ARTICLES

LEASES REPUDIATED: THE APPLICATION OF THE CONTRACTUAL DOCTRINE OF REPUDIATION TO REAL PROPERTY LEASES

CELINA CHEW*

I. INTRODUCTION

Until recently, the contractual principle of repudiation and contractual principles in general were excluded from the law governing real property leases.[1] The reasons for this exclusion stemmed from the traditional characterisation of the real property lease as a conveyance rather than a contract, a view which in turn was based upon the agrarian origins of the lease. Traditionally, the conveyance of the leasehold interest was considered to be the foundation of the lease. Since repudiation depends on a loss of bargain and since the bargain in a lease contract was thought to have been fulfilled upon conveyance and execution of the lease (and was therefore incapable of being lost), repudiation was thus thought to be inapplicable to leases.

* LLB(Hons)(UWA).

1. Repudiation was held to be inapplicable to leases in *Total Oil Great Britain Ltd v Thompson Garages (Biggin Hill) Ltd* [1972] 1 QB 318. Frustration was held to be inapplicable to leases in *Lobb v Vasey Housing Auxiliary (War Widows Guild)* [1963] VR 239; *Leighton's Investment Trust Ltd v Cricklewood Property and Investment Trust Ltd* [1943] KB 493; *Firth v Halloran* (1926) 38 CLR 261. The principle of mitigation of damages was held to be inapplicable to leases in *Maridakis v Kouvaris* (1975) 5 ALR 197 but see also *Vickers & Vickers v Stichtenoth Investments Pty Ltd* infra n 146.

In recent times, however, the lease has come to be used for commercial purposes thereby bringing the contractual implications of its nature increasingly into prominence. In *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*[2] ("*Tabali*") the High Court of Australia recognised the changing nature of the lease in holding that the principle of repudiation now applies to real property leases.

However, although the applicability of repudiation is now settled in Australia, there has been little judicial consideration of *how* repudiation applies to leases. This further question has two aspects. The first is the extent to which the theoretical aspects of contractual repudiation can be assimilated into the proprietary law of leases. The second is the manner in which the mechanics of repudiation may be applied to leases.

This article begins with a discussion of the nature of repudiation, the structure of the lease and the theoretical basis upon which the former may be applied to the latter. The article then briefly considers the acts which may constitute repudiation and the consequences of repudiatory termination in the leasehold context, including the impact of such termination on contractual termination clauses in a lease. The final section considers the extent to which the application of repudiation supersedes the traditional proprietary remedies.

II. REPUDIATION DEFINED

An act of contractual repudiation occurs when a party puts "himself in breach by evincing an intention, by words or conduct, of repudiating his obligations under the contract".[3] The doctrine of repudiation was developed by the common law for reasons of commercial convenience[4] but, although the widespread acceptance of the doctrine testifies to its value, the law has had difficulties in finding a satisfactory basis for its operation.[5]

2. (1985) 157 CLR 17.
3. 9 *Halsbury's Laws of England* (4th edn 1974) para 546.
4. *Frost v Knight* (1872) LR 7 Exch 111 Cockburn J, 113-114: "[When there is repudiation,] it is for the common benefit of both parties that the contract shall be taken to be broken as to all its incidents, including non-performance at the appointed time; as by an action being brought at once, and the damages consequent on non-performance being assessed at the earliest moment, many of the injurious effects of such non-performance may possibly be averted or mitigated."
5. K E Lindgren J W Carter and D J Harland *Contract Law in Australia* (Sydney: Butterworths, 1986) para 1933.

Of the various rationales suggested, the inevitable breach theory has been pre-eminent.[6] On this rationale, the law allows the innocent party to anticipate an actual future breach of an obligation which the repudiating party presently refuses to perform, on the basis that such future breach is inevitable.[7] Thus, no actual breach occurs at the time the contract is terminated; the cause of action arises only because the law allows the injured party to act on the future breach. The term "anticipatory breach" reflects this particular view of the way in which repudiation operates.

A problem arises, however, where the breach of the future obligation is a refusal rather than an inability to perform. The repudiating party may retract the refusal before the time for performance arises. Thus, for the purposes of this theory, the law must deem the future breach legally inevitable even though it may not be factually so. It does this where the party's refusal to perform the obligation can be said to be unequivocal and the injured party acts on or accepts the refusal.[8] This legal fiction produces the anomaly that it is an act of the innocent party which completes the breach giving rise to a right to terminate, rather than an act of the party in breach.[9]

The inevitable breach basis of repudiation has been rejected by some judges and commentators.[10] Their view is summarised by Lord Wrenbury in *Bradley and Others v Newsom, Sons & Co*:

> There can be no breach of an obligation in anticipation.... If there be a contract to do an act at a future time, and the promisor, before that time arrives, says that when the time does arrive he will not do it ... [h]is breach is a breach of a present binding promise, not an anticipatory breach of an act to be done in the future.[11]

6. Ibid.
7. Ibid.
8. Ibid.
9. H R Limburg "Anticipatory Repudiation of Contracts" (1925) 10 Cornell LQ 135, 140: "The breach of a contract must be the act of the party committing the breach. It cannot be the act of the *injured* party." Lord Esher MR in *Johnstone v Milling* (1886) 16 QBD 460, 467 described the situation in this way: "[A] renunciation of a contract ... does not, by itself amount to a breach of contract but may be so acted upon and adopted by the other party as a rescission of the contract as to give an immediate right of action."
10. Limburg supra n 9; S Stoljar "Some Problems of Anticipatory Breach" (1974) 9 MULR 355; *Manedelanto Compania Naviera SA v Bergbau-Handel GmbH The Mihalis Angelos* [1970] 3 All ER 125 Denning MR, 196-197; Edmund-Davies LJ, 202; Megaw LJ, 209-210 (*"The Mihalis Angelos"*).
11. [1919] AC 16, 53-54.

This is the gist of the implied term/present breach theory. The *presently binding promise* which is breached by the repudiating party is an implied term that both parties to the contract will be ready and willing to perform the contract during its currency.[12] Thus, when the repudiating party refuses to perform the contract, there is a breach of this implied term and it is this actual or present breach which grounds the right to terminate.

This reasoning disposes of the need for the fiction of legal inevitability to justify an immediate right of action. The implied term/present breach theory also does away with the anomaly of the cause of action depending on an act of the injured party. The right of the injured party to terminate arises *as soon as* there is a refusal of sufficient seriousness to amount to repudiation of the contract: that is, where there is an actual breach of the term of readiness and willingness to perform the contract during its currency.

There are, however, many cases which require that the injured party *accept* the repudiation before termination is effected.[13] How may these cases be reconciled with the implied term/present breach theory? It is submitted that the act of *acceptance* is still essential under the implied term/present breach theory but here the injured party's act of acceptance does not complete the breach and ground the right to terminate. Instead, acceptance operates as notification to the repudiating party of the injured party's intention to exercise the right to terminate.

Although it may be argued that the implication of such a term of readiness and willingness is as much a legal fiction as the inevitable breach theory, such an implication, in a commercial context, may be justified on the grounds that parties to commercial transactions enter into contracts in the expectation that such contracts will be performed and not abandoned. Thus, Chief Justice Jordan in *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* stated:

> One essential promise which is implied in every contract is that neither party will without just cause repudiate his obligations under the contract whether the time for performance has arrived or not ...[14]

12. Supra n 5; *The Mihalis Angelos* supra n 10; *Bradley and Others v Newsom, Sons & Co* supra n 11.
13. *Heyman and Another v Darwins Ltd* [1942] AC 356, 362; *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235.
14. (1938) 38 SR(NSW) 632, 646.

It is submitted, therefore, that the implied term/present breach theory is the preferable basis for anticipatory breach. Under this theory, anticipatory breach may be seen merely as a species of discharge by actual breach and both doctrines may be generally subsumed under a single principle of repudiation. Thus, in all cases of repudiation, a right to terminate the contract arises as soon as a breach (of the requisite seriousness) is committed. The injured party is then faced with an election whether to exercise this right to terminate or not. This election does not complete the breach but instead operates as notification to the repudiating party of the injured party's intention to exercise the right to terminate. If no such act of notification occurs, there is no exercise of the injured party's right to terminate and the contract continues.

A. A brief history of the lease

It was not always the case that contractual principles were excluded from real property leases. Indeed, the lease conferred a contractual interest on the grantee of the lease (the lessee) before it gave a proprietary interest.[15] The lease, therefore, is not inherently incapable of being governed by contractual principles. However, due to historical circumstances, this contractual aspect of the lease was for a long time overshadowed by its proprietary element; but essentially, a lease is a contract where, in return for consideration (the rent), a possessory interest is granted to the lessee for a term of years.[16]

The lease first developed in the period prior to the thirteenth century, in the context of money-lending,[17] an occupation not regarded favourably by society or the Church.[18] Thus, money-lending lessees

15. F Pollock and F Maitland *The History of English Law* 2nd edn (Cambridge: University Press, 1898) cited in J F Hicks "The Contractual Nature of Real Property Leases" (1972) 24 Baylor L Rev 443; T F T Plunckett *A Concise History of the Common Law* 5th edn (London: Butterworths 1986) cited in A J Bradbrook S V McCallum and A P Moore *Residential Tenancy Law and Practice - Victoria and South Australia* (Sydney: Law Book Co, 1985).
16. D J Hayton *Megarry's Manual of The Law of Property* 6th edn (London: Stevens & Sons Ltd, 1982) 332.
17. The lease began in the thirteenth century when landowners, in an attempt to circumvent the Church's prohibition on usury, granted a possessory interest, for a term of years, to money-lenders in return for money: Plunckett supra n 15, 571-573 cited in Hicks supra n 15, 448.
18. "The termor, therefore, is not unnaturally placed in very bad company among usurers and other scoundrels who prey upon society": Plunckett supra n 15, 571-572, cited in Hicks supra n 15, 448.

were given little protection of their possession by the law.[19] The lessee, however, was not completely without protection. The remedies based on the contract between the parties were available to the lessee. The courts only denied the lessee the use of real actions to protect possession: that is, the lessee had no rights against third parties.[20] By definition, therefore, the lessee had no interest in the land.[21]

Eventually, the lease became widely used for agriculture, giving it a new-found respectability.[22] From the thirteenth century onwards, the courts granted the lessee new actions to protect the lessee's interest.[23] The possessory interest of the lessee thus became as effectively protected as that of the freeholder and came to be regarded as an interest in land rather than a mere contractual right. The lessee's contractual rights were, however, still available by virtue of the contract by which the leasehold interest was granted. The lessee thus had contractual as well as proprietary rights.

