

PROPERTY

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UNTENANTABLE PREMISES – A QUESTION (SOMEWHAT) RESOLVED

A recent case is relevant to landlords, tenants and home owners going through unfortunate situations such as those in Christchurch, or properties in general affected by fire, flood or severe damage. The High Court decision¹ sheds some light on when a property is 'untenantable', which, depending on the answer, might result in contracts between parties being prematurely terminated.

Background

The tenant had entered into a lease of the first floor of a three-storey commercial building at 2 Kingsland Terrace in Auckland. The lease was to commence on 1 September 2007. However, the landlord had permitted the tenant to gain early access to carry out alterations and improvements to the premises.

On the first day of the lease, the lights were turned on. Unfortunately, unbeknown to the tenant, the painters it had engaged had covered up the halogen ceiling lights with masking tape. When the lights were turned on, the masking tape ignited and a serious fire occurred causing extensive damage, particularly to the first floor. The damage was such that the tenant was unable to remain in occupation of the premises.

An insurance assessor was immediately engaged and it was determined that the repairs would take approximately eight to nine months.

Two months after the fire the landlord's solicitors wrote to the tenant advising that the lease would terminate one month from the date of the notice.

The tenant disputed the landlord's right to terminate the lease. Regardless of the damage, they were still interested in pursuing the lease arrangements that they had with the landlord. The tenant was of the view that as they did not have an issue with the time frame that it would take to repair the premises, the landlord did not have a right to terminate the lease on its own account.

Lease

The parties had entered into a standard Auckland District Law Society and Real Estate Institute of New Zealand 8th edition form of lease. The case centered around clause 26.1 of the lease which read:

"Damage to or Destruction of Premises

- 26.1 If the premises or any portion of the building of which the premises may form part shall be destroyed or so damaged
- a. as to render the premises untenable then the term shall at once terminate; or
 - b. in the reasonable opinion of the Landlord as to require demolition or reconstruction, then the Landlord may within 3 months of the date of the damage, give the Tenant 1 month written notice to terminate and a fair proportion of the rent and outgoings shall cease to be payable from the date of damage."

Decision

The determining factor of the case was whether the premises were 'untenantable'. In this instance, the damage to the leased first floor premises was extensive. In particular, the roof, support structures and the ceilings had to be demolished and reconstructed. Metal framing and bracing had to be removed and replaced. Destroyed air conditioning systems and electrical fittings similarly had to be removed and replaced. In fact, most of the first floor had to be demolished and reconstructed.

The tenant's solicitors argued that if a tenant wished to remain a tenant, and was happy to be bound by the terms of the lease despite damage to the premises, then the premises must be deemed tenantable for the purposes of clause 26.

The High Court disagreed. It held that the word 'untenantable' is an objective state to be determined on specific relevant facts. The focus of the inquiry must be whether the premises were capable of being used for the specific purpose, and for the specific term for which the lease was entered into in the first instance. According to the High Court, the tenant's purposes are inextricably linked with the permitted use of the premises.

In this case, ten months of the agreed four-year lease term were needed to repair the structural and internal damage. Regardless of the tenant's desire to hold on to the premises, at the point when the landlord terminated the lease, the premises could only be described as untenantable. They were not capable of being used for the tenant's purposes or indeed the purposes of the lease. Hence, the lease terminated automatically when the premises were 'untenantable'.

This case is an important reminder that even when parties enter into contractual relationships using commonly used standard contract forms (ie leases and agreements for sale and purchase), they may not be suitable for all business arrangements or circumstances. In any situation where a 'standard' contract is being used consideration must always be given to whether the 'standard' clauses fit the needs of the parties. Those needs must be clearly communicated at an early date - before **any** documentation is signed. This will ensure that each parties' needs are protected in the event that unforeseen circumstances arise in the future.

1 Russell v Robinson

Our Commercial Property senior personnel are:

Deborah Miller

Partner
t: (09) 979 2134
e: miller@brookfields.co.nz

Ian McCombe

Partner
t: (09) 979 2159
e: mcombe@brookfields.co.nz

Chris Paterson

Partner
t: (09) 979 2173
e: paterson@brookfields.co.nz

Howard Johnston

Partner
t: (09) 979 2161
e: johnston@brookfields.co.nz

Brett Abraham

Partner
t: (09) 985 6910
e: abraham@brookfields.co.nz

John Delugar

Partner
t: (09) 985 6913
e: delugar@brookfields.co.nz

Sandy Donaldson

Senior Associate
t: (09) 979 2195
e: donaldson@brookfields.co.nz

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Auckland
t: 09 379 9350
f: 09 379 3224

Manukau
t: 09 262 2145
f: 09 379 3224

Wellington
t: 04 499 9824
f: 04 499 9822