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✦ CHARTERED SURVEYORS ✦

Dilapidations: Diminution in Value

CPD Foundation
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SUMMARY

- Quick revision: *What is a dilapidations claim?*
 - Damages
 - RICS Guidance Note and the Protocol
- Classification of claims
- The role of the valuer
- Landlord's intentions
- General advice

WHAT IS A DILAPIDATIONS CLAIM?

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Building A –
in
compliance



Building B –
actual
repair

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WHAT IS A DILAPIDATIONS CLAIM?

- Mainly commercial property
- “Terminal”
- Damages claim
- The starting point: the contractual claim
 - Includes consequential losses

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WHY A “DAMAGES” CLAIM?

- Can only claim for the loss suffered, if any

- *Ruxley v Forsyth*



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S18(1) LIMITATION

“Limb 1”:

*Damages for a breach of a covenant or agreement to keep or put premises in **repair** during the currency of a lease, or to leave or put premises in repair at the termination of a lease ... shall in no case exceed the amount (if any) by which the value of the reversion ... in the premises is diminished owing to the breach...*

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LIMB 1:

- Damages for repair breaches cannot exceed diminution in value of landlord's reversion

LIMB 2:

- There will be no damages for repair breaches where the building is to be demolished



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THE BALTIC SURVEYOR

- Damages mean *money*, not replacement: financial restitution, not physical restitution
- Damages cannot put the landlord in a better situation that he was in before – i.e., no betterment



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GUIDANCE NOTE AND PROTOCOL

- RICS “Dilapidations in England and Wales”, 7th edition (September 2016)
- Dilapidations Protocol



DIFFERENT TYPES OF CLAIM

1. Cost of works
2. Straightforward
3. Deeper analysis
4. Possible futures

TYPE 1: COST OF WORKS

- Majority of cases fall in this category
- Where landlord's loss is equivalent to cost of works
- Building A/Building B
- Valuation input generally not necessary



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TYPE 2: STRAIGHTFORWARD

- Cost of works less supersession/dilution
- Three methods:
 - Comparables
 - “Stand in the Street”
 - Analysis
- *Shortlands*
- Valuation input probably required



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TYPE 2: STRAIGHTFORWARD

Same in valuations A and B

1	Estimated rental value ("ERV")		29,500
2	Years' purchase in perpetuity at:	8.00%	12,5000
3	Investment value		<u>368,750</u>
4	Investor's acquisition costs at:	4.75%	16,721
5	Gross development value ("GDV")		<u>352,029</u>
6	Sale costs at:	2.75%	9,681
7	Net sale proceeds		<u>342,348</u>

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TYPE 2: STRAIGHTFORWARD - VALUATION A

In compliance: 50-week project

7	Net sale proceeds		342,348
8	Scott schedule work		0
9	Less supersession		<u>0</u>
10	Net cost of work attributable to the outgoing tenant		0
11-20	Work and other costs		109,625
21	Profit to purchaser at:	20.00% of GDV	<u>70,406</u>
22	Total deductions unrelated to purchase price		<u>180,031</u>
23	Gross cost		<u>162,317</u>
24-27	Value in compliance with covenants at the date of expiry		<u>148,011</u>

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TYPE 2: STRAIGHTFORWARD - VALUATION B

In actual: 54-week project

7	Net sale proceeds per line 7 on Valuation A		342,348
8	Scott schedule work	100,000	
9	Less supersession	32,507	
10	Net cost of work attributable to the outgoing tenant	67,493	
11-20	Work and other costs	202,191	
21	Profit to purchaser at: 20% of GDV	70,406	
22	Total deductions unrelated to purchase price		272,597
23	Gross cost		69,751
24-27	Value in actual condition at the date of expiry		63,284

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TYPE 2: STRAIGHTFORWARD - DIMINUTION

Diminution summary

Valuation A: value in compliance with covenants	148,011
Valuation B: value in actual condition	63,284
Diminution in the value of the landlord's reversion	84,727
But say	£85,000

TYPE 3: DEEPER ANALYSIS

- Very theoretical
- Avoid premature approximation
- Consider likely medium and long-term future
- Probability analysis and deferment
- Other things to consider: beneficial breaches, schedules of condition...



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TYPE 4: MULTIPLE POSSIBLE FUTURES

- Similar to Type 3
- Very rare!
- Where future of the building or landlord's intentions are uncertain
- Consider all of the possible options



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BRUNTWOOD (AFTER)



LANDLORD'S INTENTIONS

The Scott Schedule contains the **true views** of NAME being the building surveyor appointed by the Tenant to prepare the document.

I NAME confirm that in my opinion:

All the works set out in the Scott Schedule are **reasonably required** to remedy any breaches of the Tenant's covenants or obligations.

Where it is considered that items in the Schedule of Dilapidations are likely to be superseded by works to be carried out by the landlord or are likely to be superseded by the landlord's intentions for the property then:

- This has been stated in the Response/Scott Schedule
- Particulars have been given of the material on which the tenant or tenant's surveyor relies
- The items to which this view is relevant have been identified.

The costings **are reasonable**.

GENERAL ADVICE - LANDLORDS

- Don't let the tail wag the dog
- Don't rely on the money
- Do the works (but see above)
- Do *the works*
- **Be reasonable**

GENERAL ADVICE - TENANTS

- Plan ahead
- Take advice
- Do the works
- ***Be reasonable***



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GENERAL ADVICE

- Think about costs
- Everyone thinks it's unfair
- ***Be reasonable***



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DILAPIDATIONS INSURANCE?

- Fixes tenant's maximum exposure
- Based on rights of light model
- New product
- Tenants only

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