IN THE COURT OF APPEAL OF NEW ZEALAND

I TE KŌTI PĪRA O AOTEAROA

CA35/2018
[2018] NZCA 240

BETWEEN	OMV NEW ZEALAND LIMITED Appellant
AND	PRECINCT PROPERTIES HOLDINGS LIMITED Respondent

Hearing:	24 May 2018
Court:	French, Ellis and Woolford JJ
Counsel:	A M Stevens and E P P Maclaurin for Appellant R J Gordon and N J G Smith for Respondent
Judgment:	6 July 2018 at 10 am

JUDGMENT OF THE COURT

A The appeal is dismissed.

B Costs are to be fixed in accordance with [35] of this judgment.

REASONS OF THE COURT

(Given by Ellis J)

[1] Precinct Properties Holdings Ltd (Precinct) is the owner of Deloitte House, in Wellington. Since 2009, Precinct has leased the ninth and tenth floors to OMV New Zealand Ltd (OMV).

[2] The building was damaged in the 2016 Kaikōura earthquake. OMV says the damage has rendered it untenantable, and the lease has automatically terminated.

Precinct denies that and has claimed for unpaid rent, seeking summary judgment in the High Court.

[3] OMV now appeals a decision of Associate Judge Smith denying its application for a stay of the High Court proceedings.[1] A stay would have the effect of halting the progress of Precinct's application for summary judgment pending reference of the wider dispute between the parties to arbitration. Leave to appeal was granted by the High Court.[2]

[4] In the event that OMV's appeal is allowed, there is a subsidiary issue as to whether it has submitted to the jurisdiction of the High Court.[3]

Background

[5] The lease began in 2009 and was renewed in both 2012 and 2015. It was due to expire on 30 November 2020. The lease is in the standard ADLS form.

[6] The Kaikōura earthquake hit on 14 November 2016. The building was damaged and was closed on 17 November 2016 until further notice. Following the earthquake, Precinct excluded OMV and other commercial tenants from the premises until at least 13 March 2017. On 20 March 2017 written engineering clearance supporting resumption of occupation was received.

[7] Prior to that, on 2 February 2017, OMV gave notice that, due to the earthquake damage, the premises were untenantable and termination had been triggered in accordance with cl 26(a) of the lease, which provides:

> **26. Total Destruction**
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> **IF** the premises or any portion of the building of which the premises may form part shall be destroyed or so damaged:
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> (a) as to render the premises untenantable then the term shall at once terminate or…

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1 *Precinct Properties Holdings Ltd v OMV New Zealand Ltd* [2017] NZHC 2926 [HC decision].
2 *Precinct Properties Holdings Ltd v OMV New Zealand Ltd* [2017] NZHC 3230.
3 We also record that an application to adduce further evidence about the hearing in the High Court was withdrawn because it was rendered unnecessary by the provision of a transcript.

[8] Precinct did not accept cl 26(a) had been engaged. On 8 June 2017, Precinct filed a statement of claim together with an application for summary judgment in the High Court. The claim referred to OMV's non-payment of rent and sought a declaration that the property was not untenantable. Precinct later filed an amended statement of claim and an amended summary judgment application in which Precinct directly claimed a total of $258,243.36 for unpaid rent said to have been due on 13 March, 1 April, 1 May, 1 June and 1 July 2017. Credit was given for the compulsory closure of the premises prior to 13 March 2017. Costs on an indemnity basis were sought in accordance with the terms of the lease.

[9] OMV's position has always been that the issue of untenantability, together with further complaints it has which are said to justify the cancellation of the lease (including alleged misrepresentations by Precinct as to the earthquake rating of the building) must be referred to arbitration under cl 44.1 before Precinct can progress its summary judgment application. Clause 44 is headed "Arbitration" and materially provides:[4]

> 44.1. UNLESS any dispute or difference is resolved by mediation or other agreement, the same shall be submitted to arbitration of one arbitrator who shall conduct the arbitral proceedings in accordance with the Arbitration Act 1996 and any amendment thereof or any other statutory provision relating to arbitration.
>
> …
>
> 44.3. THE procedures prescribed in this clause shall not prevent the Landlord from taking proceedings for the recovery of rent or other monies payable hereunder which remains unpaid or from exercising the rights and remedies in the event of such default prescribed in clauses 28 and 29 hereof.[5]

[10] When OMV filed documents in response to the High Court proceedings it expressly did so under protest to jurisdiction. More specifically, OMV applied for a stay of the summary judgment proceedings and referral of the dispute to arbitration.

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4 Clause 44.2 deals with the process for selecting an arbitrator.

