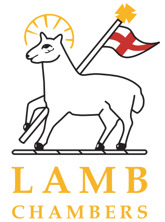
Break option conditions and standards of repair



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The standard absolute conditional clause and its inherent problems

The longer the lease and the higher the rent the more crucial it becomes effectively to be able to exercise a break option if such exercise is desired. It goes without saying that so far as the tenant is concerned, an invalid exercise condemns the tenant to continuing obligations in respect of rent and repair in particular until such time as the option presents itself again, if at all. This can be a highly expensive consequence not only for the tenant but in some unfortunate circumstances for professional advisers also. Conversely, there are fruits to be enjoyed by landlords with a good covenant and possibly no queue of potential new tenants to fill the void. In respect of leases concluded during the boom years, leases were of course granted at high rents with upward only rent reviews, and in such circumstances the ability to keep on the hook a tenant paying above the market rate is of course all the more desirable.

The problem from the point of view of the tenant is that in most cases the standardly drafted break option is qualified by the requirement that the tenant shall have observed the covenants in the lease. Typically the condition is drafted in absolute terms. For example that featuring in the *Simons v. Associated Furnishers Limited* case in 1931 which provided:

"If the company shall desire to determine the present demise at the expiration of the first five or ten years of the said term and shall give to the lessor six calendar months previous notice in writing of such their desire and shall up to the time of such determination pay the rent and perform and observe the covenants and conditions on their part hereinbefore contained then immediately on the expiration of such five or ten years as the case may be the present demise and everything therein contained shall cease and be void, but without prejudice to the remedies of either party against the other in respect of any antecedent claim or breach of covenant".

As will have been observed, the obligation is drafted in terms which appear to impose an absolute obligation in respect of observance of the covenants as a condition precedent to the operation effectively of the break option. Indeed the cases are to this effect. The approach seems to be that certainly in respect of options drafted in this absolute way, a breach of a condition, albeit a trivial breach, will be fatal from the point of view of the tenant. For an early example of this, see *Finch v. Underwood* [1876] 2 ChD 310.

There has even been some argument as to whether compliance with the covenants in the lease is required at the date of service of the notice exercising the option alone, or at the date of the expiry of the notice, or both. In some cases it has been contended that perfect compliance with all covenants is required throughout the lease before valid exercise of such an option can take place (see below). In most cases however, if a breach or breaches have been remedied by the time actually or apparently stipulated in the lease, such breaches will not be a bar to operation of the break - see *Grey v. Friar* (1854) 4 HL Cas 565.

The date for compliance of the obligations of the lease will obviously turn to a large extent upon the precise wording of the particular break option. In the *Bass Holdings* case the Court of Appeal held that the usual phraseology which required compliance "up to" the break date was to be construed so as to mean that there should be no outstanding breaches at the break date. Earlier breaches will not preclude an effective operation of the option. Care has to be taken however in

the drafting of the option or in advising clients whether or not to agree the terms of the lease or an assignment. It is perfectly possible to have a form of wording which does indeed require the tenant to have complied with all the obligations contained in the lease throughout the duration of the term. However such an obligation these days would seem to be very onerous and in any event would be unlikely to be acceptable to most tenants.

The sting from the point of view of the tenant can be removed by ensuring that the break option is qualified to the extent of requiring "reasonable" compliance with or performance of the tenant's covenants. In fact, such clauses are less frequently to be found than the absolute clauses and may even, ironically, be double-edged so far as the tenant is concerned. One would have thought that the importation of a concept of reasonableness into such situations would assist a tenant in resisting any contention by a landlord that a minor defect in repair precludes the effective operation of such a clause. It has sometimes been argued that the concept of reasonableness can be used as a stick with which to beat the tenant. It was said by Paull J. in *Gardner v. Blackhill* [1960] 1 WLR 752 at 759 that:

"By inserting the word "reasonably" the parties not only intended to mean, but must be deemed to have meant, that the tenant can exercise his option provided that he behaves during his tenancy in a way in which a reasonably minded tenant might well behave".

It has been suggested that this approach opens the door to the Court to scrutinise the behaviour of the tenant not only at the effective date of termination of the tenancy but throughout the term. It is possible therefore to imagine a scenario in which at the date of termination there has been full compliance with the appropriate conditions but the tenant has otherwise throughout the term been in constant breach of covenants. It is submitted that the case is in fact not authority for this proposition but it is conceivable, although perhaps unlikely, that a Court could in such circumstances conclude that there has not been reasonable compliance by the tenant sufficient to entitle an effective operation of the break clause.

