles apply to residential as well as commercial leases technically remains open until contract principles are submitted in a case on a residential lease.

There are good reasons for drawing a distinction between commercial and residential leases in the matter of applying contract law. The residential lessee is less likely to bargain over the terms of the lease, and is less likely to have legal assistance in entering the leasehold agreement than the commercial lessee. Thus, the residential lease is less likely than the commercial lease to conform to the contractual model of the 'meeting of the minds'. The residential lessee has a greater personal, emotional and social stake in the premises as 'home' than does the commercial lessee who treats the premises either as an investment or as a fixed-cost resource of doing business. Thus the residential lessee is less financially and emotionally able than the commercial lessee to meet the expectations of the lessor, for which he will be held accountable in contract. On the other hand, as will be discussed in the 'possibilities' section *infra,* the residential tenant, if provided with legal assistance and representation, can be protected in

[63] Due to the greater scope of damages, *see* pp.18-20 *infra.*
[64] See Bradbrook, *cit.* at note 19, *supra*, at 605, but note that common law still prevails for residential tenancies in Western Australia, Tasmania and the Northern Territory.
[65] See the discussion at pp.21-22 *infra.*

many ways far better by contract law than land law. When courts do come to the issue of applying contract law to residential tenancies, they will face the dilemma that residential tenants are better able to enjoy the benefits of contract law but far less able to shoulder its burdens than their commercial counterparts.

Although, as explained here, many issues in the two-to-three-year-old contractualisation of lease law remain undecided. Throughout the remainder of this paper, it will be assumed that the judges will be taken literally and that the law of contract potentially applies to any lease on any issue and on any set of facts.

2. Landlord-Tenant Disputes

There are several aspects of landlord-tenant disputes (as we have come to know them under land law) which have significantly changed due to the cases on the contractualisation of lease law already decided and discussed herein. Landlord-tenant disputes have traditionally been carried on through eviction by the lessor, 'moving away' by the lessee, withholding rent by the lessee, suit on the lease by either party or resort to statutory protection by the lessee. While actions by the lessor have not yet been dealt with, the decided cases severely limit the tenant's traditional avenues of redress.

(a) *Abandonment of the Premises*

The landlord's traditional answer to the tenant's complaints has been "if you don't like it, get out". Under the contractualisation of lease law, the advice now has a more-sinister and self-serving effect: the tenant who 'gets out' repudiates the lease and may not only lose his right to the premises but may also have to pay hefty damages to the landlord.[66]

Under land law principles, when the tenant abandoned the premises, the landlord had a choice: he could either refuse to accept the abandonment and sue the tenant for rent, in which case he must do nothing inconsistent with the tenant's right to possession,[67] or he could accept the abandonment, and thus accept possession in lieu of rent.[68] The tenant, too, thus had a corollary choice: if he was sued for rent he could return to the premises and pay rent or, if his abandonment was accepted, he could forget about the premises and the rent. In most cases, where both parties were unsatisfied with the relationship, aban-

[66] On the other hand, in making such a statement the landlord may himself be repudiating the lease, see p.25 *infra*.

[67] *Maridakis* v. *Kouvaris*, *supra fn.* 52 at 199. If the landlord did do something inconsistent with the tenant's right to possession (in *Maridakis*, reletting the premises) this was, in land law terms, a 'surrender by operation of law' and the landlord lost all right to rent thereafter.

[68] This was an express surrender of the lease. If the landlord received rent thereafter, he was held to have waived the right of possession. *Matthews* v. *Smallwood* [1910] 1 Ch.777 at 786-788 (K.B.). See also Stephen J., in *Sargent* v. *ASL Developments Ltd.* (1974) 131 C.L.R. 634, 646 (H.C.).

donment would be accepted. The parties would go their separate ways: the landlord finding a more acceptable tenant and the tenant finding a more acceptable premises and/or landlord.

Contractualisation does away with the need for the landlord to choose between possession and damages: the landlord can have *both* and has a strong incentive to sue rather than to let the tenant go and to look for another tenant. If the landlord chooses to accept the repudiation of the lease by the tenant who has moved out, he can sue for damages, as in *Progressive Mailing* or the *Wood Factory*: but if, as the 'innocent party', he elects not to accept the tenant's repudiation, he can still sue for damages[69] in holding the tenant to his contract to pay rent. The change from land law is that the tenant can be made to pay rent for premises which he has no right to occupy. Even if the tenant relents and pays the rent, he can be denied entry to the premises and required to continue paying the rent.

(b) *Withholding the Rent*

In each of the cases in which the issue arose (except for *Shevill's case*)[70] the judges were unanimous in holding that an intentional refusal to pay a significant amount of rent for a significant period of time was a fundamental breach of the lease,[71] entitling the lessor to both revoke the lessee's right to possession and sue for consequential damages. Therefore, the traditional tenant's response to a landlord who refused to make essential repairs or the traditional tenants' union tactic of organising rent strikes have become far more dangerous for the tenant.

Tenants have always known that they risked eviction for withholding rent. The risk may have been worth taking where the premises were in such a condition or the tenants' union had sufficient support that the landlord would not be able to find another tenant. The tenant had no greater risk than eviction because, as the holder of an interest in land, failure to pay rent was merely a breach of a condition subsequent which deprived the tenant of his interest in the land.

[69] Greig and Davis, supra fn. 37 at p.1419 *et seq.*

[70] *Progressive Mailing House Pty. Ltd.* v. *Tabali Pty. Ltd. cit. supra fn.* 20. *Wood Factory Pty. Ltd.* v. *Kiritos Pty. Ltd., supra fn.* 50. *Ripka Pty. Ltd.* v. *Maggiore Bakeries Pty. Ltd., supra fn.* 41. In *Gallic Pty. Ltd.* v. *Cynayne Pty. Ltd., supra fn.* 55, the lease had expressly deemed the covenant to pay rent as a fundamental term.

[71] Mason J. in *Progressive Mailing, Id.* 381. Wilson J. in *Progressive Mailing, Id.* 382 (but of his comments in *Shevill* v. *The Builders' Licencing Board, supra fn.* 6 at 798-799). Brennan J. in *Progressive Mailing, Id.* 383 (agreeing with Mason J. on this point, although rejecting the idea that any default of rent would be sufficient). Deane J. in *Progressive Mailing, Id.* 389 (agreeing with "other members" on this point). Samuels J.A. in *Wood Factory, Id.* 116 ("refusal" or "withholding"). Priestly J.A. in *Wood Factory, Id.* 137 ("The tenant was in again breach of its rent covenant . . . this state of affairs seems to me to amount to repudiatory conduct . . ."). McHugh J.A. in *Wood Factory, Id.* 145 (*per Progressive Mailing*). Gray J. in *Ripka, Id.* 634. *Cf.* Gibbs C.J., in *Shevill* v. *The Builders' Licencing Board, supra fn.* 6 at 795 ("slight" failures to pay rent not fundamental breach).

