

Please relief me

When can a tenant seek relief, and on what terms will it be granted? Jonathan Ross investigates



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In the case of *Patel v K&J Restaurants Ltd* [2010], the Court of Appeal had to decide whether the tenant was in breach of the user and alienation covenants in the lease of the premises. If so, were such breaches capable of remedy and had they been remedied, and should relief from forfeiture be granted?

At first instance, the judge had found in favour of the tenant and had dismissed the claim for forfeiture and possession, ordering the landlord to pay all of the tenant's costs of the proceedings. The Court of Appeal reviewed the law in some detail and came to different conclusions to the judge. Its decision is of substantial importance to practitioners in this field as it makes clear how the courts will look at such matters in the future.

Factual background

The claimants, Mr & Mrs Patel, are the freehold owners of premises at 116 Tottenham Court Road, London W1 comprising five floors. The ground floor and basement are used for restaurant purposes and each of the upper floors contains a residential flat. By the lease dated 18 May 2005, the premises were demised to the defendant tenant, K&J Restaurants, for a term of 20 years from 25 December 2004.

The lease provides that the premises are not to be used for any illegal or immoral purpose and, unless permitted to do so, the tenant is not to assign, underlet or part with or share the possession or occupation of the ground and basement floors.

On 28 February 2008, the claimants served a notice pursuant to s146 of the Law of Property Act 1925 upon K&J Restaurants upon the basis that one of the residential flats had been used for prostitution and that this

was an irremediable breach. The claimant gave seven days notice of their intention to enforce their rights to recover possession of the premises.

In April 2008, the claimants served a further notice under s146. This notice covered both the previously alleged immoral use and further alleged breaches of covenant in connection with the underletting or parting of possession with the restaurant premises. Unlike the first notice, this notice required the breaches to be remedied insofar as they were capable of remedy.

Although steps had already been taken by K&J Restaurants to deal with the illegal and immoral use, and to seek to deal with any breach of the alienation covenant in connection with the restaurant premises, the claimant proceeded with possession proceedings. It was the claimants' case that the breaches were irremediable and that it should be entitled to forfeit the lease and recover possession.

Legal background

Provided that a lease includes a right of re-entry, a landlord is entitled to seek to forfeit in the event of any breach. However, unless the breach relates to non-payment of rent, a landlord cannot seek to forfeit without first serving a s146 notice. Such notice has to specify the particular breach complained about and, if the breach is capable of remedy, require the tenant to remedy the breach. The notice has to also require the tenant to make compensation in money for the breach. If the tenant does not remedy any breach, insofar as it is capable of remedy, within a reasonable time following the service of the s146 notice, and/or make reasonable compensation in money, then the landlord can seek to recover possession of the premises.

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Examples of irremediable breaches are insolvency; assigning, underletting or parting with possession of the premises without the landlord's consent; carrying out unauthorised alterations; and immoral use. Examples of breaches that are capable of remedy are failure to repair, failure to comply with the permitted use, or failure to make payment of sums due.

The distinction between irremediable and remediable breaches is important in that, if a breach is remediable, the s146 notice must require the tenant to remedy the breach and the landlord must allow a reasonable time for so doing before it can seek to forfeit.

Forfeiture of commercial premises can be effected by the landlord either commencing possession proceedings, or by simply re-entering the premises and taking possession. A landlord will normally only seek to re-enter where there is no dispute as to the breach because, if it were to unlawfully enter the premises, it could be liable for substantial damages to the tenant.

A tenant who is in breach of covenant has a right to seek relief from forfeiture from the court. The extent to which the court will grant relief will depend upon the nature of the breach and the conduct of the tenant. Where the breach is deliberate and irremediable, a tenant is going to face a much sterner test in successfully seeking relief. The court is, however, particularly mindful of the value of any lease and, where a lease does have value, a tenant can generally expect to be able to secure relief from forfeiture as the court will often not consider that the penalty of losing a valuable lease will fit the crime.

Relief from forfeiture for immoral use

The court first considered the law as to whether immoral use constituted a remediable or irremediable breach of covenant and whether there had been a breach and, if so, what the consequences should be.

Case law has established that there is a distinction between direct immoral use by the tenant on the one hand,

and immoral use by a sub-tenant that is not permitted by the tenant on the other hand. In so far as the tenant is responsible for the immoral use, then this is an irremediable breach. If it is the sub-tenant that is responsible then the breach is capable of remedy, but only if the tenant takes reasonable steps to deal with the breach without delay.