Since the main purpose of the lease, at this time, was agricultural, land and its possession were the focal points of concern.[24] The typical agrarian lessee was self-sufficient and fully prepared to self-provide any of the services (such as water, heating and repairs) needed for the running of a farm.[25] The lessor's main obligation was to convey the interest in land to the lessee. In these circumstances the lease was

19. Hicks supra n 15, 449: "Upon ouster the lessee's sole remedy was an action on the covenant against his lessor; he had no rights against third parties. The lessee's term was subject to the dower interests of the lessor's widow, and the lessor could alienate free from the rights of the lessee."
20. Ibid; Bradbrook et al supra n 15, 120.
21. F Cohen "Dialogue on Private Property" (1954) 9 Rutger L Rev 357, 359-374. Cohen compares contractual rights and proprietary rights and suggests that the former apply only as between the contracting parties, whereas the latter apply against the world at large.
22. Hicks supra n 15, 449. The rise of the mortgage as a more satisfactory security device allowed the term of years to be disassociated from the unsavoury aspects of money-lending.
23. Ibid, 450. Specifically, the action quare ejecit infra terminum was granted in 1235, allowing the ejected lessee to be restored to the land. Later, the right to damages for ejectment was granted by a form of trespass, de ejectione firmae. By 1499, this last remedy had developed to allow the lessee to recover possession of the land.
24. Ibid.
25. J B Harvey "A Study to Determine Whether the Rights and Duties Attendant Upon the Termination of a Lease should be Revised" (1966) 54 Calif L Rev 1141, 1145; A J Bradbrook *Poverty and the Residential Landlord-Tenant Relationship* (Canberra: AGPS, 1975) 2.

reduced to a conveyance of an interest in land and rent which issued from the land was linked with the estate in land, becoming seen as the consideration for possession.[26] Consequently, the idea arose that rent was payable to the lessor for the conveyance of the leasehold only. This is not to say that the contractual element of the lease was eliminated. Rather, this aspect of the lease was not utilised, there being no need for detailed covenants to regulate the obligations of the parties.

The idea of rent being co-extensive with the estate in land has been referred to as the "possession-rent relationship",[27] or, preferably, the "possession-rent equation".[28] As long as the lessee retained the estate in land, the lessee could not terminate the lease for repudiation on the part of the lessor. This is because repudiation depends on the loss of the substance of the bargain. With regard to leases, the conveyance of the estate in land to the lessee was thought to constitute substantial performance of the contract by the lessor. A breach on the part of the lessor which did not disturb the lessee's interest in land was not considered serious enough to justify the termination of the lease.[29]

The twentieth century has seen the lease being increasingly used for commercial and residential purposes.[30] The requirements of an urban lessee differ dramatically from those of an agrarian lessee. For example, an urban lessee of a multi-dwelling building occupies only part of a building, whilst services such as plumbing and electricity must be provided by the lessor for the whole building.[31] In commercial leases, there may be equipment on the premises which the lessee requires for its business and the lessee may depend on the lessor to maintain and allow the lessee to use such equipment.

In most modern lease agreements these additional concerns are dealt with by covenants of great variety, defining the rights and obligations of each party in detail. There are usually standard clauses stipulating that the provision of such services be the task of the lessor.[32]

26. Hicks supra n 15, 450; J M Quinn and E Phillip "The Law of Landlord-Tenant: A Critical Evaluation of the Past with Guidelines for the Future" (1969) 38 Fordham L Rev 225, 228, 229.
27. Quinn and Phillip supra n 26, 228.
28. The expression "possession-rent equation" more clearly indicates the idea that rent was thought to be the quid pro quo for possession.
29. Quinn and Phillip supra n 26, 230.
30. Hicks supra n 15, 451-452.
31. Quinn and Phillip supra n 26, 231.
32. Ibid.

This appears to be a sensible solution since the lessor usually owns the building. However, the problem is not in the allocation of responsibility for services but in what can be done to enforce the performance of such services. It is here that the traditional proprietary remedies fail the modern lessee.

The inclusion of commercial covenants revitalised the contractual aspect of the lease, which had fallen into disuse. Land law, however, was slow to accommodate this change and clung instead to the idea that rent was given in exchange for the conveyance only. The new covenants were merely *tacked on* to the existing possession-rent equation and were not considered part of the foundation of the lease. Thus, the failure to perform one of these covenants (if it did not interfere with the tenant's possession) did not give rise to a right to terminate the lease.

The lease in the twentieth century has been described as a two-level relationship.[33] The first level comprises the possession-rent equation, while the second level comprises the covenants of services. Breach of a first-level obligation gives rise to the first-level remedy of the termination of the estate whilst breach of a second-level obligation only gives rise to an action for damages. The covenants of services are relegated to a position of secondary importance in relation to the conveyance.

This view is unrealistic in the context of today's urban leases and the failure to allow the lessee to terminate for the non-provision of such services is a failure to recognise the fundamental importance of such services in the modern lease.

It would be erroneous to say that contractual principles were never allowed to apply to real property leases. Statements to the effect that contractual principles do not apply to leases[34] refer to the inapplicability of those principles to the termination of the lease. Traditionally, termination of an estate in land could only be effected by proprietary measures because termination involved the divesting of a proprietary interest. The continued exclusion of contractual principles with regard to termination of leases led to easily avoidable injustices, prompting the courts to reconsider this area of law.

33. Ibid, 233-234.
34. Supra n 1.

B. The applicability of contractual principles to leases

In *National Carriers Ltd v Panalpina (Northern) Ltd*[35] ("*Panalpina*") the House of Lords examined traditional objections to the general applicability of contractual principles to leases and held that leases could be frustrated. Their Lordships considered that there were basically two objections:

1. The conveyance of the leasehold interest was the foundation of the lease and any contractual obligations under it were merely incidental.
2. The allocation of risk in leases followed that of a sale of land transaction. That is, on the execution of the lease, the risk passed to the lessee.

In answer to the first objection, Lord Wilberforce said:

> [I]f the argument is to have any reality, it must be possible to say that frustration cannot occur because in any event the tenant will have that which he bargained for, namely, the leasehold estate. Certainly, this may be so in many cases.... but there may also be cases where this is not so. A man may desire possession and use of land or building for, and only for, some purpose in view and mutually contemplated.... In such a case the lease, or the conferring of an estate, is a subsidiary means to an end, and not an aim or end of itself.[36]

Therefore, where the conveyance of an estate in land is not the primary purpose of the lease, conveyance by the lessor upon execution of the lease will not constitute substantial performance of the contract. If it can be shown that certain covenants form a sufficiently important part of the lease then refusal or failure to perform such obligations will substantially deprive the lessee of the bargain, giving rise to the right to terminate.

Rejection of the first objection robs the second of the basis upon which it proceeds. The allocation of risk objection depends upon a high correlation between the character of the lease and a sale of land transaction. Both were previously characterised as predominantly conveyances of interests in land and the lack of executory obligations

35. [1981] AC 675.
36. Ibid, 694. His Lordship was supported by Lord Roskill ibid, 714: "However much weight one may give to the fact that a lease creates an estate in land in favour of the lessee, in truth it is by no means always in that estate in land that the lessee is interested. In many cases, he is interested only in the accompanying contractual right to use that which is demised to him by the lease and the estate in land which he acquires has little or no meaning for him."

under the lease after execution reinforced this lease-as-conveyance concept. However, the resurgence of the contractual aspect of the lease means that a close analogy between the two transactions cannot be maintained. Therefore, the argument, that the allocation of risk in leases should naturally follow that in sale of land transactions, loses its cogency.

Although *Panalpina* deals with frustration, the applicability of their Lordships' reasoning with regard to repudiation was supported by the majority of the High Court in *Tabali*.[37] This was despite the following remarks by Justice Brennan:

> Discharge of contract by frustration and discharge by repudiation ... are distinct modes of termination.... There is no valid analogy between the implication of a term that determines a lessee's interest on the happening of a frustrating event and the implication of a term empowering a lessor to elect to determine a lease before the expiry of the term granted in the event of repudiation by the lessee....[38]

It is submitted that this difference referred to by Justice Brennan does not preclude the *Panalpina* reasoning from applying to repudiation for two reasons. First, the reasoning of their Lordships turned on the character of the lease rather than on any feature peculiar to the doctrine of frustration. It merely rejected the idea that the foundation of a lease is always comprised of the conveyance alone. Secondly, although the two doctrines arise under different circumstances and with different consequences,

> nevertheless the test for deciding whether any failure [or] inability to perform by one party is sufficient to discharge the other is the same whichever doctrine is being invoked.[39]

This test is whether a loss of bargain can be established. It is this loss of bargain (whether by a supervening event or the conduct of one party) that justifies termination. The inadequacy of property law which the courts sought to redress was the absence of a right to terminate the lease when the *substance* of the lease is lost, where that which is lost is *not* the leasehold interest. The contractual principles of frustration and repudiation offer a solution to the problem.

37. Supra n 2 Mason J, 28; Brennan J, 41; Deane J, 52.
38. Ibid, 41.
39. *The Hermosa* [1980] 1 Lloyd's Rep 638 Mustill J, 648.

C. The benefits offered by repudiation

Repudiation offers the parties to a lease two benefits: first, the right to terminate and secondly, the availability of loss of bargain or prospective damages.

1. The right to terminate

With repudiation, the injured party obtains a right to terminate the lease where there was none under property law. Previously, a refusal to perform an obligation which did not disturb the possession-rent equation did not give rise to a right to terminate. Under the doctrine of repudiation, the party can terminate the whole lease if such a refusal or failure to perform amounts to, or evidences, the loss of the substance of the contract. In this way, the modern lessee can protect its bargain where the fulfilment of certain covenants is as important to the lessee as the conveyance of the estate in land.

2. The availability of loss of bargain or prospective damages

The termination of leases by proprietary methods only entitles the injured party to damages which have accrued prior to termination of the estate. Once termination has been effected, there is no lease in existence and no subsequent obligations to perform can arise or be breached. Post-termination damages, flowing from the "breaches" of such subsequent obligations, are thus not recoverable.

Repudiation, however, is based on the promisor's renunciation of the whole contract. This necessarily involves the promisor breaching all future obligations under that contract. As the injured party may recover damages to compensate for damage caused by the promisor's breach, the injured party also recovers the loss of the whole bargain, including prospective damages.