Now that contractualistion has replaced the law of surrender with the law of fundamental breach, the landlord has no worries about finding another tenant. He can not only evict the tenant but sue the tenant either to cover the rent until he finds another tenant, as in *Progressive Mailing,* or perhaps for the whole unexpired term of the lease whether or not he finds another tenant, as in the *Wood Factory.* While the treatment of withholding rent as a fundamental breach has thus pulled the 'teeth' of this tactic against the landlord, it has also opened the possibility that the tenant will have to pay rent for two premises: the new occupied premises and the old premises subject to the breached lease, which the tenant no longer has the right to occupy.

Another pitfall for organised rent strikes has not yet been canvassed in the cases. If a lease is now a contract, inducing its breach is now a tort.[72] The landlord may sue the tenants' organisation for inducing breach of the lease and the tenant may sue the organisation or counsel advising withholding rent for negligent misrepresentation.[73a] The landlord may also be able to get injunctions or orders of specific performance of the lease which will subject tenants to penalties of contempt of court should they continue to withhold rent.[73b]

(c) *Suit on the Lease — Calculation of Damages*

Since the measure of damages was not an issue in any of the cases,[74] the courts merely allowed the lessors' claims to stand, creating inconsistent precedents on the measure of damages for fundamental breach of a lease. The courts will have to decide this issue soon.

In the small group of cases canvassed in this article thus far, there are now three contradictory methods of awarding damages for fundamental breach of a lease. The first, exemplified by *Ripka* and *Gallic,* is the one most consistent with traditional land law: rent in arrears and unpaid rent to the date of possession by the lessor. The second moves away from what would be recoverable under traditional lease law and is exemplified by *Progressive Mailing*: rent in arrears, unpaid rent to the date of possession by a new lessee and the costs of finding a new lessee. The third moves fartherest from traditional principles

[72] *Cf.* Fleming, *The Law of Torts* (6th ed., Sydney, Law Book Company Ltd., 1983) pp.651-652.

[73a] *See Id.* pp.604-612. Damages would presumably, for the ill-advised tenant, be the damages owed to the landlord for repudiation of fundamental breach, which would not be owing had the tenant not been advised to withhold the rent. *See* the comments of Mason J. in *Progressive Mailing, supra fn.* 20 at 381-382 (Counsel's advice no defence to repudiation in withholding rent).

[73b] Meagher, Gummow and Lehane, *Equity: Doctrines and Remedies* (Sydney, Butterworths, 1984, 2nd ed.) p.507.

[74] Although it apparently was an issue in *Progressive Mailing,* at the Court of Appeal level, supra fn. 20 at p.377, the judges on the High Court dealt with the damages as either recoverable or not recoverable rather than considering how they ought to be measured. In the *Wood Factory,* the issue of damages was handled as an issue of when repudiation (or, in Priestly J.A.'s terms, surrender) took effect, if at all, although McHugh J.A. did address the measure of damages as well, supra fn. 50 at 146-147.

and is exemplified by the *Wood Factory*: all unpaid rent during the term of the lease, whether in arrears or *in futuro*, regardless of possession by the lessor or any third party (although any payments by third parties are credited against the lessee's obligation).

Choosing among these measures is really a matter of construing the promises in the lease. In the *Ripka-Gallic* approach, the lessee is implicitly assumed to have promised: "I will pay you rent if and for as long as I have the right to possess the premises". In the *Progressive Mailing* approach, the lessee is implicitly assumed to have promised: "I will pay you rent for the term of the lease unless someone else takes up this obligation". In the *Wood Factory* approach, the lessee is implicitly assumed to have promised: "I will pay you, unconditionally, the sum of money described in the lease as rent, as provided therein". Of course, the wording and circumstances of the lease will help the court to determine the true meaning of the lessee's promise to pay rent, as in any other contract.

It is submitted that the *Ripka-Gallic* approach is most consistent with contract law and good economics. It is obvious that the right to possession is the consideration for the promise to pay rent. The *Ripka-Gallic* approach ties these two together: the lessee's obligation to pay rent ends when the consideration for that obligation (the lessor's duty to deliver possession) ends. In terms of expectation losses,[75] the lessor's reasonable expectation had the lessee performed the lease was that the lessee would pay rent while he had the right to possession. If *Progressive Mailing* goes too far, the *Wood Factory* goes beyond the pale in making the lessee guarantor of the rent for the whole term of the now-defunct lease, as if the lessee had pledged to pay a sum of money without any consideration in terms of right to possession. Allowing a claim for rent beyond the date of possession also offends contract notions of the duty to mitigate damages.[76] It can lead, as in the *Wood Factory* itself, to lessors allowing third-parties to occupy the premises rent-free or *releasing the premises* at a lower rent *and charging* the self-created loss off to the ex-lessee.[77] The *Ripka-Gallic* approach puts the duty on the lessor to take all reasonable steps to mitigate his losses by putting a new lessee into possession, at the level of rent in the original lease, as soon as possible. If any claim for rent after the termination of the lease is allowed, it should be supported by proof that the lessor has been unable, despite all reasonable measures, to relet at the rent in the breached lease and that the lessor

[75] Greig and Davis, supra fn. 37 p.1352.

[76] *Id.* 1388-1389.

[77] The judges in *Wood Factory*, supra fn. 50, made much of the fact that the third party had an obligation to pay rent even though it failed to do so. In calculating the lessor's damages, default by a third-party is immaterial. The Court of Appeal, instead of requiring the lessor to make appropriate arrangements with the third-party to recover rent for its occupation, allowed the lessor to shift its loss to the lessee, who could not sue the third-party in contribution. *Cf.* The argument of McHugh J.A. *Id.* 146-147.

has not, for example, unreasonably denied the lessee the right to find a *replacement* tenant.

In economic terms, rent is an occupation cost of housing. The most efficient measure of damages is one which assures continued occupation at market rent. The *Ripka-Gallic* approach does this by putting the occupation cost on the party with the right to occupation (lessor, lessee or new lessee), creating a strong incentive to put a rent-paying occupier into possession as soon as possible. The other methods allow the lessor to shift the occupation costs to the ex-lessee and underutilise the premises. These alternatives are recipes for empty buildings, unearned income and exploitative landlords.

(d) *Statutory Regulation of Tenancy*

Nai and *Gallic* present disturbing examples of how the contractualisation of lease law can be used to manipulate statutes regulating tenancy and tenant's rights. In *Nai,* Zelling J. accepted a submission that s.10 of the Landlord and Tenant Act (S.A.) 1936, (providing a duty on the lessor to give notice before re-entry) did not apply because the termination of a lease for repudiation or fundamental breach was not a 're-entry'.[78] The act of the lessor in taking possession was simply renamed to take the lessor's conduct outside the name for such conduct referred to in the statute. In *Gallic,* the reverse exercise was performed with regard to 'forfeiture'. The Northern Territory's *Real Property Act* s.192(IV) allowed "any lessor where . . . the lease became forfeited . . ." to summon a person before a judge in chambers to show cause why the person summoned should not give up possession to such a lessor. Kearney J. held that acceptance by the lessor of repudiation by the lessee constituted a 'forfeiture' and thus s.192(IV) applied.[79] If the statute is drafted in the language of land law, the court now has a choice whether to address the case in land law terms and apply the statute or to address the case in contract law language and hold that the statute does not apply.