5 Clauses 28 and 29 relate to the landlord's rights of distraint and re-entry for non-payment of rent.

Associate Judge Smith's judgment

[11] Associate Judge Smith denied the application for stay and refused to refer the claim to arbitration. He held that:

(a) cl 44.3 applies regardless of whether the landlord's claim for rent is disputed by the tenant;[6]

(b) a construction limiting cl 44.3 to circumstances where there is no bona fide defence for the tenant would "unjustifiably water down the intended effect of cl 44.3";[7] and

(c) staying the claim for rent while the other matters raised by OMV are referred to arbitration would undermine the intention behind cl 44.3.[8]

[12] The Associate Judge also distinguished the circumstances of the present case from those in *Hi-Tech Investments Ltd v World Aviation Systems (Australia) Pty Ltd* on the ground that in that case there was a dispute about the quantification of the rent said to be owing.[9] The Associate Judge accepted that so long as the lessor is pursuing recovery for rent or other monies identified in the lease as being payable by the tenant, the lessor's claim may be brought in court.[10]

[13] Precinct's application for summary judgment was then scheduled for 4 December 2017, but has been adjourned pending the outcome of this appeal.[11]

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6 HC decision, above n 1, at [36].
7 At [37].
8 At [37].
9 At [39]; citing *Hi-Tech Investments Ltd v World Aviation Systems (Australia) Pty Ltd* HC Auckland CIV-2006-404-3579, 13 October 2006. The tenant had accepted that the result of a rent review was an increase in the rent payable but disputed the landlord's ability to demand further increases six weeks and six months later after the initial review.
10 At [45].
11 *Precinct Properties v OMV New Zealand Ltd* HC Wellington CIV-2017-485-476, 4 December 2017 (Minute).

Grounds of appeal

[14] OMV challenges the Associate Judge's decision on the grounds that he:

(a) failed to give sufficient effect to cl 44.1 and art 8(1) of the first schedule to the Arbitration Act 1996;

(b) wrongly applied cl 44.3 notwithstanding that it does not override the mandatory arbitration cl 44.1; and

(c) failed to apply the approach adopted in *Hi-Tech Investments* and (wrongly) preferred the approach in *Drake City Ltd v Tasman-Jones.*[12]

[15] Alternatively if the Court does have jurisdiction, OMV submits that the Associate Judge erred in suggesting the "pay now, argue later" principle applies to preclude OMV from contending that the lease does not remain in force and that no rent is therefore "payable".

Ancillary issue — jurisdiction

[16] On 2 February 2018, Precinct filed a memorandum indicating its intention to support the decision of Associate Judge Smith on other grounds, relying on r 33 of the Court of Appeal (Civil) Rules 2005. If necessary, Precinct wishes to argue that by filing its substantive opposition to the summary judgment application, OMV submitted to the jurisdiction of the High Court.[13]

[17] OMV's position on that issue is that Associate Judge Smith has twice ruled that there has been no such submission to jurisdiction and that, absent an appeal, those rulings cannot now be contested by a side wind.[14]

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12 *Drake City Ltd v Tasman-Jones* [2016] NZHC 899.

13 This ground was pleaded by Precinct in its notice of opposition dated 22 August 2017 but was not referred to by Associate Judge Smith in his judgment denying the stay application.

14 Those rulings are said to be: *Precinct Properties Holdings Ltd v OMV New Zealand Ltd* HC Wellington CIV-2017-485-476, 1 August 2017 (Minute) at [2] and [7(h)]; and *Precinct Properties Holdings Ltd v OMV New Zealand Ltd* HC Wellington CIV-2017-485-476, 26 September 2017 (Minute) at [7].

[18] On 19 March 2018, Cooper J issued a minute indicating that this issue could be dealt with at the hearing of the substantive appeal.

Discussion

[19] OMV says the dispute about whether the premises were untenantable is properly captured by cl 44.1, and must be determined by arbitration before the determination of a claim for rent under cl 44.3. Mr Stevens, counsel for OMV, effectively submits that the words "monies payable hereunder" in cl 44.3 mean that the clause could not operate if there was a dispute about whether the rent was payable at all (as there is here). He also calls in aid the Supreme Court's observations in *Zurich Australian Insurance Ltd v Cognition Education Ltd* about the operation of art 8(1) of the first schedule to the Arbitration Act. Article 8(1) provides:

> A court before which proceedings are brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting that party's first statement on the substance of the dispute, stay those proceedings and refer the parties to arbitration unless it finds that the agreement is null and void, inoperative, or incapable of being performed, or that there is not in fact any dispute between the parties with regard to the matters agreed to be referred.

[20] And in *Zurich*, the Supreme Court observed:[15]

> Under art 8(1), a stay must be granted unless the court finds that the arbitration agreement is null and void, inoperative or incapable of being performed or it is immediately demonstrable either that the defendant is not acting bona fide in asserting that there is a dispute or that there is, in reality, no dispute. It follows from this that an application for summary judgment and an application for a stay to permit an arbitration to take place are not different sides of the same coin. In principle, the stay application should be determined first and only if that is rejected should the application for summary judgment be considered.