Although in the *Bassett* case the Court did find for the tenant it was said by Griffiths LJ. that:

"In my view, it is permissible to look at the conduct of the tenants throughout the term to determine whether or not they have reasonably performed and observed the several stipulations contained in the Fifth Schedule".

It will be seen therefore that two starkly different approaches present themselves on the cases, largely dependent upon the nature of the clause concerned. The absolute clause will require strict compliance at the effective date whereas the qualified clause affords the Court a discretion which generally will operate to the advantage of the tenant but may in some unusual cases ironically be to the tenant's detriment.

See also *Reed Personnel Services PLC v. American Express Limited* [1997] 1 EGLR 229.

None of this paints the law in an especially attractive light from the point of view of the lay client. To have to tell a client that because a strip of wallpaper is hanging loose or there is a prominent stain on a carpet or some peeling paint work which it would take a few hundred pounds to remedy, the combined effect or individual effect is that of imposing a continuing obligation on the tenant to pay possible hundreds of thousands of pounds in continuing rent. All this makes the law look an ass. In *Mannai Investment Company Limited v. Eagle Star* [1997], the House of Lords, albeit by a three/two majority, balked at arriving at what might have been seen as a perverse conclusion in relation to a break clause notice. In that case as may now be well known, by miscalculation the notice had mistakenly stipulated 12th January as the termination date when it should have been 13th January. The Court of Appeal unanimously allowed the landlord's appeal to the effect that

the notice was ineffective and, only by a three/two majority did the House of Lords overturn this decision in favour of the tenant. Some words of Lord Hoffmann may be apposite:

"... the case is by no means straightforward. The Clause does not require the tenant to use any particular form of words. He must use words which unambiguously convey a particular meaning, namely an intention to terminate the lease on 13th January. In Hankey v. Clavering [1942] 2 KB 326, where the notice to quit said "21st December" instead of "25th December" Lord Greene MR said at pages 328, 330, "the whole thing was obviously a slip" on the part of the landlord but that the notice was invalid "however much the recipient might guess, or however certain he might be" that it was a mere slip. So even if the recipient was certain that the landlord actually wanted to terminate his tenancy on the right date, which was 25th December, so that the necessary intention was unambiguously communicated, the notice was bad. One is bound to be left with the feeling that something has gone wrong here. Commonsense cannot produce such a result; it must be the result of some rule of law. If so, what is that rule and is it correct?"

In the speech which followed, Lord Hoffmann persuasively demonstrated that we use words to convey a meaning and if the meaning has unambiguously been received by the reasonable recipient, the purpose has been achieved. The majority view was that the construction of the notice had to be approached purposively and the question was how a reasonable recipient would have understood the notice, bearing in mind its context. The purpose of the notice was to inform the landlord of the tenant's decision to determine the lease in accordance with the break clause and a reasonable recipient with knowledge of the terms of the lease and of the appropriate anniversary date would have been left in no doubt that the tenant wished to determine the lease on 13th January but had simply wrongly described it as the 12th. Accordingly the notice was held valid. Can such an approach be transposed into the present context? It seems that we have not yet reached that stage. Although such an approach may carry the day in respect of the drafting of such notices, purely formal requirements apparently still have to be strictly observed. For example in that case the House of Lords said that if the notice had been required to be on yellow paper, a notice on blue paper would not be valid.

See further in this regard *ICS v. West Bromwich Building Society* [1998] 1 WLR 896 at 912 and 913.

