

# Bulletin

June 2013

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Welcome to the June edition of Clyde & Co's Real Estate Bulletin prepared by members of our real estate and property litigation team. Our bulletins are aimed at keeping you up to speed with recent key developments in the real estate practice area.

In this issue we examine the issues to be considered in assessing a tenant's liability for terminal dilapidations, and discuss the case of *Sunlife Europe Properties Limited v Tiger Aspect Holdings Limited (1) Tiger television Limited (2)* (2013).

Next we look at the impact of the proposed reforms in the Law Commission's Consultation Paper No 210 regarding Rights to Light. Two members of our dispute resolution team then give an insight into the implications of the heavily publicised Growth and Infrastructure Bill.

We also discuss the differentiating factors and the relevance of whether an item is a 'fixture' or a 'fitting' in a sale of a property or in a dilapidations claim, and examine the recent case of *Earl of Cardigan v Moore* (2012).

Finally we look at break clauses, and discuss the important recent case of *Marks & Spencer Plc v BNP Paribas Securities Services Trust Company (Jersey) Limited and another* [2013] EWHC 1279 (Ch), where it was held that the tenant should not be short changed when exercising a break clause part-way through a quarter.

If you would like further information on any issues raised in this newsletter please contact one of the Clyde & Co representatives, listed on the last page of this newsletter.



## Terminal dilapidations – the facts, law and a practice example

Georgina Redsell, Associate

The lack of development prospects has meant that many commercial landlords have looked to their tenants to fully comply with their repairing obligations at the end of their leases. In the light of difficult trading conditions many tenants have vacated, often having carried out very limited or no repairs. This has led to a significant rise in terminal dilapidations claims.

The case *Sunlife Europe Properties Limited v Tiger Aspect Holdings Limited (1) Tiger Television Limited (2) (2013)* deals with many of the current issues to be considered in assessing a tenant's liability for terminal dilapidations.

### The facts

The Claimant (**Sunlife**) was the owner of combined office and retail premises at Soho Street and Soho Square, London. The premises had been let to the Second Defendant (**Tiger**) under two leases with full repairing covenants. The leases were for a term of 35 years and came to an end on 14 November 2008.

Sunlife claimed £2.172 million in terminal dilapidations.

It was Tiger's case that Sunlife's claim was capped by the amount of the diminution in value of the premises as a result of Tiger's breaches of the repairing covenants, which its expert said was no more than £240,000.

The thrust of their argument was that in order to let the premises in 2009, Sunlife would have had to carry out a significant upgrade and refurbishment. If Tiger had carried out the maintenance and repair required by its obligations, the premises could only have been let at a very substantial discount.

Tiger later accepted that, subject to some fairly minor improvements (such as an upgrade of the main toilets), the premises could be let to a tenant of the appropriate type if Tiger had complied with its covenants.

### The law

Mr Justice Edwards-Stuart found that the measure of recoverable loss in a terminal dilapidations claim is the lower of:

1. The total of (a) the cost of remedying the defects and (b) any rent actually lost and other expenses actually incurred whilst the defects are being remedied; and
2. The diminution in the value of the landlord's reversion, as at the term date, caused by the breaches – i.e the statutory cap contained in section 18(1) of the Landlord and Tenant Act 1927.

He also reached the following conclusions on the law in relation to arguments frequently advanced by tenants who fail to carry out repairs:

1. The tenant is entitled to perform its covenants in the least onerous way open to it and this should be the starting point in any assessment for damages.
2. The tenant is required to deliver up the premises in good and tenantable condition and with the M&E systems in satisfactory working order but not with new equipment or equipment that has any particular remaining life expectancy.
3. Where there are covenants against making alterations to the premises the tenant is not entitled to deliver up the premises in a condition that involves any material alteration to the building or fixtures as demised. The fact that the landlord can consent to any such alteration does not affect the basic obligation.

1. Where the requirement to put and keep the premises and fixtures in good and tenable condition involves the replacement of plant that is beyond economic repair, the tenant is required to replace it on a like for like or nearest equivalent basis. The tenant is not required to upgrade it or bring it into line with current standards.
2. Any claim by the landlord is subject to the general rules that: (a) he cannot recover costs that he could have avoided by acting reasonably; and (b) he cannot recover the cost of remedial work that is disproportionate to the benefit obtained.
3. Where there is a need to carry out remedial work, however, the fact that the landlord has carried out more extensive work than was caused by the breach does not prevent the landlord from recovering such costs as would have been necessary to remedy the breach.
4. Where market conditions at the end of the lease mean that some sort of refurbishment or upgrade is required to enable the landlord to re-let, a tenant is not liable for costs to the extent that such works would be rendered abortive by the need to upgrade or refurbish the building (i.e supercession).

