COURT DECISIONS

The summaries appearing before the court decisions published in The Valuer do not form part of the judges' and assessors' decisions and are provided only as a brief summary of the reported cases. Members are urged not to rely on these summaries for a complete synopsis, but to read the judgments in full.

In the matter of the Rules of the Supreme Court of Queensland and In the matter of a Lease from ANZ Executors & Trustee Company Limited and/or Queensland Treasury Corporation and The National Mutual Life Association of Australasia Limited

(In the Supreme Court of Queensland, 10 April 1991, Mackenzie J.)

Lease interpretation – Effect of words "disregarded matters" in lease – Rental determination by valuer acting as an expert – Lease incentives – Open market value – Confidentiality clauses.

Lessee leased levels 35 and 36 in Central Plaza One, Brisbane. One of the assumptions of the rent review determination in the lease was that the premises be available to lease "without payment of premium, granting of a rent-free period, or the offering of any other incentive by the landlord".

The lease also set out a number of assumptions to be made in the rent review determination and a number of matters to be disregarded. One of the provisions stating "the open market rent at the relevant date shall be determined by the expert making the assumptions but disregarding the disregarded matters and having regard to the open market rental values current at the relevant review date".

The lessee sought a declaration under the Supreme Court Rules as to the meaning of this clause, plus several others.

It was argued by the lessee that "disregarding the disregarded matters" really meant that any expert appointed to determine the open market rental should adjust or discount rental figures to take account of any incentives or rent-free periods.

The lessors challenged the lessee's rights to seek an order under the Supreme Court Rules and the meaning attached to the disputed clauses.

Held: *The expert appointed to determine the open market rental applicable under the lease would have to take into account the incentives being paid to other tenants in the market.*

MACKENZIE J: The applicants seek declarations as to the true meaning and effect of the provisions relating to rent review in an instrument of lease of commercial premises occupied by them on Floors 35 and 36 of the Central Plaza One building. The relevant provisions are clauses 4.10.1, 4.3 and 4.4 of the lease which are in the following terms:

"4.10.1 The open market rent at the relevant Review Date shall be determined by the Expert (acting as an expert and not as an arbitrator) and shall be such as he shall decide should be the Base Rent for the Premises at the relevant Review Date making the Assumptions but disregarding the Disregarded Matters and having regard to open market rental values current at the relevant Review Date.

4.3 'The Assumptions' means the following assumptions at the relevant Review Date:

4.3.1 That the Premises are fit for and fitted out and equipped for immediate occupation and use (provided that the review rent shall not include any component to reflect the worth of any improvements carried out at the Tenant's expense) and that no work has been carried out on the Premises by the Tenant, its sub-tenants or their predecessors in title during the Term which has diminished the rental value of the Premises, and if the Premises have been destroyed or damaged they have been fully restored.

4.3.2 That the Premises are available to let by a willing landlord to a willing tenant, as a whole, without payment of a premium, granting of a rent free period or the offering of any other incentive by the Landlord, but with vacant possession, and subject to the provisions of this Lease (other than the amount of the rent but including the provisions for rent review), for a term equal to the Term.

4.3.3 That the covenants contained in this Lease on the part of the Tenant have been fully performed and observed.

4.4 The Disregarded Matters' means:

4.4.1 Any effect on rent of the fact that the Tenant, its sub-tenants or their respective predecessors in title have been in occupation of the Premises.

4.4.2 Any goodwill attached to the Premises by reason of the carrying on at the Premises of the business of the Tenant, its sub-tenants or their predecessors in title in their respective businesses.

4.4.3 Any increase in rental value of the Premises attributable to the existence at the relevant Review Date of any improvement to the Premises and carried out by

the Tenant pursuant to the Agreement for Lease dated October, 1988 or otherwise with consent where required otherwise than in pursuance of an obligation to the Landlord or its predecessors in title either:

4.4.3.1 By the Tenant, its sub-tenants, or their respective predecessors in title during the Term, or during any period of occupation prior thereto arising out of an agreement to grant such Term, or

4.4.3.2 By any Tenant or sub-tenant of the premises before the commencement of the Term so long as the Landlord or its predecessors in title have not since the improvement was carried out had vacant possession of the relevant part of the Premises."

The dispute essentially concerns the effect of the requirement in clause 4.10.1 that the 'disregarded matters' be disregarded.

A preliminary point was taken by the respondents that this is a case to which the principles stated by Mason J (as he then was) in *Codelfa Construction Pty Ltd v. State Rail Authority of New South Wales* (1982) 149 CLR 337 at pp. 352-3 apply. The relevant passage from the judgment of Mason J is as follows:

"The true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible of more than one meaning. But it is not admissible to contradict the language of the contract when it has a plain meaning. Generally speaking facts existing when the contract was made will not be receivable as part of the surrounding circumstances as an aid to construction, unless they were known to both parties, although, as we have seen, if the facts are notorious knowledge of them will be presumed.