The availability of prospective damages is a great advantage that termination under repudiation has over termination by proprietary methods. Under the latter, the lessor wishing to recover damages for the value of the whole lease must be careful to avoid terminating the lease and must sue for damages for the breaches as they are committed. This means that the injured party must wait until the end of the term of the lease before that party is able to recover the loss of the whole bargain. This may be inconvenient where the repudiation has occurred

early in a long-term lease since, by the end of the term, the promisor may no longer be solvent, available or alive, or the provisions of statutes of limitation may preclude any action for recovery of damages.

D. The effect of the proprietary element on the application of contractual principles to leases

The proprietary element in the lease cannot be ignored when applying contractual principles. Indeed, *Panalpina* recognised only that leases were no longer immune from frustration, rather than that all leases were capable of being frustrated. Their Lordships in that case restricted the possibility of leases being frustrated to "rare"[40] cases because land, by its nature, is virtually indestructible; it would only be on rare occasions that land, as the basis of a lease contract, would be lost.

Although an event causing "mere expense and onerousness"[41] will not frustrate a lease, a contract may be frustrated by the loss of the commercial venture of the contract.[42] The modern lease, being a commercial device, is susceptible to this type of frustrating event, an event which does not depend on the destruction of the land itself. Thus, the nature of land as an obstacle to the application of frustration or repudiation in this situation is restricted in scope.

The High Court in *Tabali*[43] was also cautious in affirming the applicability of repudiation to leases. The reason for this, as Justice Mason pointed out, is the interest in land which is involved:

> Repudiation ... of a lease involves considerations which are not present in the case of an ordinary contract. First, the lease vests an estate or interest in land in the lessee and a complex relationship between the parties centres upon that interest in property. Secondly, this relationship has been shaped historically in very large measure by the law of property....[44]

There appear, therefore, to be two aspects to the proprietary element of the lease. Their Lordships in *Panalpina* referred to the *nature of*

40. Supra n 35 Lord Hailsham of St Marylebone LC, 689.
41. Ibid, 700. The cases referred to include *Krell v Henry* [1903] 2 KB 740 and *(WJ) Tatem Ltd v Gamboa* [1939] 1 KB 132. See S G Starke and P F P Higgins *Cheshire and Fifoot's Law of Contract* 3rd edn (Sydney: Butterworths, 1974) 688-689.
42. Compare the "Coronation cases": Starke and Higgins supra n 41, 688-689.
43. Supra n 37.
44. Supra n 2, 33-34.

land, while Justice Mason in *Tabali*,[45] refers not to the land itself but to the *interest in land* as the factor affecting the application of repudiation to leases: the land and the interest in the land are two distinct concepts.

Their Lordships in *Panalpina* apparently saw no difficulty with the interest in land being terminated by contractual principles. Their concern was with the likelihood of such termination arising, given the nature of the subject matter. The High Court in *Tabali*,[46] however, was more concerned with the interest in land aspect of the proprietary element of the lease. This aspect has two major facets:

1. The similarity to a freehold estate

The degree of similarity which a particular leasehold interest bears to a freehold interest will affect the likelihood of that lease being repudiated. A freehold interest is not susceptible to termination under repudiation since it involves no major executory obligation after conveyance: no loss of bargain is possible. Upon conveyance, the contractual relationship between the parties is ended. Therefore, the more a lease resembles a sale of land transaction, the less susceptible it is to repudiation. In *Tabali* Justice Deane said:

> [I]t should be accepted that, as a general matter and subject to one qualification, the ordinary principles of contract law are applicable to contractual leases. The qualification is that the further one moves away from the case where the rights of the parties are, as a matter of substance, essentially defined by executory covenant or contractual promise to the case where the tenant's rights are, as a matter of substance, more properly to be viewed by reference to their character as an estate (albeit a chattel one) in land with a root of title in the executed demise, the more difficult it will be to establish that the lease has been avoided or terminated pursuant to the operation of the ordinary principles of frustration or fundamental breach.[47]

His Honour used a 99 year lease of unimproved land on payment of a premium and at nominal rent as an example of the latter. This type of lease greatly resembles a pure conveyance of land and, in that sense, is not much different from a freehold estate. The diminished role played by the contractual element in this type of lease makes it much less receptive to contractual principles. At the other extreme, leases of

45. Ibid, 27-33; also Brennan J, 40-41.
46. Ibid.
47. Ibid, 53. A fortiori, the operation of principles of repudiation.

multi-dwelling buildings for high rents are much more receptive to contractual principles because the contractual element in these leases is more prominent. It can be seen, therefore, that not all leases are susceptible to repudiation: it is only "contractual" leases which, because of their prominent contractual element, have this distinction. The degree of similarity that a lease bears to a freehold estate is a question of fact. It is suggested, however, that some factors to be taken into consideration in deciding this question are the length of the lease, the nature of the leased premises, the amount of rent payable and the number and nature of executory covenants which have been promised.

2. Liability of the lease to termination by some proprietary measure

Justice Brennan in *Tabali* thought that the interest in land in a lease could not be terminated under repudiation unless it could be initially terminated by some proprietary measure. His Honour said:

> [A] lessor's inability to determine a lessee's interest except where it is liable to forfeiture precludes the lessor from rescinding the lease for anticipatory breach, but it does not follow that the ordinary contractual principles relating to anticipatory breach do not apply to a lease where the lessee's interest is liable to forfeiture.[48]

The proposition that a lessee's liability to forfeiture is a prerequisite to the application of repudiation was noted by Justice Priestley in *Wood Factory Pty Ltd and Others v Kiritos Pty Ltd*[49] ("*Wood Factory*"):

> [T]he ratio [of *Tabali*] is that the rules of contract law which permit a party to a contract ... to elect to terminate it by "accepting" ... repudiatory conduct ... will apply to a lease when both (i) the landlord is in a position to forfeit the lease and (ii) the conditions for application of repudiation doctrine are fulfilled....[50]

If this is so, then the scope of the doctrine in relation to leases is severely restricted, since the availability of repudiation as a means of terminating the lease will depend on, and be restricted to, the same circumstances as those which also give rise to a right to forfeit the lease. The right to forfeit generally depends on an actual breach of either a condition or a covenant (if the latter is provided for). Repudia-

48. Ibid, 43.
49. [1985] 2 NSWLR 105.
50. Ibid, 132.

tion, however, does not necessarily involve actual breach (as in failure to perform) but may consist of a *refusal* to perform which, nevertheless, results in the loss of the bargain. Justice Brennan's remarks would appear to exclude the right to terminate in this case.

This prerequisite to repudiation appears to have resulted from a combination of proprietary and contractual rules. In contract law, when a contract is terminated for repudiation, the accrued interests are not divested. Justice Dixon in *McDonald and Another v Dennys Lascelles Ltd* said:

> [T]he contract is not rescinded from the beginning. Both parties are discharged from the further performance of the contract, but rights are not divested or discharged which have already been unconditionally acquired. Rights and obligations which arise from the partial execution of the contract ... continue unaffected ... the contract is determined so far as it is executory only....[51]

Under property law, the interest in land is vested in the lessee upon execution of the lease. It is an accrued benefit and, according to contract law, is not divested when the contract is terminated for repudiation. Thus, it would appear that the estate in land cannot be terminated through termination under repudiation itself, but must be effected by some proprietary measure.

This analysis is unsatisfactory because it fails to recognise that the lease is not an absolute grant of an interest in land unlike, for example, a conveyance of a freehold estate where, upon execution of the sale of land, the freehold estate is vested in the purchaser and the contractual relationship between the parties ends. In the case of the modern lease, there is a continuing contractual relationship[52] between the lessor and the lessee, with several implications:

(a) In a lease, the lessee's interest in land is for a specified period only. Unlike the grantor of a freehold estate, who has no obligations or rights with regard to the land after conveyance, the lessor has a reversion to protect. This in itself gives rise to a relationship between the parties in which each is answerable to the other for the proper use of the land and the observation of the terms upon which that relationship is built.

51. (1933) 48 CLR 457, 476-477.

52. In *Panalpina* supra n 35, 705 Lord Simon said: "Moreover, the sale of land is a false analogy. A fully executed contract cannot be frustrated; and a sale of land is characteristically such a contract. But a lease is partly executory: rights and obligations remain outstanding on both sides throughout its currency. Even a partly executed contract is susceptible of frustration in so far as it remains executory: there are many such cases in the books."

(b) There is a range of executory obligations (covenants of service) which arise after the execution of the conveyance and which may be as important to the parties to the lease as the conveyance.

(c) The leasehold interest itself is an "executory" obligation, in the sense of not being fully performed. This interest consists of the right to quiet enjoyment for a term of years: the lessor covenants to refrain from interfering with the lessee's use of the premises. Being executory, this covenant (or at least that portion of it which is unperformed at the time of termination) is discharged upon the termination of the lease for repudiation. In this way, termination under repudiation terminates both the lease contract and the estate in land.

On this reasoning, it is not necessary for the estate in land to be liable to termination by some proprietary measure before termination under repudiation can be effected. The principle of repudiation is capable of terminating the estate on a purely contractual basis. Acceptance of the above analysis allows repudiation to be truly described as a method of determining a lease, without the prop of property law. This analysis reflects both the contractual and proprietary elements of the lease. Each element has a different sphere of operation: the former deals with the rights of the lessee vis-a-vis the lessor, whereas the latter deals with the rights of the lessee vis-a-vis third parties. Because repudiation involves the rights of the lessor vis-a-vis the lessee, the influence of the proprietary element on its operation is minimal.

III. THE TERMINATION PROCESS

The termination process under repudiation consists of the establishment of the right to terminate and the exercise of that right.

A. The right to terminate

The right to terminate arises when loss of the bargain is established. This requirement can be formulated thus: has the promisor renounced his obligations in a way which makes the continuance of the contract on the part of the innocent party pointless and so justifies the termination of the contract? A breach or pattern of breaches of sufficient seriousness is required for an affirmative answer.[53] Thus, the question of what conduct constitutes repudiation is an evidentiary one. The particular facts of a situation play a crucial role in the determination of this question: the usefulness of authorities and precedents is limited. Nevertheless, some common covenants may be considered.[54]

1. Lessor's covenants

The lessor's main covenant is that of quiet enjoyment. Although it is fundamental,[55] this covenant is not a *condition* of the lease, since substantial interference with the lessee's quiet enjoyment is required before the covenant is breached. In contrast, a condition may be breached by a trifling deviation in performance of the obligation. Similarly, the implied covenant that furnished premises be fit for human habitation cannot be characterised as a condition.

