

# **PLA BIRMINGHAM EVENT**

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## Speakers

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Details of the presenters CV's can be found online at [www.wilberforce.co.uk](http://www.wilberforce.co.uk)

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# Tenant default

## A review of the remedies available to a landlord by Julian Greenhill

### Introduction

1. The purpose of this talk is to:
  - (i) bring together in summary the main methods by which a landlord can seek to enforce obligations contained in a lease in the event that the tenant defaults in performing those obligations *during the term of the lease*;
  - (ii) identify some of the considerations that are relevant to determining which remedy or remedies to pursue in a given case.
2. So, the situation under consideration is that the tenant has breached a covenant contained in a lease during the term of the lease. What options are available to the landlord?

### Option 1 - Bring a money claim

3. The landlord can seek a payment of money from the tenant. A claim against the tenant for payment of a sum of money can be either a claim for a debt or for damages, depending upon the obligation that has been breached.

### Debt claim

4. A debt claim is available where the sum in question is fixed by the terms of the lease. The most obvious example is a claim for arrears of rent. But often there are other sums due under a lease which are fixed in such a way as to be a debt due to the landlord. For example, sums reserved as rent such as insurance premiums paid by the landlord, or service charges will usually be due as a debt. Equally, the landlord has a claim in debt when he has entered onto premises and carried out work to remedy a disrepair where the lease reserves to the landlord a right to do so<sup>1</sup>.
5. A debt claim, if it is available, has distinct advantages over a claim for damages. The various rules applicable to a claim in damages (the need to prove loss and causation, and to satisfy requirements as to remoteness and the duty to mitigate) do not apply to a debt claim<sup>2</sup>. And, chiefly for that reason, a debt claim may be readily susceptible to summary judgment under CPR Part 24. So a landlord may be able to obtain judgment against a defaulting tenant in a relatively short space of time on a debt claim.

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<sup>1</sup> Jervis v Harris [1996] Ch 195

<sup>2</sup> For example in the case of mitigation see White and Carter (Councils) Limited v MacGregor [1962] AC 413

## Damages

6. A claim for damages during the term raises more complex considerations. There are a number of points to bear in mind before concluding that a claim for damages is the best route to addressing the default of a tenant during the term.
7. Three points in particular need to be borne in mind in relation to most claims for damages during the term of the lease:
  - a. Such a claim won't usually change anything on the ground. It does not actually get the covenant performed. So if the landlord's primary concern is the actual act or omission constituting the breach, bringing a claim for damages may afford the landlord little comfort.
  - b. The measure of damages due on such a claim may be hard to assess and small. Often it will simply be the diminution in the value of the reversion subject to the lease which may be a small amount, particularly if there is still quite a long time left to run on the term of the lease. This is because the valuation assumes the reversion is to be valued subject to the lease and so takes account of the right of the landlord to enforce the covenants in the lease.
  - c. All the rules in relation to damages claims generally will apply – it is necessary to prove causation, loss, remoteness, and there will be a duty to mitigate<sup>3</sup>.
8. Take the specific example of the tenant failing to perform its obligations under a covenant to keep the premises in repair. During the term a claim for damages is rarely the best remedy for disrepair due to:
  - a. the application of the Leasehold Property (Repairs) Act 1938. The 1938 Act limits the entitlement of a landlord to sue for damages or enforce forfeiture in the case of a lease granted for a term of not less than seven years which has at least three years unexpired at the relevant time. The regime of the 1938 Act is as follows:
    - i) the landlord may neither sue nor forfeit unless he first serves a notice under s146 of the Law of Property Act 1925 on the tenant informing the tenant of his right to serve a counter-notice under the 1938 Act<sup>4</sup>;
    - ii) within 28 days the tenant can serve a counter-notice the result of which is that the landlord cannot bring further proceedings without the leave of the Court<sup>5</sup>;
    - iii) leave will only be given where the landlord can prove on the balance of probabilities that the immediate remedying of the breach is necessary in order to save him from substantial loss or damage by meeting one of five specific grounds set out in the Act<sup>6</sup>; and

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<sup>3</sup> *Luminar Leisure v Apostole* [2001] 3 EGLR 23

<sup>4</sup> s1(2), (4)

<sup>5</sup> s1(3)

<sup>6</sup> s1(5) and *Landmaster v Thackery* [2003] 2 EGLR 30

- iv) the court may impose such conditions as it thinks fit<sup>7</sup>.
  - b. the fact that damages for disrepair during the term are limited at common law to the diminution in the value of the reversion<sup>8</sup>; and
  - c. such a claim does not have the effect of getting the repair work actually done.
9. So in the case of disrepair, forfeiture or carrying out the works pursuant to a clause in the lease which permits the landlord to enter onto the premises and remedy the disrepair himself (which gives rise to a debt claim for the monies expended<sup>9</sup>) is likely to be more useful.
10. Nevertheless a claim for damages during the term may be substantial, particularly if the term is nearing its end and the tenant does not enjoy security of tenure with the result that the lease will fall in soon with the covenant breached.
11. In addition, a number of recent cases in the law of damages in contract suggest that the Courts may be more willing to allow a claimant to deprive a defendant of profits made out of a breach of contract. In a case for breach of a restrictive covenant damages can be assessed by reference to a share of the profit made by the covenantor from the breach, that being the price of a hypothetical release of the covenant, regardless of whether injunctive relief is also sought or is even available. But this will only be appropriate if the case is an “exceptional” one in which such a measure is “a just response” to the breach in question<sup>10</sup>. What might constitute such an exceptional case is not easy to say, but an example in a landlord and tenant context might be provided by the breach of an absolute covenant against sub-letting which enabled a tenant to extract a far greater revenue from the land than he was paying to his landlord, by virtue of a new use which the parties did not contemplate at the date of the lease<sup>11</sup>.
12. Furthermore, in the case of a money claim, the landlord may have other persons on whom it can turn to seek relief in respect of a tenant default such as a surety or former tenant. In particular in the case of lease entered into prior to 1 January 1996 (“old leases”) under the old common law rule the original tenant will remain liable on the covenants in the lease throughout the term, though the Landlord and Tenant (Covenants) Act 1995 confers certain protection on a former tenant by requiring, for example, that the landlord give notice in accordance with s17 of the 1995 Act as a precondition to suing in certain cases.
13. These points notwithstanding, often late or non-payment or non-performance is a sign of a deeper malaise in the tenant, of an inability to fulfil its obligations generally. If the tenant persistently fails to meet its obligations the landlord is faced with the unwelcome and onerous prospect of having to bring repeated actions for debt or damages. And none of this is of much use if, absent a substantial surety, you fear that the tenant is impecunious and may not have the money or assets against which to enforce a judgment.

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<sup>7</sup> s1(6)

<sup>8</sup> *Crewe Services and Investment Corporation v Silk* [1998] 2 EGLR 1

<sup>9</sup> *Jervis v Harris* [1996] Ch 195

<sup>10</sup> *Wrotham Park Estate v Parkside Homes* [1974] 1 WLR 798; *World Wide Fund for Nature v World Wrestling Federation* [2008] 1 WLR 445

<sup>11</sup> I am grateful to Daniel Hochberg for a valuable discussion on this point.

## Option 2 – terminate the lease by forfeiture

14. The most obvious alternative is to seek to terminate the lease altogether by forfeiture.

15. Forfeiture of the lease requires that, in addition to there being a breach of covenant:

- a. There is an express proviso for forfeiture contained in the lease (If there is no such express proviso then the landlord will only obtain an option to forfeit the lease for breach of a “condition” contained within it, in other words an obligation on the part of the tenant which, either expressly or by necessary implication, is an obligation upon the performance of which the survival of the lease is made conditional<sup>12</sup>. Timely payment of rent will not usually be a condition of the lease in this sense.
- b. The landlord must not have waived the right to forfeit for the breach in question. Waiver occurs where the landlord, with knowledge of the breach and before electing to forfeit, does some act which, objectively considered, unequivocally recognises the continued existence of the lease. The classic case of waiver arises where the landlord demands<sup>13</sup>, accepts or sues for rent falling due after the breach of covenant giving rise to the right to forfeit (though there is no waiver in suing for rent which fell due prior to the breach<sup>14</sup>).
- c. Because the test is objective, waiver can occur by accident or unintentionally<sup>15</sup>. In one recent case it was held that the right of a tenant to appropriate payment to a particular debt means that, if a landlord accepts payment towards outstanding rent arrear he is bound by the tenant’s appropriation, even if that means the debt is thereby appropriated to a debt arising after the right to forfeit resulting in a waiver<sup>16</sup>. If forfeiture is an option a landlord might want to pursue it is essential to make sure that rent accruing due after the right to forfeit has arisen is not demanded or accepted by the landlord. Particularly in a large corporate landlord, this will require immediate and careful management of the different persons or departments at the landlord who are responsible for carrying out the landlord’s various functions under the lease. All too often the person responsible for rent collection on behalf of the landlord is not told soon enough to reject the next payment of rent and a waiver occurs.
- d. In cases of non-payment of rent, unless the requirement is expressly excluded by the proviso, the landlord must also have formally demanded the rent.
- e. In cases other than non-payment of rent, the landlord must have served a notice under s146 of the Law of Property Act 1925:

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<sup>12</sup> Doe d Lockwood v Clarke (1807) 8 East 185

<sup>13</sup> A demand for rent has been held at first instance to have the same effect as an acceptance, but the point was left open by the Court of Appeal recently in Greenwood Reversions v World Environmental foundation [2009] L&TR 2.

<sup>14</sup> In re A Debtor [1995] 1 WLR 1127

<sup>15</sup> John Lewis Plc v Viscount Chelsea (1993) 67 P&CR 120; Seahive Investments v Osibanjo [2009] L&TR 16

<sup>16</sup> Thomas v Ken Thomas Ltd [2007] L&TR 21

- i). specifying the breach complained of;
- ii) requiring the breach to be remedied if possible; and
- iii) requiring compensation if the landlord requires it.

