

# Understanding how an option for renewal works

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The judgement of Her Honour, Mullins J of the Queensland Supreme Court in *JV Pub Group Pty Ltd v Red Carpet Real Estate Pty Ltd* (delivered on 22 September 2014) is a salient reminder of how important it is for both parties to a lease to understand how an option for renewal works.

In this article, Special Counsel Anthony Boge outlines important aspects of the judgement.

## Key Points

- For a tenant it is important to understand the steps it needs to take to exercise an option for renewal and the time frame for taking those steps
- For a landlord it is important to be aware of conditions that must be met for exercise of an option and how the landlord should respond to any purported exercise of the option or a failure to exercise the option.
- If a landlord wants to take advantage of the tenant's failure to exercise the option then it must not act inconsistently with that position.

## The facts

A tenant occupied a shop at Broadbeach under a retail shop lease that contained an option for renewal. The option had to be exercised by the tenant no later than 31 August 2013. The tenant did not give any notice of the exercise of the option by that date. The obvious conclusion to be drawn from these simple facts is that the option for renewal of the lease lapsed at that point (and that is exactly what Mullins J later found to be the case when the matter came before her).

The matter did not end with the lapsing of the option, however, because the landlord's agent did something rather strange. On 26 November 2013, almost three months after the last date for the exercise of the option had passed, the landlord's agent sent a letter to the tenant referring to the upcoming expiry date of the lease as well as to the option for renewal and asked the tenant to advise, by a specified date, whether the tenant would be exercising the option for the further term. The landlord's agent's letter indicated that it was a notice given under section 46 of the *Retail Shop Leases Act*.

Unfortunately, the landlord's agent's letter was entirely misconceived. Section 46 of the *Retail Shop Leases Act* requires that, where a retail shop lease contains an option for the tenant to renew the lease, the landlord must give a notice to the tenant of the date by which the tenant must exercise the option (which is called "the option date"). The landlord's notice must be given at least two months before the option date. Quite obviously, the date for the giving of the section 46 notice had passed when the landlord's agent sent its letter to the tenant.

The tenant sent a letter to the landlord on 19 December 2013 in which the tenant purported to exercise the option for renewal. Subsequently, the tenant's representative sent an email to the landlord's agent enquiring about the landlord's proposal for the rent. The landlord's agent responded by advising that the landlord was happy to keep the rent at the existing level. The tenant's representative informed the landlord's agent that the tenant declined the landlord's offer in relation to the rent and elected to use the process in the lease (for a market review of the rent).

It is not clear whether the prospect of a market review of the rent was the catalyst for the landlord's next step but, at this point, the landlord's solicitors wrote to the tenant's solicitors to say that the notice purporting to exercise the option was out of time and that the option terms did not apply.

The tenant applied to the court for a declaration that the tenant had validly exercised the option for renewal.

## **The Court's findings**

Although Mullins J found that the tenant obtained the benefit of a new lease, the tenant did not do so on the basis that it had validly exercised the option for renewal. The option lapsed when the tenant failed to exercise it within the required time frame.

Having found that the option to renew the lease had lapsed, Mullins J turned her mind to the effect of the landlord's agent's letter of 26 November 2013 and the tenant's attempt to exercise the option.

While the landlord's agent was wrong in law in suggesting to the tenant that the tenant could still exercise the option under the lease, Mullins J found that the landlord's agent's letter was clearly an invitation to the tenant to exercise the option. The letter was characterised as an offer to lease the premises on the same terms as if the option had been exercised. The tenant's letter purporting to exercise the option for renewal was taken to be an acceptance of the offer. At that point there was a concluded agreement for lease.

## **Conclusion**

What the case shows is how important it is for both parties to a lease to understand how an option for renewal works.

An option for the renewal of a lease is generally considered a valuable right of a tenant. A tenant must understand the steps it needs to take to exercise an option and the time frame for taking those steps (remembering that compliance with time limits will almost always be essential to the proper exercise of an option).

It is equally important for a landlord to be aware of conditions that must be met for exercise of an option and how the landlord should respond to any purported exercise of the option or a failure to exercise the option. This is particularly the case if the landlord considers there is a commercial advantage to be gained from avoiding the renewal of the existing lease. If a landlord wants to take advantage of the tenant's failure to exercise the option then it must not act inconsistently with that position. If, after the time for exercise of the option has passed, the landlord engages in conduct that suggests to the tenant that the option is still available, the landlord may be offering to enter into a new lease with the tenant. Acceptance of that offer will bind the landlord to a new lease.

If you need assistance with an option for renewal of a lease, please contact HopgoodGanim's [Commercial and Retail Leasing](#) team.

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