The immoral use related to the sub-tenant of flat 2 using the premises for prostitution. In, or about, August/September 2007 the police made Mr Albright of K&J Restaurants aware of their concern about the comings and goings of men to and from the flat. Mr Albright satisfied himself, at that time, that there was nothing untoward but the police then spoke to him early in November 2007 and told him that the flat was being used as a brothel. Mr Albright took no action as a result of this telephone conversation. He claimed that the police had said that they would write to him confirming the position and he had been waiting for formal confirmation. On 30 January 2008, the police attended and obtained evidence that the flat

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was being used for prostitution and served notices to this effect on the claimant and K&J Restaurants. Mr Albright then took urgent steps to obtain possession of flat 2; any immoral use had ceased by 6 March 2008 when possession was secured. The question for the court was whether Mr Albright had acted reasonably and quickly enough in dealing with the matter? The judge at first instance thought he had, but the Court of Appeal disagreed; it did not think that he should have waited for receipt of the formal notice from the police before acting. It held that a tenant must take some action where he has either knowledge or reasonable grounds for suspecting immoral use by a sub-tenant, and that Mr Albright should have made further enquiries in November 2007. The very fact that Mr Albright was able to investigate and secure possession of the flat very quickly once the police notice was served made it clear that it was unacceptable not to have done anything at all beforehand.

Accordingly, because of the failure to take satisfactory steps sufficiently promptly, there had been an irremediable breach of covenant, and the court held that the first s146 notice was valid because the breach was not capable of remedy.

The court then considered whether to grant relief from forfeiture in relation to this breach. The claimants argued that a significant stigma had attached to the premises due to the immoral use and they relied on previous case law where the court had shown a strong aversion to granting relief in such case. K&J Restaurants argued that, if they had not acted sufficiently quickly to begin with, they had taken steps to deal with the matter eventually and no stigma had attached to the premises in any event. Both the trial judge and the Court of Appeal agreed that relief was in order. The court, in particular, took into account the fact that the tenant had not been directly responsible for the immoral user, and that the very nature of Tottenham Court Road was such that any stigma from immoral use could not easily attach to the particular premises. The court also took account of the value of the lease and the substantial profit that would accrue to the claimants should they recover possession. It considered that this would amount to a

windfall profit out of all proportion to any damage suffered.

Relief from forfeiture for unlawful alienation

The breach related to a management agreement that K&J Restaurants had entered into with MP Catering Limited (MPC). K&J Restaurants had previously managed the restaurant and a Mr Leale was the person responsible for the actual management. In 2007, a somewhat complicated arrangement was entered into whereby MPC was incorporated with all of its shares being owned by K&J Restaurants or Mr Albright, but with all the profits from the business going to Mr Leale and his business partner. The management agreement entitled MPC to occupation of the restaurant and the question for the court was whether this amounted to a parting or sharing with possession. K&J Restaurants argued that MPC simply occupied the premises as its agent and the judge had agreed with them at first instance upon the basis that MPC carried out the business under the tenant’s control.

The Court of Appeal saw the matter differently. They noted that MPC had its own right to use and occupy the premises and, although this was not to the exclusion of K&J Restaurants, it did involve a sharing of occupation and was in breach of the lease. While the ownership of the business had not been transferred, MPC was using the premises for its own profit and had an enforceable right under the management agreement to access and use of the premises for its own benefit and not just as agent for K&J Restaurants.

The court therefore held that the second s146 notice was valid. It then went on to consider when the breach had been remedied and whether to grant relief. The court noted that, although K&J Restaurants had taken steps to change the locks and exclude MPC on 31 March 2008, MPC had taken court action in order to re-occupy and they had not actually vacated the premises until after the trial. The court therefore held that there had been no remedying of the breach prior to a trial. However, it was in agreement with the judge that relief from forfeiture was appropriate. The court did not consider that there had been a deliberate sharing

of possession or attempt to conceal the same, and it did not think that the actual breach was especially serious in itself.

As MPC had vacated the premises after the trial anyway, the court did not have to consider any terms for relief from forfeiture in connection with securing vacant possession, but it considered that the trial judge should have ordered relief subject to steps then being taken to satisfactorily remedy the position (and K&J Restaurants giving an undertaking not to repeat any of their previous breaches).

Costs

Having held that both s146 notices were valid, and that the tenant was in breach, it held that K&J Restaurants should pay all of the costs of the claimants. It then turned its attention as to whether those costs should be paid on the standard basis or on the indemnity basis, which allows for a greater recovery of costs. After considering the previous authorities, the court considered that relief from forfeiture should be given on the more generous basis. The reason for this decision was that the purpose of relief is to put the landlord back in the position in which he would have been if there had been no breach and, accordingly, costs should be awarded on the most generous basis possible.

Conclusion

It can be seen from this case that a tenant has to be very careful about not breaching covenants in a lease, especially where a lease might be valuable and a landlord may have every incentive to seek to forfeit. However, while there will be serious ramifications for a tenant in terms of liability for costs and having to take steps to remedy the breaches, it will be unusual for the court to refuse to grant relief from forfeiture unless the breaches are especially serious or wilful.

Clearly, where a tenant sublets, it needs to appreciate that it has to act urgently when it becomes aware of any breach by its subtenant and that it needs to seek to ensure that all necessary consents are obtained for any arrangement whereby a third party is entitled to access to, or occupation of, the premises. ■