At the least, the State Parliaments ought to quickly rewrite their statutes so as to cover 'leases' and 'contracts', 'forfeitures' and 'terminations', 're-entries' and 'acceptances of repudiation' etc. alike. This could have the side-effect of further muddying the distinction between leases and licences but, since *Progressive Mailing,* the distinction means less than it ever has. Otherwise, there is a danger that the new concept of a lease as a 'contract of tenancy' will be used as the loophole in the protection of tenants which the concept of 'licence' has at times been.[80] It is also even more necessary for tenancy statutes to expressly

[78] Supra fn. 54 at 350-351.

[79] Supra fn. 55 at 38.

[80] *See e.g.* Teh, *Residential Tenancies Handbook — Victoria,* (Sydney, Butterworths, 1982), para.114; Lang *Residential Tenancies Handbook — New South Wales,* (Sydney, Law Book Company Ltd.), 1986, p.43 ("licencees who are boarders or lodgers" vs. "licencees who may be subject to the legislation").

state that they operate 'notwithstanding agreement to the contrary', since courts tend to assume that parties can contract out of statutes,[81] so that it cannot be assumed that grantors of interests in land can evade statutes by draughtsmanship.

POSSIBILITIES FOR THE APPLICATION OF THE LAW OF CONTRACT TO LEASES

The cases decided thus far are but a peek through the keyhole at the potential for contractualisation to restructure the law of leasehold. If the judges are indeed serious about applying the law of contract to leases as if they were any other contracts, a whole range of possibilities lies open. This section will examine a few.

1. Frustration

The next probable stepping-stone in the walk toward full contractualisation of lease law is the application of the doctrine of frustration to leases. The House of Lords in *National Carriers* accepted the idea in principle and the judges in *Progressive Mailing* seemed to take frustration on board with repudiation and fundamental breach as being equally applicable to the lease.[82]

True frustration, as opposed to mere disappointment,[83] occurs rarely in practice. Thus most claims of frustration submitted to the courts will likely be rejected. Some states make statutory provision for aspects of frustration of a residential lease.[84] The courts will have to decide what, if anything, the common law of frustration of contract will add to these statutory provisions for leases.

However, there are several examples of cases where the courts might hold that a lease has been frustrated. Some likely examples are:

(1) where the demised premises have been totally destroyed by an act of God or by a third party,[85]

(2) where the premises have been rendered uninhabitable (in the case of a residential lease) or inaccessible by act of God or a third party,[86]

[81] *Halsbury's Laws of England* (4th ed, Vol.9, London, Butterworths, 1974) p.289.

[82] *See* Mason J., supra fn. 20 at 378. Deane J., *Id.* 388. *See also* Greig and Davis, supra fn. 37 pp.1326-1331.

[83] *Cf.* Greig and Davis, *Id.* 1304 ("the application of the doctrine is, in essence, a dispensation by the court . . . It follows that a decision whether or not a contract has been frustrated must depend upon the judicial appreciation of the facts of the particular case . . ."). Regarding leases specifically, *see National Carriers,* supra fn. 28 at 692 (per Lord Hailsham) at 697 (per Lord Wilberforce) and at 708 (per Lord Russell – "second answer of the *Pinafore's* captain on the subject of *mal de mer*").

[84] *Residential Tenancies Act* 1975 (Qld.) s. 14.
Residential Tenancies Act 1978 (S.A.) s. 71.
Residential Tenancies Act 1982 (Vic.) s. 114.

[85] *Cf. Taylor* v. *Caldwell* (1863) 122 E.R. 309 (Q.B.)

[86] *Robertson* v. *Wilson* (1958) 75 W.N. (N.S.W.) 503 (N.S.W.S.Ct.). But the length of time during which the inaccessibility or uninhabitability occurred must take up a significant proportion of the term to constitute frustration and not mere inconvenience; *National Carriers, supra fn.* 28.

(3) where the land has been resumed by the Crown[87], or the lessor has otherwise lost the ability to grant exclusive possession unexpectedly and through no fault of his own.

Some other cases where the courts may and should find frustration include:

(1) where the premises are unexpectedly rendered unsuitable for a purpose clearly intended by the parties,[88]
(2) where the premises are unexpectedly rendered (in the case of a commercial lease) commercially worthless in a way not foreseeable by the parties,[89]
(3) where the lessee is unexpectedly, through no fault of his own, unable to carry out his obligations under the lease, for example due to involuntary transfer or unemployment (in the case of a residential lessee), or involuntary bankruptcy (in the case of a commercial lessee).[90]

The effect of a successful claim of frustration will be to terminate the lease from the date of the frustrating event.[91] Thus, the lessee will lose the right to possession but will be free of the duty to pay rent and any other obligations under the lease. Of course, if the lessee remains in occupation after the effective date of termination, he will owe *pro rata* rent for each day of actual occupation: whether it is called 'mesne profits' or *quantum meruit*[92] is not important, although *quantum meruit* makes more sense in these circumstances. In addition, Victoria and New South

[87] *Cf. Brisbane City Council* v. *Group Projects Pty. Ltd.* (1980) 54 A.L.J.R. 25 (H.C.) (frustration of land use deed).

[88] *Cf. Krell* v. *Henry* [1903] 2 K.B. 740 (C.A.) This is the basis of the application of the doctrine in America. See *Restatement (2d) of the Law or Property (Landlord and Tenant)* (Vol.1, Washington, American Law Institute, 1977) para. 9.3.

[89] Admittedly, this is going to be the issue where the court decides if the party seeking relief from the contract has been deprived of the benefit for which he bargained or merely inconvenienced. *Cf. e.g. Ringstad* v. *Gollin & Co. Pty. Ltd.* (1924) 35 C.L.R. 303 (H.C.). That is why the word "worthless" is used in the text, as the courts will probably hold that a diminution in value is a part of the business risks of the contract. *But cf.* American law of frustration, which draws a more clear distinction between 'impossibility' of performance and 'commercial frustration' of the 'expected value' of performance in *Restatement, Id.* para. 9.3 Reporter's Note 2.

[90] This is being taken as the equivalent in a residential lease of the normal contractual bases of 'impossibility of performance in the manner contemplated' or 'delay in the possibility of performance'. *See e.g.* Greig and Davis, *op.cit.* pp.1309-1312. Alternatively, the courts may follow the principle from contract law, *Id.* 1241-1252 that delay or inability to perform is a fundamental breach. The essential difference is whether the delay or inability is caused by a third-party or is an expression of the intent of the breaching party not to perform. It is submitted that the frustration principle makes more sense here (unless the tenant has voluntarily quit or requested the transfer) because in most cases the tenant as employee has no choice, so that the cause of the inability to perform is the tenant's employer not the tenant. *But cf.* the application of the fundamental breach principle to a commercial lessee in the *Wood Factory, supra fn.* 50.

[91] Greig and Davis, op. cit. p.1331.

[92] *Id.* 1332-1336.

Wales have special statutory provisions for the frustration of contracts generally, which should assist lessors and lessees.[93]

In economic terms, applying frustration to leases where applicable makes good sense. The lessor recovers possession and can put the premises to a more-efficient use. The lessee is freed from the duty of putting more resources into a dead loss and can find another premises to accomplish his original purpose.