The only breach irremediable as a matter of law is a breach of a covenant against assignment or underletting – all others turn on their facts and so to be safe the wording requiring a breach to be remedied “if it is capable of remedy” should be included in the notice.

- f. The notice must then give a reasonable time for compliance. It is a question of fact in all the circumstances what constitutes a reasonable time. Logically it is better to err on the side of giving more time rather than less, though the client will often be eager to keep the period as short as possible.
- g. There are a number of exceptions to the application of section 146. In particular in the case of a breach of a condition against bankruptcy s146 does not apply at all to (a) agricultural land (b) mines (c) a public house (d) a furnished house or (e) a case where objectively the personal qualifications of the tenant are important to the preservation of the value of the property<sup>17</sup>. Further, in all other cases of bankruptcy (including company insolvency) s146 only applies for one year from the bankruptcy. After one year the landlord can forfeit without serving a s146 notice and the court has no power to grant relief.

16. Moreover the tenant<sup>18</sup> has the right to seek relief from forfeiture. In a case of non-payment of rent the tenant will generally get relief if he or she pays the arrears and costs within six months of the forfeiture. The discretion to grant relief is based on solid principles and the payment of the arrears is an invariable condition of it being given, though the time within which the payment is to be made is in the discretion of the Court<sup>19</sup>.

17. One example of exceptional circumstances that can lead the court to refuse relief is where the landlord has granted a third party an interest within the six month period, but has done so reasonably and injustice would be caused by the grant of relief. In a case where the tenant has led the landlord to believe that relief might not be sought, the Court will consider whether the third party is bound by the claim for relief, or the reasonableness of the third party’s conduct in the light of its knowledge<sup>20</sup>.

18. In cases other than non-payment of rent the court has a wide discretion<sup>21</sup>, but the court has always leaned against forfeiture in a case where the tenant can, in substance, remedy the breach and pay the costs of forfeiture – in such a case relief will be granted save in exceptional circumstances.

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<sup>17</sup> s146(9) of the Law of Property Act 1925

<sup>18</sup> so too do mortgagees and sub-lessees have an entitlement to claim relief and seek that the lease be vested in them

<sup>19</sup> *Eastaugh v Crisp* [2007] EWCA Civ 638

<sup>20</sup> *Bank of Ireland Home Mortgages v South Lodge Developments* [1996] 1 EGLR 91

<sup>21</sup> *Shirayama Shokusan v Denovo* [2005] EWHC 2589 (Ch)

19. The remedy of forfeiture has a number of advantages:

- a. relief against forfeiture, if it is sought by the tenant, is usually only given on terms that the breach in question is remedied – so in that case, unlike a money claim, forfeiture does result in the act or omission being put right.
- b. conversely, if no relief is sought by the tenant, then the landlord will put an end to the lease and can thereby rid himself altogether of an impecunious or troublesome tenant. So where there is a persistent failure by the tenant to perform, forfeiture means the landlord can avoid being faced with the problems of having to keep on suing the tenant if it persists in failing to pay the debt or perform the obligation in question, and then having to recover the sums due out of the tenants assets.
- c. moreover the landlord can thereby get the premises back earlier than he otherwise would and, in favourable market conditions, may be able to re-let them quickly at a higher rent.
- d. and once the lease is forfeit damages for breach of the covenant would tend to be measured on the basis that the landlord has vacant possession.

20. But nonetheless forfeiture requires careful consideration before it is exercised. In particular:

- a. forfeiture, especially for a breach other than non-payment of rent, is not necessarily a speedy solution. It still requires time eg to serve s146 notices and give time for the breach of be remedied, followed by time to resolve proceedings and / or any claim for relief;
- b. during the so-called “twilight period” after proceedings have been served the landlord can no longer enforce the covenants in the lease against the tenant<sup>22</sup>. If the forfeiture proceedings are contested and / or relief is sought there can be a long period during which it is not known whether the lease has come to an end. During that period the collection of rent and enforcement of covenants in the lease is difficult to achieve;
- c. forfeiture is a drastic remedy. Once the landlord has chosen to forfeit he cannot reverse his decision and it would be a rash landlord who took it for granted that his tenant will seek relief. So the landlord he must be prepared for the property to be vacated. In a falling market the landlord will not easily find a new tenant and may wish he had been left with ongoing remedies against a struggling tenant;
- d. forfeiture will end the lease as against any surety too, though not until the proceedings are finally determined.<sup>23</sup>

21. Finally, something should be said about the means by which forfeiture can be effected. Forfeiture can be effected by either peaceable re-entry or service of a claim for possession. The choice between the two methods is an important one. Peaceable re-entry is often favoured by clients as the quickest and most

<sup>22</sup> Associated Deliveries v Harrison (1984) 50 P&CR 91

<sup>23</sup> Ivory Gate v Spetale [1998] 2 EGLR 43

aggressive way of dealing with recalcitrant tenants. But it can cause significant problems for the landlord too in practice - it is a “dubious and dangerous method of determining a lease”<sup>24</sup>.

22. Among other things:

- a. It is not available where premises are let as a dwelling<sup>25</sup> including mixed use premises<sup>26</sup>.
- b. It carries a risk of criminal liability. It is an offence to use or threaten violence for the purpose of securing entry to a property if there is someone on the premises opposed to the entry and the person using the violence knows that<sup>27</sup>. So it is essential to re-enter out of hours, and even then it is important to exercise caution in carrying out the re-entry to ensure no-one is present on the premises.
- c. If you cannot clearly establish the right to forfeit you may incur liability for unlawful eviction and the other side may be able to persuade a court to grant an injunction letting them back into possession pending determination of an application for relief from forfeiture.
- d. And even if these hurdles can be overcome, it is often the case that the landlord gains little or nothing by actual re-entry because of the right to relief. The tenant retains the right to seek relief from forfeiture where the landlord peaceably re-enters. If the tenant applies for relief from forfeiture, then the position pending the relief hearing is in practice little different to that which pertains while proceedings for forfeiture are pending save that there is the important, and by no means necessarily desirable, distinction that the landlord is in actual possession of the premises. He cannot easily market them but he has responsibility for securing them and becomes bailee of the tenant’s chattels.
- e. So, unless there is a good chance that the tenant cannot or will not seek relief from forfeiture, peaceable re-entry may well create more problems than it solves.

23. Peaceable re-entry can, however, have particular advantages in the case of an insolvent tenant. Permission of the Court is required to commence a claim for forfeiture against the property of a bankrupt, but permission is not needed to forfeit by peaceable re-entry<sup>28</sup>. The position is different in the case where the tenant is subject to an administration order, in which case permission is needed<sup>29</sup>.

24. For completeness, it should be remembered that it is now recognised that a lease is capable of being terminated by acceptance of a repudiatory breach of the lease, ie. a breach which is serious enough as to evince an intention on the part of the landlord or the tenant no longer to be bound by the tenancy<sup>30</sup>

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<sup>24</sup> per Lord Templeman in *Billson v Residential Apartments* [1992] 1 AC 494

<sup>25</sup> Protection from Eviction Act 1977, s2

<sup>26</sup> *Patel v Pirakaraban* [2006] 1 WLR 3112

<sup>27</sup> Criminal Law Act 1977 s6

<sup>28</sup> *Re Lomax Leisure* [2000] Ch 502

<sup>29</sup> See Schedule B1 paragraph 43(4) of the Insolvency Act 1986 and *Metro Nominees (Wandsworth) Ltd v Rayment* [2008] BCC 40.

<sup>30</sup> *Hussein v Mehlman* [1992] 2 EGLR 87

(though it remains unresolved how this interrelates with the remedy of forfeiture and the right to seek relief from forfeiture).

### **Option 3 – take direct action to remedy the act or omission**

25. It may be open to a landlord to take direct action to remedy an act or omission by the tenant. But this remedy will usually only be available if the landlord has expressly reserved to himself a right to take such steps. The most common example of such a reservation is that under which a landlord reserves to himself the right to enter, remedy disrepair to the premises and then recover the cost from his tenant (the so-called “Jervis v Harris” clause<sup>31</sup>).
26. Absent such a covenant, and unless a right to self-help arises at common law (eg the breach in question causes a nuisance actionable by the landlord himself which he is entitled to abate at common law), the landlord would be well-advised not to seek to remedy the breach himself by entering onto the premises as that will be a trespass.
27. Reliance on a clause enabling the landlord to remedy the breach in question has several advantages. In the case of remedying a disrepair, the landlord has control over the work and can get them done promptly. Furthermore it is now settled that the landlord can recover the cost of the works as a debt without having to satisfy the requirements of the Leasehold Property (Repairs) Act 1938 or to prove loss etc<sup>32</sup>.
28. However, there is still the need to obtain access from the tenant (or seek an injunction to gain access – which could be refused on the balance of convenience). And the landlord runs the risk in anything other than a clear case of liability for trespass if the right has not arisen or preconditions such as notice requirements are not met. By adopting this remedy the expenditure will fall on the landlord in the first instance and he may not succeed in recovering the costs from the tenant if the tenant becomes insolvent in the meantime. Even if the tenant has the money, the recovery process can be protracted as there may be scope for the tenant to argue that the costs incurred were unreasonable. For all these reasons this remedy is most appropriate where the landlord’s overwhelming priority is to ensure the actual act or omission is remedied quickly, even at the risk of bearing the cost himself.