"It is here that a difficulty arises with respect to the evidence of prior negotiations. Obviously the prior negotiations will tend to establish objective background facts which were known to both parties and the subject matter of the contract. To the extent to which they have this tendency they are admissible. But in so far as they consist of statements and actions of the parties which are reflective of their actual intentions and expectations they are not receivable. The point is that such statements and actions reveal the terms of the contract which the parties intended or hoped to make. They are superseded by, and merged in, the contract itself. The object of the parol evidence rule is to exclude them, the prior oral agreement of the parties being inadmissible in aid of construction, though admissible in an action for rectification.

"Consequently when the issue is which of two or more possible meanings is to be given to a contractual provision we look, not to the actual intentions, aspirations or expectations of the parties before or at the time of the contract, except in so far as they are expressed in the contract, but to the objective framework of facts within which the contract came into existence, and to the parties' presumed intention in this setting. We do not take into account the actual intentions of the parties and for the very good reason that an investigation of those matters would not only be time consuming but it would also be unrewarding as it would tend to give too much weight to these factors at the expense of the actual language of the written contract.

"There may perhaps be one situation in which evidence of the actual intention of the parties should be allowed to prevail over their presumed intention. If it transpires that the parties have refused to include in the contract a provision which would give effect to the presumed intention of persons in their position it may be proper to receive evidence of that refusal. After all, the court is interpreting the contract which the parties have made and in that exercise the court takes into account what reasonable men in that situation would have intended to convey by the words chosen. But is it right to carry that exercise to the point of placing on the words of the contract a meaning which the parties have united in rejecting? It is possible that evidence of mutual intention, if amounting to concurrence, is receivable so as to negative an inference sought to be drawn from surrounding circumstances."

Mr Douglas QC relied particularly on the last paragraph quoted. He submitted that this was not a case in which it was appropriate to make a determination under O. 64. The genesis of the argument is to be found in the affidavit of Anthony Charles Cotter who deposes that the respondents, who are successors in title to the owner who originally negotiated the lease have not been able to have access to the files of Hawthorne, Cuppaidge and Badgery who were the solicitors then involved in the transaction, nor those of the previous owner.

One piece of correspondence that they have obtained relates to the negotiations for the lease and indicates that a proposed clause 4.11.4 had been not incorporated in the lease. That clause had been proposed by the lessees and was in the following form:

"4.11.4 The landlord will on request by the expert provide to the expert full details of all completed rental negotiations or determinations within the building which have occurred within a period of one year prior to the date of such request and/or the relevant review date and such details shall include all matters touching or concerning such negotiations or determinations and without limiting the generality of the foregoing will include full details of any incentive with respect to a transaction referred to by the landlord either in its submission to the expert or in response to the expert's request. The details will be provided by the landlord within 21 days from the request of the expert. A copy of such material will also be provided by the landlord to the tenant and the tenant may make a written submission to the expert in respect of it."

It was submitted by Mr Douglas QC that this was particularly significant having regard to the interpretation contended for by the respondents and to the passage from *Codelfa* (supra) relied on by them. However, his submission was not limited to this

particular matter. It extended to the proposition that until all aspects of the negotiations had been scrutinised the respondents could not be certain that there were no other factors affecting the interpretation of the written instrument.

The proposed clause 4.11.4 would have taken its place in the lease in connection with procedures for resolving differences in the event of lessors and lessees failing to agree on the rental following its review. Clause 4.8.3 provides that if the parties fail to agree within 60 days of service of the review notice the sum of rental is to be determined by an expert pursuant to clause 4.10. That sum becomes the rental. Clause 4.11.1 obliges the expert to advise the parties forthwith of his appointment and 4.11.2 permits each to make a written submission to him within 21 days of that notice.

I digress to say, for the sake of completeness, that the lessees also proposed a clause 4.11.3 which would have provided for a right of reply to the initial submissions to the expert within a prescribed time. It is not relevant therefore for present purposes except to indicate that clause 4.11 appears to have been as much concerned with questions of procedure rather than substance.

To come to a conclusion on the preliminary objection it is convenient to construe prima facie what the relevant provision of the lease means for the purpose of determining whether on any view the deletion of the proposed clause 4.11.4 or any undisclosed aspect of the discussions leading up to the execution of the lease might conceivably affect the issue of the meaning of clause 4.10.1.

Under the lease the expert's duty is to determine the "open market rent". It is to be determined in accordance with the following principles:

(a) he is to make the "assumptions";

(b) he is to disregard the "disregarded matters"; and

(c) he is to have regard to open market rental values current at the relevant review date.

