# Dilapidations Update

Legal Excellence + Commercial Sense

Cleaver Fulton Rankin

## INTRODUCTION

- Aaron primarily acts on behalf of high profile retail tenants in his role as Director in the Dispute Resolution Team at Cleaver Fulton Rankin. Aaron advises a range of clients in contested property matters such as Landlord and Tenant disputes, dilapidations, adverse possession, derogation from grant, rent recovery and forfeiture. His Commercial Litigation Practice has significantly grown in recent years. He has recently advised in high value mediations and other forms of alternative dispute resolution.
- Maria is a Solicitor within the Dispute Resolution Department at Cleaver Fulton Rankin. She regularly advises on a range of contentious property matters to include Landlord and Tenant disputes, dilapidations, rent recovery and forfeiture. Maria has recently advised in alternative dispute resolution procedures to include mediation.

## What today is all about?

- Review of dilapidations
- With assistance of case law
- Looking at the principles flowing from this
- Acknowledging that Northern Ireland is different to other jurisdictions
- Looking at alternative means of resolving disputes, namely mediation
- Assessing how this impacts your practice

## How Northern Ireland is different to other jurisdictions

- No equivalent to The Law of Property Act 1925, Landlord and Tenant Act 1927 or the Leasehold Property Repairs Act 1938.
- Fundamentals of dilapidations are set out in the Conveyancing Act 1881 and the Business Tenancies (Northern Ireland) Order 1996.
- Current RICS Dilapidations Guidance Notes sets the protocol.
- Due to lack of dilapidations precedents in NI, English dilapidations cases may be referred to but not treated as binding precedents.

## First and Foremost - The Lease

- The very first thing that we will do is to review the lease documentation and assess the obligations therein. It is important that we are given the full bundle of title. The bundle will sometimes include an Agreement for Lease or a Schedule of Condition. These documents may extend or reduce the Tenant's obligations or they may help to qualify those obligations. I will come back to this is due course.
- Ultimately the Lease records the deal done between the parties
- The Lease may only be amended by further Deed e.g. Deed of Variation or formal Licence

## The Demised Premises

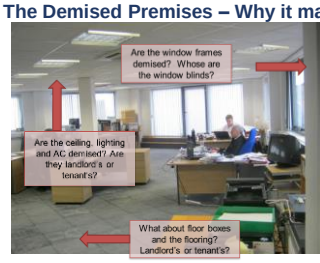
## The Demise

- What, precisely, has the landlord demised to the tenant?
- Position might be obvious if the tenant is leasing the whole building but considerable difficulties can arise with multi-let properties
- Whilst most modern leases are specific about extent of the demise confusion can still arise
- In default of clear wording, the demise includes the interior and exterior of leased premises

## The Demised Premises

- Mistake 1: Having a poor description of the "Demised Premises" in the lease
- Mistake 2: Inaccurate, black and white floor plans

## The Demised Premises – Why it matters



## The Demise


## COVENANT TO REPAIR

- Covenant may limit liability e.g. by reference to schedule of condition or excluding 'fair wear and tear'
- Covenant may extend liability e.g. "maintain renew cleanse repaint redecorate and otherwise keep the building in good and tenantable condition"
  (wording from lease in Credit Suisse v Beegas [1994] 4 All ER 803)

## Repair and/or Reinstatement

- Very often a Lease will contain a repair clause and a reinstatement clause or a later document will require reinstatement.
- Tenants often fall foul of reinstatement.
- The premises may have been kept in good repair striking out the Landlord's first remedy however the Landlord may then resort to a re-instatement clause. Equally the Landlord may assess both claims and prefer to bring a claim for re-instatement.
- Practical Example – Up-Market Restaurant Premises in South Belfast.
- Repair Clause -To repair and during the said term to keep the demised premises (save and except the main structure thereof)…in good and tenantable repair and condition (except in respect of any injury or deterioration occasioned by ordinary wear and tear or by accidental fire or by lightening tempest or other inevitable accident or by any defects for which the Lessor my be liable in repair in the roof and walls) and make good any stoppage of or damage to the drains of the demised premises or the building caused by the negligence of the Lessee, his workmen, servants, employees or licences;

## Repair and/or Reinstatement

By a licence to complete a substantial renovation of the restaurant premises the Tenant later agreed with the Landlord to:-

- "…At the expiration or sooner determination of the Lease required by the Lessors well and substantially to reinstate the premises but not improve in such manner as the Lessors and their Building Surveyors shall direct…"
- The premises were left in relatively good condition on the grounds that the Landlord may have preferred to re-let them as restaurant premises. The Landlord however heavily relied on the re-instatement obligations to improve its claim/windfall. The Landlord directed that the premises should have been re-instated to a shell finish.
- The Landlord's claim was presented at a level of circa £130K and was eventually settled at circa £40K

## Reinstatement – why is it important?

**£5 sq ft** **£20 sq ft**

A landlord's view: Valley gutter, generally free from defects, there are isolated missing cover caps, note the gutter is free flowing.