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<sup>31</sup> after Jervis v Harris [1996] Ch 195

<sup>32</sup> Jervis v Harris *ibid*

#### Option 4 – claim for an equitable remedy - specific performance or injunction

29. After some doubt in the past, it is now settled (at first instance) that specific performance is available as a remedy for breach of a tenant covenant in an appropriate case<sup>33</sup>. Specific performance is an appropriate remedy in the case of a breach of a positive covenant by a tenant to do something other than pay a sum of money to the landlord. Where the tenant has omitted to do something that he should have done an order for specific performance would compel him to correct that omission.
30. The remedy is equitable and thus discretionary and not available as of right. It will usually require the landlord to show that:
- a. damages are not an adequate remedy;
  - b. the acts required to be performed to remedy the breach can be clearly and precisely identified;
  - c. that none of the other remedies available to the landlord is obviously more appropriate eg entry under a landlords reservation of the right to enter and carryout the work himself;<sup>34</sup>
  - d. the landlord has a legitimate interest in the covenant being performed and is not seeking the remedy for an ulterior purpose; and
  - e. the balance of hardship favours the grant of specific performance.
31. As with other equitable remedies, the landlord may jeopardise his entitlement to specific performance if he delays too long in seeking it.
32. Specific performance has the advantage that it gets the covenant performed at the tenant's expense. It approximates most closely to putting the landlord in the position he would have been in had the tenant not defaulted. But the main disadvantage with specific performance is that unless it can be shown to be urgent, the landlord will only get it after trial, and even then by reason of its discretionary nature it is difficult to obtain and uncertain.
33. Conversely, where a tenant has breached a negative covenant in a lease ie. committed an act it should not have done, it may be appropriate to seek an injunction to prevent future breach. Equally an injunction could be sought to prevent an anticipated breach in an appropriate case such as where the landlord finds out that the tenant is about to make an unlawful assignment, or commence an unlawful use of the premises.

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<sup>33</sup> Rainbow Estates v Tokenhold [1999] Ch 64

<sup>34</sup> The absence of such a clause was a relevant factor in Rainbow Estates v Tokenhold

## Option 5 - Distress or CRAR (Commercial Rent Arrears Recovery)

34. In relation to arrears of rent there is another remedy available to the landlord. Distress for rent is the ancient remedy pursuant to which a landlord can recover arrears of rent, without going to court, by seizing and, if necessary, selling goods found on the premises demised by the lease.
35. This remedy has been abolished and partially replaced with a new regime called Commercial Rent Arrears Recovery (“CRAR”) under Part 3 of the Tribunals, Courts and Enforcement Act 2007. But the relevant provisions of the 2007 Act have still not been brought into force at the time of writing. So, for the present distress remains available to landlords faced with arrears of rent.

### Distress

36. As soon as the rent is in arrear, the landlord is entitled either personally or by his bailiff to enter the premises and seize such chattels as are sufficient to provide reasonable security for the outstanding rent and his expenses. No formal demand is required to be made or notice given. But in the ordinary way the landlord must physically enter onto the premises in order to seize goods. It is insufficient to simply post notice of distress through a letter box, and the entry onto the tenant’s premises must be lawful.<sup>35</sup> Seizure is effected by the goods being identified and a declaration made that they are being seized for distress. The goods can then be held (“impounded”) until payment or sale of the goods to realise the arrears.
37. However, the landlord has no entitlement to distrain for any greater amount than is due to him in an action for recovery of rent. So, for example, the entitlement to distrain can be defeated by a cross-claim for breach of covenant by the landlord.<sup>36</sup> And certain goods are protected from distraint such as goods in actual use, perishables, tools, books and other equipment necessary for the personal use of the tenant in his trade. And fixtures, not being chattels, also cannot be distrained upon.

### CRAR

38. When distress is eventually replaced by CRAR, the entitlement of the landlord to enforce through the seizure of goods will be significantly curtailed but, within narrower confines, preserved.
39. The new regime will apply only to commercial premises where the lease is evidenced by writing.<sup>37</sup> It can be used to recover rent (and interest and VAT thereon) but not any other sum, even if reserved as rent<sup>38</sup>. So it cannot be used to recover service charges. The arrears in question will be required to reach a statutorily prescribed minimum amount (which has not yet been set) and the amount recoverable is reduced by permitted deductions including any set-off for a cross-claim.<sup>39</sup>
40. Enforcement must be carried out by an authorised enforcement agent. Notice of enforcement has to be given to the tenant in advance, and in response the tenant is entitled to apply to the court and seek that

<sup>35</sup> Evans v South Ribble BC [1992] QB 757

<sup>36</sup> Eller v Grovecrest Investments Ltd [1995] QB 272

<sup>37</sup> ss74, 75 of the Tribunals, Courts and Enforcement Act 2007

<sup>38</sup> s76 of the Tribunals, Courts and Enforcement Act 2007

<sup>39</sup> s77 of the Tribunals, Courts and Enforcement Act 2007

the notice of enforcement be set aside or the CRAR process stayed.<sup>40</sup> Further the landlord is entitled to serve notice on a sub-tenant identifying the amount of the arrears due to the landlord and requiring that the sub-tenant pay his rent directly to the landlord until the notified amount has been discharged<sup>41</sup>.

### **Remedies not mutually exclusive**

41. These different remedies are by no means mutually exclusive. For example, a claim for forfeiture would usually also include a claim for damages, as would a claim for specific performance which would include a claim for damages in the alternative in case the Court refused specific performance.
42. But a claim for forfeiture cannot be combined with a claim for specific performance as the two are inconsistent, forfeiture being the exercise of an option to terminate the lease, and specific performance being a claim for an order that the lease be enforced in accordance with its terms. Forfeiture by proceedings will be rendered ineffective by the inclusion of a claim for specific performance of the lease sought to be forfeited.<sup>42</sup>

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<sup>40</sup> s78 of the Tribunals, Courts and Enforcement Act 2007

<sup>41</sup> s81 of the Tribunals, Courts and Enforcement Act 2007

<sup>42</sup> *Calabar Properties v Seagull Autos* [1969] 1 Ch 451

# Rigging the hypothetical market

by Jonathan Karas Q.C.

## Introduction

1. When rental growth in the market is “softening”, stagnant or in decline, landlords will often aggressively seek to make up for the loss of growth (or decline) in the value of their portfolios by seeking rent increases upon review which would not be available in the real world. Another way for landlords to make up shortfalls is by seeking cash payments from tenants to settle dilapidations claims intended to compensate them for “losses” but which in reality they may not have sustained.

## The theory: rent reviews

2. The “commercial purpose” of rent review provisions in leases is well known. “The general purpose of a provision for rent review is to enable the landlord to obtain from time to time the market rental which the premises would command if let on the same terms on the open market at the review dates. The purpose is to reflect the changes in the value of money and real increases in the value of the property during a long term”<sup>43</sup>.
3. The most common method of achieving this purpose is to provide a formula by which a valuer can value a hypothetical lease on terms similar to the existing lease by reference to up to date rents.<sup>44</sup> The Court of Appeal has said in *Basingstoke & Deane BC v Host Group Ltd*<sup>45</sup>:

Of course rent review clauses may, and often do, require a valuer to make his valuation on a basis which departs in one or more respects from the subsisting terms of the actual existing lease. But if and in so far as a rent review clause does not so require, either expressly or by necessary implication, it seems to us that in general, and subject to a special context indicating otherwise in a particular case, the parties are to be taken as having intended that the notional letting postulated by their rent review is to be a letting on the same terms (other than as to quantum or rent) as those still subsisting between the parties in the actual existing lease. The parties are to be taken as having so intended, because that would accord with, and give effect to, the general intention underlying the incorporation by them of a rent review clause in their lease.

4. In theory, therefore, rents on review should, unless the parties have agreed otherwise, reflect the actual rental value of the lease in the “real” world.

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<sup>43</sup> *British Gas Corporation v Universities Superannuation Scheme Ltd* [1986] 1 WLR 398, 401 per Browne-Wilkinson V-C. See too *Equity & Law Life Assurance Society plc v Bodfield Ltd* [1987] 1 EGLR 124, 125 CA per Dillon LJ; *Basingstoke and Deane BC v Host Group Ltd* [1988] 1 WLR 348, 353-355, CA.

<sup>44</sup> *Basingstoke and Deane BC v Host Group Ltd* [1988] 1 WLR 348, 355, CA

<sup>45</sup> *Basingstoke and Deane BC v Host Group Ltd* [1988] 1 WLR 348, 355, CA

### **The theory: claims for dilapidations**

5. A claim for a breach of a tenant's repairing obligations is a breach of contract. In principle, therefore, damages should compensate the landlord for his reasonably foreseeable losses subject to the usual rules of causation and remoteness. Because of the nature of dilapidations claims, damages are often assessed by reference to the price achievable on two hypothetical transactions: a sale of the premises in repair, and a sale of the premises in the condition in which they were left.

### **The practice: the scope of this talk**

6. If the theory about the commercial purpose of rent review clauses were always reflected in their terms, the rents upon review would reflect the market. In a falling market, however, landlords will do their best to ensure that the rents fall as little as possible.
7. Likewise, if claims for breaches of tenant's repairing obligations were determined or settled in accordance the theory, then the landlord would be no more nor less out of pocket than if the tenant had complied with its obligations. Landlords, however, may seek to arrange their affairs in such a way that they appear to have suffered notional losses which in practice tenants may find it hard to rebut.
8. The purpose of this talk is to give you a flavour of the sort of arguments and issues which can arise. It is not intended to be a comprehensive overview of the law of rent review or dilapidations but it may make you astute to the sort of weapons which a landlord may seek to deploy. I intend to concentrate primarily on rent review but will have something to say about dilapidations at the end.

## **RENT REVIEW**

### **1. Upwards only clauses**

9. The most usual way for a landlord to insure itself against a *fall* in the market is to agree an "upwards only" rent review clauses. While these clauses are no longer invariably found, they are still very common indeed. In a rising market where landlords have a strong negotiating position, tenants are still often willing to agree them. While not achieving growth in rent, it will ensure that on a rent review the rent will not fall. Further, because landlords have little to lose in instigating the review procedure (the rent cannot fall) they encourage landlords to argue for rent increases (allowing for settlement favourable to the land before the issue is determined by a third party because the tenant does not want to take the risk of a decision which is even more unfavourable to him).