Although they are not conditions, the fact that these two covenants are implied by law demonstrates their importance. A substantial breach of either covenant would give rise to a right to terminate. What constitutes a substantial breach, however, is again a question of fact in every case.

53. This requirement of seriousness may be demonstrated in the two ways specified by Lord Diplock in *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 849: (1) where a party's failure to perform has the effect of depriving the other party of the substantial benefit of the contract (so-called "fundamental breach"), and (2) where the failure to perform amounts to a breach of condition.
54. For further discussion of this area, see W D Duncan *Commercial Leases* (Sydney: Law Book Co, 1989) 167-169.
55. It is implied into every lease and in fact arises from the very relationship of landlord and tenant: R Brooking and A Chernov *Tenancy Law and Practice: Victoria* 2nd edn (Sydney: Butterworths, 1980) para 99.

There are usually other express covenants in a lease regulating the obligations of the parties. The parties are entitled to stipulate that any one of these express covenants be a *condition*, the slightest breach of which would ground the termination of the lease.[56] In the absence of such stipulation, a covenant may be found to be a condition by inference from the circumstances surrounding the contract.[57]

2. Lessee's covenants

The main obligation of the lessee is to pay rent. The High Court in *Shevill v The Builders' Licensing Board*[58] ("*Shevill*") held that this was not generally an essential covenant (that is, a condition) of the lease, although it may be made so by the express intentions of the parties or by implication from the circumstances. This characterisation of the covenant accommodates the view that a failure to pay one instalment of rent does not necessarily indicate an intention to abandon the lease. However, if the breach is such as to lead to the inference that the lessee will not pay any rent in the future, repudiation will be established.

None of the numerous other covenants usually found in the lease[59] can be considered essential in the absence of express words or persuasive evidence to the contrary. Further, repudiation is not to be lightly inferred. Justice Mason in *Tabali* said that mere breaches of covenant alone, without more, would not constitute repudiation of the lease. Although his Honour noted that "it is of some significance that the instances in which courts have held that a lessee has repudiated his lease are cases in which the lessee has abandoned possession of the leased property",[60] he specifically rejected the contention that abandon-

56. *Photo Production Ltd v Securicor Transport Ltd* supra n 53 Lord Diplock, 849; *Shevill and Another v The Builders' Licensing Board* (1982) 149 CLR 620 Gibbs CJ, 627.
57. The test is that enunciated by Jordan CJ in *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* supra n 14, 641-642: "The test of essentiality is whether it appears from the general nature of the contract considered as a whole, or from some particular term or terms, that the promise is of such importance to the promisee that he would not have entered into the contract unless he had been assured of a strict or substantial performance of the promise ... and this ought to have been apparent to the promisor."
58. *Shevill* supra n 56.
59. For example, covenants concerning sub-letting, rates and taxes, insurance, waste, repairs, and the yielding of possession upon expiration of the lease.
60. Supra n 2, 34.

ment of possession is necessary to constitute repudiation by the lessee.[61]

B. The exercise of the right to terminate

Unequivocal conduct evincing an intention to terminate is necessary to constitute an effective election to terminate. The question of what amounts to such unequivocal conduct, in a leasehold context, depends greatly on the facts. However, some guidance may be gleaned from case law dealing with acceptance of surrender by operation of law and the right to forfeit a lease. Although the way in which the election arises in each of these remedies is different, the manner in which termination is effected is the same: by an unequivocal act evincing an intention to terminate the lease. The relationship between repudiation on the one hand, and surrender and forfeiture respectively on the other, is discussed more fully later in this article.

Surrender of a lease has traditionally taken one of two forms: the relinquishment of possession of the premises; and the grant of a new lease.[62] With regard to relinquishment of possession, it appears a change in possession is essential for the surrender to be "accepted" by the lessor.[63] Surrender is not complete until the lessor takes possession in such a manner as to estop the lessor from denying that the lease is at an end.[64] This is achieved, for example, where the lessor enters and re-lets the premises to another lessee, who then goes into occupation. The lessor is not taken to have assumed possession if entry is only to make repairs.[65] With regard to the grant of a new lease, the acceptance of a new lease inconsistent with the existing lease is sufficient.[66] However, the acceptance of a void lease will not effect surrender.[67]

61. Ibid.
62. *Woodfall* lists these and several other methods of surrender: V G Wellings *Woodfall's Law of Landlord and Tenant* 27th edn (London: Street & Maxwell, 1978) 863ff ("*Woodfall*").
63. *Andrews v Hogan and Others* (1952) 86 CLR 223, 252-253. Also *Cummins v Matheson* [1955] VLR 389; *Watson v Webb* (1948) 66 WN(NSW) 42; *Spinks v Mundy and Others* [1957] SR (Qld) 234.
64. Duncan supra n 54, 190.
65. *Woodfall* supra n 62. For further discussion of what amounts to surrender, see Brooking and Chernov supra n 55, para 204 and Duncan supra n 54, 187-192.
66. *Davison d. Bromley v Stanley* (1768) 4 Burr 2210; 98 ER 152.
67. *Barclays Bank Ltd v Stasek and Another* [1957] Ch 28. See also *Woodfall* supra n 62, 865.

The right to forfeit a lease arises upon the breach of a particular covenant or some other event, as stipulated in a forfeiture clause in the lease. An exercise of this right usually depends on the terms of the forfeiture clause, a question of fact. However, since the typical forfeiture clause is a proviso for re-entry,[68] the courts have developed a body of law, regarding forfeiture, based on the proviso for re-entry.

Where the clause expressly provides for re-entry, it is settled that the lessor can exercise the right to forfeit only by actual re-entry or its equivalent, an action for recovery of possession.[69] The law does not appear to recognise any other method of exercising the right to forfeit.[70] Until recently, the authorities appeared to favour the view that mere service of a writ unequivocally demanding possession, without issue, is sufficient to exercise the right to forfeit.[71] However, the English Court of Appeal in *Canas Property Co Ltd v KL Television Services Ltd*[72] decided that communication (or the issue of a writ) to the lessee was also necessary. This is in accordance with the favoured rule in contract law that acceptance of repudiation must be communicated to the promisor.[73]

Apart from these examples from property law,[74] the rules developed in contract law also provide some guidance as to what constitutes an exercise of the right to terminate a lease. For instance, the rejection of the promisor's performance has been held to be a sufficient exercise of the right to terminate, as has the making of an alternative contract; the disposal of the subject matter of the contract; and an act on the part of the promisee disabling himself from performing the contract.

C. The consequences of termination

The two major consequences flowing from termination of a contract are the discharge of unperformed duties of both parties and the liability of the party in breach to pay damages in substitution for unperformed

68. Brooking and Chernov supra n 55, para 218.
69. *Moore v Ullcoats Mining Co Ltd* [1908] 1 Ch 575.
70. Brooking and Chernov supra n 55, para 220.
71. *Jones v Carter* (1846) 15 M & W 718, 726; 153 ER 1040, 1043.
72. [1970] 2 QB 433.
73. *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525, 550. Compare *Poort v Development Underwriting (Victoria) Pty Ltd (No 2)* [1977] VR 454, 459.
74. See also *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623 for recent consideration in the High Court as to what may amount to repudiation of a contract. Noted in (1989) 63 ALJ 773.

obligations. Although the discharge aspect of termination is logically prior to the damages aspect, the latter will be discussed first for sake of convenience.

1. Damages

Where the lease is terminated for repudiation, the lessor can recover unliquidated damages for the period after termination. Loss of bargain damages usually consist of all future rental, less the rent obtainable had the premises been re-let at the best rate available at the time.[75]

The future instalments of rent are recoverable on the basis of anticipatory secondary obligations.[76] Although the anticipatory secondary obligation is directly related to termination, the question arises as to whether termination is a prerequisite to the recovery of loss of bargain damages. A second question relating to this relationship between termination and loss of bargain damages is whether termination always results in the recovery of loss of bargain damages.

(i) Is termination a prerequisite to the recovery of loss of bargain damages?

On the face of it, it would appear that termination will always be required if loss of bargain damages are to be recovered; this is because it is by termination that the future obligations are discharged giving rise to the substitutory anticipatory secondary obligation to pay loss of bargain damages.

75. See Duncan supra n 54, 170 describing the usual formulation for the measure of damages following repudiation and citing *Lamson Store Service Co Ltd v Russell Wilkins and Sons Ltd* (1906) 4 CLR 672 Griffith CJ, 684. Duncan also notes that the method adopted in assessing damages will depend on the circumstances of the case and the attitude taken by the lessor: see *Peet and Co Ltd v Rocci* [1985] WAR 164 Rowland J, 178.

76. Lord Diplock in *Photo Production Ltd v Securicor Transport Ltd* supra n 53, 848: "[B]reaches of primary obligations give rise to substituted or secondary obligations on the part of the party in default, and ... may entitle the other party to be relieved from further performance of his own primary obligations."
His Lordship continued, 849: "[T]here is substituted by implication of law for the primary obligations of the party in default ... to pay monetary compensation to the other party for the loss sustained by him in the consequence of their non-performance in the future.... This secondary obligation is additional to the general secondary obligation; I will call it the anticipatory secondary obligation".

However, Chief Justice Barwick in *Ogle v Comboyuro Investments Pty Ltd*[77] suggested that termination is only required where the loss of bargain damages are alleged to flow from an anticipatory (as opposed to "actual") breach of the contract. In reaching this conclusion, his Honour appears to have relied on the inevitable breach theory of anticipatory breach under which there is no breach until acceptance of the repudiation of the future obligation. The act of acceptance completes the breach and thereby grounds the right to terminate the contract. The consequence of this theory is that termination appears to be required for the recovery of loss of bargain damages flowing from an anticipatory breach amounting to repudiation but, anomalously, is not required for the recovery of loss of bargain damages flowing from an actual breach amounting to repudiation. This is because repudiation under an actual breach is assumed not to require an act of acceptance to "complete" the breach.

It is submitted that, in the anticipatory breach situation, the significance of the innocent party's "acceptance" of the breach lies not in a completion of the breach but in an election by that party whether to exercise the right to terminate which arises as a consequence of the repudiatory conduct. This is essentially the position under the implied term theory, which is suggested to be a preferable rationalisation of anticipatory breach and repudiation. Under the implied term theory, anticipatory breach is considered as a species of actual breach, and in this redefined situation, the injured party is always faced with an election whether to exercise the right to terminate, whether the breach is "actual" or "anticipated".