A tenant's view: Valley gutter showing widespread corrosion, missing fixings and covers caps, the waterproof membrane is severely deteriorated.

## SCHEDULES OF CONDITION

- In our experience, tenants generally don't get the right protection.
- The tenant's expectations that they should be able to walk away from the building liability free in 3 or 5 years time, is rarely met.
- The images are almost always too poor to use, are black and white, and fail to give any meaningful protection.
- The descriptions are often poorly considered; words such as 'numerous', 'widespread', or 'extensive' rather than real quantities are used. This makes it difficult to get a claim against a tenant when, despite being sure that the whole of the building is in poor condition, you can't prove it.
- Schedules of condition often go missing and we're often left with the evidential difficulty in trying to establish what the condition may have been a number of years prior.
- The impact is generally lost after a number of years, especially if the documents are poorly drafted or the defects are extensive.

## SCHEDULES OF CONDITION

- A landlord will want to give away as little as possible.
- Don't be surprised that the language differs in landlord's Schedule of Condition compared to tenant prepared one.
- Landlords often object to phrases such as 'wide spread' or 'severally' and as a result there is more detailed docs with quantities.
- A tenant's view should of course be rather different, there are a few ways of approaching this. The tenant is more likely to try for very general comments in a very broad document or in a very detailed document to suit, but comments which give maximum reduction of their liabilities. Such phrases may include 'widespread' or 'severely' rather than quantifying the extent. Comments may include, for example, 'the roof sheets are severely degraded'… 'the roof bolts are extensively degraded'… 'the gutters are corroded', etc., but this approach is often rejected by landlords, the fall back is lots of quantities and lots of detail.

## CASE STUDY – BREAK OPTIONS

- Tenant leased commercial premises from the Landlord. Those premises were of a substantial size.
- The Tenant purported to serve a break notice terminating the tenancy in January 2010.
- The premises were originally let for 15 years. The break notice was served at 10 years.
- "…If the Tenant shall be desirous of determining the present Lease at the end of the first 10 years of the term…it shall deliver to the Landlord not less than 12 months prior notice in writing and shall pay all rents and service charges and shall have performed and observed to a reasonable extent all the covenants and conditions hereinbefore contained."
- The lease contained a covenant to "…repair and keep in repair the whole interior of the premises". It also contained redecoration requirements.
- The Landlord's Surveyor estimated the state of disrepair at circa £400K.

## CASE STUDY – BREAK OPTIONS

- The Tenant's Surveyor estimated the value of disrepair/re-decoration at circa £200K.
- The key point was that the building was in disrepair at the break date.
- The argument centred on the wording of the break clause.
- The Tenant argued that it had reasonably complied with its covenants and that the Landlord should be estopped from relying on the strict requirements of the same because of representations allegedly made by the Landlord during break discussions.
- The Tenant asserted that the Landlord had entered into negotiations and made representations to the effect that the Tenant could stay in the building for as long as necessary and that they would deal with dilapidations thereafter.
- The Tenant's potential exposure stood in excess of £5million – being the value of the dilapidations plus the additional 5 years of rent.
- The matter proceeded to Mediation and ultimately resolved on confidential terms.
- **BUT LEARN THE LESSON – both sides had heavy cost consequences. Our recommendation – in advance of the break date and actively negotiate with the Landlord.**

Cases

## Hammersmatch Properties (Welwyn) Limited v Saint-Gobain Ceramics and Plastics Limited Saint Gobain Abrasives Inc [2013] EWHC 2227 (TCC)

- Purpose built 1930s industrial and office building
- Lease dated 14 December 1984
- c1999 discussions came about regarding redevelopment and lease surrender
- Lease end 2009 with a dilapidations schedule prepared for c £6.8m
- Tenant initially intended to undertake works and prepared tenders
- Unsuccessful mediation in September 2010

## Mr Justice Ramsey's 'checklist'

Consideration was given to established dilapidations principles:

- A covenant to keep in good repair is not engaged unless there exists a state of disrepair, that is a deterioration from some previous physical condition:
- *Post Office v Aquarius Properties Ltd*
- *Anstruther Gough Calthorpe v McOscar*
- *Lister v Lane*
- *Ravenseft Properties Ltd v Davstone (Holdings)*

## Mr Justice Ramsey's 'checklist'

- If there is a state of disrepair it has to be established that the item is below the standard of repair contemplated by the covenant and, if so, what remedial work is needed to restore that item to that standard?