2. Repudiation/Fundamental Breach by the Lessor

Although all the cases thus far have concerned repudiation or fundamental breach by a lessee, it is inconceivable that the courts would one-sidedly hold that a lessor could not repudiate or fundamentally breach a lease. There are two acts of a lessor which go to the heart of a lease and deprive the lessee of the essence of his bargain:

1. Repudiation of the lessee's right to exclusive possession of the premises for the term of the lease.[94] If the lessor:
   (a) fails or refuses to grant exclusive possession to the lessee at the outset of the lease,
   (b) harasses the lessee with a view toward forcing the lessee to abandon the premises,
   (c) enters the premises without the consent of the lessee,
   (d) attempts to grant an inconsistent lease to another party for any part of the demised premises for any part of the term, or
   (e) unilaterally changes the terms of the lease without the consent of the tenant,

   these would be acts repudiating the lease.
2. Breach of the duty to provide the premises in an agreed or reasonably contemplated condition.[95] This is based on the assumption that the promise to pay rent is conditional on the provision of a given standard of housing service. If breach of the lessee's promise to pay rent

[93] *Frustrated Contracts Act* 1959 (Vic.).
Frustrated Contracts Act 1978 (N.S.W.).
Neither Act expressly excludes leases or defines "contract" in such a way as to exclude them.

[94] *Cf.* The "covenant of quiet enjoyment" implied by land law Sackville and Neave, op. cit. pp.675-679 and the obligation not to derogate from the grant, *Id.* pp.680-682. The major differences are (1) the breadth of the tenant's rights in contract and (2) the extensive measure of damages in repudiation/fundamental breach, compared to land law. These rights are also restricted (*Residential Tenancies Act* 1975 (Qld.) s.8, *Landlord & Tenant Act* 1958 (Vic.) s.111, *Landlord & Tenant (Amendment) Act* 1948 (N.S.W.) s.88D, *Residential Tenancies Act* 1978 (S.A.) s.49) or augmented (Vic. s.104, N.S.W. s.88A-B, S.A. s.47) by statutory provisions pertaining to residential leases. Regarding commercial leases, see *Retail Tenancies Act* 1986 (Vic.) s.17, *Retail Shop Leases Act* 1984 (Qld.) s.15, *Commercial Tenancy (Retail Shops) Act* 1985 (W.A.) s.14.

[95] *Cf.* The "implied condition of suitability for the use contemplated by the parties" in American contractual law of leases, *Restatement (2d)*, op. cit., Chapter V and the statutory trend in Australia (Qld. s.7(a)(ii) and S.A. s.46, *Ibid.* and *Residential Tenancies Act* 1980 (Vic.) ss.97-100). *Cf. also Calabar Properties Ltd.* v. *Stitcher* [1983] 3 All E.R. 759 (C.A.).

is a fundamental breach of the lease, as decided in the cases canvassed in this paper, then breach of the condition on which this promise is based must equally be a fundamental breach. Admittedly, it may be difficult for a court to determine what the agreed or implied standard is and whether a given breach is sufficiently 'substantial', but no more difficult than in the case of any other contract. Among the relevant evidence would be:[96]

(1) the language of the lease,
(2) the discussions of the parties,
(3) the standards of the community,
(4) any past practice or course of dealing by the parties.

This would be a significant improvement for lessees over land law, where merely delivering possession, regardless of the condition of the premises, seemed sufficient.[97]

If the lessor repudiates or fundamentally breaches the lease, the lessee, as the innocent party, must then elect whether or not to continue the contract and sue for damages resulting from the breach, or to terminate the contract and sue for consequential damages.[98] The lessee can make the election expressly or by course of conduct.[99] If the lessee elects to continue the lease, he remains liable to pay rent and continues to have the right to possession: but he can sue for damages resulting from the breach. Such damages would probably be nil in the case of repudiation unless the lessee were actually forced out of possession, but in the case of fundamental breach of the condition of providing housing services, the lessee could recover the costs of upgrading the premises to the agreed standard. If the premises were rendered uninhabitable by the lessor's refusal to make repairs, the lessee could recover the costs of temporary accommodation.

Alternatively, the lessee could elect to terminate the lease and sue for consequential damages. In this case, the lessee surrenders the right to possession, ceases to be under a duty to pay rent and may recover damages for loss of the lease. The nature of the damages will depend upon which theory of damages the courts accept. Under the *Ripka-Gallic* theory, the end of the duty to pay rent would cover the lessee's loss. Under the *Progressive Mailing* theory, the lessee would recover the cost of removal and the cost of temporary accommodation until new housing arrangements are made. Under the *Wood Factory*

[96] *Cf.* Greig and Davis, op. cit. pp.538-585.

[97] *Cf.* Sackville and Neave, op. cit. pp.682-685 (residential lease) *Bradford House Pty. Ltd.* v. *Leroy Fashions Group Ltd.* (1983) 5 T.P.R. 32 affd. 5 T.P.R. 351 (Full F.Ct.). This result is not surprising, given that land law is concerned only with paramount rights to possession, while contract law is primarily concerned with enforcing the expectations of the parties.

[98] Greig and Davis op. cit. p.1254 *et seq.*

[99] *Id.* pp.1257-1264. This issue arose in the *Wood Factory supra fn.* 50 and *semble* that the lessor did not have any obligation to formally communicate his election to the lessee. *Cf.* also *Ripka,* supra fn. 41 at 635.

approach, the lessee would recover the difference between the rent payable in the lease and the cost of housing, whether temporary or permanent, for the unexpired term of the lease.

In addition, the application of contract remedies should give the lessee equitable protections not available under land law.[100] The lessee should be able to apply for an injunction to restrain an anticipated or actual repudiation or fundamental breach.[101] The lessee may also be able to obtain an order for specific performance of the landlord's obligations under the lease.[102] On the other hand the restrictions normally applying to equitable remedies would apply. The lessee must not have unreasonably delayed bringing his action[103] and must not have himself acted unconscionably.[104]

3. Misrepresentation

As referred to in the discussion of *Gallic*, misrepresentation has already been raised as a defence to fundamental breach. In *Gallic,* the defence was held to have been expressly excluded by the wording of the lease.

However, the failure of the court in *Gallic* to dismiss misrepresentation out of hand, along with *dicta* in the other cases that it is the law of contract and not merely the law of repudiation and fundamental breach which applies to leases, suggests that misrepresentation is available either as a cause of action or a defence to an action on a lease. This approach to a lease is a distinct product of the contractualisation of lease law: 'misrepresentation' by a grantor makes no particular sense.

Given that leases are often entered into after discussions between the parties and that, especially in residential leases, the parties often contract on the basis of the discussions rather than the wording in the lease, misrepresentation has a potentially wide application to leases. Courts are far more willing to look at oral agreements in contract than at parol evidence of the meaning of a grant.[105] Therefore, contractualisation suggests that courts may be more willing to consider evidence of the parties' discussions in determining their respective rights under a lease.

