

Legal Update | Property

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Further Information

Justin Lethlean
Partner

telephone | +61 3 9640 4312
facsimile | +61 3 9205 2055
email | justin.letllean@middletons.com

Steven Mackay
Partner

telephone | +61 2 9513 2428
facsimile | +61 2 9513 2399
email | steven.mackay@middletons.com

middletons | *straight talking*

Significant changes to the Victorian law of co-ownership

Victoria's Property (Co-ownership) Act 2005 makes significant changes to the law of co-ownership.

The *Property (Co-ownership) Act 2005* (Vic) (Act) came into operation on 1 February 2006. Section 5 of the Act amends the Property Law Act 1958 (Vic) (Property Law Act) by replacing the entire Part IV for a new one. Part IV relates to co-owned land and goods.

The Act makes significant changes to the law of co-ownership. Most important of the changes is that the Victorian Civil and Administrative Tribunal (VCAT) will now be the sole forum for certain disputes between co-owners. Joint venture partners who co-own land may need to bring their dispute to VCAT.

Application for sale or division of land or goods

In Victoria, two or more people can own land or goods as joint tenants or tenants in common.

Prior to the Act, co-owners had to apply to the Supreme or County Courts for an order for the sale of land or goods and division of the sale proceeds or physical division of the land or goods or a combination of both. These applications were called 'partition' applications.

Litigation concerning co-owned land will now have to be brought in VCAT. This is intended to remove the formality, expense and delay of having the matters heard in the courts.

The Act provides that on an application for the sale or division of land or goods, VCAT 'may make any order it thinks fit to ensure that a just and fair sale or division of land or goods occurs'. This discretion conferred on VCAT is wider than that formerly applying to partition applications in the courts.

In exercising its discretion, VCAT must consider some of the following matters:

- the use being made of the land or goods
- the practicality of dividing the land or goods
- whether a co-owner has any particular links with or attachment to the land or goods.

This means that VCAT has the power to make detailed factual enquiries into the conduct of co-owners before making an order under the Act.

VCAT continues the policy that an order will be made for a sale and division of the proceeds unless VCAT considers it fairer to grant some other relief.

Co-owners can still bring a claim in the Supreme or County Courts in relation to 'domestic partner' claims under the Property Law Act, partnership disputes under the Partnership Act 1958 (Vic) and testator's family maintenance claims. Jurisdiction over property disputes between spouses still vests in the Family Court.

As joint venture disputes do not fall exclusively within the courts' jurisdiction, it may mean that joint venture disputes regarding co-owned land may have to be brought at VCAT.

Despite the Act expressly excluding the jurisdiction of the Supreme and County Courts to hear applications under Part IV of the Act, the division of jurisdiction between the courts and VCAT in relation to certain property disputes between co-owners is not clearly defined.

Accounting and compensation between co-owners

The Act confers wide discretionary powers on VCAT to make an order for a co-owner to account or compensate another co-owner on the grounds of 'fairness'. A co-owner may seek an order in VCAT for accounting or compensation from another co-owner whether or not an application has been made for sale or division of land or goods. Therefore, co-owners are at risk of having their interests in land and goods decreased by a VCAT order.

In making an order for accounting or compensation on an application for sale or division, VCAT may take into consideration improvements, maintenance, insurance, rates, mortgage repayments, contributions to purchase money or other outgoings for which co-owners are liable. Although the Act does not confine the scope of matters on which VCAT can make an order, there must be a connection between the costs or expenses and the land or goods.

Where a co-owner makes an application for accounting or compensation (whether or not as part of an application for sale or division), VCAT may order (among other things) that a co-owner who has received more than the share of rent or other payments from a third party in respect of the land or goods to which that co-owner is entitled to account for that rent or other payments to the other co-owners.

Excluding operation of the Act

The Act does not expressly prohibit parties excluding the jurisdiction conferred on VCAT. If the parties wish to exclude the operation of the Act, it will be prudent to evidence the parties' intentions in a written agreement. This does not mean that the express exclusion is conclusive, but provides evidence of the parties' intentions.

What this means in practice

The changes to the law of co-ownership means that co-owners will have to respect the interests of other co-owners.

It is important that co-owners keep complete records of any expenditure and improvements they make in relation to the land or goods. Even matters which co-owners consider to be insignificant

should still be documented as it may assume considerable importance when assessed by VCAT. Failure to do so may leave co-owners exposed to the risk of having their share decreased by a VCAT order.

Rohan Ingleton | Partner
Carlyna Chhen | Solicitor

First Right of Refusal Over Peppercorn

The rights and obligations under first right of refusal clauses need to be clearly spelled out in leases.