### **2. Formulae which inflate the rent payable**

10. The landlord will often seek to agree a formula which allows for an increase beyond real market levels. Even if the formula has not been agreed with such a result in mind, landlords may seek to advance constructions which have this result. For instance, before the "presumption of reality"

became settled, arguments used to be run over whether the hypothetical lease included a rent review clause. Depending on the market, a (hypothetical) tenant might well pay more for a lease without a rent review clause knowing that its rent would not be the subject of an increase. It was settled in *British Gas Corporation v Universities Superannuation Scheme*<sup>46</sup> that clear and unambiguous words will be required if rent review provisions are not to be included in the lease. It is possible, however, to find leases with such clear and unambiguous words<sup>47</sup>.

11. During the last recession one of the most hotly contested issues were those which arose in the “headline rent” cases. As these cases show the Courts are reluctant to construe such formulae in the landlord’s favour in the absence of very clear words. It is illustrative to consider these cases but it is necessary to understand the background.

### **Fitting out periods**

12. A tenant who takes a new lease will usually need to fit out the premises to make them suitable for his occupation. It is common to give the tenant a rent free period in which to fit out the premises based upon an estimate of how long fitting out will take.
13. A tenant whose rent is being reviewed will already have had the benefit of a period to fit out the premises: he is usually in occupation enjoying the benefit of the lease at the time the review takes place. It is intelligible, therefore, that landlord and tenant should agree that upon review the notional letting should be on terms that the tenant has already had the benefit of a rent free period for fitting out. The tenant is thus prevented from arguing that the reviewed rent should be reduced by reason of the hypothetical letting not taking account of the tenant’s need to fit out the premises.

### **Other inducements**

14. In a falling market where supply of premises exceeds the demand for them landlords may give to tenants other inducements to take premises. These may include rent free periods. They may include the landlord making capital contributions to fitting out costs or his taking a surrender (or an assignment) of other premises which the tenant wishes to quit. The “rent” reserved by the lease may be one figure, but in these circumstances the rent reserved by the lease does not reflect what the tenant actually pays for the premises.

### **Treatment of incentives upon rent review**

15. Following the last slump in commercial property prices in the early 1990’s it was argued that the drafting of some leases allowed the landlord to achieve a “headline” rent, i.e. the rent which would be agreed to become payable after a rent free period over and beyond that necessary to cover fitting

<sup>46</sup> [1986] 1 WLR 398 approved in *Equity & Law Life Assurance plc v Bodfield Ltd* [1987] 1 EGLR 124

<sup>47</sup> See e.g. the lease in *Pugh v Smiths Industries Ltd* [1982] 2 EGLR where the rent review clause was on the terms of the actual lease “but excluding therefrom the provisions of this clause”£.

out and granted as an inducement to take the lease<sup>48</sup>. It is certainly possible that the draftsmen thought that this is what they were achieving when they produced the leases.

16. On the other hand, to ignore pure inducements which would be given to tenants on an actual letting in the market at the date of the rent review would result in tenants paying *more* than the current market rent for the premises. Given the commercial purpose of rent reviews, this would be a surprising result in the absence of clear words. Indeed, the approach of the Court has been to presume that rent review clauses do not require the determination of a “headline” rent on review.

*Co-operative Wholesale Society Ltd v National Westminster Bank plc*<sup>49</sup>

The rent review clause required the assumption

That any rent-free period or concessionary rent or any other inducement whether of a capital or revenue nature which may be offered in the case of a new letting in the open market at the relevant rent review date shall have expired or been given immediately before the relevant date of review.

This was held to mean that the willing lessee had been allowed into possession to carry out any necessary fitting out work before the date on which the hypothetical lease was granted. Therefore, the only effect which it had was to remove any argument that there might otherwise have been that the willing lessee would negotiate a reduced rent on account of a period for fitting out but not receive any rent free period. (Appeal allowed)

*Scottish Amicable Life Assurance Society v Middleton Potts & Co*<sup>50</sup>

**The rent to be agreed or determined**

The best yearly open market rent (at the rate payable following the expiry of any rent-free periods or periods at concessionary rents which might be granted on a new letting of the Demised Premises or of comparable premises in the open market on the relevant Review Date) at which the Demised Premises might reasonably be expected to be let in the open market on the Relevant Review Date without a fine or premium ....

It was held that the rent should be determined as that which would be agreed after the end of a rent free period for fitting out and *not* at the end of a further rent free period given as a “pure” inducement. (Appeal dismissed)

*Prudential Nominees Ltd v Greenham Trading Ltd*<sup>51</sup>

The rent was to be reviewed on the assumption that

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<sup>48</sup> See *Hill and Redman’s Guide to Rent Review*, Barnes (2001) para 3.90 for this meaning of the expression “headline rent”.

<sup>49</sup> [1995] 1 EGLR 97

<sup>50</sup> *Ibid.*.

<sup>51</sup> *Ibid.*.

No reduction or allowance is to be made on account of any rent free period or other rent concession which is a new letting might be granted to an incoming tenant.

This did *not* require a headline rent to be determined. A headline rent must mean an *increase* on the rent that would otherwise be on account of a rent free period. The reference to a “*reduction*” in rent could not, therefore, have the effect of prescribing a headline rent. Despite this reasoning, what the draftsman must have meant remains obscure.<sup>52</sup> (Appeal allowed)

*Broadgate Square plc v Lehman Bros Ltd*<sup>53</sup>

### **The reviewed rent was to be**

The best yearly rent which reasonably be expected to be payable in respect of the premises after the expiry of a rent free period of such length as would be negotiated in the open market upon a letting of the Premises as a whole by a willing lessor to a willing lessee ....

The wording in this case was held to be unequivocal. The landlord was entitled to a head-line rent. (Appeal dismissed)

17. These four cases establish a consistency of approach. Until the Court of Appeal heard these cases together, landlords had been able to use these clauses to argue for headline rents and that tenants should pay more than the going rate for what they were enjoying. Now if this is to be achieved using words providing for the disregard of inducements, very clear drafting will be needed. For instance, in the subsequent case of *St Martin's Property Ltd v Citicorp Investment Bank Properties Ltd*<sup>54</sup> the Court considered a provision under which the rent was to be ascertained on the assumption that

The said willing tenant or tenants do not seek a rent free period nor any reduction in rent to allow them the equivalent of a rent free period or any reduction in rent calculated to allow for any rent free period shall be ignored.

It was held that this clause was sufficiently ambiguous for the court to conclude that the draftsman was not intending a headline rent. Again, however, it is perhaps difficult to see what else he could have meant.

### **3. Applying the formula to the facts of a case**

18. Landlords may also look at what are seemingly standard formulae and see how they can be exploited having regard to the particular facts of a case. A particularly important example of this is the “disregards” which apply to the hypothetical premises by reference to which the valuation is to take place.

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<sup>52</sup> See *Hill and Redman's Guide to Rent Review*, Barnes (2001) para 3.89 n 1 where the author makes an interesting speculation on what was intended.

<sup>53</sup> *Ibid.*

<sup>54</sup> [1998] EGCS 161

19. Where the tenant has carried out improvements to the premises at his own expense he often believes that he should not have to pay rent for his own improvements and that they should be disregarded on later rent reviews. It has been decided, however, that in the absence of a provision in the rent review clause that tenant's improvements be disregarded, the reviewed rent (where it is set by reference to the value of the premises) is to be ascertained taking account of the improvements. This is because the improvements become part and parcel of the realty and of the demised premises and a direction in a rent review clause to find the rental value of the demised premises must, in the absence of a stipulation to the contrary, include the value of the improvements<sup>55</sup>.
20. In practice, however, there is now usually a provision in rent review clauses providing that the value of improvements carried out by the tenant is to be disregarded when ascertaining the open market value of the demised premises. What works are to be disregarded will be a matter of the precise terms of the lease and a wise landlord should scrutinize the terms and the premises to be valued closely.
21. For instance, it is common to find provision that improvements carried out by "the tenant" are to be disregarded. Plainly questions may be raised as to who carried out works of improvement. This requirement will be satisfied if the tenant can show that he has made an arrangement with a third party, (typically, but not necessarily, a contract) under which the third party agreed with the tenant to do the specific works involved in effecting the improvements<sup>56</sup>. But sometimes improvements will be carried out in other circumstances and it is important to ascertain whether an improvement falls within the wording of the disregard.
22. More likely to be fruitful to the landlord is that it is often provided that the improvements to be disregarded are only those carried out "with the landlord's prior written consent". It is important, therefore, that the tenant obtain the landlord's consent to improvements if he is to ensure they are disregarded upon rent review.<sup>57</sup> It is surprising how often tenants fail to do this. If they do not, the landlord will be entitled to insist that they are taken into account.
23. It is instructive to consider the case of *Hamish Cathie Travel England Ltd v Insight International Tours Ltd*<sup>58</sup>. In that case, the High Court held that where works had been completed before the landlord's consent was obtained they were not to be disregarded upon rent review and it was too late to obtain the landlord's consent. This seems unimpeachable. On the other hand, the judge also held that one could not read the disregard as applying to improvements "to which the landlord shall have given written consent or in respect of which the landlord's consent had been unreasonably withheld". This, however, is doubtful: where the parties have agreed that a landlord's consent to alterations may not be unreasonably refused, it is difficult to see how sensibly they could also have intended

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<sup>55</sup> *Ponsford v HMS Aerosols Ltd* [1979] AC 63, [1978] 2 All ER 837; *Laura Investment Co Ltd v Havering London Borough Council* [1992] 1 EGLR 155.

<sup>56</sup> See *Durley House Ltd v Viscount Cadogan* [2000] 1 WLR 246, [2000] 1 EGLR 60; *Scottish & Newcastle Breweries plc v Sir Richard Sutton's Settled Estates* [1985] 2 EGLR 130. There may be some event, such as a provision in a deed, which estops the landlord from contending that it was someone other than the tenant who carried out the improvement: *Daejan Investments Ltd v Cornwall Coast Country Club* (1984) 50 P & CR, [1985] 1 EGLR 77.