And

- The appropriate standard of repair is such repair as having regard to the age, character and locality of the premises, would make them reasonably fit for the occupation of a reasonably minded tenant of the class who would be likely to take them:
- *Proudfoot v Hart*
- *Mason v Totalfinaelf UK Ltd*

## Mr Justice Ramsey's 'checklist'

- The standard of repair is an objective one which is to be ascertained by reference to the circumstances at the date of the lease and what a reasonably minded tenant would require to render the premises reasonably fit for use as a place from which to run its business:
- *Fluor Daniel Properties Limited and others v Shortlands Investments Limited*

## Mr Justice Ramsey's 'checklist'

- The question is what would be required to make the premises reasonably fit for occupation, not what an incoming tenant would require at the end of the lease
- *Westbury Estates v Royal Bank of Scotland*
- *Carmel Southend Limited v Strachan and Henshaw Limited*

## Mr Justice Ramsey's 'checklist'

- (a) The appropriate standard of repair must take account of the age of the building. The obligation is not to return the premises to the condition that they were in at the start:
  - *Mason v TotalfinaElf (UK)*
- (b) In considering the appropriate standard of repair it is relevant to consider the user clause in the lease:
  - *Simmons v Dresden*

## Mr Justice Ramsey's 'checklist'

- When considering whether replacement rather than repair is the appropriate standard , Mr Justice Ramsey considered 4 factors:

1. Replacement is only required if repair is not reasonably or sensibly possible: *Dame Margaret Hungerford Charity Trustees v Beazeley [1993] 2 EGLR 149 and Carmel Southend Limited v Strachan and Henshaw Limited [2007] 3 EGLR 15.*
2. It is for a claimant to prove relevant disrepair and that it is of such an extent or nature that repair is not reasonably or sensibly possible: *Mason v TotalfinaElf (UK) [2003] 3 EGLR 91.*
3. Where a reasonable surveyor might equally well advise either repair or replacement, damages are to be assessed by reference to the cost of repair unless replacement would be cheaper: *Riverside Property Investments v Blackhawk Automotive [2005] 1 EGLR 114; Carmel Southend Limited v Strachan and Henshaw Limited [2007] 3 EGLR 15.*
4. The fact that an item has exceeded its indicative life expectancy so that it would or might be economic for a prudent owner to replace it does not mean that it is not in a good and safe working order repair and condition: see *Fluor Daniel Properties v Shortlands [2001] 2EGLR 103 at 111G and Westbury Estates v RBS [2005] CSCH 177 at [35-37].*

Alternative Dispute Resolution

## MEDIATION

- Confidential process whereby a neutral third party spends, typically, a day with the parties to a dispute and tries to facilitate a settlement.
- The Mediator does not act as a judge or arbitrator. He expresses no views of his own as to the rights and wrongs of the dispute or the likely outcome of any litigation.
- In the Civil Courts in Northern Ireland there has been a recent trend to include Mediation.
- As part of the judicial process of review, particularly in respect of commercial actions, the Court has the power to suggest to the parties that they consider alternative forms of dispute resolution, apart from litigation.
- Sometimes, mediators may be called on to evaluate the claim or issue and the strengths and weaknesses of a particular case (evaluative mediation).
- The mediation agreement will usually require the parties to treat all discussions and documents as confidential and without prejudice. Usually, what is said or written cannot be used in later proceedings if the mediation does not settle, but there are some limited
- The parties have complete choice over the selection of the mediator and can therefore choose the mediator who is most appropriate for the dispute.

## MEDIATION

**Advantages**

- Mediation provides a private forum in which the parties can gain a better understanding of each other's positions and work together to explore options for resolution through a neutral third party.
- The mediation process allows more creativity and flexibility over settlement options than the court or arbitration process.
- Mediation can be used in almost any kind of case, from small claims through to complex high value multi-party disputes and appeals.
- Conversely, the parties cannot choose a judge if the matter goes to full trial.
- The legal costs, lost opportunity costs and management time can be reduced through mediation.
- Mediation can produce outcomes that might not be possible via determination by the court or arbitration e.g. A new lease agreement: an agreement to allow tenant's contractor to undertake work or other outcome not available in court proceedings

## MEDIATION

- The assistance of a mediator is a powerful tool for overcoming a lack of co-operation in mediation; the mediator may even terminate a mediation where he considers that a party is not participating in good faith. There is a misconception that settlements reached in mediation are not enforceable.
- Most mediation agreements stipulate that the settlement reached in mediation will be enforceable as a contract once it is in writing and signed. There are other forms of giving effect to an agreement reached at mediation, including by court orders.

## MEDIATION

**Disadvantages**

- If unsuccessful, mediation will add time and cost to the process of resolving the dispute.
- There is a fear that mediation will expose the client's hand or strategy. As nothing said in mediation may generally be used in later proceedings, the risk in mediation is the inadvertent release of information to the other side that may give some indication of future litigation strategies or may alert the opponent to possible avenues of inquiry if the dispute does not settle at mediation. Generally, however, strategic discussions will occur in private session with the mediator, who is acutely aware of his duties of confidentiality.
- Mediation is "non-binding" and some argue that an uncooperative party could manipulate its voluntary nature. The assistance of a mediator is a powerful tool for overcoming a lack of co-operation in mediation; the mediator may even terminate a mediation where he considers that a party is not participating in good faith. There is a misconception that settlements reached in mediation are not enforceable.
- The mediator cannot order or require disclosure, although the extent of disclosure can be agreed between the parties as part of the process.
- Parties who consider that they have a strong case, may feel that this is not adequately recognised through the mediation process. If this is the case, it may be worth considering a more evaluative approach to mediation.

Questions

Cleaver Fulton Rankin

Thank you