In *Peppercorn Holdings No 1 Pty Ltd v DDH Graham Ltd & Ors* [2006] QSC 156 (Peppercorn Case), the Supreme Court of Queensland held that a first right of refusal clause to purchase a property was not breached by a landlord entering into a new lease of the property with the tenant's competitor prior to offering the property for sale to the tenant. The Peppercorn Case involved a tenant (Tenant) bringing proceedings against the responsible entity of an unlisted property trust (RE), the custodian (Custodian) and three companies being competitors of the tenant (Competitors) which entered into a heads of agreement (Heads) and new leases (New Leases) for the relevant properties.

Facts

The facts of the Peppercorn Case were that:

- The Tenant operated child care centres on 9 different properties in Queensland and New South Wales (Properties) leased from the Custodian. Each of the leases (Old Leases) contained a first right of refusal for the Tenant to purchase the Property (Tenant's Rights). The Old Leases were due to expire on or around June/July 2006. The Old Leases did not contain options to renew.
- The Tenant made an offer to the RE regarding the sale of the Properties to the Tenant in late February 2006. Negotiations were not successful.
- In April 2006, the RE was approached by the Competitors regarding the sale of the Properties and the businesses being conducted on the Properties. The RE notified the Tenant that it was 'close to doing a deal' with the Competitors. The Tenant responded that it was 'not interested'. However, later that month the Tenant wrote to the RE asserting that its endeavours to sell the Properties were in breach of the Old Leases.
- In mid-May 2006, the RE and the Competitors entered into the Heads. Under the Heads, the parties agreed to work in good faith

towards formulating and executing written agreements under which the Competitors would:

- lease the Properties
- purchase the assets of the businesses
- subject to the Tenant not exercising the Tenant's Rights, enter into put and call option agreements with respect to the Properties.
- In early-June 2006, the Custodian entered into the New Leases with the relevant entity of the Competitor in respect of the Properties. The New Leases contained options which if renewed, would extend the term of the Competitor's control over the Properties to 25 years.
- In mid-June 2006, one of the Competitors made an offer to the landlord to purchase the Properties, subject to the Tenant not exercising the Tenant's Rights and the existence of the New Leases (Competitor's Offer).
- On the next day after the Competitor's Offer was made, the landlord made an offer to the Tenant to sell the Properties subject to the New Leases for the same price as the Competitor's Offer.

Tenant's Arguments

The Tenant lodged a caveat over the Properties and brought proceedings against the RE, Custodian and Competitors seeking remedies to the effect that:

- if the Tenant purchased the Properties, it should not be bound by the New Leases
- the landlord should be required to offer to sell the Properties to the Tenant prior to the New Leases being executed.

One of the Tenant's main arguments was that the commercial intent and value of the first right of refusal under the Old Leases would be defeated if the RE and Custodian could burden the Properties with the New Leases. This would result in the Tenant being unable to occupy the Properties for up to 25 years (during which the Properties would be occupied or controlled by the Competitors). The court noted that there was considerable force in this argument.

Court's Decision

The court ultimately decided against the Tenant on the grounds that the first right of refusal clause (together with a number of provisions in the Old Leases) envisaged the Properties might be encumbered and that the legal authorities cited by the Tenant were distinguishable. If the Properties had to be offered to the Tenant unencumbered and with vacant possession, then this would be a serious restriction on the owner's ordinary property rights and must not be easily concluded.

Interestingly, the Peppercorn Case did not discuss any obligation on the landlord to act in good faith in respect of its dealings with the Tenant.

Practical Tips

In view of the Peppercorn Case:

- A landlord (including a responsible entity and custodian/trustee) should ensure that any first right of refusal granted by it is expressed in a manner which clearly allows the landlord to enter into further leases without breaching the terms of the first right of refusal.
- A tenant should ensure that if it wishes to obtain the benefit of a first right of refusal which also restricts the landlord from leasing out the property, then the lease should be very clear in establishing this because such a term will not be easily inferred by the courts.
- If the property is critical to the tenant's strategic operation, the tenant should consider securing an option under the lease in addition to the first right of refusal to purchase the property otherwise the tenant might lose the right to occupy the property to a competitor.
- Potential purchasers and third parties entering into agreements which are subject to a first right of refusal should be cautious in ascertaining the extent of the first right of refusal, whether or not the relevant clause has been complied with by the landlord and if possible, obtain suitable warranties and indemnities from the landlord in relevant circumstances.

Steven Mackay | Partner

Lily Tran | Solicitor