<sup>57</sup> *Hamish Cathie Travel England Ltd v Insight International Tours Ltd* [1986] 1 EGLR 244.

<sup>58</sup> *Ibid.*

that a landlord who unreasonably withholds his consent can be entitled to rely upon his unreasonable refusal on subsequent rent review. The “officious bystander” test points to the implication of a term. Nevertheless, this shows the sort of argument which landlords may deploy and on which they can succeed.

24. There are statutory provisions for the disregard of improvements in the Landlord and Tenant Act 1954 s.34. This applies where the court has to determine the rent to be paid under a new tenancy ordered to be granted of business premises. These statutory provisions are sometimes incorporated into rent review clauses. The statutory disregard, however, does not apply to improvements carried out not under the current tenancy and more than 21 years ago, and the disregard only applies where the premises have been comprised in tenancies to which the Act applies at all times since the improvement was completed. If the statutory provisions are to be incorporated into a rent review clause good drafting therefore requires that appropriate modifications are made<sup>59</sup>. The statutory provision as enacted in 1954 were substantially modified in 1969<sup>5</sup> and in some older leases it may be necessary to decide whether it was the original or the amended version which is to apply<sup>60</sup>.
25. Possible difficulties for tenants (and gains for landlords) arise where the tenant has carried out the work but before the grant of the current tenancy.
- a. Where the work was carried out under a previous tenancy of the premises by a previous tenant these are not “improvements” to the demised premises as they were let and not improvements by the tenant. The disregard of “improvements by the tenant” will not apply.
  - b. Where the tenant under the current tenancy has carried out the work under a previous tenancy of the premises, it is sometimes argued that if the rent review clause directs that there be disregarded any improvement carried out by “the tenant”, that work is to be disregarded since it was carried out by the tenant. While this will be a matter of construction in each case, in most instances (in the absence of express provision) this suggestion is likely to be wrong. Michael Barnes Q.C. in Hill & Redman’s *Guide to Rent Review* states:

“There are two reasons why in such a case the value of the work is to be taken into account. First, the work in question is not an improvement as that word is to be understood in the context of a provision in the current lease. In the provision an improvement means an improvement to the premises as demised, not an improvement which itself created the premises as demised<sup>61</sup>. Second, it may be that

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<sup>59</sup> See per Slade LJ in *Brett v Brett Essex Golf Club Ltd* [1986] 1 EGLR 154 at 157.

<sup>60</sup> See *Brett v Brett Essex Golf Club Ltd* [1986] 1 EGLR 154, in which it was held by the Court of Appeal that the reference was to the former unamended version of the Act even though the lease was granted after the amendments had been effected.

<sup>61</sup> Compare *Brett v Brett Essex Golf Club Ltd* [1986] 1 EGLR 154 the tenants had erected a golf clubhouse on land demised to them in 1973. That lease was surrendered and a new lease granted to them in 1978. The second lease required that under rent reviews there should be disregarded ‘any effect on rent of any improvement carried out by the tenant or a predecessor in title of his otherwise than in pursuance of an obligation to his immediate landlord’. The Court of Appeal held that in the context of the above provision in the second lease the clubhouse was not an improvement and so was not to be disregarded. In *Panther Shop Investments Ltd v Keith Pople Ltd* [1987] 1 EGLR 131 the tenants had during an earlier lease constructed a back extension and a separate storage building on the demised premises. The required disregard was of any improvement carried out by the lessees. Again, it was held that the works

the context requires some qualification to be placed on the word 'tenant', the obvious qualification being that it means the tenant in his capacity as the tenant under the current lease. A similar qualification had been applied in a similar context by the House of Lords when considering the original provisions of the Landlord and Tenant Act 1954<sup>62</sup>. It follows that if a tenant taking a new lease wishes that the effect on value of improvements which he has carried out under a previous lease should be disregarded on rent reviews under the new lease he should insist on the inclusion of a clear express provision to this effect. The Landlord and Tenant Act 1954 was amended by the Law of Property Act 1969 so as to provide for such a result when the rent is determined for new leases granted under the Act, but subject to substantial qualifications."

- c. Where the tenant carries out the work not as tenant under a previous tenancy but in contemplation of the grant of the current tenancy and before that tenancy is actually granted, then it may be that even though not carried out by the "tenant" before he became tenant (strictly so called) they will be disregarded<sup>63</sup>. The question will be one of construction in the circumstances in each case. If the works were referable to the current tenancy, their value will probably be disregarded, but if referable to some prior interest of the tenant, they will be taken into account<sup>64</sup>.

26. It is also common to provide that improvements shall be disregarded except when carried out pursuant to an obligation to the landlord. This provision is also found in s.34 of the Landlord and Tenant Act 1954. A number of points should be noted.

- (1) An improvement may be carried out by the tenant pursuant to a statutory obligation as well as pursuant to an obligation to the landlord. Covenants in leases often require that the tenant is to comply with statutory obligations. In such a case the improvement is not to be disregarded since, notwithstanding the effect of statute, it is still carried out pursuant to an obligation to the landlord<sup>65</sup>.
- (2) Where there is a qualified covenant restricting alterations improvements are often permitted by a licence granted by the landlord. Such licences often contain provisions

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had to be taken into account on the ground that an improvement meant an alteration to the existing premises and not some previous works which were a part of the premises as demised. In *Scottish & Newcastle Breweries plc v Sir Richard Sutton's Settled Estates* [1985] 2 EGLR 130 at 137 Judge Baker QC described an improvement as an alteration or addition to a building which the landlord has provided, so that what is contemplated is that the landlord provides a building and the tenant then adds something to it or improves it in some way.

<sup>62</sup> *East Coast Amusement Co Ltd v British Transport Board* [1965] AC 58, sub nom *Re Wonderland, Cleethorpes, East Coast Amusement Co Ltd v British Railways Board* [1963] 2 All ER 775.

<sup>63</sup> Compare *Hambros Bank Executor and Trustee Co Ltd v Superdrug Stores Ltd* [1985] 1 EGLR 99; *Scottish & Newcastle Breweries plc v Sir Richard Sutton's Settled Estates* [1985] 2 EGLR 130.

<sup>64</sup> *Scottish & Newcastle Breweries plc v Sir Richard Sutton's Settled Estates* [1985] 2 EGLR 130.

<sup>65</sup> *Forte & Co Ltd v General Accident Life Assurance Ltd* (1986) 54 P & CR 9, [1986] 2 EGLR 115

that the tenant shall carry out the permitted improvements in a certain way, for example to a proper standard, in accordance with specified plans or within a specified time. Such obligations are merely ancillary and are subsidiary to the main purpose of the licence which is to grant permission for the works<sup>66</sup>. Even a term in a licence that the provisions of the lease shall apply to the altered premises as if the premises in their altered state had originally been comprised in the lease does not prevent the application of the disregard<sup>67</sup>.

- (3) On the other hand, the licence may expressly provide that the works are deemed to be carried out pursuant to an obligation to the landlord. This must mean that the disregard is not to apply with the result that the valuation on a subsequent rent review is to take into account the improvements in question<sup>68</sup>.
- (4) If a licence to carry out an improvement requires that the tenant shall remove the improvement at the end of the term that obligation in the licence will not normally be a term of the hypothetical lease<sup>69</sup>.

#### 4. Confidentiality

27. Landlords may also seek to influence the outcome of rent reviews is to keep evidence which is harmful to their cases away from the tribunal. Landlords keep comparable transactions and other relevant material confidential. This may have some limited success. In the case of arbitrations, however, a determined tenant with sufficient resources should be able to compel the production of relevant material.
28. The method by which valuers assess the rent on a rent review is to have regard to actual transactions which may then be compared with the transaction assumed to be taking place. By this comparison an inference can be made as to rent which would be agreed on the notional transaction<sup>70</sup>.
29. In a falling market it may well be in landlords interests to keep confidential the terms of transactions which may provide evidence of the state of the market and which could be used against them on rent reviews. Landlords, therefore, will commonly seek to keep confidential the terms of comparable transactions.
30. On the other hand, where the rent is to be determined by an arbitrator

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<sup>66</sup> *Godbold v Martin The Newsagents Ltd* [1983] 2 EGLR 128; *Historic Houses Hotels Ltd v Cadogan Estates* [1993] 2 EGLR 151; *Daejan Properties Ltd v Holmes* [1996] EGCS 185. Cf *Ivory Gate v Capital City Leisure Ltd* [1993] EGCS 76.

<sup>67</sup> *Historic Houses Hotels Ltd v Cadogan Estates* [1993] 2 EGLR 151

<sup>68</sup> *Daejan Properties Ltd v Holmes* [1996] EGCS 185

<sup>69</sup> *Pleasurama Properties Ltd v Leisure Investments (West End) Ltd* [1986] 1 EGLR 145.

<sup>70</sup> See *Land Securities plc v Westminster City Council* [1993] 1 WLR 286 generally; see also *Living Waters Christian Centre v Fetherstonhaugh* [1999] 28 EG 121.

- (1) where the landlord has or has had possession, custody or control of documentation providing evidence of comparable transactions, such material can properly be the subject of an order for disclosure in an arbitration<sup>71</sup>; and
- (2) a third party may be the subject of an order requiring it to produce relevant documentation to an arbitration<sup>72</sup>.

