

Article Information

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Court Considers Valid Exercise of Lease Option

A recent decision of the NSW Court of Appeal in *Jong v Advanced Dental Services Pty Ltd* [2019] NSWCA 318 considers whether an email exchange between a lessor and a lessee was a valid exercise of an option to renew a lease.

Facts

Yeoh Yong Jong (**Appellant**) leased premises to Advanced Dental Services Pty Ltd (**Respondent**). The lease was for a term of five years with two options to renew the lease, each for a period of five years.

Prior to expiration of the initial term of the lease, the Appellant emailed the Respondent notifying the Respondent that “it states in the lease that exercising the option for another 5 years must be done 3-6 months prior to the end of the term” and asked the Respondent to “advise me immediately if you are re-signing for another 5 years or if you wish to vacate”. The Respondent replied to the email on the same day stating that, “Yes I would like to renew the lease for another term”.

In the months following, the parties communicated further about the renewal of lease. However, these communications did not result in an executed or registered lease. Eventually, the relationship between the Appellant and the Respondent broke down and the Respondent terminated the lease.

The Appellant commenced proceedings in the District Court claiming that the Respondent had exercised the first option to renew the lease and had repudiated the renewed lease by vacating the premises prior to the new expiry date. The trial judge dismissed the claim on the basis that the Respondent had not exercised the option to renew and had been occupying the premises under the holding over provisions of the lease. Therefore, the Respondent had validly terminated the initial lease.

The Appellant appealed the District Court’s decision. The Appellant claimed damages for loss of rent under the renewed lease.

Decision

A majority (per Meagher JA and Brereton JA) concluded that the option was not validly exercised and the appeal was dismissed with costs.

Meagher JA held that whether an option has been validly exercised depends:

first as a matter of construction on what is required [under the lease] for its valid exercise and, secondly on whether the conduct of the person purporting to exercise it has satisfied those requirements [45].

Brereton JA agreed with Meagher JA and added that the subsequent, post-contractual conduct of the parties is admissible as evidence as to whether a contract was formed. He stated that:

the question whether an option has been exercised is, in substance, a question of whether the offer of a new term (the option) contained in the lease *has been accepted in accordance with its terms*, so as to create a contract [emphasis added] [54].

The case is authority for the proposition that for the valid exercise of an option to renew a lease, it is necessary for the lessee to:

- comply with the terms of the lease for the exercise of an option; and
- show a clear and unequivocal intention to exercise the option in accordance with the lease terms.

Reasoning

In the present case, the lease required the lessee to serve on the lessor written notice of the exercise of the option during a specific period.

The Respondent's reply was not notice for the purpose of this clause as the reply that it 'would like to renew the lease':

- described 'a present state of inclination or preference' that it would like to renew the lease rather than an 'absolute and unqualified acceptance to exercise the option';
- it did 'not purport to constitute an exercise of the option'; and
- there was 'nothing in the immediate context of the email exchange which suggest[ed] otherwise' [51].

As to the 'immediate context of the email exchange' (the emails on 6 January 2014), the Appellant's email referred to a 're-signing' and this could be understood by the Respondent as a negotiated renewal rather than an exercise of an option [50]. Further, the Appellant's email asked the Respondent to 'advise me immediately if you are re-signing'. However, the Respondent was entitled to exercise the option at any time within 3-6 months prior to the expiry of the lease; immediate notice was not required. According to the Meagher JA, this made 'it more likely that her request was to be understood as enquiring more generally as to [the Respondent's] intentions in relation to the renewal of the lease' [50].

Further (per Brereton JA), the subsequent conduct of the parties demonstrated that the parties had not regarded the exchange of emails on 6 January 2014 as being an effective exercise of the option [54].

In Conclusion

This case serves as a cautionary reminder to lessees seeking to exercise an option to renew a lease. The Court has confirmed that for an option to be validly exercised, the lessee must comply with the lease terms and express a clear and unequivocal intention to accept the offer of the option to renew the lease.

- The lessee must comply with the lease terms to validly exercise a lease option - lessees should review these terms before seeking to exercise the option.
- The lessee must demonstrate a clear and unequivocal intention to exercise a lease option - a simple way to do this is to state that the option is exercised pursuant to the relevant clause number in the lease and comply with the notices clause in the lease.