Chief Justice Barwick's analysis cannot be maintained under the implied term theory of repudiation.[78] In a sense, termination is a requirement for the recovery of loss of bargain damages (in both "actual" and "anticipated" breach situations) because the contract must be ended before such damages can arise. If the contract is still on foot, the claimant has not lost the benefit of the future obligations. Termination, in the sense of the ending of the contract, must therefore be a prerequisite of the recovery of loss of bargain damages. However, his Honour appeared to be using the term, in the context of anticipatory breach, to indicate an event giving rise to a cause of action where there would otherwise be none.

77. (1976) 136 CLR 444, 450.
78. See text at 88-90.

(ii) Will termination always result in the recovery of loss of bargain damages?

Although termination is directly related to loss of bargain damages, the act of termination should not be confused with or characterised as the cause of the loss of bargain damages. A promisee cannot avoid the basic requirements of proving causation and remoteness when claiming damages after termination.[79] Assessment of damages is a process separate from the termination process and proof of termination is not proof of loss of bargain.

In order to recover loss of bargain damages, the promisee must show loss of bargain and that this was caused by the promisor's breach. Usually, where termination arises under repudiation, loss of bargain damages are also proven because such termination only arises where a loss of bargain is established. However, even in such cases, the fact of termination should not remove the need for the injured party to prove loss by reference to the principles of causation and remoteness.[80]

The need to separate the process of quantifying damages from that of termination is especially clear in the case of termination under an express contractual right to terminate.[81] In the context of leases, these rights usually arise in the form of forfeiture clauses.

Prior to *Shevill*, the lessor, after terminating the lease under a re-entry clause, could recover rent for the balance of the term less whatever could be recovered by repossessing or re-letting. This right was usually protected by a clause providing that, upon the occurrence of one of a number of breaches or events, the lessor may re-enter the premises *without prejudice* to any other remedy which the lessor might otherwise have for breach of covenant.[82] The right to forfeit could,

79. The promisee must prove these requirements according to the rule in *Hadley and Another v Baxendale and Others* (1854) 156 ER 145. This point is made in M Hetherington "Contract Damages for Loss of Bargain Following Termination: The Causation Problem" (1983) 6 UNSWLJ 211.

80. An illustration of this need is to be found in *The Mihalis Angelos* supra n 10 wherein, although the plaintiff was able to show a right to terminate the contract, the plaintiff could not prove that loss was entirely attributable to the defendant's breach and was entitled to recover only nominal damages.

81. *Yeoman Credit Ltd v Waragowski* [1961] 1 WLR 1124; *Overstone Ltd v Shipway* [1962] 1 WLR 117; *Financings Ltd v Baldock* [1963] 2 QB 104.

82. In *Shevill* supra n 56, Clause 9(a) of the lease provided:
"The Lessor and the Lessee COVENANT AND AGREE:
(a) That if the rent hereby reserved or any part thereof shall be unpaid for the space of fourteen (14) days after any of the days on which the same ought

however, arise upon a breach of a minor covenant or even some other event not amounting to a breach.[83] Loss of bargain damages would not be recoverable if there was a breach of a minor covenant and in the case of a non-breaching event, no damages would be recoverable at all.

It may be argued that although such events or breaches of minor covenants do not of themselves constitute a loss of bargain, the fact that they lead to termination justifies the recovery of loss of bargain damages.[84] The fallacy in this contention is that the claimant is relying on the act of termination as the basis for quantifying damages where, in fact, the claimant should be looking to the reason for termination. The nature and effect of the breach itself should form the basis for the assessment of damages recoverable because the breach is the source of

> to have been paid in accordance with the covenant for payment of rent herein contained (although no formal or legal demand shall have been made therefor) or if the Lessee commits or suffers to occur any breach or default in the due and punctual observance and performance of any of the covenants obligations and provisions of this lease or of any Rules made hereunder or if the Lessee be a company an order is made or a resolution is effectively passed for the winding up of the Lessee (except for the purpose of reconstruction or amalgamation with the written consent of the Lessor which consent shall not be unreasonably withheld) or if the Lessee goes into liquidation or makes an assignment for the benefit of or enters into an arrangement or composition with its creditors or stops payment of or is unable to pay its debts within the meaning of any relevant Companies Act or ordinance or if execution is levied against the Lessee and not discharged within thirty (30) days or if the Lessee (being an individual) becomes bankrupt or commits an act of bankruptcy or brings his estate within the operation of any law relating to bankrupts then and in any one or more or either of such events the Lessor at any time or times thereafter shall have the right to re-enter into and upon the demised premises or any part thereof in the name of the whole to have again repossess and enjoy the same as its former estate anything herein contained to the contrary notwithstanding but without prejudice to any action or other remedy which the Lessor has or might or otherwise could have for arrears of rent or breaches of covenants or for damages as a result of any such event and thereupon the Lessor shall be freed from and discharged from any action suit claim or demand by or obligation to the Lessee under or by virtue of this Lease."

See *Shevill* ibid, 623-624.

83. For example, in *Shevill* supra n 56, the right to forfeit arose variously: on failure to pay rent; on the commission of any breach not remedied within thirty days of notice; or where the lessee (if a company) went into liquidation or there was an order for winding up.

84. *Austin and Another v United Dominion Corp Ltd* [1984] 2 NSWLR 612; *W & J Investments Ltd v Bunting and Another* [1984] 1 NSWLR 331; *Citicorp Australia Ltd v Hendry and Others* [1985] 4 NSWLR 1.

the injured party's loss. The act of termination does not cause the loss of bargain; in fact, it breaks the causal chain between the breach and the eventual loss of the bargain.[85] In *Shevill* Chief Justice Gibbs said:

> [I]t does not follow from the fact that the contract gave the respondent the right to terminate the contract that it conferred on it the right to recover damages as compensation for the loss it will sustain as a result of the failure of the lessee to pay the rent and observe the covenants for the rest of the term.[86]

It may also be argued that since the insertion of a termination clause is agreed upon by both parties, the promisor, by acquiescence, impliedly undertakes to pay loss of bargain damages upon such a clause taking effect. However, the High Court has indicated that it is not inclined to attach such a consequence to the existence of the right to terminate. It has also rejected the notion that predication of the right to terminate on certain covenants evidences the essential nature of those covenants: that is, the notion that the slightest breach of such covenants would constitute a loss of bargain. Both these contentions can be disposed of by Justice Wilson's suggestion in *Shevill*[87] that forfeiture clauses were included primarily to provide an avenue by which the landlord could be rid of an unwanted tenant. His Honour stated:

> It is one thing to be able to rid oneself of an unsatisfactory tenant; but it is quite another, requiring a clear expression of intention, to be able to hold the evicted tenant liable for whatever damages might be suffered as a result of the premature termination of the tenancy.[88]

85. *Cooden Engineering Co v Stanford* [1953] 1 QB 86 Jenkins LJ, 102 quoting the remarks of Salter J in *Elsey & Co Ltd v Hyde* (1926) unreported. The latter case is noted in C G Jones and R Proudfoot *Notes on Hire Purchase Law* 2nd edn (London: Butterworths, 1937) 107: "The reason that they have suffered is that they have [the leasehold] put on their hands before they have received very much money in respect of [it]. That is not the result of the [lessee's] breach of contract, in being late with his payments, it is the result of their own election to determine the [lease]."
86. Supra n 56, 627.
87. Ibid Wilson J, 636-637: "Some of those covenants cover matters of comparatively minor importance such as the maintenance of the lawns or of the painting of the premises. It is understandable that the parties should agree that the lessor should have a right to re-enter and forfeit the lease if the rent is not paid or the covenants not observed, but the intrinsic nature of the obligations in question lend no support to an inference of essentiality carrying in the event of default and termination a right to damages for the loss of the contract."
88. Ibid, 637.

Although the landlord is entitled to remove an unsatisfactory tenant, it would be "quite unjust"[89] for the landlord to recover loss of bargain damages as well, especially where the tenant may have been quite willing and able to perform the rest of the covenants but was only tardy in performance. The adoption of this view also discourages the lessor from terminating for any slight deviation from the lessee's obligations.

The High Court in *Tabali* confirmed that termination under an express contractual right does not automatically allow the recovery of loss of bargain damages. It also reinforced the link between recovery of loss of bargain damages and repudiation which was established in *Shevill*. In *Tabali*, the right to terminate the contract arose on two bases: repudiation and the forfeiture clause. Justice Deane applied the general rules of contract, saying that the "landlord was not obliged to elect between the two grounds for terminating the lease: it was entitled to rely upon them both."[90] On the question of damages, the court focused on the question of whether repudiation had been established and awarded damages on that basis. Justice Mason said:

> The well recognized distinction between common law rescission and termination pursuant to a contractual power supplies no reason in principle why such damages are recoverable by the innocent party in one case and not in the other, *provided of course that the exercise of the power is consequent upon a breach or default by the defendant which would attract an award for such damages.*[91] (emphasis added)

The view that the link between repudiation and prospective damages is not broken by termination via a proprietary measure is also evident in *Buchanan v Byrnes*,[92] where the recovery of post-termination damages was allowed for termination under a proprietary measure because repudiation had already been established and the damages flowed from this. This view also explains the remarks of Chief Justice Jackson in *Hughes v NLS Pty Ltd*:

89. Ibid Gibbs CJ, 628: "[I]t would require very clear words to bring about the result, which in some circumstances would be quite unjust, that whenever a lessor could exercise the right given by the clause to re-enter, he could also recover damages for the loss resulting from the failure of the lessee to carry out all the covenants of the lease - covenents which, in some cases, the lessee might have been both willing and able to perform had it not been for the re-entry."
90. Supra n 2, 55.
91. Ibid, 31.
92. (1906) 3 CLR 704.

> The damages sought here are for the lessee's repudiation and abandonment of the whole contract, and this occurred ... before any surrender of lease occurred.... It is for this breach of contract that the lessor sues. Until surrender, he can sue for rent as such; after surrender, he is limited to damages for loss of rent flowing from the lessee's breach of contract.[93]

In this case, the acceptance of surrender also constituted an acceptance of repudiation, thus allowing prospective damages, flowing from the latter, to be recovered. Since repudiation was thought not to be applicable to leases at the time the case was decided, the result could not be explained in these terms. It is submitted that a truer picture is presented when the word "surrender" is replaced with "termination" in the remarks above.

The statement by the High Court in *Shevill* that any loss of bargain damages recoverable upon termination under a contractual right requires "clear words",[94] combined with the fact that repudiation is not easily established or lightly inferred, has led to the suggestion[95] that a clause providing for a special sum of damages in the event of termination should be added to the lease. However, if this clause is activated by a breach, the rule against penalties becomes relevant. As such clauses survive termination, this topic will be discussed below.