The "assumptions" are in summary the following:

(i) that the premises are fit for and fitted out for immediate occupation and use and the rental value has neither been enhanced nor diminished by anything done by the tenants;

(ii) that the premises are available to let with vacant possession by a willing landlord to a willing tenant without payment of a premium, the granting of a rent free period or the offer of any other incentive by the landlord;

(iii) that the covenants by the tenant have been performed.

The consequence of making these assumptions, in my view, is that finding the open market rental value of premises unaffected by factors that would distort that value is the object of an exercise.

The "disregarded matters" are:

(i) any effect on the rent of the fact that the tenants have been in occupation;

(ii) any goodwill attaching to the premises by reason of carrying on the business of tenants on the premises;

(iii) any increase in rental value attributable to the existence of improvements to the premises carried out by the tenant pursuant to the lease or with the landlord's consent;

(iv) any cash premium, rent-free period or other incentive which may be payable by a lessor to a lessee for a lease or entry into a lease or to compensate a lessee for costs of relocating.

Once again if one eliminates these matters as factors in determining the rental the purpose of the exercise, in my view, is to eliminate factors distorting the true value of the premises. Viewed in that way and having regard to the context in which the proposed clause 4.11.4 would have appeared, there is not, in my view, any cogent reason for supposing that its deletion affects what would otherwise be the irresistible inference as to the intention of the parties.

The only inference that can be drawn concerning the deletion, in my view, is that for some reason, most likely the preservation of commercial confidentiality, the landlords were not willing to provide information concerning incentives of tenants in Central Plaza One to the expert as part of his process of making his determination. It is true that this may make his task more difficult because he would have to rely on less reliable information as to such incentives and the like. Nonetheless that is not, in my view, a factor that affects the plain meaning of the relevant provisions. I am not prepared to find that the fact that the proposed clause 4.11.4 was deleted could affect the intention expressed in the written instrument.

Mr Douglas QC submitted that if allowances were made in the process of assessing the open market rent for any cash premium, rent-free period or other incentive, that could not be said to be disregarding those matters. I do not accept this. The critical element of the exercise is to ascertain the open market rent for the premises. What has to be disregarded is the distortion of the true values that may occur if factors such as cash premiums, rent free periods or other incentives have an effect on the rental actually paid by a tenant of premises which are being used as comparable premises in the process of valuing. To achieve a true level of value it is those distortions that have to be disregarded. To treat "disregard" as the equivalent of "ignore" achieves the result that a true value is not achieved.

On the broader issue that if the respondents have the opportunity to peruse all material relevant to the negotiations they may discover something that will affect the true construction of the agreement, I am of the view that, given what seems to me to be a quite unambiguous expression of principle in the words used in the document, it would be remarkable if information casting a shadow of ambiguity over it was discovered.

In all the circumstances I am satisfied that this is a case in which I can proceed to a determination under O. 64.

It is clear from what I have said that the proper interpretation of the lease entitles the applicants to succeed in principle. The respondents advanced an argument that I should not make a declaration as that may be an unnecessary step.

In support of this proposition an affidavit of Philip Ross Willington, a registered valuer, was tendered to the effect that there was a sufficient cross-section of

premises, comparable to the applicants' premises, for the purpose of assessing market rental where the rental was struck without any premiums, rent-free periods, incentives or the like being offered or given by the landlord. Therefore a valuer could determine from that cross-section a free market rent for the applicants' premises or other premises in Central Plaza One without the need to consider any cases in which incentives and the like were offered. Therefore, it would become academic and unnecessary to enter upon any consideration of the proper approach to "disregarded matters".

It will, of course, be entirely for the expert to decide whether he can perform his task in the way suggested by Mr Willington or whether he feels it necessary to take premises in which incentives and the like have been offered into account as well in performing his valuation. Nothing in this judgment is intended to impose a fetter on his independent professional judgment in that regard.

However, the question of how he approaches the question of valuation if he does take into account premises where there have been incentives and the like offered is separate and distinct from the question of what premises he takes into account. If he decides to take such premises into account, in my opinion there is at least a risk that the process of valuation may miscarry if he is not given guidance as to the proper meaning of clause 4.10.1. Therefore I am not satisfied that I should refrain from making a determination of the true meaning and effect of the lease.

My opinion as to the meaning of the relevant provisions has been set out in the foregoing parts of these reasons. Having regard to this, all that is necessary in my view is to make a declaration in terms of paragraph 3 of the summons filed on March 8 1991. I declare accordingly. The respondents are ordered to pay the applicants' costs of and incidental to the application including any reserved costs to be taxed. *(Members should note that* The Valuer *has been advised that the above decision is on appeal. – Editor)*