Misrepresentation involves presenting a false picture of the relevant facts to another party which induces that party to enter into a contract. In this case, the lessor might give false information to a prospective lessee concerning the condition of the premises, the amenities available, the

[100] This is on the assumption that the doctrines of repudiation and fundamental breach will give the lessee new rights at law which will be enforceable at equity. It is not to suggest that the lessee has not always had access to equitable remedies to enforce his (quite limited) rights under the lease as a grant. See Sackville and Neave, op. cit. p.714.

[101] Greig and Davis, op. cit. p.1491.

[102] *Id.* p.1470.

[103] *Id.* p.1479 (where the delay produces injustice to the lessor).

[104] *Id.* pp.1476-1479.

[105] The essential difference is that, in contract, the court is seeking to ascertain the intent of the part*ies* (note the plural) while in construing the grant of an interest the court is seeking to ascertain the intent of the grantor alone. *Cf. Halsbury's Laws of England*, op. cit., Vol.9, p.149 and Vol.12, p.615.

proximity to transport, schools, shopping, etc., or the lessor's ability to convey exclusive possession for the whole term of the lease, for example. The lessee might give false information about his ability to pay rent, the numbers of persons to occupy the premises or the uses to which the premises will be put.

The major issue in a case of false inducement, after the falseness of the information and its role in actually inducing the other party to enter the lease,[106] will be the mental state of the party giving the information.[107] If he intended to give a false impression, or did not care whether he gave a false impression, which he knew or had reason to know that the other party would rely upon as an inducement, then this is fraud and the other party has the same election as in repudiation: to terminate the lease and sue for damages or to continue the lease and sue for damages.[108] The difference from repudiation is that damages are limited to the costs of relying upon the false information (rather than expectation losses) which may be quite low in the case of a lease. Also, as Lindgren *et al* point out,[109] proving the defendant's mental state is notoriously difficult.

Negligently giving false information comes under the tort of negligent misrepresentation which has, in principle, been available to lessees (along with everyone else) since the 1960's.[110] Suffice it to say here that the courts have limited its application to a defendant whom the plaintiff would reasonably rely upon to have specialised knowledge.[111] The lessor could almost never sue the lessee on these grounds and the lessee might only be able to sue the lessor when the lessor was a land agent or someone in the profession of letting premises, perhaps not even then.[112] If successful, the measure of damages is only the cost of reliance upon the information,[113] in addition to termination. However, unlike fraud, the lessor can easily evade liability for negligent misrepresentation by disclaiming it in the lease, as in *Gallic*.

Finally, there is 'innocent' misrepresentation, where the party giving the information did not know and had no reason to know that the information was false.[114] This should be relatively easy to prove in the absence of a mental state requirement, provided that the court is satisfied that the innocent party would not have entered the lease knowing that the

[106] *i.e.* The issues of 'reliance' on the information and of its 'materiality'. *See* Lindgren, Carter and Hartland, *Contract Law in Australia* (Sydney, Butterworths, 1986) pp.334-335.
[107] *Id.* 335-348.
[108] *Id.* 339.
[109] *Id.* 337-338.
[110] Fleming, op. cit. p.604 *et seq.*
[111] *i.e.* a 'special relationship', *Id.* 605 *et seq.*
[112] *Cf.* The position of an estate agent *selling* (as opposed to leasing) land, where the Australian courts (unlike their Canadian and New Zealand counterparts) seem unwilling to find a special relationship. *Id.* 606.
[113] *Id.* 611-612.
[114] Lindgren, Carter and Hartland, op. cit. pp.346-348.

information was false.[115] The remedy is termination,[116] which can be far more significant in the case of a lease than in many other contracts in terms of benefit to the innocent party. However, there is no right to damages.[117]

It should be stressed in considering the lease that silence can be a 'representation' in the sense described here of presenting a false picture.[118] If the lessor presents true and glowing statements about the rent, the location and the amenities of the premises but says nothing about the cockroaches and rats inside or the deafening construction noise next door, he has misrepresented the premises. The main issue in these cases would probably be the ability of the reasonable person in the lessor's shoes to discover the undisclosed defect.[119] If the defect might easily have been noticed by a routine view of the premises, the court would probably refuse a remedy, perhaps on the ground of non-reliance. However, since the leasehold is normally a longer-term relationship made on the basis of information about a fixed asset, and since the parties often begin negotiations with unequal information about the asset, 'misrepresentation by silence' should be at least as common in leases as in other contracts (if not more so).

4. Collateral Warranties

Again, owing to how leases, especially for residential use, are typically negotiated, collateral promises must be rather common between lessees and lessors. As long ago as 1919, the High Court accepted that such collateral agreements under leases could be enforced, in the case of *Hoyt's Pty. Ltd.* v. *Spencer.*[120]

It is quite common for a party, in the course of negotiations, to make a promise or representation about his future conduct which appears nowhere in the written lease, but which the other party relies upon in signing the lease. The lessor might say "you can stay as long as you want, I'll renew the lease" or "no worries, I'll look after the leaking toilet before you move in" or even "don't worry about that notice requirement in the lease — it's just a formality!!". The lessee might say "I don't have late-night parties" or "I won't buy a dog" or "my firm will comply with all local laws".

Not all of these, however, would be certainly enforceable under the current law of collateral warranty. The first issue will be whether the promise

115 *Id.* 347-348.
116 *Id.* 347.
117 *Ibid.*
118 *Id.* 331.
119 Analogous to the distinction between a 'latent' and a 'patent' defect in the sale of goods. *Cf. Sale of Goods Act* 1923 (N.S.W.) s.19(2). In the American contractual law of leases, the lessee may presume that visible defects will be remedied before the lessee takes possession, without losing the right to sue for misrepresentation, unless the circumstances are such as to suggest an implied agreement to excuse the lessor. See *Restatement* (2d), *op.cit.* para. 5.1, comment c.
120 (1919) 27 C.L.R. 133, 139 (proposition (b)) and 146 ("full play").

really was made a part of the lease. The court must decide whether the promisee really did, in his own mind, rely upon the promise in agreeing to the lease or whether he would have signed the lease knowing that the promisor was lying.[121] The other issue will be a major loophole in the law of collateral warranty in Australia generally: the collateral promise is not enforceable if it is contradicted by the written lease.[122]

The effect of the 'consistency' requirement in limiting the enforceability of collateral warranties by the terms of the written lease causes special problems in the case of the residential lease, which is normally unilaterally imposed by the lessor. The lessor can exclude his own liability for breach of collateral promises he makes by writing a clause into the standard-form lease stating that collateral warranties are not enforceable.[123] In practice, the lessee is normally unable to write the lease to exempt himself from liability in this way, or to negotiate about the exclusion clause.[124]

5. Control of the Effects of Economic Power by the Law of Contract[125]

In land law, an interest in land is the grantor's to give. The right to dispose of one's property as one will – or not to dispose of it at all – has been hard-won[126] and is basic to the values of our society.[127] The idea of 'fairness' does not enter into the question: no one has a 'right' to an interest in another's land and it would be 'unfair' to require an individual to meet someone else's concept of fairness in deciding how to deal with his own property.