5. Where a tenant is in breach of covenant the court is entitled to infer that the remedial work is necessary to remedy the breach unless the tenant demonstrates to the contrary.

Upon applying these principles the Judge found that the landlord was entitled to recover £1.4 million, being the diminution in value of the premises.

Despite numerous arguments raised by Tiger, this case is a useful reminder of what will and will not be assessed in this type of claim and that tenants should not expect to escape liability for the cost of reasonable repairs.

*For more information about terminal dilapidations, please contact Georgina Redsell or your usual Clyde & Co contact.*



## Rights to light – will the proposed reforms see the light of day?

*Keith Conway, Consultant*

Responses to the Law Commission Consultation Paper No 210 regarding Rights to Light recently closed. The views of developers, landowners and practitioners continue to be polarised. There is a sharp contrast between promoting developments, particularly having regard to the shortage of housing and the need for regeneration, and protecting the amenity that landowners currently enjoy.

### Influencing the right to light – latest influences

More recent decisions of the Courts have reconfirmed that developers cannot assume they can appropriate rights to light and simply buy them off if and when a claim is made. For example, in the 2010 *Heaney* case the developer was ordered by the Court to pull down the infringing parts of the completed development. In the 2007 *Tamaraes* case the Court looked to compensate the owner of the right to light by apportioning to it a significant part of the developer's profit gained as a consequence of the appropriation.

As a result developers' attempts to gain certainty by negotiations continue to be fraught with difficulties as 'advised neighbours' will refuse to openly negotiate and insist that they have a right to seek an injunction rather than be awarded damages by the Court. Developers may turn to insurers to provide some better certainty in their development and finance appraisals. However, this is often a significant additional expense and crucially does not resolve the right to light and other issues between developers and their neighbours.

In order to promote 'the correct balance' and provide a 'more transparent, fairer and easier' environment the Law Commission have suggested four changes to the law:

- Abolish the ability of a neighbour to acquire a right to light by prescription (i.e. long enjoyment of over 20 years)
- A new statutory test to clarify when damages should be granted instead of an injunction
- A new statutory Notice of Proposed Obstruction ("NPO") requiring neighbours to make clear to developers whether they will be applying for an injunction to prevent an interference with their rights to light

- Allow developers to apply to the Lands Tribunal to discharge or modify rights to light that are obsolete or have no practical benefit

### Future abolition of rights to light being acquired after 20 years enjoyment

The Law Commission's view (shared by developers) that rights to light acquired by 20 years uninterrupted enjoyment (known as 'prescription') should be abolished was not shared by most landowners or their advisers. However, as the previous Law Commission's 2011 proposal in respect of other easements was to retain 'prescription', any reform will need to further consider the desirability of a different regime for rights to light.

Prospective purchasers of land have for many years had to assess what can be built on land taking into account the possibility that neighbours may seek to prevent or restrict development. The real issues are not the creation of rights to light by long enjoyment but the fact that the land owner (or developer) subjected to the right to light does not observe the acquisition of the rights to light as it would in the case of, for example, a right of way. Further, there is great uncertainty surrounding whether and when those rights will be enforced (if at all) and if so whether this will be by way of an injunction preventing an infringement (whether proposed or complete). Additionally there is great uncertainty in respect of damages or the level of compensation to be paid to the neighbour, assuming an injunction is not granted, and whether this will be by way of a share of the developer's profit caused by the infringement (the 'ransom basis') or by way of a hypothetical negotiation between a willing developer and a willing neighbour (the 'non ransom basis') to acquire or release the right to light.

## Achieving more certainty

The seemingly unfair issue for developers is the ability of a neighbouring owner (residential or commercial) to assert a valid right to light but take no further action and thereby blight any proposed development notwithstanding the grant of a planning permission. The neighbour may, negotiate solely on a 'without prejudice' basis whilst 'openly' contending it reserves and will rely upon its rights to seek an injunction. As demonstrated in the *Heaney* case this might lead to an order to demolish the infringing parts of the development if the developer proceeds to build notwithstanding the neighbour's reservation of rights. As a result of the *Heaney* case, the Law Commission has recommended two reforms:

- A statutory test: A statutory test determines when the Court should grant an injunction which focuses on whether the grant of an injunction to stop the infringing part of a development or, if built, to demolish that part would be disproportionate having regard to the relative oppression to the developer and neighbour; and
- A 'put up or shut up' notice (the NPO): Whilst the final details ideally require more thought, the essence of the proposal is that a developer would serve a NPO attaching details of its proposed development and the neighbour would then have to serve a counter notice within a four month period stating whether it objects to the proposed development. If a counter-notice is served the developer and neighbour then have a four month window to negotiate, at the end of which the neighbour is required to issue proceedings for an injunction. If the neighbour does not issue proceedings for an injunction that right is lost in respect of the proposed development or one which causes no greater infringement. The neighbour's remedy in damages is unaffected by the NPO.

