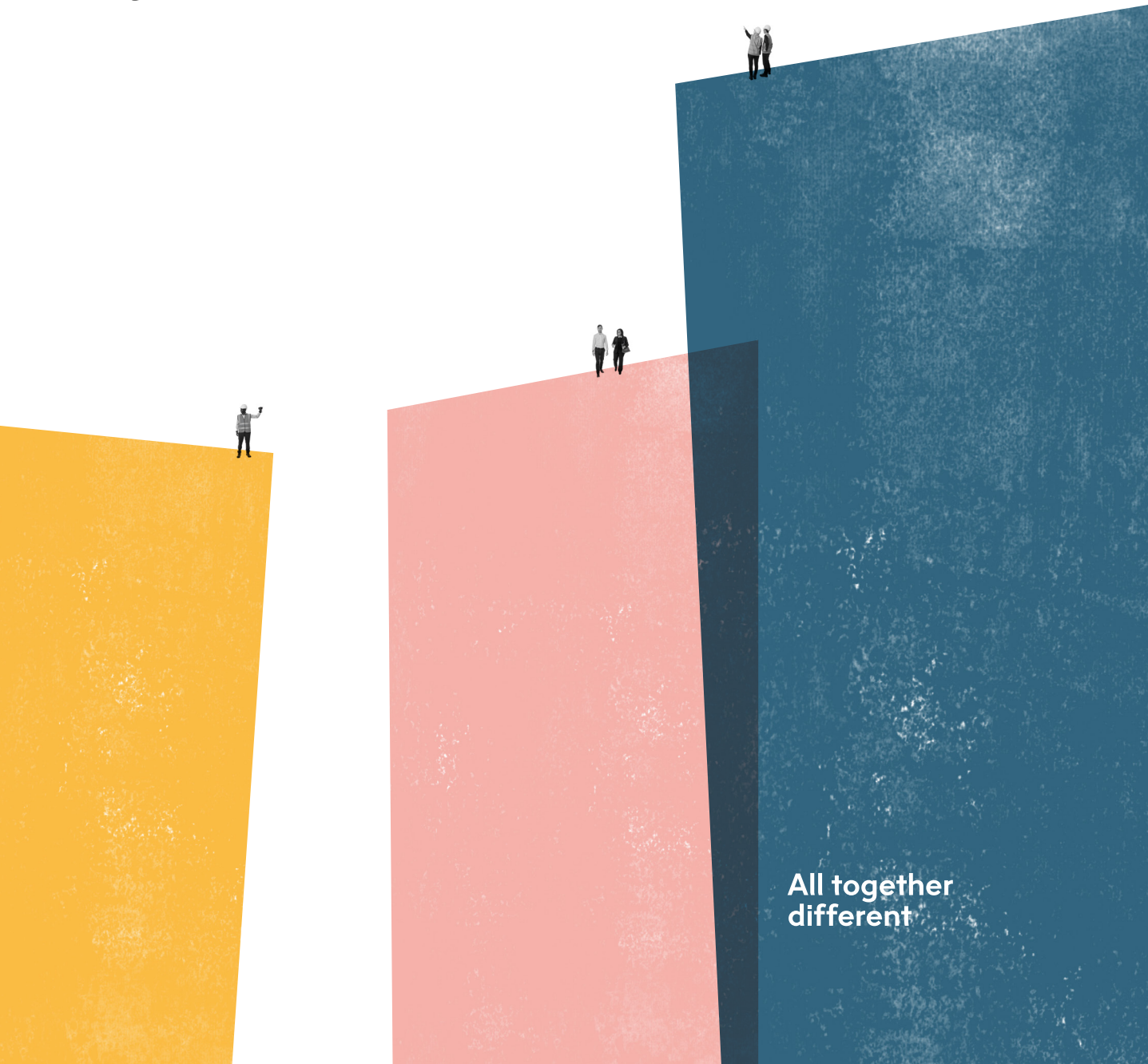


HOLLIS

Dilapidations – a guide for occupiers



All together
different

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What is dilapidations?

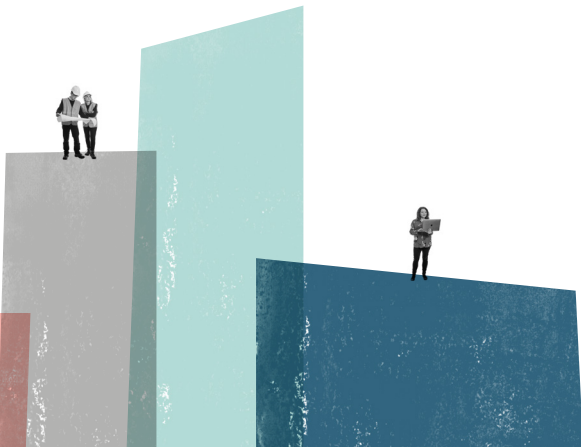
In almost all commercial tenancies there will be obligations relating to the condition and layout of the property. Occupiers – and, usually to a lesser degree, landlords – can hold such obligations and these are set out in the lease agreement. A failure to comply with these obligations will result in a claim for what is commonly known as dilapidations.