2. Discharge and survival of contractual obligations

In general, terms which create primary contractual duties between the parties are discharged upon termination. However, not all contractual obligations are discharged: those which regulate the parties' rights and liabilities may survive. An agreed damages clause falls into this latter category as it is a term which purports to pre-estimate the amount of damages payable by the promisor for particular breaches of the contract. The function of such clauses is to avoid the problem of proving loss in a claim of damages, thus saving time and expense. In this way, it serves as a valuable device.[96]

However, the courts frown on the inclusion of agreed damages clauses which, instead of being genuine pre-estimates of loss, are included "by way of threat"[97] to the promisor as penalty clauses. Such

93. [1966] WAR 100, 102.
94. Supra n 56, 628.
95. D H Hodgson QC "Recent Cases" (1981) ALJ 349.
96. A S Burrows *Remedies for Torts and Breach of Contract* (London: Butterworths, 1987) 288.
97. This clause was inserted to intimidate the other party into performing its obligations.

clauses are unenforceable. In *Dunlop Pneumatic Tyre Co Ltd v New Garage & Motor Co Ltd*[98] Lord Dunedin set down several guidelines for determining whether a clause is a penalty.[99] These guidelines were added to by the High Court in *O'Dea and Others v Allstates Leasing System (WA) Pty Ltd and Others*.[100]

An agreed damages clause may state that a stipulated sum becomes payable on the breach of one or more covenants of varying importance. However, since the High Court's decisions in *Shevill* and *Tabali* to the effect that loss of bargain damages are only available for repudiation or breach of an essential term (condition) of a lease, such agreed damages clauses are especially liable to construction as penalty clauses. This is because the loss of bargain damages stipulated by such a clause would usually be greater than the sum which would arise from some of the breaches.[101] Accordingly, since *Shevill*, such agreed damages clauses

98. [1915] AC 79.
99. In summary:
    1. The description of a clause, by the parties, as a "penalty" or "liquidated damages" is not conclusive.
    2. The classification is to be made by reference to the circumstances existing at the time the contract was made.
    3. The sum is a penalty if it is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.
    4. There is a presumption that a clause is a penalty when a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious, and others but trifling, damage.
    5. A clause will be a penalty if the breach consists only in not paying a sum of money and the sum stipulated is greater than the sum which ought to have been paid.
100. (1983) 152 CLR 359. The High Court held an agreed damages clause to be a penalty for two reasons:
    (i) There was no rebate with regard to future rent;
    (ii) There was an absence of any provision for crediting the amount received by the lessor from the sale of the goods against the sum payable by the lessee which included the residual value at the end of the lease.
101. *Pigram v Attorney-General (NSW)* (1975) 132 CLR 216 Barwick CJ, 221. See also J W Carter and J Hill "Repudiation of Leases: Further Developments" [1986] The Conveyancer 262, 268: "[I]n cases where there *is* a repudiation ... the term will be a penalty because a term which is a penalty *vis-a-vis* one breach is a penalty in all cases." (emphasis added) Thus, the characterisation of an agreed damages clause as a penalty depends not on the facts of the case or the particular breach involved but on the form of the clause. In order to ensure that an agreed damages clause is enforceable, the drafter must be certain that the estimate of damages is appropriate to each breach which gives rise to it. The inclusion of more than one agreed damages clause is thus prudent and necessary.

require modification, specifically where the lessor is relying on a contractual right to terminate and when no repudiation is established or condition breached. Some modifications suggested by Professor Lang[102] include:

1. The right to re-enter and the accompanying right to loss of bargain damages should be confined to serious breaches of covenant only. Predication of this right on minor or "any" breaches may indicate that the sum is not a genuine pre-estimate, given the enormous range of losses which may arise from the different breaches. Lang suggests that the re-entry clause be modified in two ways: (a) the nature of the breach activating the power be confined to serious, persistent and continuing breaches; and (b) the power of re-entry be limited to specific covenants encompassing matters such as payment of rent, repair, user and assignment.

2. The following matters should be deleted as grounds for re-entry from standard re-entry clauses, being unfair or unnecessary for the protection of the lessor: (a) The lessee's winding up, bankruptcy, reconstruction, or arrangements with creditors; these are non-breaches and the lessor's rights, if affected by these events, may be protected on other bases - for example, a consequence of many of the events above will be the inability to pay rent and the lease can be terminated on that basis; and (b) the levying execution provision.

3. Portions of such clauses that preserve the lessor's other remedies should be deleted and the lessor's contractual remedies should be dealt with in separate clauses since these are different matters altogether.

If the changes proposed above are adopted, the only value of the agreed damages clause would be as a quantification of damages arising from repudiation only.[103] A clause incorporating Lang's modifications

102. A G Lang "Session 6: Enforcement, Remedies and Termination" in *Seminar on Drafting and Understanding Commercial Leases* (Sydney: NSW College of Law, 1987) 211, 219.

103. Because, although the clause may genuinely pre-estimate the damages, it would nevertheless be unenforceable by the law of penalty clauses: see text accompanying n 101.

would not allow the lessor to recover loss of bargain damages for termination under a contractual power upon a breach of contract not amounting to repudiation. The "serious breaches" to which Lang suggests the right of re-entry and recovery of loss of bargain damages be restricted, would have to be breaches amounting to repudiation because any lesser breach would only allow recovery of lesser damages and the sum stipulated would not be a genuine pre-estimate. This may lead the lessor to deem covenants which are not essential to be conditions so that a breach of any of them would amount to repudiation, thereby allowing loss of bargain damages to be recovered.[104] This course of action would be circular because the courts would once again be faced with a situation in which the damages claimed are not commensurate with the actual loss suffered by the plaintiff and the need to prove causation and remoteness in the assessment of damages would again be circumvented. Thus, although commendable, these changes do not bring about the desired effect since they do not allow the lessor to recover loss of bargain damages for termination under a contractual power upon a breach of contract not amounting to repudiation.

It is submitted that loss of bargain damages should be awarded only where there is repudiation. In all other cases, the actual loss must be proven before such damages may be recovered. Any agreed damages clause providing for the recovery of loss of bargain damages upon breaches which are not sufficiently serious to amount to repudiation should be struck down as a penalty clause, unless the claimant can show that there is a debt already existing before termination.[105] The courts are generally reluctant to construe the rental obligation as such a debt.

D. Mitigation of damages

Although the principle of mitigation of damages has been held not to be applicable to leases,[106] it has been argued that this position must

104. Carter and Hill supra n 101, 267.
105. See *IAC (Leasing) Ltd v Humphrey* (1972) 126 CLR 131.
106. *Maridakis v Kouvaris* supra n 1 was, until recently, the only case on this matter in Australia. In that case, Ward J held that there is no duty to mitigate with respect to leases. He relied on the remarks of Homer J in *Boyer v Warbey* (1953) 1 QB 234, 246-247: ibid, 199. However, in the recent case of *Vickers & Vickers v Stichtenoth Investments Pty Ltd* infra n 146, Bollen J has held that since *Tabali* supra n 2, *Maridakis v Kouvaris* is not good law and the principle of mitigation of damages does apply to leases.

be reconsidered, given the applicability of repudiation to leases.[107] Although this is desirable, it would be erroneous to think that acceptance of the mitigation principle depends on acceptance of the applicability of repudiation. The assessment of damages should be separated from the issue of termination;[108] mitigation is relevant to the former and not the latter. Mitigation issues may arise whenever damages are awarded. Thus, it is curious to note that although damages were recoverable for breach of covenant even before it was accepted that leases could be terminated by contractual principles, there was little critical consideration of the mitigation principle in the leasehold context, the general consensus merely being that the principle was inapplicable in the leasehold context.

The most common situation in which mitigation arises in the leasehold context is where the lessee is the wrongful party and the duty to mitigate would be on the lessor. Thus, the main reasons for denying a duty to mitigate arise in the context of a lessor's duty to mitigate and from the fact that the major form of mitigation available is the reletting of the premises. First, it was thought that once the leasehold is transferred, the lessee is, for that term, the owner of the premises and the lessor should not interfere in the lessee's place. However, the idea of lessee as owner is less persuasive given the extensive lessor participation after execution in modern leases.[109]

Secondly, it was argued that the lease was a personal relationship between lessor and lessee and that the lessor should not have a new lessee thrust upon him.[110] This objection may be answered by pointing to the duty to mitigate which applies in the context of employment contracts, which are equally personal.[111]

A third, more general, reason given was that the law ought not to protect the wrongdoer (lessee) and that a lessee, by his wrongful act, should not require the lessor to take positive action to protect his compensation.[112] This objection may be disposed of by saying that the

107. K Mackie "Repudiation of Leases" (1988) 62 ALJ 53, 63.
108. See infra 106, Section III.C.1.
109. See text at 92-93.
110. This argument was raised in *Wohl v Yeley* 161 NE 2d 339 (1959) and is noted in A J Bradbrook "The Application of the Principle of Mitigation of Damages to Landlord - Tenant Law" (1979) 8 Syd LR 15, 19.
111. *Brace v Calder and Others* [1895] 2 QB 253.
112. Bradbrook supra n 110, 18-19.

duty imposed on the lessor is no greater than that imposed on any injured party in the case of an ordinary contract.

The most important objection is the danger of unwittingly effecting a surrender of the lease by re-letting and making all post-surrender damages unavailable. This objection may be illustrated as follows. Where the lessee wrongfully abandons the premises before the expiration of the term of the lease, there are three courses open to the lessor:

(a) the lessor may accept the lessee's abandonment and retake possession of the premises for himself;
(b) the lessor may refuse to accept the lessee's abandonment and allow the lease to continue, collecting the rent as it accrues; or
(c) the lessor may attempt to re-let the premises in mitigation. [113]

In (a), a surrender takes place and the lessor is able to recover only the rent accrued as liquidated damages. In (b), there is no surrender and no mitigation of damages. In (c), the lessor may be construed as having accepted a surrender of the lease by re-letting even though it is in an attempt to mitigate damages.

Although this interpretation of (c) may be avoided if the lessor makes it clear that the re-letting is on the lessee's behalf, this rationalisaton encounters two problems. First, because surrender takes place "independently, and even in spite of, intention",[114] re-letting by the lessor, regardless of motive, may nevertheless be construed as a surrender. Secondly, the lessee has given no real authority for the lessor to re-let on the lessee's behalf. These problems may be partially overcome by acceptance of the proposition that if the lessor, before re-letting, notifies the lessee that the re-letting is on the lessee's behalf[115] and the lessee makes no objection, then no surrender is implied since the lessee can be taken to have agreed to the re-letting.