31. If relevant comparable material is agreed between the parties to the transaction to be “confidential” this should not prevent its disclosure in an arbitration. This issue has been considered in New Zealand. In *Re Dickinson*<sup>73</sup> a tenant sought on a rent review to put evidence before an arbitrator of comparable transactions which were subject to confidentiality clauses and issued sub poenas against the tenants of the comparable premises requiring them to provide details of the transactions. The landlords of the comparable premises sought to set aside the sub poenas. The New Zealand Court of Appeal held that the Court had jurisdiction to set aside sub poenas at common law as an abuse of process having regard to competing interests including the interest of confidentiality. In this case it declined to do so, Cooke P stating as follows:

It is understandable that an organisation such as [the Lessors]... with very large funds under its care should be anxious to maintain rental levels in its building as high as reasonably possible. Any commercial lessor is likely to have the same approach. Perhaps in these times of economic stringency it is not surprising that confidentiality clauses have begun to appear in commercial leases of this kind. But, for very many years, leases of commercial premises in New Zealand cities have to a large extent been fixed by rent review procedures. They are a major or a least a significant element of the New Zealand economy. Generally speaking, the leases authorising or requiring such procedures speak of market rents or use some similar formula such as fair rent. In *Modick RC v Mahoney* [1992] 1 NZLR 150 this Court stressed the importance of the ability of valuers or umpires to be able to refer to genuine market rents: that is to say rents freely arrived at in negotiation between the parties, by contrast with those arrived at in the captive circumstances of rent fixations.

Such genuine market rentals are not always easy to discover, and when discovered they may be of great importance in assisting an umpire in carrying out his difficult task of assessment. It is a fair inference in the present cases that the rents agreed for [the comparable premises] may well be of true significance for the umpire concerned with the [subject premises]. Of course one infers as much without any detailed knowledge of the situation and without in any respect seeking to fetter him, but it is desirable that he should be able to get at the truth of these allegedly comparable rentals. Plainly, details will be required such as the terms of collateral contracts offering side benefits and the like.

The contention for the lessor of the [comparable premises] does not withstand analysis. In effect it is an attempt, in the interests of lessors, to prevent true market rents from being ascertained. But in the current economic climate it is plainly in the public interest that fair levels of rent be arrived at in our main cities. One has only to consider the apparently

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<sup>71</sup> See Arbitration Act 1996 s.34(2)(d).

<sup>72</sup> See Arbitration Act 1996 s.43

<sup>73</sup> [1992] 2 NZLR 43

extensive unlet areas in newly constructed buildings to appreciate that unrealistically high levels are not in the public interest. One sympathises, as I have said, with the responsibility of the lessor for the funds in its case but, in my opinion, the overriding public interest is in a fair a fixation of market rents as possible.

This reasoning is equally applicable in England. It is hard to fault it. The New Zealand Court of Appeal went on to consider an objection to the sub poenas based on the New Zealand Bill of Rights Act 1990 and gave it short shrift: given that the sub poenas were reasonable to uphold them was in the public interest. Any similar arguments in this jurisdiction based on the European Convention on Human Rights should be treated in the same way.

32. Nevertheless where there is a genuine commercial interest in confidentiality, the Courts will respect it. In the case of *South Tyneside Borough Council v Wickes Building Supplies Ltd*<sup>74</sup> on the facts of the particular case the Court was unwilling to order disclosure of a confidential transaction involving B&Q in a rent review involving its rival, Wickes. The issue of confidentiality, therefore, was quite acute. Even so, the Court held that “in some cases, a confidentiality clauses may be overridden where, for example a clear need for the documents is demonstrated and considerations of commercial sensitivity are not present or at least not present in the acute form to be found in the present case. In other cases, confidentiality will be a very relevant factor telling in favour of setting aside a witness summons”
33. If an expert witness has made relevant inconsistent statements in a report tendered in an earlier arbitration, the production of such a report can be compelled by a witness summons and the search for the truth will usually outweigh the confidentiality of the earlier arbitration<sup>75</sup>.
34. Similarly, an agreement by a party with another not to give evidence will be unenforceable. In *Harmony Shipping Co SA v Saudi Europe Line Ltd*<sup>76</sup>:

If there was a contract by which a witness bound himself not to give evidence before the court on a matter which the judge said he ought to give evidence, then I say that any such contract would be contrary to public policy and would not be enforced by the court. It is the primary duty of the courts to ascertain the truth and when a witness is subpoenaed he must answer such questions as the court properly asks him. This duty is not to be taken away by some private arrangement or contract by him with one side or the other.

In *Fulham Football Club Ltd v Cabra Estates plc*<sup>77</sup> it was held that there was no objection on grounds of public policy to a covenant whereby a party to a commercial transaction involving the disposition of land undertook to support, and to refrain from opposing, planning applications by the other party for the development of land. On the other hand, the Court of Appeal made it clear that<sup>78</sup>

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<sup>74</sup> [2004] EWHC 2428 (Comm)

<sup>75</sup> *London & Leeds Estates Ltd v Paribas Ltd (No. 2)* [1995] 1 EGLR 102

<sup>76</sup> [1979] 1 WLR 1380 at 1386

<sup>77</sup> [1994] 1 BCLC 363, CA.

<sup>78</sup> *Ibid.*, at 391.

This does not mean of course that a witness could be prevented by agreement from giving evidence on sub poena, because this could involve an interference with the course of justice.

35. Of course, it is only in the context of *arbitrations* that these remedies are open to tenants. If the determination of the rent is to be made by a third party as *expert*, then the expert has no powers to require the landlord to divulge relevant material (though it is possible for landlord and tenant to agree between themselves as a matter of *contract* that relevant document must be disclosed). Such an expert has no power at all to require third parties to disclose documents. This makes determination by an expert that much more uncertain unless an expert with detailed knowledge of the particular local market is chosen.

## 5. Admissibility

36. Questions may also arise about the admissibility of evidence. The relaxation of the hearsay rule makes it harder to keep evidence away from arbitrators or courts<sup>79</sup>. On the other hand, there are still arguments which landlord may deploy to limit the evidence available to the arbitrator. It is important to be astute to these arguments. One of the most contentious arises when attempting the “profits” method of valuation.
37. The “profits” method of valuation involves a valuer trying to estimate the profit which would be likely to be earned by a tenant who operate a business at premises and then attributes a part of that profit to the rent which such a tenant would be willing to pay. This method of valuation is common in the leisure industry and properties such as car parks where the “comparable” method of valuation is considered unreliable – indeed, it may be impossible to find true comparables.
38. Very often landlords will want to seek what profits the tenant is making. Sometimes, however, tenants will seek to rely upon their trading accounts. Either way the trading accounts cannot be taken into account.
39. In the case of *Cornwall Coast Country Club v Cardgrange Ltd* [1987] 1 EGLR 146 one of the issues on an “open market” rent review was whether the tenant should give discovery of documents relating to the profits earned by its gaming business. Scott J held that there was no doubt that the arbitrator was entitled to take into account the income-earning capacity of the premises but went on to hold (in essence) that unless the evidence would have been available in the market to prospective lessees it was not admissible since it would not have influenced the deal which would have been struck between the hypothetical parties.
40. In the case of *Electricity Supply Nominees Ltd v London Clubs Ltd* [1988] 2 EGLR 152 Hoffman J took a similar approach. At 152-153, Hoffman J said (emphasis supplied) he said

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<sup>79</sup> Civil Evidence Act 1995 s.1. Contrast the previous law: *Town Centre Securities v Wm, Morrison Supermarkets* [1982] 2 EGLR 114; *Rogers v Rosediamon Investments (Blake Market)* [1978] 2 EGLR 48; *English Exporters (London) Ltd v Eldonwall Ltd* [1973] Ch 415.

In the *Cardgrange* case, which also concerned the accounts of a casino, Scott J followed the principle laid down by the House of Lords in *Lynall v Inland Revenue Commissioners* [1972] AC 680 and held that the only admissible evidence of the profit-earning capacity of the casino was evidence available to a prospective lessee in the open market. In this appeal, Mr Neuberger has submitted that the learned judge was wrong. He said that evidence of actual earnings, even if not available in the open market, was admissible to test the value of expert estimates of what the profit-earning capacity would have been. If it showed, as appeared here to be the case, that actual profits were nothing like what the expert said the market would have assumed, the arbitrator would be entitled to take that into account in assessing the value of the expert's evidence. In my judgment, this submission is based upon a false assumption about the issue before the arbitrator. He is concerned not with the actual earning capacity but with how the market would have assessed earning capacity. The open market may be a false market in the sense that it is based upon false assumptions, but it is still the open market. I do not see how information about profitability which the market did not know can be relevant to the question of what the market would have thought.

The cases in which post-review-date transactions are admissible seem to me to stand on quite a different basis. An open market transaction at a later date may, by applying the presumption of continuity, afford a legitimate basis for an inference that a transaction on similar terms would have taken place at an earlier date. Of course the presumption may be rebutted by showing that the market, at the later date, was possessed of information not previously available. But there is no reason in principle why relevant inferences cannot be drawn from subsequent events. But this is not the kind of reasoning upon which the tenants in this case want to rely. I am therefore not persuaded that Scott J was wrong and I propose to follow his decision.

41. Subsequently, Browne-Wilkinson V-C in *Urban Small Spaces Ltd v Burford Investments Co Ltd* [1990] 2 EGLR 120 confirmed that these cases represent the law. He plainly considered that he was bound to assume the *Electricity Supply Nominees* and *Cardgrange* cases about the admissibility of evidence. In that case an arbitrator made an order for discover of documents relating to rents received by the tenant from licensees occupying parts of the premises. He held that the fact that documents might be inadmissible in evidence was not in itself a reason for refusing disclosure and he refused to overturn the arbitrator's decision. The Vice-Chancellor said (emphasis supplied):

Assuming, as I must for present purposes, that the decisions of Scott J in *Cornwall Coast Country Club v Cardgrange Ltd* and Hoffmann J in *Electricity Supply Nominees Ltd v London Clubs Ltd* are correct as to the admissibility of such evidence for the purpose of fixing the rent, the question of what is a discoverable document is not limited to documents admissible in evidence: all information and documents which may be used either in making the parties' case or in destroying the other parties' case must be discovered."

