

Delivering a final farewell

Notices In uncertain times, a tenant may seek to operate its break clause. In the first of three articles, *Andrew Ross* and *Rachel Wevill* offer practical advice. Illustrations by *Clare Nicholas*

Break clauses come under particular scrutiny in a recession. Tenants may be tempted to view an option to break as a chance to dispose of or renegotiate liabilities under a lease. Landlords will want to resist early termination of tenancies in a falling market and will look for ways to invalidate break options. Whatever the angle, a break clause will be strictly interpreted by the courts and it is advisable to examine its terms before attempting to exercise it. This article discusses some of the issues that arise when a tenant opts to break.

Read the lease

The terms of break clauses should be read literally. If it wants to avoid disputes, the tenant should comply with all the lease terms. The tenant and its advisers should consider the following questions before serving a break notice.

● Who serves the notice, and on whom?

This is not always as obvious as it would seem. Unless the lease states that the break is personal, it will generally be exercisable by successors in title, without the need for registration. Where the lease is silent on the issue, the break will be exercisable by the tenant alone. The break notice must be served by the correct party on the correct party. It will normally be served by the tenant or its agent, not necessarily by the occupier of the premises. The recipient should be the landlord, not necessarily the party that receives the rent or manages the property.

Practical measures: The tenant – or its lawyers – can check the landlord’s details by examining the superior title, checking the most recent rent review memorandum and

seeking written confirmation from the landlord.

● When should the notice be served?

Time is usually of the essence. If the break date is drafted by reference to the lease term, it will be necessary to review the definition to ensure that the notice contains the correct break date. Unless other provisions override this, where the term is expressed to begin on a certain date, it will generally include that date. If the term runs from a certain date, that date will be excluded.

Practical measures: The notice must be served the correct number of months before the break date so that it expires on that date. If the break clause is not clear on this point, the notice should contain a form of wording that may save it from being invalid if an incorrect break date is used. This will be different in every notice. In some cases, repeating the description of the break date set out in the clause, rather than merely specifying a date, may be sufficient.

● What must the tenant do?

The *Code for leasing business premises in England and Wales* states that “the only preconditions to tenants exercising any break clauses should be that they are up to date with the main rent, give up occupation and leave behind no continuing subleases”.

Modern leases often have minimal conditions precedent; specified conditions must be strictly performed and performance may be assessed over the entire term. A landlord may even be able to use a remedied breach to prevent the exercise of a break. Absolute conditions are construed as such; those that are not absolute require care.

Fitzroy House Epworth Street (No 1) Ltd v The Financial Times Ltd [2006] EWCA Civ



329; [2006] 06 EG 174 examined the meaning of a requirement for material compliance with covenants. It concluded that this is an objective test. Material compliance is assessed partly by reference to the landlord’s ability to relet or sell the property without delay or additional cost.

Practical measures: The tenant can commission a compliance audit, with surveyors’ advice, allowing sufficient time to assess any breaches and, if necessary, remedy them before the break notice has to be served. It can ask the landlord to confirm any necessary steps in order to comply with preconditions. Landlords may not provide this information or delay in doing so until the tenant is at risk of failing to comply with the conditions by the break date. This is a particular risk with regard to repairing covenants. The tenant may have to repair to a higher standard than required by the lease

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to avoid losing the break for non-compliance. If the landlord agrees to waive any conditions, this should not be done on a without prejudice basis; it must be clear to which of the conditions the waiver applies.

The tenant could pay disputed sums without prejudice to its position that these are not owing, to ensure that there can be no doubt about its compliance with covenants. If rent is payable in advance, the whole quarter's rent must be paid on the relevant payment date, even where the break date falls in the middle of a quarter.

● **How should notice be given?**

Most leases do not specify a form of notice. Where a break option stipulates a means of service, whether that method is mandatory or illustrative will depend on the terms of the lease. Even if it is mandatory, service in a manner that does not negatively affect the recipient will often suffice. The tenant must

ensure that the recipient receives the notice – proof of postage will not be adequate.

Practical measures: Ideally, the tenant should serve the notice personally on all the known addresses of its landlord, solicitor and managing agent. It should disclose the existence of any agency, if it uses an agent to send the notice, retain evidence of service and ask the landlord to acknowledge receipt. The notice should relate to the entire premises unless the lease states otherwise. The tenant should ensure that it has sufficient time to resend the notice if there is any doubt that the landlord has received the original.

● **Going wrong**

Prudential Assurance Co Ltd v Exel UK Ltd [2009] EWHC 1350 (Ch); [2009] PLSCS 200 (see also p94) illustrates how important it is to get the “who” element

right. A warehouse was let to two companies that were part of the same group: one trading, one dormant. The tenants’ solicitor served a notice that referred only to the trading company. The court held that the break notice was invalid.

Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd [1997] 24 EG 122; [1997] 25 EG 138 established the principle that a minor defect in a contractual notice will not necessarily invalidate the notice if the reasonable recipient, with knowledge of the factual background, would not be perplexed by such an error.

Cases since *Mannai* show that this rarely helps where the wrong party has been named. If a parent or group company, rather than the tenant, has served a break notice, a letter from the tenant to the landlord confirming that it was served by an agent can sometimes save the notice.

If a tenant has inadvertently served a defective notice and the landlord has treated it as being valid, and by this has induced the tenant to, for instance, enter into a contract for new premises, the tenant may be saved by the principle of estoppel. In such a situation, the landlord may be prevented from denying the notice's validity.

Mending the break

Tenants sometimes serve break notices and then change their minds. This may happen when the notice period is long and a tenant's circumstances change, a tenant cannot find alternative premises or it hopes that threatening to break will enable it to renegotiate the lease terms. However, a break notice is unilateral and cannot be withdrawn, even if the parties attempt to agree to the withdrawal.

Where the break terminates the existing tenancy, the tenant will occupy under a new lease after the break date. By implication, this may be on the same terms as the old lease save as to term. The new lease may be on a quarterly periodic basis and therefore protected by the Landlord and Tenant Act 1954. If negotiations to vary the lease have taken place on the mistaken basis that the old lease is continuing, the new tenure might be a tenancy at will, which can be terminated immediately on notice. Once a variation has been made by deed, it is treated as a new lease containing the terms of the old lease subject to the variation.

HM Revenue & Customs has recognised the potential problems faced by tenants wanting to withdraw a break notice with the landlord's agreement. The old lease will be treated as continuing, for stamp duty land tax purposes, if the landlord and tenant agree to the withdrawal of the notice before the break date.

The old lease can sometimes continue after the service of a break notice in two situations. The first is when the notice is arguably invalid; perhaps the tenant or the landlord has been wrongly named. In this case, the parties may agree that the notice is invalid and is ineffective to terminate the lease. The agreement should be recorded in writing to obviate later disputes. The second applies where the tenant has not complied with the conditions of the break clause.

Since most such clauses require vacant possession, remaining in the premises and continuing to use them may render the break notice ineffective. The landlord may say that it has waived the conditions and will treat the tenant as a trespasser and therefore liable to pay an amount equal to double the passing rent under the Distress for Rent Act 1737.

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