The law of contract is based upon different premises to those of the land law. Where land law is rooted in the feudal notion of a grant by a superior to an inferior,[128] contract is rooted in ideals of individual equality and independence. In contract one does not grant rights to the other: there is a 'meeting of minds', a mutually-beneficial exchange, which each party enters willingly for his own benefit.[129] To be sure, the reality

[121] *Cf.* Greig and Davis, op. cit. pp.497-503.

[122] Supra fn. 120.

[123] As in the *Gallic* case, supra fn. 55. *But cf.* the discussion in Greig and Davis, op. cit. pp.509-513, of alternative means to protect the interest of the promisee.

[124] But the doctrine of construction *contra proferendum* may assist the lessee in these circumstances. See pp.34-35 infra.

[125] *Cf.* Clarke, "Unequal Bargaining Power In The Law of Contract" (1975) 49 A.L.J. 229. See also Bradbrook, op. cit. pp.612-613 on the possibility for application of the consumer protection and anti-monopolisation provisions of the *Trade Practices Act* to leases.

[126] *See* Holdsworth, *A History of English Law* (5th ed., Vol.III, London, Methuen & Co., 1942) pp.105-125; Vol.VII, pp.193-238; Vol.IV, pp.420-467.

[127] *Cf.* The definition of ownership by Cohen, "Dialogue On Private Property" (1954) 9 *Rutgers Law Review* 357.

[128] The title of the Australian Consumers' Association argument for tenancy law reform, supra fn. 18, is instructive.

[129] Atiyah, *An Introduction To The Law Of Contract* (3rd ed., Oxford, Oxford University Press, 1981) pp.5-6.

of contract may rarely meet the ideal:[130] but the ideal generates the rules and the rules determine how the cases will be decided.

The change in the conception of a lease from a grant to a contract must, on this analysis, have the potential of profound change in the law of leasehold. Throughout the traditional law of leases there is a subtle bias toward the lessor (the term 'landlord' is instructive here): the lessee has no right to anything unless the lessor has expressly deigned to grant something in the lease, or unless common or statutory law has deigned to give the lessee some form of protection against the unbridled will of the lessor. In contract, the fundamental issue is always "what did the parties agree upon?" or, here, "did the lessee agree in law to the provision in question?". For the first time since the 1400's, the lessee has the potential to be something more than a mere 'termor',[131] having nothing more to protect than a passing interest in the land. In contract, the lessee is an equal, bargaining over his rights and interests.

Australian courts have never had the courage to follow through on the implications of the theory of contract law. Many of the doctrines of construction and equity, designed to limit the effects of economic power in contract, which were developed in England, often seem to have arrived in Australia weak, prostrate and stunted from the long, hot voyage. Yet they are here, and these doctrines of *non est factum, contra proferendum,* unconscionability, and relief from penalties, limited though they often have been to drunken or stupid plaintiffs and other isolated, stereotypic cases,[132] are open to be applied to leases, if the courts now do consider leases to be contracts. The results for most leases may be no different than under land law, but these legal avenues are in a process of development in contract law generally,[133] and the prospects for the future are better.

(a) *Non est factum*

The plea of 'non est factum' as a defence to a signed document is quite old.[134] The essence of the plea is that the signer did not know what he was signing.[135] It applies in principle to any signed document, so it ought to apply to a lease whether it is a grant or a con-

[130] See *e.g.*Cheshire and Fifoot, *The Law Of Contract* (4th ed., Sydney, Butterworths, 1981) pp.24-27.

[131] *Cf.* Pollock & Maitland, *The History of English Law* (2nd ed., Cambridge University Press, 1968) pp.106-117. It is one of those anomalies of public policy that the conversion of the lessee's interest from a 'mere' personal right to an interest in land in the 1400's was designed to protect him from the unbridled will of the lessor — specifically from eviction. See supra fn. 1. Now, to give the lessee more effective protection, this must be undone and the lessee's right is being made personal again. The difference, of course, is that personal rights are protected far better under the modern law of contract than they were in the 1400's and that an interest in land means far less today than it did in the 1400's.

[132] Infra fn. 140, 150, 151.

[133] *See* Greig and Davis, op. cit. pp.939-985.

[134] Holdsworth, op. cit., Vol.VIII, p.50 traces it back to the reign of King Edward I (1290-1307).

[135] *Gallie* v. *Lee* [1971] A.C. 1004 at 1021 (H.L.) ("radically different in character from that which the signer thought it was") (*per* Viscount Dilhorne).

tract,[136] although there are no Australian cases applying the defence to a lease.

In principle, a party to a lease ought to be able to apply the defence of *non est factum* to an 'adhesion' term[137] in a lease which was not negotiated by the parties.[138] It is quite common that the parties will consider the rent, the nature of the premises and perhaps one or two ancillary items such as subletting, but then enter into a lease which is found to contain terms never discussed or agreed by the parties: for example on use of the premises, on duties of repairs, on risks should the premises be destroyed, etc. On a theory of contract, the parties should be bound only on those terms of a lease on which they agree.[139]

However, in Australia, the courts have not given much use to *non est factum.* The High Court has held that the plaintiff must be under some special disability such that he could not understand the nature of the document.[140] On this approach, a party to a lease could only raise *non est factum* if he did not know he was signing a lease and if he was too far below normal mental ability, too impaired or had too little knowledge of the language in which the lease was written to be expected to know it was a lease. There is also Australian authority to the effect that *non est factum* does not apply to the terms (as opposed to the nature) of a contract.[141]

While *non est factum* has potential to prevent lessors (who normally write leases) using an agreement on matters a,b, and c to allow them to dictate aspects d through z of the lessor's life, it is presently too limited to have much impact. Rarely if ever will a plaintiff combine lack of knowledge of the fact that a document is a lease with a special handicap as required by the High Court. Where *non est factum* does apply, the effect is that the lease is not enforceable against the party raising the defence.[142]

[136] The defence actually applied to deeds before contracts. *See Foster* v.*Mackinnon* (1869) 4 L.R.C.P. 704 at 712 (C.P.).

[137] *Cf.* Cheshire and Fifoot, *op. cit* p.26 ("contrat d'adhésion" in French law). 'Adhesion' is used here in the sense that the non-agreed term *adheres* to other terms actually agreed by the parties.

[138] *Cf.* The discussion in Greig and Davis, op. cit. pp.610-613 on controlling adhesion terms in contract generally through this plea or analogous methods.

[139] Such a variance is analogous to a material variance between offer and acceptance, which clearly fails to produce an enforceable agreement. *See e.g. Davies* v. *Smith* (1938) 12 A.L.J. 258 (H.C.). In effect, the lessee has said, for example, "I offer to pay you $X for each month of exclusive possession of Y" and the lessor has said "I offer you exclusive possession of Y if you will have no children or pets, insure the premises against risk, go to bed at 10 p.m. each night and pay me $X for each month you are in exclusive occupation". The parties are not *ad idem.*

[140] *Petelin* v. *Cullen* (1975) 49 A.L.J.R. 239 at 241-242 (H.C.).

[141] *Goodfellow* v. *Life Assurance Co. of Australia Ltd.* [1920] V.L.R. 296 (Vic. Full Ct.) (per Schutt J.).

[142] As in *e.g. Petelin's case,* supra fn. 140.