The other situation to be considered is where the lessor is the wrongful party and the duty to mitigate would be on the lessee. Here, the major form of mitigation is the sub-letting of the premises by the lessee. In this case, there is no danger of surrender and most of the above objections to re-letting do not apply, except the one regarding

113. Ibid.
114. *Lyon v Reed and Others* (1844) 153 ER 118.
115. Bradbrook supra n 110, 24.

the lease as a personal relationship. The main obstacle to this form of mitigation is inclusion in the lease of a covenant partially or absolutely restricting the tenant's ability to alienate the leasehold without the lessor's consent. The effect of this covenant is statutorily ameliorated in that such consent cannot be unreasonably refused,[116] since the covenant was inserted to protect the lessor from undesirable lessees. The lessor would be acting unreasonably in rejecting a sub-lessee who meets reasonable commercial standards of credit and reputation.

It is submitted, therefore, that the objections to mitigation by re-letting or sub-letting may be wholly or partially disposed of. There are valid reasons for a duty on the lessor (if not the lessee) to mitigate in a reasonable manner and such a duty should exist, despite the law laid down in *Maridakis v Kouvaris*.[117]

Mitigation of damages recoverable upon termination under repudiation may be contrasted with mitigation where there is no repudiation. Where there is no repudiation, the duty to mitigate only arises if the estate in land is not terminated. The main consideration in mitigation here, therefore, is to avoid the danger of inadvertently effecting surrender. There is no such danger in the context of repudiation as the estate is in any case terminated. Moreover, the recovery of damages under repudiation does not depend on keeping the estate in land "alive" but flows instead from the breach which constitutes the repudiation.

Problems regarding mitigation in the context of repudiation arise when the repudiation is not accepted. There are two opposite views on this issue: either, the injured party may hold the lease open and recover the agreed price on performing its obligations or, although the injured party has an election, it has a duty to mitigate by accepting the repudiation.

116. (WA) Property Law Act 1969 s 80(1).

117. Bradbrook supra n 110, 20-21: "[T]he public interest is not served by the present law, which tacitly encourages the landlord to keep an asset out of the economy by rewarding him for so doing. Other arguments relate to the problem of maintaining the physical condition of the property. The fact that the present law on surrender encourages landlords to neglect their property after abandonment increases the likelihood of damage through vandalism, accidental fire, deterioration in appearance and decline in value. In extreme cases, this may lead to the surrounding neighbourhood declining in desirability, resulting in a fall in local property values." This article by Bradbrook was cited with approval by Bollen J in *Vickers & Vickers v Stichtenoth Investments Pty Ltd* infra n 146, where his Honour held that the principle of mitigation applies to leases.

In *White and Carter (Councils) Ltd v McGregor*[118] ("*McGregor*") the House of Lords (by a three:two majority) adopted the first view. It is submitted, however, that the decision was based on the view that there is no duty to mitigate until there is a breach.[119] According to the inevitable breach theory, the breach arises only upon the acceptance of the repudiation. Thus, the duty to mitigate only arises subsequent to acceptance. Under the implied term/present breach theory, the duty to mitigate arises as soon as the repudiation occurs: that is, when the refusal to perform is made. Although the latter view appears to make the election to terminate illusory, this is not necessarily so, as an injured party is only obliged to do that which is reasonable in mitigation. Some guidance as to what is reasonable may be found in the remarks of Lord Reid in *McGregor*:

> [I]f it can be shown that a person has no legitimate interest, financial or otherwise, in performing the contract rather than claiming damages, he ought not to be allowed to saddle the other party with an additional burden with no benefit to himself.[120]

However, judging from the facts of that case, there appears to be little scope for application of the "no legitimate interest" qualification. The plaintiffs in that case would have been adequately compensated by damages and would have had nothing to gain by performing their obligations.[121] Nevertheless, they were allowed to claim the agreed price for performance of the contract.

Lord Denning in *Attica Sea Carriers Corporation v Poseidon Bulk Ferrostaal Reederei GmbH*[122] was critical of this decision and compared this situation with that of specific performance. His Lordship said:

118. [1962] AC 413.
119. See also *Anglo-African Shipping Co of New York Inc v J Mortner Ltd* [1962] 1 Lloyd's Rep 81.
120. Supra n 118, 431.
121. In that case, an advertising contract existed between the plaintiffs and the defendant by which the plaintiffs agreed to advertise the defendant's business on their litter bins for a period of 156 weeks. The defendant cancelled the contract. The plaintiffs, instead of claiming damages for breach, proceeded to carry out their obligations and then claimed payments from the defendant for the agreed price: see Burrows supra n 96, 279.
122. [1976] 1 Lloyd's Rep 250.

> [T]he plaintiff ought, in all reason, to accept the repudiation and sue for damages - provided that damages would provide an adequate remedy for any loss suffered by him. The reason is because, by suing for the money, the plaintiff is seeking to enforce specific performance of the contract - and he should not be allowed to do so when damages would be an adequate remedy.[123]

Thus, with regard to the duty to mitigate and as with specific performance, where damages are adequate, specific relief, including the action for an agreed sum, should not be granted.

In the leasehold context, factors which should be considered in assessing reasonableness in mitigation include whether the mitigating party has shown or offered to show the premises to prospective lessees and whether the mitigating party has advertised the premises in the appropriate medium. The courts may also look to the vacancy period between abandonment and re-letting as a factor in determining reasonable diligence.[124]

Thus, where the injured party can be adequately compensated by damages, so that it is of no real benefit for the injured party to perform the contract, that party's wish to perform should be outweighed by the sheer waste of doing so. Economic efficiency would dictate that the injured party mitigate by stopping performance rather than hold the contract open and claiming the agreed price.

123. Ibid, 255. Burrows supports Lord Denning's view that the *McGregor* approach runs counter to the traditional approach to specific performance: see Burrows supra n 96, 282.

124. G Weissenberger "The Landlord's Duty to Mitigate Damages on the Tenant's Abandonment: A Survey of Old Law and New Trends" (1980) 53 Temp LQ 1, 23.

IV. DOES REPUDIATION RENDER PROPRIETARY REMEDIES OTIOSE?

In 1925, Professor McCormick predicted that:

> [T]he law of landlord and tenant will be assimilated to the law of contracts generally. When the process is complete ... the old rules as to the effect of surrender by operation of law, forfeiture, ... will wholly disappear and will be supplanted by the principles governing the effect of repudiation, breach, and rescission of other contracts.[125]

However, the extent to which proprietary remedies, particularly forfeiture and surrender, are supplanted by repudiation depends on whether those remedies may be theoretically subsumed under contract law and whether there are any benefits offered by such remedies above and beyond those offered by repudiation which would ensure their survival in the future.

A. Forfeiture

There are three grounds upon which the right to forfeit may arise:[126]

1. Breach of condition;
2. Disclaimer; and
3. Breach of covenant where the lease contains a proviso for re-entry.

Forfeiture upon breach of condition can be regarded as an application of repudiation since both doctrines are grounded in the loss of a bargain. Forfeiture upon disclaimer can similarly be so regarded, since the lessee disclaiming is in effect saying "I am no longer your tenant", constituting a direct repudiation of the relation of lessor and lessee.

It is more difficult to assimilate forfeiture upon breach of a covenant not amounting to a condition (the third situation above) with the principle of repudiation. Nevertheless, the argument that this form of forfeiture can be regarded merely as an application of the principle of repudiation receives some support from Justice Owen in *Campbell v Payne and Fitzgerald*:

125. C T McCormick, "The Rights of the Landlord Upon Abandonment of the Premises by the Tenant" (1925) 23 Mich L Rev 211, 222.

126. Brooking and Chernov supra n 55, para 208.

> [A] right to forfeiture might arise if the tenant committed such a breach of covenant as to show that he was repudiating the contract, or it might arise, in the case of any breach of covenant, however trifling, if the parties had agreed that a breach of covenant should create a forfeiture. This was, of course, only an application of the general law of contract....[127]

The first method described by Justice Owen involves breach of a covenant (not amounting to a condition) by the lessee which shows that "he was repudiating the contract".[128] It follows that this method of forfeiture, by its description, may also be regarded as an application of repudiation where the breach involved constitutes a loss of the bargain. However, it must be recognised that not all breaches giving rise to the right to forfeit by this method will involve a loss of bargain and that only those rights to forfeit upon breaches constituting loss of bargain will qualify as repudiation. Rights to forfeit that arise only from the express terms of the contract and which do not amount to repudiation cannot be assimilated into the principle of repudiation.

There are several incidents of the general law of forfeiture which may stand in the way of assimilating those methods of forfeiture which could initially be considered as applications of repudiation. One of these is the statutory requirement that the lessor give notice and require the lessee to remedy the breach (upon a breach of a condition or covenant) before effecting termination.[129] There is no corresponding requirement under repudiation.

The reasons for this requirement of notice and the extent to which it may be dispensed with must be examined. The notice requirement appears to arise from the same source as that of relief against forfeiture. The courts generally treat the forfeiture power as security against default[130] and the lessee is given the opportunity to remedy any default on its part so as to preserve its interest. Such an opportunity may be denied if, in all the circumstances, it would be inequitable to grant the lessee the opportunity to remedy. For example, where a substantial amount of rent has not been paid over a long period and the lessee has shown a disregard for the premises.[131]

127. (1953) 53 SR(NSW) 537, 539.
128. Ibid.
129. (WA) Property Law Act 1969 s 81(1).
130. *Howard v Fanshawe* [1895] 2 Ch 581; *Gill and Another v Lewis and Another* [1956] 1 All ER 844.
131. *Tabali* supra n 2.

While it is agreed that upon a lessee's breach of a mere covenant, that lessee should be given the opportunity to rectify the default before the drastic step of forfeiture is taken, the same consideration ought not to be given to a lessee for breach of a condition because of the seriousness of such breach. This modification of the application of the requirement of notice would not constitute a radical change to the settled law and would not be contrary to the reason for the existence of the requirement. It would, however, remove another obstacle to the process of assimilating forfeiture on breach of condition to the principles of repudiation.