42. "Such evidence" mentioned by the Vice-Chancellor (as he then was) was information "which would not be available to the public at large in negotiating the hypothetical rent" (not simply trading account evidence). The Vice-Chancellor plainly considered that Scott J and Hoffman J had held that such evidence was *inadmissible*.

43. This is the state of the law. It is fair to say that many surveyors do not like it. It prevents them having regard to the most obvious and reliable evidence as to what the premises are actually worth. Are there ways around this? It has been suggested that the provision of the Arbitration Act 1996 which came into force after these cases were decided provides a way around the authorities. Under Arbitration Act 1996 s. 34(2)(f), “subject to the right of the parties to agree any matter” (under s.34(1)), the arbitrator has a discretion whether or not to apply “strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material”. It is highly doubtful whether this suggestion is correct.
- (1) It is axiomatic that a decision which takes into account immaterial matters is unlawful: this is a well established principle see e.g. *Hollington v F. Herthorn & Co* [1943] 1 KB 587; *Associated Provincial Picture Houses v Wednesbury Corpn* [1948] 1 KB 223. If *Cardgrange* and the subsequent cases are correct, then it is inherent in the exercise of ascertaining an “open market rent” in accordance with the formula agreed that only matters known to the open market are material: that is the nature of the exercise which the parties have agreed must be undertaken. To have regard to such matters would be unlawful and an arbitrator cannot exercise his power under Arbitration Act 1996 s.34 to render material that which is immaterial.
- (2) To have regard to such matters would go behind what the parties have agreed (if *Cardgrange* is correct) as an inherent part of the formula. The arbitrator’s power is expressly subject to the right of the parties to agree any matter. The power under section 34 cannot be used to re-write what the parties have agreed in the rent review clause.

## 6. Restrictions on alienation

44. The final way which I want to consider and in which landlords may seek to protect their positions on rent review is to put restrictions on alienation in order to limit transactions which might prove unwelcome to the landlord on rent review. Such terms, if carefully drafted, may be effective. Whether tenants can be persuaded to accept such terms will very much depend on the state of the market when they take their leases and whether they have been well advised.
45. Comparable transactions may comprise sub-lettings or assignments of comparable premises. They may even include sub-lettings and assignments of the premises demised by the lease in respect of which the rent review is taking place. Landlords may seek to restrict these transactions if they will have an adverse affect on the value of their premises.

### Absolute prohibitions on alienation

46. A landlord may place an absolute prohibition on alienation. This is unlikely to prove acceptable to most commercial tenants. Further, unless such a clause was to be disregarded on rent review, it might well have an adverse affect on the rent which was to be fixed for the premises.

### *Qualified prohibition on alienation*

47. The landlord may seek to limit alienation without his consent. In such circumstances, the law implies a term that such consent is not to be unreasonably withheld<sup>80</sup>.
48. The landlord is entitled to be told the true nature of the transaction, and in the case of an underletting is entitled to be told the terms on which the underletting is to be taken place.<sup>81</sup> The provision to the landlord of “heads of terms” may be sufficient for the landlord to make its decision but it may still be reasonable to require further approval of detailed terms<sup>82</sup>. A landlord may not, however, be entitled to be told the amount of a premium payable on an assignment<sup>83</sup>.
49. Where a tenant proposed to underlet part of the demised premises at a substantial premium and at a rent that fell well below the market rent obtainable for the premises, and it was shown that the proposed rent was so low as to raise reasonable doubts as to the landlord being able to recover the full amount of arrears under Law of Distress Amendment Act 1908 s.6, it was held that the landlord’s refusal of consent was reasonable. The possible deficiency of undertenants’ rents in case of distress and the fears which might be entertained by a prospective purchaser or mortgagee from the landlords were sufficient justification for the defendants’ refusal of consent to the proposed underletting.<sup>84</sup>
50. If a transaction will have an adverse effect on the landlord’s reversion, this is a matter which can provide good grounds for refusing consent provided that the adverse affect is not merely theoretical<sup>85</sup>. Thus a landlord *may* reasonably withhold consent to a transaction at less than market value but he must have reasonable grounds on which to object on such grounds; if the advice which he receives is unreasonable, then his refusal will be unreasonable<sup>86</sup>.
51. On the other hand, a landlord may be in substantial difficulty if it seeks to argue that it is acting reasonably in withholding consent to a genuine open market transaction if its reason for doing so is that it will have an adverse impact on rent review. It is not normally reasonable for a landlord to seek to impose a condition which is designed to increase or enhance the rights that he enjoys under the lease: it is no, for instance, reasonable to require the tenant to wait until rental values improve before subletting<sup>87</sup>. A landlord on a rent review is entitled to the market rent (see above). Accordingly, if the substance of the objection to a transaction is that the transaction will tend to show what the true state of the market is (in the hope that he will secure a rent above the market rent), then in essence the landlord is seeking to increase the rights which he enjoys under the lease. Thus,

<sup>80</sup> Landlord and Tenant Act 1927 s.19(1).

<sup>81</sup> *Fuller’s Theatre and Vaudeville Co v Rolfe* [1923] AC 435.

<sup>82</sup> *Dong Bang Minerva (UK) Ltd v Davina* [1995] 1 EGLR 48.

<sup>83</sup> *Kened v Connie Investments* (1995) 70 P & CR 370, CA

<sup>84</sup> *Re Town Investments Underlease, McLaughlin v Town Investments* [1954] Ch 301 approved in *Pimms v Tallow Chandlers Co* [1964] 2 QB 547.

<sup>85</sup> *International Drilling Fluids Ltd v Louisville Investments (Uxbridge) Ltd* [1986] Ch 513; *Ponderosa International Development Inc v Pengap Securities (Bristol) Ltd* [1986] 1 EGLR 66.

<sup>86</sup> See *Blockbuster Entertainment Ltd v Leakcliff Properties* [1997] 1 EGLR 28; *Luminar Leisure v Apostole* [2001] 42 EG 140;

<sup>87</sup> See eg *Mount Eden Land Ltd v Straudsley Investemnts Ltd* (1996) 74 P & CR 306, CA

for instance, it has been held that a landlord would not be reasonable to require the tenant to wait until rental values improve before subletting<sup>88</sup>.

### Pre-conditions to alienation

52. It has been held that it is open to the parties to avoid the qualifications imposed by Landlord and Tenant Act 1927 s. 19 by imposing pre-conditions to a sub-letting or assignment: see *Bocardo SA v S & M Hotels Ltd*<sup>89</sup>. Thus, it is possible to provide that no underletting can take place at a rent of less than the full market rent obtainable without taking a fine or premium: such pre-conditions have the advantage that the onus will remain on the tenant to prove that it falls within the condition since such a clause will not fall within Landlord and Tenant Act 1988 s.1<sup>90</sup>.
53. One could also, for instance, include pre-conditions which prevent transactions otherwise than on the terms of the head-lease<sup>91</sup>. On this basis, there is nothing, in principle, to preclude a covenant that any sub-letting shall be on the same terms as to rent as the head-lease. To be effective to “protect” the landlord, of course, the drafting must be in such a way as to preclude side agreements which can be used by the tenant on rent review to show that the rent reserved was more than the true market rent<sup>92</sup>.
54. A recent example consistent with these conclusions is *NCR v Riverland Portfolio No. 1*<sup>93</sup> where it was held that the fact that a tenant proposes to grant an underlease at the market rent in consideration of a reverse premium payable by the tenant to the subtenant did not detract from the fact that the rent to be reserved was indeed the market rent and the landlord was thus not entitled to object to the transaction.
55. The extent to which such clauses will be acceptable to tenants will depend on the market. In a falling market, they will be unacceptable. On the other hand, in a strong market landlords may be able to impose such terms. Tenants should be very wary about accepting such terms. When are market falls, such terms can make alienation difficult.<sup>94</sup>

### DILAPIDATIONS

56. Prior to 1927 it had been held that the measure of damages for disrepair at the end of term was generally the reasonable and proper cost of the necessary repairs together with (where appropriate)

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<sup>88</sup> See eg *Mount Eden Land Ltd v Straudsley Investemnts Ltd* (1996) 74 P & CR 306, CA

<sup>89</sup> [1980] 1 WLR 17, CA

<sup>90</sup> *Homebase Ltd v Allied Dunbar Assurance plc* [2002] 1 P & CR 1 (first instance), and see [2002] EWCA Civ 666 at [16], [20], CA.

<sup>91</sup> *Ibid.*.

<sup>92</sup> See *ibid.*.

<sup>93</sup> [2005] 1 P & CR 3

<sup>94</sup> John Mayhew, property director of Homebase was widely reported in the press following the House of Lords rejection of its application for permission to appeal as stating that the House of Lords had stifled open debate on the restrictive nature of commercial property leases, many of which contain upwards-only rent reviews.

loss of rent during the carrying out of the works and (possibly) subject to some allowance for betterment<sup>95</sup>. In *Joyner v Weeks* [1891] 2 QB 31, 43 Lord Esher MR stated

“The rule is that, when there is a lease with a covenant to leave the premises in repair at the end of the term, and such covenant is broken, the lessee must pay what the lessor proves to be a reasonable and proper amount for putting the premises into the state of repair in which they ought to have been left”

57. The modern approach, consistently with cases such as *Ruxley Electronics & Construction Ltd v Forsyth* would be that where expenditure required to be done to an asset to remedy a breach of contract is out of proportion to the benefit to be obtained, the appropriate measure of damages will be the diminution of value of the asset. That this is the modern approach in dilapidations cases is supported by dicta of the Court of Appeal in *Latimer v Carney*.<sup>96</sup>
58. Indeed, even looking at older authority, it is likely that a rigid application of *Joyner v Weeks* did not represent the law and that assessing damages cannot be treated as overriding the general common law principles by which damages for breach of contract are to be assessed:
- (a) although the “rule” was a “convenient rule” there is not binding authority that it was or is applicable to all circumstances (see *Joyner v Weeks* *ibid.* *Tito v Waddell (no. 2)*<sup>97</sup>;
  - (b) indeed for the “rule” to apply it is clear that the Court must find that the landlord must have suffered actual damage: see *James v Hutton*<sup>98</sup>;
  - (c) even in the 19<sup>th</sup> century the Courts in considering the proper measure of damages in the case of a covenant to keep in repair considered the proper approach was to look at the actual losses which could be said to have been reasonably contemplated to the landlord’s reversionary interest rising from the breach of covenant upon the principles set out in *Hadley v Baxendale*: see *Ebbetts v Conquest*<sup>99</sup>; see too *Yates v Dunster*<sup>100</sup> (cost of repair basis but deduction made from cost of repairs of the amount which the premises would, after repair, be more valuable than they had been before they fell into disrepair).
59. Be that as it may, the Landlord and Tenant Act 1927 s.18 provides a statutory cap on the measure of damages. The effect of Landlord and Tenant Act 1927 s.18 is that the “reinstatement” basis is not available as a measure of damage for breach of a covenant to repair where the cost of reinstatement exceeds the diminution in value to the reversion.
60. This limit on the damages recoverable, however, does not prevent landlords seeking to inflate their claims. A landlord may feel encouraged by a number of points.

