The Dilapidations Consultancy

Dilapidations: The devil in the detail

James McAllister, Director of The Dilapidations Consultancy, explores some common and costly mistakes often made by ill-informed tenants of commercial leasehold property.

Introduction

Dilapidations can be a costly, and often unforeseen, entry in the balance sheet of any commercial property occupier holding a lease with express repairing responsibilities. This can leave a very bitter aftertaste for tenants looking to vacate a property they may have outgrown, or perhaps more topically, wish to downsize from.

Ignorance, as always, is no defence. So the unwary tenant who dutifully files away their lease upon taking the property, never to read it again, may be in for an unanticipated expense when it comes to leaving the premises. Of course, this is compounded if already operating on a tight margin, thereby threatening the financial wellbeing of the business. This is an all too familiar tale with potentially disastrous consequences in the current economic climate.

The Detail

Any tenant occupying premises under a commercial lease will invariably be expected to keep the demised areas of their premises in good and substantial repair, including regular decoration intervals, often specified in the lease. There is usually also a prohibition on structural, and even non-structural alterations, along with an ongoing duty to ensure general compliance with statutory obligations; this typically includes the electrical supply, gas appliances and asbestos control/management. So if the lease is so clear on the tenant's responsibilities, why do so many tenants fall foul of their duties to their own financial detriment?

In the first instance, most tenants are so focussed on their core business that property repairs become nothing more than a trivial inconvenience that can be dealt with when absolutely necessary, i.e. lease expiry. This connotes a general reluctance to budget for, and expend, funds on maintaining a building the business doesn't own. Furthermore, "the business simply doesn't have the financial means to implement a programme of planned preventative maintenance" is a familiar response. This is the first costly mistake. For those tenants smart enough to recognise that a stitch in time really does save nine will attend to the few missing roof tiles before the ravages of a few British winters (and summers) warrants the need to sort out the dry rot outbreak, the extensive internal damp staining and partially collapsed ceiling: *Day v Harland Wolff Ltd [1953]*. In fact, a prudent tenant might even consider certain routine works in the context of 'repair' even though the subject matter may not be technically in 'disrepair', but the performance of these works would prevent the far more significant potential consequences further down the line. This makes a business case for doing a small and inexpensive job early on.

Of course, many tenants catch the initial dilapidations virus long before they realise it will lead to a full blown cold - that is before they even take occupation of their new leased premises. Unaware of the implied legal ramifications of the seemingly innocuous terms 'put', 'keep' and 'leave' in the context of the repairing covenant, the ill-informed tenant might believe their obligation only to 'keep' the demised premises in repair means they can ignore the disrepair that pre-existed the lease term. Unfortunately, the case of *Payne v Haine [1847]* reiterates that the term 'keep' carries with it an implied obligation to firstly 'put' in to repair and also to 'leave' in repair upon lease expiry. Therefore, unless the tenant taking on a run-down property in a parlous condition had the foresight to commission and engross to the lease a Schedule of Condition, they may find they are inheriting an onerous burden with an immediate liability. This comes before the tenant even steps foot in the premises.

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To add to this poorly advised tenant's misery, any inherent defects existing within the premises will also be their responsibility, even if they emanate from a design fault at the time of construction. Accordingly, *Ravenseft Properties Ltd v Davstone (Holdings) Ltd [1979]* will come as an unpleasant surprise to any tenant believing that damage arising from an inherent defect is the responsibility of the Landlord, unless, of course, the remedying of that defect will result in giving the Landlord back something wholly different than that demised: *Brew Bros v Snax Ltd [1970].* It would therefore be prudent for a tenant taking on a sizeable property on a long lease term to also obtain a detailed pre-acquisition survey to identify any such inherent defects long before signing the lease, and thus assuming a liability to repair.

Worthy of note, however, is that 'disrepair' does not exist, legally speaking, unless there has been deterioration in a previous physical condition (determined by the condition when constructed), together with resultant damage. Therefore, to the layman, a leaking roof on a modern warehouse might be considered to be in disrepair, but if this was a fault at the time of construction, and assuming no further deterioration or damage to the property has arisen since, then there is no 'disrepair' and with it, no breach of repairing covenant: *Post Office v Aquarius Properties Ltd [1987].* But before the obstinate tenant embraces this as an advantageous legal quirk, the situation can turn, particularly where the tenant is only responsible for the internal fabric and the Landlord has covenanted to repair the structure and exterior: *Janet Reger International Ltd v Tiree Ltd [2006]*. In this case the Landlord was able to resist the tenant's call to repair a defective damp proof membrane which had led to excessive dampness within a basement where the tenant was unfortunately displaying lingerie for sale.

A defaulting tenant may also find that they are funding the Landlord's post-lease works, which perhaps, in hindsight, they ought to have done, and which might include certain improvements as a natural by-product of the repair process. Is that fair? Well yes, if using new materials is more cost effective or simply a better way of effecting the repair: *Elite Investments Ltd v TI Bainbridge Silencers Ltd [1986].* Taking things a step further, the appropriate repair can also include complete renewal: *Lurcott v Wakely [1911]*, but not simply because a 'convenient' opportunity may have arisen for the Landlord to replace that asbestos-cement roof with crinkly tin and re-charge the tenant for the privilege: *Secretary of State for the Environment v Euston Centre Investments Ltd [1994]*. And we must remind ourselves that only when a component is incapable of further patch repair should we consider full replacement: *Scottish Mutual Assurance Plc v Jardine Public Relations Ltd [1999].* So tenants can take some comfort in an 'overhaul' if this amounts to an adequate repair; replacement, of course, being the last resort.

There is a silver lining to what would appear to be a very gloomy prospect for any tenant taking on, or currently occupying leasehold property. Firstly, and taking advantage of the economic situation, tenants can negotiate harder in diluting repairing responsibilities, or at least improve on the inducements offered to take properties in anything less than impeccable condition. This might include a longer rent-free period beyond the market norm, a reverse premium to attend to the outgoing tenant's repairs, and perhaps the inclusion of a Schedule of Condition to record those existing defects thereby obviating them from any future dilapidations claim. With some careful tax planning, those tenants filing accounts under FRS12 may wish to include within their accounts a firm valuation of current accrued dilapidations liability under the banner of 'Provisions'. This assumes the Contingent Liability (i.e. dilapidations) is material in nature. Rather than plucking random figures out of the ether, a detailed Dilapidations Assessment by a third party will stand up to the scrutiny of the taxman, with the added bonus of deferring the recognition of taxable profit. So even where the dilapidations liability is unavoidable, it can assist the balance sheet if properly managed.

Conclusion

So is Dilapidations pure doom and gloom for tenants? Well if they never read the lease and shirk their responsibilities, then it goes without saying. On the other hand, proactive tenants seeking to curb, and even mitigate, their future dilapidations liability by dealing with disrepair at an early stage will avert an otherwise inevitable claim for damages at lease expiry. This is at least one way of reducing the financial burden on a leasehold business occupier and is, in the current climate, a detail worthy of further attention.

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