The unreported decision in *Osborne Assets Limited v. Britannia Life* in 1997, albeit simply a decision in the County Court, does not give great cause for hope. The case involved a tenant failing to comply with conditions necessary to break its lease as a result of redecorating premises with two coats of paint rather than the three required by the lease. Since this was held not to be a compliance of the appropriate covenant a further twenty years of rental liability ensued. This seems to be the prevailing approach even in circumstances where the landlord's ability to re-let the premises as a result of the breach of covenant is completely unaffected and would be regarded perhaps as no more than a trifling matter to be put right by any incoming tenant or possibly ignored altogether. In the earlier case of *Kitney v. Greater London Council Properties* [1984] the tenants did their best by bringing in a building surveyor to inspect the property and report on the appropriate works in preparation for the break. However a couple of corroded window frames were overlooked which would have cost no more than about £700 to put right and there was some other failure in respect of decorations also. Although there were some remarks from the Court to the effect that the break option should not be regarded as a privilege only to be enjoyed by the tenant in circumstances of especially strict compliance with the obligations in the lease - nonetheless it was held that there had been sufficient non-compliance to defeat the tenant. In *West County Cleaners v. Saly* the Court of Appeal did in fact find that an option for renewal of a lease was a privilege which required strict compliance of the terms and conditions upon which it was granted before it could be exercised and so the tenants had disqualified themselves by reason of their breaches of covenant, albeit that the breaches were only trivial, from exercising their option to renew. The breach in question was that the tenants had not painted the ceiling in every third year of the term and had not done any painting in the last year of the term. Nonetheless the

premises were kept in a fair state of repair and the landlord who lived next door to the premises and had frequently been in them, had never complained about the state of repair, although on one occasion she had complained about the garish decoration carried out by a sub-tenant. Once again the tenant failed.

A similarly adverse decision was made from the point of view of the tenant in the *Bairstow Eves* case in 1992. In that case the suggestion was that the breach would only be a sufficient breach if it were to carry with it an entitlement to substantial damages. The argument was rejected by the Court of Appeal which held that the condition precedent could not be re-written to exclude from account a subsisting breach on the ground that only nominal damages would be recoverable.

Is there any comfort for a tenant? Most of these cases seem to have involved allegations of breaches of repairing covenants. One way through in some cases may be to draw a distinction between the extent of repair and the standard of repair. Often the repairing covenant will require the tenant to keep the premises in good and substantial repair. There is longstanding authority to the effect that:

"It is a monstrous thing to say that because a person puts nails into the walls of a house he must take them out and fill up the holes, or commit a breach of the covenant of a repairing lease." - see Perry v. Chopzner *(1893) 9 TLR 488.*

In other cases it has been held that there has been no breach of covenant to keep in repair a fifty year old building merely because there were hairline cracks in the brickwork (*Plough Investments v. Manchester City Council* [1989] 1 EGLR 244). It is of course long established (see *Proudfoot v. Hart* (1890) 25 QBD 42) that the question of good and tenantable repair has to import a consideration of the age, character and locality of the house or premises and a consideration of whether it would be reasonably fit for the occupation of a reasonably minded tenant of the class who could be expected to take it. That was the case in which there was the famous comparison between what was acceptable in Grosvenor Square and that which would be acceptable in Spitalfields. So, for example, where an old building is let, the lessee by his repairing covenant is bound only to keep up the premises and not to give back premises which are new premises. In order to determine the standard of repair by the covenant, the age and general condition of the premises when demised may be taken into account. Accordingly, this approach may be a peg upon which to hang an argument in the context of questions of effective operation of a break clause. However, even this argument has its limitations because if the repair covenant is to the effect that the tenant has to keep the property in repair, it is again long established that "to keep in repair presupposes the putting into it" - see *Proudfoot v. Hart*. Although the standard of repair may not have to be high, nonetheless if particular parts of the property are undoubtedly in disrepair, it will not avail the tenant simply to argue that they were in disrepair at the inception of the lease. By accepting a covenant to keep the property in repair, the tenant undertakes to put into repair that which is properly described as in disrepair.

One possible, again unusual, way out would be to argue that the condition imposed is unlawful by reason of some statutory regulation or other statutory provision. This was the case in *Plummer v. Tibsco* in the case decided in somewhat different circumstances in 1999. However such opportunities rarely present themselves. Query whether the Unfair Terms in Consumer Contracts Regulations 1994 or 1999 may in some circumstances be invoked - it is submitted that in most circumstances this will not be the case.

Until the run of authorities which presently exists is disturbed in the appellate courts, it seems that landlords will have the whip hand and tenants will be on the back foot. Those advising in such circumstances can but do their best to seek a qualified break clause condition but of course the ability to do so will depend upon market conditions and the strength of bargaining position.

Otherwise, the best that can be achieved is to ensure that clients are well aware of the stringencies involved in such terms and make the best preparations possible well in advance before the effective determination date. Naturally, if it is possible to achieve settlement by "buying off" the claim, so much the better.

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