To exercise either the right to forfeit or the right to terminate for repudiation, unequivocal conduct evincing a wish to terminate is required. Because the right to forfeit is a contractual right, the steps necessary to exercise the right are determined by the terms of the lease and the terms of the lease must be complied with to terminate the tenancy. The right to forfeit most commonly appears in the form of a proviso for re-entry.[132] As noted previously, it has been established over the years that compliance here requires actual re-entry or its equivalent, an action for the recovery of the land.[133] If forfeiture under a proviso for re-entry is to be accepted as an application of repudiation, the suggestion that the lessor can exercise the right of re-entry *only* by actual re-entry or its equivalent must be set aside. They must be considered as merely two examples of the conduct required of the lessor to effect termination and not as the exclusive modes by which a lessor must exercise that right. The cogency of this view is strengthened when one considers that restrictions on the exercise of the right of re-entry appear to have emerged from historical circumstances rather than theoretical necessity.

If, however, principles of forfeiture may be regarded as an application of repudiation, then common law requirements will govern the exercise of the right to forfeit. The express terms of the lease governing this right would be irrelevant and the restrictions regarding re-entry inapplicable. Note, however, that these contractual requirements would still apply to forfeiture upon breach of a covenant not amounting to repudiation, which arises solely from the terms of the contract.

132. Brooking and Chernov supra n 55, para 218.
133. *Moore v Ullcoats Mining Co Ltd* supra n 69 and text accompanying n 69.

The fact that the right to forfeit on the breach of a covenant (not amounting to repudiation) cannot be assimilated into the common law right to terminate under repudiation means that this method of forfeiture will not be rendered superfluous by the acceptance of contractual principles as methods of terminating the lease. As Justice Wilson indicated in *Shevill*,[134] this method of forfeiture has a role to play in situations in which the lessor may wish to be rid of an unsatisfactory lessee who, although being unsatisfactory, has done nothing to repudiate the lease.

B. Surrender

There are two traditional categories of surrender:[135] express surrender and surrender by operation of law. In *Wood Factory*, however, Justice Priestley classified surrender as follows:

> [S]urrender, which can be by actual agreement between the parties; such surrenders can be express or by operation of law; there are also some surrenders by operation of law which are not the result of agreement between the parties.[136]

His Honour's division of surrender into consensual surrender and non-consensual surrender includes within consensual surrender not only express surrender but also some surrenders by operation of law.

Consensual express surrender results from an express agreement to terminate the lease whilst the agreement in consensual surrender by operation of law is implied from the circumstances. Because consensual surrender arises from agreement (express or implied) between the parties, no question of repudiation can arise. Under repudiation, the injured party does not agree to cancel the contract but is forced to do so by the refusal of the other party to perform his or her obligations.

Non-consensual surrenders by operation of law are based not on agreement but on estoppel:[137] that is, where one party does an act which is inconsistent with the continued existence of the lease and is thereafter estopped from denying the validity of the act.[138]

The traditional classification of surrender by operation of law may be reconciled with Justice Priestley's consensual/non-consensual divi-

134. Supra n 87 and 88.
135. *Woodfall* supra n 62, 810-875; Brooking and Chernov supra n 55, paras 180-188.
136. *Wood Factory* supra n 49, 120-121.
137. *Woodfall* supra n 62, 862-863; *Lyon v Reed and Others* supra n 114; *Bessell v Landsberg* (1845) 7 QBD 638.
138. Ibid.

sion. Traditionally, there are two main forms of surrender by operation of law: the grant of an interest by the landlord which is inconsistent with the existing lease; and the relinquishment of possession by the tenant.

The difference between consensual and non-consensual surrender by operation of law can be illustrated by reference to the landlord's granting of an interest. If the landlord grants a new lease to the *existing* tenant, the existing lease is surrendered consensually. Where, however, the landlord grants a lease to a *new* tenant without the consent of the existing tenant, then the existing lease is surrendered by non-consensual estoppel. Justice Priestley made a similar comparison in *Wood Factory* with regard to the relinquishment of possession by the tenant. His Honour said:

> 2. *Surrender by operation of law*: (a) Where this comes about by an agreement either manifested by or inferred from a giving up of possession by the tenant and immediate resumption of possession by the landlord, the position is the same as with surrender by express agreement. (b) ... where the tenant abandons the premises without agreement with the landlord, in circumstances manifesting his intention to put the lease to an end, and the landlord does not retake possession until some time later ...[139]

In situation (a), consensual surrender by operation of law occurs. However, if the remarks of his Honour suggest that the length of the delay between the abandonment of the premises and the repossession of them by the landlord is conclusive of the existence of an agreement to terminate, then it is submitted that this is erroneous because there may be an immediate resumption of possession even where the landlord has not agreed to the termination of the lease. The question of consent is one of intention as ascertained from the facts.

In considering situation (b), Justice Priestley pointed out that this may be further sub-divided:

> There are actually two varieties of [situation (b)]; one of which results in a surrender, and the other of which does not: (i) Where the landlord, in retaking possession does so on his own account.... Under the [*Tabali*] doctrine, upon the landlord taking possession on his own account the lease still comes to an end ... but the landlord is entitled to any damages suffered by loss of the lease. (ii) Where the landlord ... takes possession, not solely on his own account, but either on the tenant's account or for the benefit both of the tenant and himself. Then, so long as that position remains, the lease is not terminated, there is no surrender by operation of law and the tenant remains liable for the rent.[140]

139. Supra n 49, 133.
140. Ibid.

Note that in variety (i) of situation (b), where the landlord retakes possession, the termination can be described, post-*Tabali*, as "an example of surrender by operation of law *as well as a contractual termination following accepted repudiation*".[141] Prior to *Tabali*, surrender would have been the only possible interpretation of this situation. This led to problems with mitigation because, under any form of surrender, no post-termination damages were recoverable at all. Thus, landlords, preferring to recover the loss of the lease, tried to avoid effecting a surrender. This was the importance of variety (ii) of situation (b), where the landlord retakes on the tenant's account, for here, no surrender occurs and the landlord is able to recover post-abandonment damages for breaches of covenant. His Honour pointed out that as a result of *Tabali*, there is now no practical difference in result between the two varieties of situation (b) for the landlord, since repudiation gives rise to loss of bargain damages. The loss of bargain damages now recoverable under the surrender variety of situation (b) are substantially the same amount as the landlord would recover in the non-surrender variety of situation (b).[142]

It is therefore submitted that non-consensual surrender may be regarded as an application of repudiation. The two main forms of non-consensual surrender by operation of law[143] can both be seen as forms of repudiation as they both involve serious breaches. Further, the fact that no post-termination damages are available under surrender does not constitute an obstacle to the assimilation process. In both *Buchanan v Byrnes* and *Hughes v NLS Pty Ltd* post-termination damages were awarded even though surrender had taken place. This was because those damages flowed from the repudiation which had also occurred. The fact that the lease was also surrendered was merely incidental to the process of termination under repudiation.

141. Ibid (emphasis added).
142. Ibid, 133-134.
143. That is, where such surrender occurs by the lessor's grant of an inconsistent interest or by the lessee's relinquishment of possession.

V. CONCLUSION

The judges and commentators who have called for the emancipation of leases from their medieval fetters have been vindicated by the recent recognition of the contractual element of the lease. This recognition has involved, in the main, residential and commercial tenancies of urban land, as it is in these contexts that the contractual element has more prominently re-emerged. Thus, the shift away from a position of strict adherence to traditional property concepts has been motivated by two related reasons: the undeniably contractual nature of such leases and the injustice which would result from the application of traditional property rules to such leases. Although the proposition, that contractual principles are not applicable to what is essentially a contractual device, is theoretically absurd, the real impetus prompting the shift away from the application of traditional property rules has been the spectre of injustice: specifically, injustice to the modern lessee.

Property law has historically favoured the lessor and the lessee has been offered little protection regarding living conditions and the provision of services. This lack of protection was based on the fact that, historically, agrarian lessees needed no such protection. As social conditions have changed the uses of leases have adapted to these changes and the need for protection for the lessee has gradually emerged. The lot of the lessee has been considerably improved by the acceptance of the doctrine of repudiation in the leasehold context. Two important benefits have accrued to the lessee: the immediate right to terminate and the recovery of loss of bargain damages.

However, it is curious to note that whilst it was the injustice done to lessees which originally prompted the recent developments in the law of leases, such developments have primarily benefitted lessors rather than lessees.[144] There are further areas concerning lessees which may be rectified by the general application of contractual principles, for although the recent developments represent a significant break with traditional landlord and tenant law, they are only the first step in a process of updating and reforming the law of leases in keeping with current practices and requirements.

144. For example, *Shevill* supra n 56; *Tabali* supra n 2; *Ripka Pty Ltd v Maggiore Bakeries Pty Ltd* [1984] VR 629.

For instance, while the lease is no longer thought of as merely a conveyance, the covenants of the lease are still considered to be independent obligations. An implication of the interdependency of such covenant obligations would make available further remedies in situations where there is no loss of bargain. Thus, if the lessor failed to provide a service (such inaction not amounting to repudiation), the lessee could withhold rent to induce the lessor to perform its obligations. This may often be a more effective remedy than recourse to the courts, avoiding the expense and inconvenience of litigation. The application of the doctrine of unconscionability would also offer relief in an area where unequal bargaining positions have been prevalent.[145]

It remains to be seen whether and to what extent the courts will pursue these opportunities to assimilate contract law with property law. It is clear, nevertheless, that a solid base has been provided by developments up to this point, from which lessees (and lessors) may expand their armouries of contractual rights.[146]

145. For further possibilities of judicial law reform in this area see A J Bradbrook "The Role of the Judiciary in Reforming Landlord and Tenant Law" (1976) 10 MULR 459.

146. Since this paper was written, developments have occured which could not be incorporated into the body of the text due to time and publication constraints. Further cases illustrating the repudiation of leases include: *Nai Pty Ltd v Hassoun Nominees Pty Ltd* [1985-1986] ANZ Conv R 349; *J & C Reid Pty Ltd v Abau Holdings Pty Ltd* [1989] ANZ Conv R 45; *Nangus Pty Ltd v Charles Donovan Pty Ltd (in liq)* [1989] VR 184. The High Court's consideration in *Foran v Wight* (1989) 64 ALJR 1 of anticipatory breach and the function of estoppel in the context of executory real estate contracts has important implications for the development of both contract and real property law in Australia. Finally, Bollen J in *Vickers & Vickers v Stichtenoth Investments Pty Ltd* (1989) 52 SASR 90, 100 applied Deane J's comments in *Tabali* supra n 2, 52-53 in holding that "all ordinary principles of contract law", and in particular the principle of mitigation of damages, apply to leases.
See also A J Bradbrook and C E Croft *Commercial Tenancy Law in Australia* (Sydney: Butterworths, 1990) 228-263.