

A practical guide to dilapidations

Introduction

Claims by landlords for breach of a tenant's covenant to repair typically arise upon the expiry of the lease.

This fact sheet provides an overview of the dilapidations process in the commercial market and considers how to reduce the possibility of a dispute.

Repairing obligations

It is important to understand the extent of the tenant's repairing obligations. The starting point should be the lease itself and any other supplemental documents such as a licence for alterations and/or a deed of variation.

If the property in question consists of a single building, the repairing covenant will usually relate to the whole of that building. This means the tenant is liable for all repairs and the expenses involved. However, if the property consists of part of a building, such as a floor in an office building, the position is less clear. In these circumstances it is not unusual for the tenant to be responsible for works such as internal repair and decoration, with the landlord taking responsibility for the structural and external repairs.

If the covenant requires the tenant to "put and keep" in repair, this usually means that a tenant must put the property in repair even if it was out of repair at the start of the lease. Where the property is clearly in a state of disrepair at the outset, it is now common for a landlord and tenant to agree a schedule of condition prior to the tenant taking a new lease and limiting the repairing covenant accordingly.

A tenant will usually only be responsible for repairing the property and not improving it. A landlord cannot generally pass on the costs of improvement works that are necessary to attract new tenants to a property.

Approach to dilapidations

A landlord needs to consider its future plans for the property at an early stage. If the intention is to sell or re-let, the earlier the schedule of dilapidations is served on the tenant, the more chance that the tenant will carry out the work and the landlord will be able to re-let sooner. It may even be a factor in influencing an existing tenant to remain if he has insufficient funds to cover both relocation costs and dilapidation costs.

However, a landlord may equally prefer to wait until the end of the term and then serve a schedule of dilapidations with a view to negotiating a financial settlement at the end. The advantage for the landlord is that it retains control of the works and this enhances the prospects of recovering a cash settlement from the tenant.

Similarly, a proactive tenant will seek advice at an early stage. If he receives advice that the value of the property is adversely impacted by virtue of its condition, he can carry out the repairs early which will control the costs and substantially reduce any later claim by the landlord. However, if he receives advice that the condition of the property has little or no impact on its value, he may seek to challenge the landlord's claim rather than carrying out any repairs.

What can be claimed

There are limits on what a landlord can claim from a tenant in dilapidations. A

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landlord's plans for the property will be relevant in ascertaining the extent of a dilapidations claim. For example, a landlord cannot claim damages for breach of a repairing covenant from a tenant if it intends to demolish or substantially alter the property after it obtains vacant possession.

Even if the tenant may be liable for repairs, there is a statutory cap on the damages that a landlord can recover once a lease has ended. Damages cannot exceed the difference in value of the property in its condition at the end of the lease, and its value had the repairs been carried out. To illustrate, if a property's value in good repair is £100,000, but the value in poor repair is £80,000, then the damages that the landlord can claim will be capped at £20,000, no matter how costly the works required.

Despite the statutory cap, a landlord will often produce a schedule containing the anticipated costs for carrying out the repairs. However, the weight that the Court will give to such costs as evidence of the reduction in value of the property depends on whether the landlord will actually carry out the works. If the landlord has no intention of carrying out the works, then the costs are of little help. If the works have been carried out or are going to be carried out, then the costs may be a real guide. Where it is questionable whether the work will be carried out at all, the estimated costs may be a starting point but they are likely to be scaled down.

A landlord should complete the works as soon as possible following the expiry of the lease. Whilst a landlord can claim for genuine loss of rent during the time that repair works are being carried out, if the landlord has spent six months arguing with the tenant over minor matters rather than

proceeding with the work, a Court is unlikely to be sympathetic to a claim for loss of rent during this time.

Procedure

Earlier this year, a Pre-Action Protocol for dilapidations claims arising at the end of a lease was formally adopted as part of the Civil Procedure Rules. The Protocol encourages the early exchange of information about prospective claims and provides a framework and timetable to give the parties every opportunity to reach a settlement without the need for Court proceedings.

The Protocol provides that a landlord should serve a schedule of dilapidations within a reasonable time, which the Protocol suggests should be not more than 56 days after the termination of the tenancy. The Schedule should state details of the sum that the landlord is seeking to claim as damages and may include legal and surveying costs, loss of rent, and professional fees.

The Schedule should contain an endorsement that in the landlord's or the landlord's surveyor's opinion:

- a all the works set out in the schedule are reasonably required to remedy breaches
- b where endorsed by the landlord, full account has been taken of its intentions for the property
- c where endorsed by the landlord's surveyor, full account has been taken of the landlord's intentions for the property, as advised by the landlord; and
- d the costings, if any, are reasonable.

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Where the landlord is claiming a sum of money, the landlord should also provide a Quantified Demand to substantiate the monetary sum sought as damages in respect of the breaches detailed in the schedule as well as any other items of loss for which damages are sought. It should also set out whether VAT applies.

Upon receipt of the Schedule and/or the Quantified Demand, the Protocol requires the tenant to respond within a reasonable time and again 56 days is adopted as the limit. The landlord and the tenant (and/or their professional advisers) are then encouraged to meet to negotiate on a without prejudice basis. This allows the parties to have useful discussions to narrow the issues in dispute and attempt to reach a settlement.

If the parties are unable to reach a settlement, the Protocol requires the parties to consider whether an alternative dispute resolution procedure may be appropriate such as mediation. If such alternative procedures are either not appropriate or unsuccessful, the parties are encouraged to carry out a "stocktake" of the issues in dispute and identify what evidence the Court may need to resolve those issues.

If the parties cannot reach a settlement after complying with the Protocol, then the parties are free to refer the matter to the Court. Before issuing court proceedings the landlord should provide a detailed

quantification of loss which details exactly what the landlord is claiming and how the claim has been calculated. However this need not be the end of negotiations and indeed the parties should always aim to achieve an amicable resolution.

Conclusions

Dilapidations claims by their very nature can turn into complex and contentious issues, but open dialogue and realistic objectives can reduce the chances of litigation. To summarise the key points:

- Obtain professional advice at an early stage
- Read and understand your lease and any associated documents
- Keep damages claims realistic and remember the statutory cap
- Adhere to the Protocol

This information sheet has been prepared for general guidance only and is not a substitute for specific advice. For further information please contact Mark Steggles on 01892 510000 or by email at:

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