[21] We have little hesitation in rejecting that submission. The "arbitration agreement" here must be seen as cl 44 as a whole. It expressly carves out rent disputes. The more absolutist premise of art 8(1) (and of Mr Stevens' submissions) is predicated on there being no such exception. The only issue is whether the cl 44.3 exception applies here.

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[15] *Zurich Australian Insurance Ltd v Cognition Education Ltd* [2014] NZSC 188, [2015] 1 NZLR 383 at [52].

[22] And as to that issue, the purpose of cl 44.3 seems to us to be quite clear. It is a reflection of the primacy that leases generally place on the covenant to pay rent.[16] That primacy is reflected elsewhere in the lease, for example in cl 31, which provides:

> **Essentiality of Payments**
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> 31.1. **FAILURE** to pay rent or other moneys payable hereunder on the due date shall be a breach going to the essence of the Tenant's obligations under the Lease. The Tenant shall compensate the Landlord and the Landlord shall be entitled to recover damages from the Tenant for such breach. Such entitlement shall subsist notwithstanding any determination of the lease and shall be in addition to any other right or remedy which the Landlord may have.
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> 31.2. **THE** acceptance by the Landlord of arrears of rent or other moneys shall not constitute a waiver of the essentiality of the Tenant's continuing obligation to pay rent and other moneys.

[23] Similarly, the lease in its original form made it clear (in cl 1.1) that the agreed rent was payable "without any deductions". Later iterations contained express "no set-off" clauses.

[24] Nor are we able to accept that cl 44.3 operates only where there is, in effect, no dispute as to the rent that is owing. As Mr Stevens seemed to acknowledge, on that analysis cl 44.3 would only permit recourse to the courts where a tenant accepts that rent is owing but, for whatever reason, is unable to pay. In other words, its sole purpose would be to permit a lessor to obtain default judgment against an impecunious lessee.

[25] In the end, we need only record our agreement with Venning J's conclusion in *Drake City* that cl 44.3 operates as an exception to cl 44.1 and permits claims for unpaid rent to be litigated.[17] As he said:[18]

> [24] The effect of the relevant provisions of the lease, particularly cl 44.3, is to preserve Drake's right as landlord to take separate legal proceedings for the recovery of *any rent* or other monies *payable under the lease*. That is what the parties expressly agreed to. In terms of the Supreme Court test in *Zurich*

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16 Unlike the position in contract law generally where obligations are interdependent, a tenant's obligation to pay rent is generally independent of the landlord's obligations under the lease: *Chatfield v Elmstone Resthouse Ltd* [1975] 2 NZLR 269 (SC) at 275.

17 In *Drake City*, the tenant's guarantors raised various misrepresentation arguments, together with an alleged breach of the quiet enjoyment covenant in the lease, in order to avoid liability for paying rent. As here, the claim was that the rent recovery proceedings should be stayed pending arbitration of those issues.

18 *Drake City*, above n 12, (emphasis added).

> there is no dispute to refer to arbitration concerning Drake's claim for rent and outgoings.
>
> [25] The defendants' claims of misrepresentation and breach of cl 32.1 are opposed and are currently unqualified. They are properly disputes which should be referred to arbitration in terms of cl 44.1. However, the fact those disputes should go to arbitration does not prevent Drake from taking these separate proceedings to recover rent and outgoings. The parties agreed that Drake was not prevented from doing so despite the reference to arbitration of other disputes under the lease. The commercial reason for such a clause is obvious. It is the same reason parties provide for no set-off clauses in relation to rent in leases.
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> [26] Indeed cl 1.1 of the lease in this case confirms that there is no right of set-off in relation to the disputes that the defendants now seek to rely on, at least as against the claim for rent ... For present purposes, the effect of cl 44.3 remains that Drake may pursue these proceedings and its application for summary judgment for rent and outgoings.

[26] As far as the "pay now argue later" point is concerned, what Associate Judge Smith said was this:

> [34] I think the commercial purpose of cl 44.3 was that stated by Venning J in *Drake City,* namely to reflect the "pay now, argue later" intention of a typical "no set-off, no deductions" clause. In leases containing such clauses the landlord's cashflow is protected by the continued payment of rent while the disputed issue is being arbitrated (or litigated if there is no arbitration clause in the lease).

[27] We are unable to interpret this passage as meaning anything other than what it says, namely that cl 44.3 is consistent with the fact that the lease requires rent to be paid regardless of the existence of any arguable set-off. That proposition appears to us to be wholly uncontroversial. Contrary to Mr Stevens' submission, OMV may still contend that the lease has been terminated as a defence to Precinct's claim for unpaid rent. The pleading of such a defence does not amount to a pleading of "deduction or set-off".