The proposals provide that during the eight month procedure the developer cannot infringe the neighbour's right to light and the developer is only allowed to serve one NPO in any five year period. These are aspects that may need some fine tuning or reconsideration. For instance the Property Litigation Association have suggested a number of refinements including a procedure to extend the eight month period by mutual agreement if the parties wish to continue negotiations; a forum for resolving any issues that arise in relation to how the proposed development scheme will infringe a neighbour's right to light; and reconsideration of whether the imposition of a five year moratorium preventing developers serving a second NPO for a larger scheme is really striking a 'correct and fair balance'.

## Compensation

Opinions also remain divided as to the appropriate level of compensation in relation to a significant infringement where no injunction preventing development is sought or where damages in lieu of an injunction are ordered by the Court or negotiated between the developer and neighbour. If the starting point is that a neighbour should not be forced to release its right to light then the 'ransom basis' – a share of the developer's profit gained as a result of that part of the development that infringes the right to light or is gained as a result of the release – seems inevitable and arguably reasonable. This approach appears to be the currently favoured by the Courts provided that the amount awarded also 'has to feel right'. The developers have however argued for a number of alternatives designed to achieve a 'non ransom basis'. These include a hypothetical negotiation between a willing developer and a willing neighbour and a cap based on a sliding scale of the market value of the neighbour's land. The Law Commission was undecided on this topic and recognised the fact that none of the suggested alternatives provided logical or real improvements.

**Proposed applications to the Lands Tribunal to discharge or modify rights to light:** These proposals are linked to those recommending the abolition of prescription and to the unresolved issues already mentioned in respect of compensation. The Law Commission's suggestions favour a payment to the neighbour of an amount to reflect the diminution in the market value of the neighbour's property caused by the discharge or modification of the neighbour's right to light. The issue that remains to be resolved is whether the proposed jurisdiction will be limited to obsolete and abandoned rights to light and to ones that coincide with previous apertures (in which case there will be relatively few applications) or whether a much wider remit will be enacted.

**Conclusion:** Having regard to the many unresolved matters and ever present pressures on parliamentary legislative time developers and neighbouring landowners may find that despite the clear need for reforms none becomes a reality. We shall of course keep you well informed.

*Keith Conway is Chairman of the Law Reform Committee of the Property Litigation Association and a Consultant in the Clyde & Co real estate group. If you have any questions regarding rights to light, please contact Keith Conway or your usual Clyde & Co contact.*



## Understanding Ground (F) lease renewals under the Growth and Infrastructure Act

*Mike Lewis, Senior Associate*

*Liam Floodgate, Trainee Solicitor*

The heavily publicised Growth and Infrastructure Bill received Royal Assent on 25 April and amends existing legislation in relation to residential planning so as to encourage development. In the following article, we revisit the opposition to lease renewals under Ground (F) of the 1954 Act in light of the Growth and Infrastructure Act.

These changes include:

1. A right for developers to appeal directly to the Planning Inspectorate to modify planning obligations that the developer considers make schemes for development unviable. In particular, developers can make formal requests to alter or discharge affordable housing obligations in section 106 agreements so as to ensure developments are viable.
2. Widening permitted development rights so as to allow offices to be redeveloped for residential use. The following link shows the areas which are exempt from the relaxation of the permitted development rights – <https://www.gov.uk/government/publications/areas-exempt-from-office-to-residential-change-of-use-permitted-development-right-2013>
3. Allowing a developer to apply for planning consent directly from the Planning Inspectorate, where a council has ‘consistently failed to meet statutory requirements to consider applications on time.’

Whilst these measures encourage residential development there is often still the issue of terminating existing commercial tenancies prior to redevelopment. This is not a problem where the existing tenancies are contracted out of the Landlord and Tenant Act 1954 (**the Act**) and where the lease contains a break clause allowing the landlord to terminate the tenancy. However, where the tenancies are not contracted out of the Act (in the absence of the tenant agreeing to vacate) it is necessary for the landlord to oppose the tenant’s statutory right for a lease renewal under the grounds specified in the Act.

For the redevelopment of office buildings to residential buildings it is likely that the landlord will rely on Ground (F) to oppose the lease renewal.

### Summary

Ground (F) provides that the landlord must prove their intention to demolish or reconstruct the premises or a substantial part of the premises. There are many matters which assist with proving this intention, for instance building contracts and proof of financing, however in the majority of cases the sticking point is with regards to planning. With the new planning regime in place, it is thought that the Landlord’s ability will become more straightforward.

