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# TENANT PAYBACK TIME – HAS THE SUPREME COURT GIVEN THE GREEN LIGHT TO APPORTIONING RENT (IN SOME CIRCUMSTANCES)?

In the recent case of *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd and another* [2015] UKSC 72, a tenant exercised a break right and then sought to recover the proportion of the rent already paid in advance that related to the period after the lease had come to an end. The tenant argued that there was an implied term requiring the landlord to refund this sum. The Supreme Court rejected that argument.

This note considers the Supreme Court's reasoning and sets out its practical consequences for both landlords and tenants.

**BACKGROUND**

The parties had entered into a lease which was due to expire on 2 February 2018, but which gave the tenant a right, on six months' notice, to terminate the lease on 24 January 2012. The break right was conditional on (1) there being no arrears of rent on the break date; and (2) the tenant paying a break fee of £919,800 plus VAT.

The tenant served a break notice on 7 July 2011, paid the full quarter's rent which fell due on both 29 September and 25 December (i.e. the last rent payable before the lease came to an end) and, on or about 18 January 2012, paid the break fee. As a result, the lease duly came to an end on 24 January 2012.

As it had paid a full quarter's rent in advance on 25 December 2011, the tenant sought to recover the rent covering the period after the lease had ended (i.e. that part of the rent covering the period from 24 January 2012 to 24 March 2012). The tenant argued that, in the absence of an express term to this effect, this was an implied term of the lease.

The tenant's argument was successful in the High Court, but this decision was overturned by the Court of Appeal. The tenant appealed to the Supreme Court.

**IMPLIED TERMS**

A large part of the Supreme Court judgment focussed on the law on implied terms and it may be this element of the judgment that is most remembered.

The Supreme Court held that the test for implied terms set out by the Privy Council in *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 should no longer be regarded as authoritative. The correct test for whether a term should be implied into a contract is whether the proposed implied term is (1) necessary to give business efficacy to the contract or (2) so obvious that it goes without saying.

A fuller update on this issue can be found on our website.

**APPORTIONMENT OF RENT PAYABLE IN ADVANCE**

The Supreme Court rejected the tenant's arguments.

The key points arising out of the judgment are as follows:

- The Apportionment Act 1870 provides that rent should be considered as accruing from day to day and is, therefore, apportionable. The Supreme Court endorsed the century-old decision in *Ellis v Rowbotham* [1900] 1 QB 740, which decided that the Apportionment Act only applied to rent payable in arrears and not to rent payable in advance.

- There was a clear and consistent line of judicial decisions, which formed the "*backcloth*" against which the terms of this particular lease were agreed, that neither the common law nor statute allows for the apportionment of rent payable in advance. Against that background, express words would need to be included in the lease before it could be said that the parties intended the rent payable in advance to be apportioned in some circumstances.

- The lease in question was a very full and detailed document, which covered a wide range of contingencies and which had been entered into by two experienced parties with the benefit of legal advice. The court should be slow to imply terms in those circumstances.

- The proposed implied term sat uncomfortably with the express provisions of the lease, which clearly set out precisely which payments were to be made in the event of the tenant exercising its rights under the break clause.

**TENANT EXERCISES BREAK RIGHT – DOES IT HAVE TO PAY LAST QUARTER'S RENT IN FULL?**

Whilst the Supreme Court's decision suggests that, in many cases, tenants who exercise a break right will need to pay a full quarter's rent on the quarter date before the lease comes to an end – and will be unable to recover any "over-payment" referable to the period after the break date - some of Lord Neuberger's comments suggest that this will not be the position in every case.

The lease in this case provided that the rent was to be paid "*proportionately for any part of a year by equal quarterly instalments in advance*". If the lease had run its course up to February 2018 (the contractual expiry date) it was accepted that the tenant would have been entitled to apportion the rent payable in December 2017 to reflect the fact that the lease was coming to an end in the middle of the next quarter.

Applied in the context of the tenant exercising the break clause, Lord Neuberger said:

*"…if the [tenant] had paid the £919,800 plus VAT [break fee] before 25 December 2011, the claimant argues (rightly in my view) that it would have been clear on 25 December 2011 that the Lease would end on 24 January 2012, so that the claimant would only have had to pay an appropriate proportion of the Basic Rent on 25 December 2011."*

(emphasis added)

Thus, Lord Neuberger appears to have accepted the tenant's argument that, if it had paid the break fee before 25 December 2011, it would only have needed to pay an **apportioned part** of the rent falling due on 25 December 2011, because all the conditions attached to the exercise of the break right would have been fulfilled and the parties would have been certain that the lease was coming to an end on 24 January 2012. This element of the Supreme Court's decision, which seems to have been largely overlooked, may have profound implications.

