



Lease Outgoings Error Causes Multi-Million Dollar Loss

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The recent decision of the Supreme Court of Victoria in the case of *Perpetual Limited v Myer Pty Ltd* [2019] VSCA 98 has demonstrated the significant financial consequences that an apparent error can cause in long term lease agreements and the importance of correctly understanding, drafting, reviewing and testing lease provisions which determine the payment obligations of the parties.

Background

The joint owners of the Chadstone Shopping Centre in Victoria (the **Owners**) entered into a long-term lease (of 30 years with a 15 year option) in late 1998 with Myer Pty Ltd (**Myer**) as the anchor tenant. Myer's outgoing obligations included the requirement of Myer to pay a proportion of the centre's "Increase in Variable Outgoings" for the second and each subsequent year of the lease term.

Matters in Dispute

The Owners commenced court proceedings to rectify an apparent 'drafting error' and an 'obvious mistake' with the definition of 'Increase in Variable Outgoings'. The definition provided that the required payment was to be the amount which the Variable Outgoings for that accounting period exceeded the Variable Outgoings for the immediately preceding accounting period.

Instead, the Owners argued that the required payment should have been the amount of Variable Outgoings for that accounting period which exceeded the Variable Outgoings for the "Base Accounting Period". Although, the term "Base Accounting Period" was defined in the Lease (as the first full 12 month period commencing on 1 July following the lease commencement date), this term was surprisingly not used in the Lease.

Myer denied that these contentions by the Owner reflected the agreed commercial deal at the time of entering the Lease and resisted the claim for rectification of the formula used in the Lease.

Financial Loss

As a result of this discrepancy, Myer was only required to pay the increase in Variable Outgoings each year from the previous year, rather than increasing cumulatively for each subsequent accounting period from the Base Accounting Period. The difference between the two methods amounted to approximately \$20 million.

The 'error' was first identified by the Owners in 2012, but was not raised with Myer until December 2015, as the Owners needed Myer to consent to certain redevelopment proposals at the Centre.

Court Decision

The Court dismissed the Owners' application to rectify the outgoing liability in the Lease on the grounds that the Court was not satisfied that the Owners had established the true intention of the agreement and that there was a clear mistake with the drafting of the lease provisions.

In reaching this conclusion, specific attention was placed on the strong bargaining position of both parties in negotiating the lease and the fact that both parties:

"were represented in lengthy negotiations by experienced negotiators, internal solicitors and external solicitors — leading to an 'unlikelihood' of no one realising the alleged mistake before the agreement for lease was executed."

While the Court accepted that the commercial outcome of the formula was "peculiar" and not commercially convenient for the landlord, in light of the surrounding circumstances, the Court was not adequately persuaded on the basis of the very detailed evidence provided to grant the rectification sought.

Key Points

The importance of carefully understanding all of the intended components of any formula for determining a fundamental financial lease liability such as outgoings is vital, both initially when negotiating the commercial arrangements and subsequently when drafting and reviewing the required provisions.

This is especially the case with a significant ongoing financial liability in a long term lease where any problems will continue to compound.

It is vital that any such formulas should be first tested using examples to ensure that the drafting complies with the intended agreed arrangements. From a practical perspective, worked case examples should be included in the lease so that the intended and agreed operation is clear.

Additionally, as the negotiation of the amendments to a draft lease can often be complex and lengthy, involving multiple versions of the document and many people, a final critical assessment by a new set of eyes should be performed so that any small unintended errors do not have significant compounding consequences.

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