(b) *Contra proferendum*[143]

Adhesion contracts are not totally a product of the 20th century. Common law courts have long recognised that, if a term in a contract is ambiguous, one way of interpreting the contract is to reject the interpretation offered by the party who drafted the contract.[144] Thus, the court avoids allowing itself to be used as a tool for one party to impose a self-serving interpretation on the other.

The principle has already been applied to the construction of an Australian lease in *Mestros* v. *Blackwell.*[145] The issue there was whether a right of renewal granted in a lease was void for vagueness. Wells J. noted English authority that, in construing a lease the construction of the words ought "to be construed, as far as they properly may, in favour of the grantee".[146] The right of renewal was held valid and the attempt by the lessor's assignees to impugn the lessor's own lease was rejected.

The most common use of the contra proferendum rule in contract law is in respect of 'exclusion clauses'.[147] Therefore a lessee would clearly be able to submit this rule of construction should the lessor attempt to use provisions of a lease, drafted by the lessor, to exclude the application of protective legislation, to exclude collateral warranties[148] or to exclude the lessor's liability for negligence. Yet, in principle, *contra proferendum* ought to assist any lessee faced with a term in a lease drafted by the lessor, where the lessee's construction of the term is at least as reasonable as the one submitted by the lessor.[149] Thus, the rule in *Mestros* v. *Blackwell* has a significant potential to control the impact of adhesion terms in leases.

(c) *Unconscionability*

The law of unconscionability as it applies to contracts has received increasing attention in Australia in the 1980's.[150] As a developing area of law, the definition of unconscionability is still rather vague.

[143] The spelling of this term has been rather unpredictable as used in Australian courts. Often one sees '*contra preferentem*', for example. '*Contra proferendum*' means 'against the one bringing forth' in Latin and is thus descriptive. 'Contra preferentem' does not mean anything in any language.

[144] *Burton* v. *English* (1883) 12 A.B. 218 at 224 (per Bowen L.J.).

[145] Supra fn. 11.

[146] *Id.* 326-327, quoting Lord Selbourne L.C. in *Neill* v. *The Duke of Devonshire* (1882) 8 A.C. 135 at 149 (H.L.).

[147] *See* Greig and Davis, op. cit. pp.623-626.

[148] The argument was not, unfortunately for the lessee, raised in *Gallic*, supra fn. 55, where it might have changed the outcome on the misrepresentation defence.

[149] Greig and Davis, op. cit. p.625 suggest that the application of the rule to other than exclusion clauses (*e.g.* deeds of grant, covenants and insurance contracts) is actually wider than in the case of exclusion clauses, where the tendency is just to construe the clause literally rather than to reject the draughtsman's self-serving interpretation. The rule in *Mestros* v. *Blackwell* is concerned with deeds of grant (i.e. leases) and not exclusion clauses.

[150] *See e.g. Commercial Bank of Australia Ltd.* v. *Amadio* (1983) 57 A.L.J.R. 358 (H.C.) and *Taylor* v. *Johnson* (1983) 57 A.L.J.R. 197 (H.C.).

However, the essence of unconscionability seems to be that one party has unfairly exploited a disadvantage of the other in respect of bargaining power.[151] Unconscionability is one of the few exceptions (if not the only one) to the general rule that a court will not concern itself with the adequacy of consideration.[152] Thus, if one party appears to have paid the other a King's ransom for the King's knave, the issue of unconscionability at least may be raised.[153]

As in the case of *non est factum*, the High Court has severely restricted the use of unconscionability, by requiring a pitiful plaintiff. Fullagar J. in *Blomley* v. *Ryan* gave some examples: "poverty or need of any kind, sickness, age, sex, infirmity of body or mind, drunkenness, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary".[154] Yet, recalling the origins of unconscionability in equity,[155] there is no reason in principle why the plaintiff's personal life should bring tears to the eyes of the judges in order for unconscionability to apply. If the lease provides a far lower-than-average level of housing service for a far higher-than-average rent,[156] this seems to be far more objective evidence of exploitative conduct by the lessor than does the court's reaction to the lessee's age or place of birth. If the lessor seeks to use a 'no children' lease to evict a pregnant lessee in a time of housing shortage, certainly the court could justify protecting the interests of the unborn child in safe and secure housing[157] more easily than considering whether the lessee had completed high school. Perhaps a better justification for the application of unconscionability to reject a claim by a lessor is that the benefit of the lessor's claim for the lessor is grossly disproportionate considering the burden on the lessee in all the circumstances. Such a justification would proceed on the presumption that a reasonable person would not agree to a term of such gross disproportionality in the absence of exploitative conduct by the other party.

On the other hand, there are many lessees who qualify for protection under the doctrine of unconscionability as it has already been used by the High Court. The Poverty Commission found that "some

[151] *Blomley* v. *Ryan* (1956) 99 C.L.R. 362 at 415 (H.C.). (per Kitto J.).

[152] *Cf.* Greig and Davis, op. cit. p.976 with p.88.

[153] The term 'catching bargains' used by Meagher, Gummow and Lehane in *Equity: doctrines and remedies*, (2nd ed., Sydney, Butterworths, 1984) pp.385-391 is illustrative.

[154] Supra fn. 15 at 405.

[155] The doctrine arose in the protection of heirs and reversioners in estates (supra fn. 152, 153) who were normally younger sons of the landed gentry hungry for money — hardly poor, desperate wretches!

[156] *Cf.* The cases in the passages cited at footnotes 152 and 153, where gross inadequacy of consideration was a sufficient condition of invocation of the protection of the court. In economic terms, such a disparity is also evidence of market power in the lessor, as he is not a price-taker.

[157] The use of equity to protect the interests of innocent third-parties in transactions is quite common: for example, the interest of a trust beneficiary in transactions by the trustee; the interests of a *bona fide* purchaser for value in transactions between a fraud and the rightful owner; the interests of second, third and subsequent mortgagees in transaction between the mortgagor and the first mortgagee.

of society's most vulnerable groups are likely to be tenants: 35.5 percent of all migrants, Aboriginals and "disability combination" income units . . . and 25.4 percent of all sick, unemployed and invalids are private tenants, compared with the total community figure of 21.4 percent".[158] While not all of these people will be victims of unconscionable conduct, this does indicate that many lessees would be especially entitled to be considered should they allege that their leases are unconscionable.

However, if unconscionability principles are going to be of any benefit to lessees, the courts are going to have to be far more careful about remedies. So far, most of the cases have concerned contracts of guarantee, conveyances of land, etc. which the courts have then declared completely void on a finding of unconscionable conduct.[159] While this remedy was appropriate to those cases, a declaration that the lease is utterly void leaves the lessee homeless. What the lessee needs is a declaration that certain terms of the lease are void for unconscionability. Although partial nullification of a contract for unconscionability has not yet been applied, Australian courts have not ruled it out.[160]

(d) *Relief from Penalties*

'Forfeiture' has different connotations in land law and contract law. In land law, forfeiture simply implies a vesting of the grantor's reversion: the property goes back to its ultimate owner. In contract, a forfeiture is a penalty depriving a party of the benefit of his bargain. Therefore, under land law, forfeiture of the estate is a logical result of breach of a condition subsequent.[161] Under contract law, forfeiture in the way of a penalty for a breach is illegal and terms providing for it are unenforceable.[162]

Potentially, therefore, the contractualisation of lease law has major implications for the consequences of breach in a lease. Traditionally, breach of any term of a lease, irrespective of the consequences, was grounds for a re-entry, termination and eviction if the lessor wished it to be,[163] unless a statute[164] or a court in equity[165] protected the lessee from this consequence. Now, under contract, breach of a covenant in a lease, except for a 'substantial' breach of a 'fundamental'

[158] Australian Government Commission of Inquiry Into Poverty, *Law And Poverty In Australia (Second Report)*, AGPO, Canberra, 1975, p.57.