[28] Lastly, in light of our conclusion, all we propose to say about the decision in *Hi-Tech Investments*, is that its facts appear to be distinguishable from those in both *Drake City* and the present case. There is, we think, a material difference between a contested claim for an otherwise undisputed amount (as here) and a claim for a disputed amount (as there). More specifically, the summary recovery process contemplated by cl 44.3 is poorly suited to resolving what Associate Judge Abbott

regarded in *High-Tech Investments* as a challenge to the rent review mechanism itself.[19]

Conclusion

[29] In summary, cl 44.3 operates as an exception to cl 44.1 and permits claims for unpaid rent to be litigated. To the extent that a tenant believes it has a defence to such a claim (by which we mean a defence that some or all of the rent is not payable, for reasons other than the existence of a cross-claim in the nature of a set-off) that defence can be pleaded and ventilated in the context of such litigation. But claims for set-off and counter-claims relating to alleged breaches of the lease or misrepresentations by the landlord would not, in our view, qualify. Those are properly matters for arbitration under cl 44.1.

[30] In light of our conclusion on OMV's appeal it is not necessary to consider the question of whether OMV has submitted to the High Court's jurisdiction.

Costs

[31] As noted earlier, the lease specifically deals with the issue of costs. More specifically, cl 6 provides:

> **EACH** party shall pay their own solicitors costs of and incidental to the preparation of this lease however the Tenant shall pay the Landlord's solicitors costs of and incidental to the preparation of any variation or renewal of Lease or any Deed recording a rent review and the stamp duty payable, and the Landlord's legal costs (as between solicitor and client) of and incidental to the enforcement or attempted enforcement of the Landlord's rights remedies and powers under this lease.

[32] In the High Court, Associate Judge Smith noted OMV's contention that cl 6 should not be applied but in the end simply reserved costs pending the outcome of the summary judgment application.[20]

[33] Mr Stevens does not attempt to argue that, on its face, cl 6 would not apply to costs incurred in pursuit of the present matters. Rather, he asks us to exercise our

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19 *High-Tech Investments*, above n 9, at [22]–[23].
20 HC decision, above n 1, at [49].

discretion to decline to make an indemnity costs award under cl 6 on the grounds that costs on that basis would include costs that were not reasonably incurred and for steps taken that were not reasonably necessary. More particularly, Mr Stevens submits the appeal had been rendered unnecessarily complex (and costly) by Precinct:

(a) initially pursuing declaratory relief in the High Court (with no claim made for rent);

(b) amending the proceedings "mid-stream" to include a claim for rent;

(c) seeking to proceed with a summary judgment hearing, rather than resolving the stay/arbitration application first;

(d) requiring the inclusion of all of the material from the High Court proceedings in the Case on Appeal, when most of that material was irrelevant; and

(e) retrospectively raising the issue of OMV's submission to jurisdiction, under r 33.

[34] We accept the validity of only the last of these points. We agree that the submission to jurisdiction argument was without merit. OMV had always made it clear that its engagement with the issues in the High Court was without prejudice to the jurisdictional point. The Associate Judge made it quite clear he accepted that in two minutes.[21] But as for the other matters:

(a) we are unable to see any significant connection between (a)–(c) and the reasonableness of the costs incurred in this appeal;

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[21] See above n 14.

(b) but in any event:

(i) the original statement of claim was clearly underpinned by a claim for rent; it made it clear that the declaration was sought in order to establish that OMV had no defence to such a claim;

(ii) the stay application was resolved first, albeit in the context of the summary judgment proceedings; and

(c) at least some of the material to which objection was taken in the Case on Appeal was referred to by OMV during the hearing of the appeal. OMV's position that it was not relevant was predicated on its position that it was right about the interpretation of cl 44.1 and 44.3. We have found that to be incorrect.

[35] We consider that Precinct is entitled to indemnity costs under cl 6 in successfully opposing OMV's appeal but recovery should be reduced to 80 per cent of Precinct's costs to reflect the position it takes on the jurisdiction issue. Precinct is to file and serve a memorandum as to the costs incurred on an indemnity basis within 10 working days of delivery of this judgment. OMV will have 10 working days thereafter to file and serve a memorandum in response.

[36] We record that Mr Gordon for Precinct does not ask us to certify for second counsel and so we do not do so.

Result

[37] For the reasons we have given, the appeal is dismissed.

[38] Costs are to be fixed in accordance with [35] above.

Solicitors:
Izard Weston, Wellington for Appellant
MinterEllisonRuddWatts, Wellington for Respondent