In the first of a two-part article on dilapidations claims, **Jonathan Ross** examines why they seem to be on the increase and presenting courts with ever more problematic issues

Dilapidations in the dock

While substantial dilapidations claims on lease expiry ('terminal dilapidations claims') are extremely commonplace and take up a large element of a property litigator's workload, they rarely proceed to trial and reported judgments are therefore somewhat rare and far apart. In fact, the last judgment of note prior to 2013 followed the PGF II SA v Royal & Sun Alliance plc case, which was decided in 2010.

However, 2013 has been a bumper year, with three cases decided within the space of three months, having been fought all the way in the Technology and Construction Court:

- Sunlife Properties Europe Ltd v Tiger Aspect Holdings Ltd & Anor [7 March 2013]
- Twinmar Holdings Ltd v Klarius UK Ltd [19 April 2013]
- Hammersmatch Properties (Welwyn) Ltd v Saint Gobain Ceramics and Plastics Ltd [14 May 2013]

In all three, the claimant landlord succeeded overall but in varying degrees. The details and implications of these will be discussed in a subsequent issue; the first part of this article seeks to examine:

- why are terminal dilapidations claims so common?
- why, particularly in the current era of mediation and alternative dispute resolution as an alternative to litigation, terminal dilapidations cases are reaching trial and/or proving difficult to settle early
- the future for dilapidations claims.

Repair terms

The legal principles involved in dilapidations claims are generally well established and confirmed in the judgments referred to. The difficulty lies in having to adapt and apply them to the different terms of each lease, and the facts of each case. It is, however, important to understand the following:

- In construing the standard of repair required, the court has to have regard to the age, condition and nature of the premises at the time of the letting as well as the length of the lease. The longer the lease, or the newer the premises, the greater the repairing obligation will be.
- Repair should be of a standard that makes the premises fit for occupation by a reasonably minded tenant of the class who would be likely to take a letting of the premises.
- Tenant are entitled to pursue the least onerous and cheapest repairs if they will satisfy its repairing covenant, and are not obliged to upgrade to modern requirements unless there is disrepair and this is needed to meet current regulations.
- Replacement is only justified if repair is not reasonably or sensibly possible, or current regulations so require, or replacement is the cheaper option.
- Where there is a need for remedial works, the fact that the landlord chooses to carry out more extensive works does not prevent them recovering the actual cost of repairs the tenant was liable for.
- Damages for disrepair in the common law are based on the cost of works and loss of rent/rates suffered. They are not based on actual loss suffered by the landlord save that, under the two limbs of Section 18 (1) of the Landlord and Tenant Act 1927, damages cannot exceed the diminution in value caused to the reversion by the disrepair. They cannot be awarded at all if the landlord intended at lease expiry to demolish or redevelop the building so that any disrepair would be superseded.
- Insofar as supersession is concerned, it is important for a tenant to focus on those repairs that, if they had been undertaken, would have been of no value due to the landlord. It is any improvement works or alterations a landlord would have undertaken even if the property had been delivered up in repair that lead to supersession; not the works a landlord carries out to premises left in disrepair.

See you in court?

There are a variety of reasons why terminal dilapidations claims are proving so common and so litigious.

Obviously, many tenants do not seek to keep their premises in repair while they are in occupation or sub-letting and, accordingly, render themselves liable for dilapidations at lease expiry. In some cases, they may well hope that market circumstances will relieve them from any liability on the basis there will be no diminution in value, because the premises will need either substantial upgrading to meet modern market requirements, or will be suitable for redevelopment and any repairs would be rendered valueless. Often, repair is not practicable because the premises remain occupied up to lease expiry and, naturally, the tenant gives its business interests priority.

Landlords often do not do the repairs following lease expiry, preferring a cash settlement to fund other works and/or to wait to see what a new tenant wants. This creates uncertainty as to what works are actually worth undertaking. Recently, many office buildings have been converted to residential with much, if not all, of any disrepair being superseded.

Historically, leases were often granted for terms of 25 or 35 years or even longer and thereby gave rise to substantial dilapidations liabilities at lease expiry, because the tenant under a longer lease is more likely to be liable to

dilapidations

replace items or carry out major repair works. Such liability is often difficult to accurately ascertain without detailed consideration as to what the premises originally constituted, and what the requisite standard of repair should be at lease expiry given the age of the premises and the type of tenant that would have been likely to have taken them at the very start. Many longer leases have come to an end in recent years.

Recent market conditions mean that tenants are not renewing their leases but vacating, thereby giving rise to a terminal dilapidations claims. Furthermore, a large number of tenants are exercising break clauses. Clearly, landlords with empty properties that are difficult to re-let in current conditions are more likely to focus on recovering damages for not only disrepair, but for loss of rent and rates.

Tenants increasingly often wait to see what the landlord does with the premises and, in particular, whether it does carry out the repair works or not. It is, in fact, interesting to note how both landlords and tenants actually concentrate on the actions they take to deal with the premises in disrepair, on the basis that they think this will be directly relevant to a dilapidations claim whereas, in fact, as in the *Hammersmatch* case, it is the actions that a landlord would have taken if the premises had been left in repair that is primarily relevant to the question of supersession.

The sheer complexity involved in applying the law to the particular facts of each case means that court often seems the only answer. There is no denying that the law, both as to establishing the standard of repair and whether items are in repair or disrepair, as well as the law as to how damages are to be assessed, is complex and confusing and, in some cases, somewhat out of date. Accordingly, it is often difficult to assess the extent of a tenant's liability and advise on what sum should be paid or accepted in settlement. Having said this, the vast majority of claims do settle and the Dilapidations Protocol, if properly followed, should generally secure a resolution out of court.

There is also a continuing failure by some parties and/or their representatives to follow the Dilapidations Protocol and, in particular, make their cases clear to each other at an early stage. Experts on each side are often unable to agree items or, in some cases, make appropriate concessions. The ability of the parties to use a single joint expert, rather than each have their own expert, is seldom used in substantial cases. Claimants and defendants fail to make early and sensible settlement offers, or to mediate before substantial costs are incurred. Because of the need to mediate at some stage, parties are often reluctant to disclose their hand. Unfortunately, mediation often occurs at a late stage because the parties like to have full disclosure of documents and detailed expert input before they agree to negotiate and, by then, tenants are more unwilling to settle because of the costs liability that will follow.

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Finally, issues may arise from the inability of a tenant to meet its liability or settle at a reasonable figure. In the *Twinmar* case, the tenant went into liquidation without having paid anything.

Looking to the future

The future is somewhat uncertain. Nowadays, tenants take shorter leases and are a lot wiser as regard the extent of a full repairing liability. Leases are often subject to a Schedule of Condition and/or, in the case of new buildings, premises are let with the benefit of warranties from the original contractor and construction team. The Dilapidations Protocol is now part of the court rules and clearly important to follow. Claims should therefore be smaller and more capable of settlement.

The recent introduction into the court rules of a provision allowing claimants to recover an extra 10% of their damages (up to a limit of £75,000) if they recover more at trial than they have offered to settle at will, no doubt, provoke many tenants to settle to avoid this risk.

However, as long as tenants do not maintain premises in repair throughout a lease and/or do not make provision for such a liability, and market conditions remain uncertain, terminal dilapidations claims will continue. Indeed, there is now a large industry dependent on this. C

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