*The above is a very brief outline and if you are thinking of redeveloping and would like more detailed advice on obtaining vacant possession and contested lease renewals please contact Mike Lewis or your usual Clyde & Co contact.*



## Real estate litigation in practice – ‘fixtures’ or ‘fittings’?

*Mike Lewis, Senior Associate*  
*Joanna Brooke, Paralegal*

Whether an item is a ‘fixture’ or a ‘fitting’ is relevant not just on the sale of a property but also in dilapidations claims and in determining whether vacant possession has been given for the purposes of operating a break clause.

The recent case of *Earl of Cardigan v Moore* [2012], which concerned paintings in the Earl’s ancestral home and whether these could be sold separately or were part of the reality. The case offers a reminder that whilst the distinction between fixtures and fittings may appear simple, disputes can still arise.

It is generally accepted as a rule that:

- fixtures are items annexed to the land; and
- fittings are those items which are free standing.

When considering whether an item has become annexed to the land (and has therefore become a fixture), the Court in the Earl of Cardigan’s case reviewed the authorities and reconfirmed that they must have regard to two questions: the degree of annexation and, most importantly, the purpose of the annexation.

The pictures in question were fixed into recessed wall panels in the Earl’s home with large, heavy-duty hooks. Whilst the Court considered that they were fixed firmly enough to become part of the wall had this been the intention, they concluded that the paintings were capable of removal without damage if ordinary skill and care was used. Therefore, it was determined that the purpose of the annexation was to enhance enjoyment of the paintings.

The Court found that the paintings were not intended to become a fixture, and therefore remained a fitting despite the high degree of annexation. Accordingly the pictures could be sold separately and were not part of the reality.

*If you wish to discuss this case or would like to discuss your own circumstances, please contact Mike Lewis, or your usual Clyde & Co contact.*



## Marks & Spencer Refunds....

Jo Webster, Associate

In the recent case of *Marks & Spencer Plc v BNP Paribas Securities Services Trust Company (Jersey) Limited and another* [2013] EWHC 1279 (Ch) the tenant, Marks & Spencer Plc (**M&S**), established that they should not be short changed when they exercised a break clause part-way through a quarter. However, will this apply to all cases? The High Court was on this occasion prepared to imply a term into the lease entitling the tenant to a repayment of the rent from the break date to the end of the quarter. This decision is the first departure from the previously widely accepted view that in the absence of an express provision, a tenant will not be entitled to a refund of any rent or other sums paid that relates to the period after a break date.

### Background

A tenant's right to break is often conditional on the payment of all sums due under the lease up to the break date. This condition is surprisingly something which a number of tenants will nevertheless fail to comply with.

The correct advice to a tenant has always been (and still remains) to pay all payments due under the lease in full and then face any difficulties recovering any amount overpaid from the landlord attributable to the period after the break date. However, in the recent M&S case, the Court found in favour of the tenant who, having successfully operated a break, requested a refund of the rent and other payments it had made for the period after the break date.

### Facts

M&S was the tenant at The Point building in Paddington under four materially identical leases. Each lease contained the right to break by giving a certain period of notice, subject to there being no arrears of the basic rent on the break date (and payment of a penalty premium equivalent to a years rent on or before that date). Rent under the leases was payable quarterly in advance, in the usual way. Break notices were duly served at the appropriate time, and subsequently, payments of the full quarter's rent, service charge and penalty payments were made.

M&S requested a refund of the sums paid for the period after the break date. The landlords refused this stating that there was no express term in the leases that required this.

The Court rejected M&S's arguments that the express terms of the leases provided for a refund of the rent and their arguments for restitution based on unjust enrichment of the Landlord. The Court ruled in M&S's favour that on the facts of the case it was an implied term of the lease that rent paid in respect of the period after the break date must be repaid after the lease had successfully been brought to an end in accordance with the break clause. The high level of the penalty payment was a distinguishing factor and the Court felt it was unlikely that it would have been the intention of the parties for the landlords to keep the full quarter's rent as well as the penalty payment. The Court also accepted that the proportion of the service charge and insurance rent paid after the break date should also be repaid.

## Implications and points to note

- In the absence of an express term, do not apportion rent and other payments up to a break date as this is most likely to invalidate the operation of the break
- Whilst the M&S case provides a good argument that the landlord should provide re-imbusement for the amounts attributable after the break date landlords are likely not to agree this unless a penalty payment for exercising the break is also required
- It may be that some tenant's who have operated breaks in similar circumstances to the M&S case over the past years will now seek to recover any sums attributable to the period after the break

*Marks & Spencer Plc v BNP Paribas Securities Services Trust Company (Jersey) Limited and another [2013] EWHC 1279 (Ch)*

*If you would like further information on break clauses, or to discuss this case further, please contact Jo Webster, or your usual Clyde & Co contact.*

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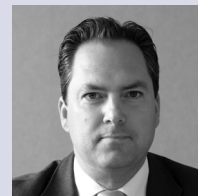
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