<sup>95</sup> See generally *Joyner v Weeks* [1891] 2 QB 31.

<sup>96</sup> [2006] 3 EGLR 12 at [24] and [60]

<sup>97</sup> [1977] Ch 106, 329-331

<sup>98</sup> [1950] 1 KB 9 at 16

<sup>99</sup> [1895] 2 Ch 377, 382-383, 387

<sup>100</sup> (1855) 11 Ex 15

61. First, a tenant who has vacated premises may have little incentive to get bogged down in substantial litigation where the entirety of his costs may be irrecoverable unless the can be confident of making a part 36 offer which the landlord will fail to beat. So a tenant may be willing to entertain a settlement at a figure higher than that which would in all likelihood be awarded in court. Unless and until a tenant makes a part 36 offer, a landlord is a little risk on costs in pursuing an inflated claim with a view to achieving a settlement – provided that the claim is not fanciful..
62. Secondly, it seems that in practice Courts are very reluctant to accept that where there is a breach of covenant, the landlord has suffered no loss at all (even when the tenants have the advice of a surveyor that no loss has been sustained) Where the landlord has done the works in question or intends to do the works, then the courts are inclined to accept that this is *prima facie* evidence of cost. This is not unreasonable. But even if the landlord does not intend to carry out the works, the courts are susceptible to arguments that disrepair at the premises must have some impact on value because, it is said, an incoming tenant (whether or not he would in fact carry out the works) would use their condition as a negotiating tool to drive down the price. Such evidence was accepted in *Shortlands v Cargill Ltd*<sup>101</sup>. Even where the premises have redevelopment potential so that ultimately the premises will be redeveloped, the works may have some value: so in *Craven (Builders) Ltd v Secretary of State for Health*<sup>102</sup> (Neuberger J held on the evidence that a buyer of the landlord's interest would have been largely uninterested in their condition would have attributed some value to the repairs because they would have assisted in short-term lettings: while the cost of remedial works was £312,500, the damages was assessed at £40,000). It is hard for the tenant to establish in the hypothetical world in which the valuations take place that there is no diminution to the landlord's interest as a result of breach of covenant<sup>103</sup>..
63. Thirdly, under s.18 (or even at common law if I am correct) if the landlord has an intention to redevelop at the end of the tenancy so that the repairs would be nugatory, then damages will be capped: the landlord will suffer no loss. But knowing that the courts will accept arguments that the state of repair may affect short term lettings pending redevelopment or the negotiating position of the purchaser or an incoming tenant, landlords do not formulate their intentions to redevelop until after they have achieved their dilapidations settlement. In some cases, landlords' positions can appear to verge on the disingenuous. In the absence of an incautious email or memorandum (of which disclosure has been obtained) or some startlingly lucky cross-examination or a shockingly weak expert opinion produced by the landlord, the tenant may face a real difficulty. Landlords know this.
64. What is the tenant's solution?
- a. an early and robust part 36 offer to put pressure on the landlord?
  - b. full disclosure of material relating to the landlords' intentions (including e-disclosure – emails and memoranda containing incautious remarks about redevelopment may well have been deleted)?
  - c. take a public spirited approach and take cases where potential redevelopment is viewed as rendering nugatory any repair in the hope of changing the judicial reluctance to find no damage?

<sup>101</sup> [1995] 1 EGLR 51.

<sup>102</sup> [2000] 1 EGLR 128

<sup>103</sup> But it does happen – see *Landeau v Marchbank* [1949] 2 All ER 172; *Mather v Barclays Bank plc* [1987] 2 EGLR 254; *Ultraworth Ltd v General Accident Fire & Life Assurance Co Ltd* [2000] 2 EGLR 115.

65. Finally, landlords should not take too much heart from my pessimism about the position of tenants. They should take note of *Business Environment Bow Lane v Deanwater Estates (No. 2)*<sup>104</sup> (total claim was in excess of £400,000; landlord received £1073.50; *indemnity* costs awarded against the landlord).

## Conclusions

66. Leases with rent review clauses underpin much of the commercial property market. Landlords who seek to exploit rent review provisions can often achieve settlements are rents higher than they could achieve either in the market or, because tenants may be wary of the risks involved, upon third party determination. Likewise, landlords who exploit tenants' covenants may find themselves with windfalls if faced with tenants who wish to avoid the trouble of litigation. When acting for landlords, you must be astute to the points which you can reasonably take to maximize returns and that involves scrutinizing the lease terms as the starting point. When acting for tenants on rent reviews, it is important to take the lease as the starting point but one should not necessarily be fazed by landlord who take nit-picking points of construction or who seek to keep confidential transactions which hide the true state of the market. On dilapidations cases, tenants should be willing to call their landlords' bluff and put the landlord at risk on costs as soon as possible.

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<sup>104</sup> [2008] EWHC 2003 (TCC).

# Damages in property related solicitors' negligence cases

By Jonathan Seitler QC

## The starting point:

- ☞ Your client, C, buys land for £10m with the intention of building its new Head Office to accommodate its 1000 members of staff.
- ☞ There is a restrictive covenant in favour of an adjoining occupier, AJ, "*not to erect ..... office buildings .....*"
- ☞ C's previous solicitors had missed it.
- ☞ That restrictive covenant would have made the land worth £700,000.
- ☞ C enters into negotiations with AJ because of the duty to mitigate.
- ☞ C ends up with a deal whereby £100,000 is paid to AJ. The restrictive covenant, however, is not relaxed, it is replaced with a covenant "*not to erect ..... office buildings to accommodate more than 500 members of staff .....*".
- ☞ With that covenant in place the land is worth £900,000, £100,000 less than it otherwise would have been.
- ☞ What is the measure of damages?

### 1. Step 1:

### 2. Step 2:

- ☞ P wants to purchase a dentist's practice and agrees a price with V - £53,750.
- ☞ The solicitor acting for P is negligent and causes a delay during which R offers £60,000, which V accepts. P tries to buy somewhere else at about the 54k mark but that falls through too.
- ☞ P then realises that he really wants that practice and three months later persuades R to sell it for £92,500. At that point it is really only worth £75,000.
- ☞ What is the measure of damages?

- A. £92,500 minus £53,750 (the difference between what was eventually paid and what P could have got it for absent the negligence) = £38,750?
- B. £75,000 minus £53,750 (the difference between what it should have cost before the negligence and what it should have cost after) = £21,250
- C. £60,000 minus £53,750 (the difference between what P could have got it for immediately after the negligence and what he could have got it for before) = £6,250.

*Simpson v Grove Tompkins & Co* (1982) Sol J 347.

*Ford v White* [1964] 1 WLR 885

*Dent v Davis Blank Furniss* [2001] Lloyd's Rep PN 534

3. **Step 3:**

In most property related prof neg cases the loss is not a loss of a right to bargain as in *Wrotham Park Estate Co v Parkside Homes* [1974] 1 WLR 798.

4. **Step 4:**

5. **Step 5:**

Day 1 = date of breach.

Why?

Sale of Goods Act 1979, section 53:

*(2) The measure of damages for breach of warranty is the estimated loss directly and naturally resulting, in the ordinary course of events, from the breach of warranty.*

*(3) In the case of breach of warranty such loss is prima facie the difference between the value of the goods at the time of delivery to the buyer and the value they would have had if they had fulfilled the warranty.*

6. **Step 6:**

7. **Step 7:**

8. **Step 8:**

*Johnson v Agnew* [1980] AC 367 (HL).

Nov 1974: the V's are in default on their mortgage and owe £100.

They are forced to, and agree sell the property to P for £110.

P fails to complete. V gets order for SP.

Order for SP cannot be enforced.

July 1975: the mortgagees sell the property and raise £80

V seeks damages in lieu against P, giving credit for the £80.

By this time there is more interest on the £20 that the mortgagee has not recovered.

Are damages measured at the date of the breach (not encompassing that extra interest) or as at the date when sp fails (encompassing it)?

*Alcoa Minerals of Jamaica v Herbert Broderick* [2002] 1 AC 371 (PC)

Claimant buys property for £1m.

Develops it and spend £500k.

Then finds there is a restrictive covenant which solicitors should have picked up.

Are damages:

- 1) The difference between what it's worth at the date of breach, with and without the restriction; or
- 2) The difference between what it's worth at the date the restriction was discovered, with and without the restriction;

Or

- 3) The difference between what its worth when the works are done / attempt to lift the restriction fails, with and without the restriction;

Or

- 4) The difference between what it's worth at the date of trial with and without the restriction?

See by analogy: *Smith v South Gloucestershire Council* [2002] 3 EGLR 1 (CA)