**IMPLICATIONS OF THE SUPREME COURT'S DECISION**

It is common for commercial leases to contain a provision for rent to be paid "*proportionately for any part of a year by equal quarterly instalments in advance*", or similar language. After all, leases do not often start on a rent payment date or finish at the very end of a quarter.

Lord Neuberger's comments suggest that, where a lease contains such a provision, tenants may only be required to pay an apportioned part of the final rent payment upon exercising a break clause, **provided that** the tenant has complied with all of the conditions attached to the break right.

This will not be possible where there are conditions that cannot be fulfilled until the break date, such as a requirement for vacant possession, or compliance with repairing obligations, both of which are common.

But in the absence of such conditions, the Supreme Court appears to have given the green light to some tenants apportioning rent in the run up to a break date.

Lord Neuberger's comments are, strictly speaking, *obiter*, and so the lower courts are not bound to follow that part of the decision. His views are likely to be highly persuasive, given his seniority and expertise in property law, but the position cannot be treated as settled.

**GIVEN THE UNCERTAINTY, WHAT SHOULD A TENANT DO?**

Upon exercising a break right, a cautious tenant might still prefer to pay the last quarter's rent in full, even where the lease contains language about apportionment and there are no more conditions attached to the break right.

The difficulty for a tenant that proceeds on this basis, however, is that it may not be able to recover any "overpaid" rent from the landlord after the lease has come to an end - even if a court subsequently decides that, on the proper construction of the lease, the tenant was only ever required to pay a proportion of the final rent payment. In view of the Supreme Court's decision in this case, it will be difficult for a tenant to argue that there is an implied term requiring overpaid rent to be refunded.

An argument that there would be a total failure of consideration for such an overpayment was considered (albeit briefly) and rejected at first instance in *M&S v BNP Paribas*. Furthermore, it may be difficult for a tenant to argue that it was operating under a mistake of law (and therefore entitled to recover any overpayment from the landlord as a claim for unjust enrichment). This is because the tenant would not have been mistaken at all: it would have made a commercial decision to pay the rent in full to avoid the risk that the break right might not have been validly exercised.

This anomaly may be addressed in subsequent cases that consider the effects of *M&S v BNP Paribas* - landlords and tenants should watch this space.

In the meantime, a pragmatic solution for tenants who find themselves in this position may be to apply to the court for an urgent declaration as to whether or not they are obliged to pay the rent in full. The courts may be prepared to consider and decide the application before the rent in question falls due, particularly where the sums at stake are sufficiently large.

**EXPRESS TERMS GIVE THE ONLY REAL CERTAINTY**

Tenants who wish to ensure that they are not obliged to pay a full quarter's rent when they exercise a break right that ends the lease between quarter days should seek to include an express term to this effect in the lease. Whether or not this can be achieved will, of course, ultimately be a question of the parties' respective bargaining power.

In this case, Lord Neuberger said that he could see force in the argument that allowing a landlord to retain rent referable to the period after the lease was terminated was unfairly prejudicial to the tenant and a pure windfall to the landlord. As a result, he said that including an express term of the lease for reimbursement would "*seem to be reasonable and equitable*".

Tenants may, therefore, consider that requesting an express term to this effect may not be unreasonable – and refer to Lord Neuberger's comments in support.

Landlords will, of course, note that these comments were made in the context of a lease which also provided for the payment of a substantial break fee.

**WHAT HAVE WE LEARNED?**

Absent an express term, tenants will normally be obliged to pay the final quarter's rent prior to a break date in full.

Where (as will usually be the case) the exercise of the break is conditional on arrears of rent being paid in full, a failure to pay the rent in full is likely to result in the purported exercise of the break right being invalid.

In this sense, the Supreme Court's decision is good news for most landlords, who will now be able to insist on the final quarter's rent being paid in full and, where the tenant fails to do so, to treat the lease as ongoing.

Where the lease provides for the final quarter's rent to be apportioned and where all the conditions attached to a break right have been complied with, a tenant may only be required to pay an appropriate proportion of the final quarter's rent. If the conditions attached to a break right cannot all be satisfied until the break date, however, this option will simply not be available to a tenant.

Lord Neuberger's comments on this point are, strictly speaking, *obiter* and the position is not completely certain. A cautious tenant may still prefer to pay the final quarter's rent in full. In that situation, however, it may be difficult for the tenant to bring a claim to recover the overpaid rent - although this produces a surprising outcome (a windfall for the landlord) and this may well be addressed in future cases.

**We would like to thank Kester Lees of Falcon Chambers, for his helpful advice and assistance on the points raised in this article. Kester appeared in the Supreme Court in *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd and another.***

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**DECEMBER 2015**

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