[159] As in the cases supra fn. 150, 151.

[160] *See* Greig and Davis, op. cit. p.978.

[161] *See* Megarry and Wade, op. cit. p.69-75. It is not even an inevitable result, as the grantor has the option of whether or not to exercise this 'right of entry', whether it be in a conditional fee, a restrictive covenant or a lease.

[162] *See* Greig and Davis, op. cit. pp.1445-1466.

[163] The lessor had only to draft the term as a 'condition' providing a right of re-entry and not merely as a 'covenant'. *See* Burn, *Cheshire and Burn's Modern Law of Property* (13th ed., London, Butterworths, 1982) p.416.

[164] Many statutes allow courts to give 'relief against forfeiture'. *See* Sackville and Neave, op. cit. p.709.

[165] *See* Meagher, Gummow and Lehane, op. cit. pp.421-426.

term or a 'repudiation', does not lead to forfeiture of a lease: the innocent party's only remedy is to sue for the costs of the breach in damages. We have already seen the beginnings of this line of reasoning in *dicta* in the decided cases.[166]

The application of this change to lease law may be the most significant for protection of the lessee. What costs does it impose on a lessor if the lessee breaches the lease by having guests in?: none, most probably, and this is no longer a cause of eviction. What damages can a lessor claim if the lessee takes in a cat in violation of the lease?: none, until the cat starts damaging the premises and then no more than the proven costs of repairing the damage. Children can no more be excluded than cats: however their parents are liable to pay for repairing their children's vandalism. A myriad of covenants which lessors commonly impose upon lessees, and which cause them no or very little monetary loss upon breach, are now unenforceable.

One consequence of this change may be that lessors begin to write 'liquidated damages' clauses on to their lease covenants which are little more than fines. In principle, if they are fines, the courts will find no liability to pay them: a 'liquidated damages' clause must be an honest and reasonable estimate of the probable costs of the breach.[167] A common example of an existing liquidated damages clause is for late rent. If the late rent charge is roughly equivalent to the prevailing market rate of interest, it looks like permissible liquidated damages: the more it goes beyond that, the more it looks like a void penalty. Attempt at forfeiture for a minor delay in payment of rent (or for breach of any other covenant) looks distinctly like repudiation by the lessor entitling the lessee to recover consequential damages. The only 'fundamental' breach by the lessee allowing termination (i.e. eviction) is a 'significant' or 'consistent' failure to pay rent.[168] Lessors are now in the high-risk position faced by other contract parties: their termination of the contract (i.e. eviction) may be a valid election of remedies or it may be a very dear repudiation — they will not know for certain which it is until the final appeal has been exhausted. It may be now less risky for lessors to forget about many breaches of covenant, even if they permit forfeiture, which should give tenants more security and more freedom from dictation by landlords.

CONCLUSION

Australian courts have embarked upon a major restructuring of both the theory and application of the law of leasehold. No one knows how far the courts will actually go, but this paper has shown that the openings for change are quite broad: having taken the first step, the road leads far indeed. Pitfalls and opportunities abound for lessors and lessees in commercial and residential

[166] Gibbs C.J. in *Shevill, cit.* at note 6, *supra*, at 795, Wilson J., *ibid.* at 798. Mason J. in *Progressive Mailing,* supra fn. 20 at p.381.

[167] *O'Dea* v. *Allstates Leasing Systems (W.A.) Pty. Ltd.* (1983) 57 A.L.J.R. 172 (H.C.).

[168] Supra fn. 166.

relationships alike. The future of the common law of leasehold is intriguing.

Some will say that the matters discussed in this paper are in a world that the majority of tenants will never even visit, let alone live in. Residential tenants are notoriously reluctant to sue, so their legal rights do not matter.[169]

Some of the tenants' reluctance to sue must be put down to land law itself. Opportunities to recover damages were rare and the landlord had manifold opportunities to take revenge through re-entry for trivial breaches of covenant. Now the tenant is virtually protected for the term of the lease (as long as he pays the rent) and can recover expectation losses under the law of contract for the landlord's breaches.

Even more of the tenant's unwillingness to sue comes from the system itself. First of all, we must acknowledge that the political ideology of many tenants' advocates in tenants' groups, consumers' groups and among legal service group lawyers is anti-common law: if the courts are considered to be the tools of the *bourgeoisie,* and Parliament to be the only salvation, tenants will not be advised to go to court even when remedies are available. Yet Parliaments have restricted tenants' rights too — by summary eviction proceedings, by statutory landlord's rights of inspection and by rent policies that prevent competition for tenants and leave tenants in well-protected hovels, for example. What the politician giveth, the politician may take away.

Still, it must be conceded that many court proceedings are too expensive for many parties to leases and may outlast the term of the lease. That is not a criticism of the law of leasehold but of court procedures generally and is yet another argument for comprehensive legal insurance and a wider variety of tribunals. Indeed, the sharply higher costs and risks of eviction and abandonment — the parties' traditional reactions to these problems — under the contractualisation of lease law make it even more imperative that effective schemes for adjudication are developed for leases. If landlords cannot re-enter at will and lessees cannot move or withhold rent, they have to go to court — or to some means of dispute resolution. Perhaps this is why tenancy mediation and arbitration is so much better-developed in North America, where leases have been treated as contracts for a long time. If Australia has now followed American contractualisation of lease law, perhaps it will now follow American dispute resolution for tenancies. Retail tenancy statutes have already done so[170] and a few states have established residential tenancy tribunals.[171]

In any event, for those who can use the common law of leasehold, there are many improvements. Contractualisation has injected the courts into tenancies more directly than they have ever been. The tools are there: it is now up to lessors, lessees and their counsel to use them.

[169] *cf.* Bradbrook, "The Role of the Judiciary In Reforming Landlord and Tenant Law" (1976) 10 M.U.L.R. 459 pp.460-461.

[170] *Retail Tenancies Act* 1986 (Vic.) s.20-22. *Retail Shop Leases Act* 1984 (Qld.) s.17-50. *Commercial Tenancy (Retail Shops) Agreements Act* 1985 (W.A.) s.21-26. *Statutes Amendment (Commercial Tenancies) Act* 1985 (S.A.) s.56 and s.68.

[171] *Residential Tenancies Act* 1987 (N.S.W.) Part 6. *Residential Tenancies Act* 1980 (Vic.) s.16-46. *Residential Tenancies Act* 1978 (S.A.) s.14-29.