Assuming it is the occupier's responsibility, a dilapidations matter is usually resolved by:

- The occupier carrying out the works required to bring the property up to the required standard; or
- The occupier paying the landlord an agreed sum (called 'damages') instead to recompense the landlord.

Identifying the extent to which there are such obligations, who has to meet them and the action that can be taken if they are not met is a specialist area which requires careful consideration by a suitably experienced chartered building surveyor.

The [dilapidations guidance note](#) published by the Royal Institution of Chartered Surveyors (RICS) provides useful information and also sets out the RICS's expectations of the performance of its members in relation to dilapidations matters.



Why should occupiers care about dilapidations?

Dilapidations claims are vitally important to any occupier because:

Cost

The cost of fulfilling repairing, and other obligations can be substantial.

Reputational risk

Dilapidations claims can end up in court.

Time

Managing a claim can take up significant time and effort.

Business risk

If occupiers do not plan properly for dilapidations, lease events could be missed/ frustrated, leases could be forfeited, or landlords may re-enter the premises to carry out urgent works - charging the costs of doing so back to the occupier.



Property:

The Potteries Shopping Centre, Stoke

Client:

SportsDirect International Plc

**Claim reduced by 97%
and settled at £5,000**



When should occupiers consider dilapidations?

Prior to signing a lease

The principle of 'buyer beware' holds as true when taking a lease of property as it does when buying it, and so occupiers should familiarise themselves with the lease terms and their dilapidations implications prior to signing the lease. A chartered building surveyor can advise on the implications of the clauses occupiers are signing up to as well as checking the condition of the premises via a [pre-lease advice survey](#). Prospective occupiers may also wish to appoint a solicitor to offer legal advice on any non-standard or onerous lease covenants.



These are some of the questions that an occupier needs to ask in order to decide how much money will need to be set aside throughout the term of the lease to finance any repairs by lease expiry:

- Is the lease being offered on a full repairing and insuring or internal repairing basis? Put simply, will you be responsible for maintaining the entirety of the building or just the internal non-structural elements?
- If the lease is granted on an internal repairing basis, have you checked that the service charge provision for repairing and maintaining the common areas is not excessive or whether your contribution is capped?
- Whether the repairing obligation is fair. Are the liabilities too onerous?
- If you have negotiated a rent-free period in a lease to compensate for a building's poor condition, will the savings in rent be sufficient to cover the costs of repairing the building in order to meet your repairing obligations?
- What are your liabilities when the lease expires?
- What proportion, if any, of alterations you carry out during the lease will need to be reinstated at the end of the lease?
- What repairs will need to be undertaken, and when, leading up to lease end?
- What needs to be redecorated and cleaned, how often and to what standard?

Property:

Warwick House, Zurich House, York House
and Infor House, Farnborough

Client:

BAE Systems

**Claim reduced by 81% and
saved the tenant £7 million**



What if the premises are in a poor state at the outset?

This is a particularly important consideration. Most commercial leases require the occupier to 'put and keep' the property in repair. Unless the landlord and occupier specifically agree otherwise, the fact that the premises were in a poor condition when the occupier took them on is largely irrelevant. The occupier is still obligated to put them right.

However, the landlord may be persuaded (at the time of the original lease signing) to agree that the premises be returned at the end of the lease in a condition similar to the state in which the occupier took them. In this case, the occupier should ensure that their condition is established, recorded and attached to the lease as a schedule of condition. The standard lease wording also needs to be varied to reflect the reduced obligations.

Schedules of condition or inventories of fixtures and fittings can also be useful in establishing the layout and configuration at lease commencement when the reinstatement liability is reviewed at lease end.

During the lease term

Regular and planned maintenance can avoid greater expense at expiry (or sooner determination) of leases. Occupiers should schedule a regular repairing and redecorating regime throughout the term. In addition, it is recommended that occupiers consider their potential future dilapidations liability in good time, and budget for that future obligation. Financial reporting standard 102 suggests that provision is made in advance and may be allowable against future taxes.

If an occupier carries out alterations to the premises, then it is likely that their landlord may require them to reinstate those alterations shortly before the end of the lease. A licence for alterations or licence to alter is often agreed which sets out the obligations of each party including how the tenant will undertake the works, the documentation/consents required, together with arrangements for reinstatement at lease end.

Near the end of the lease term

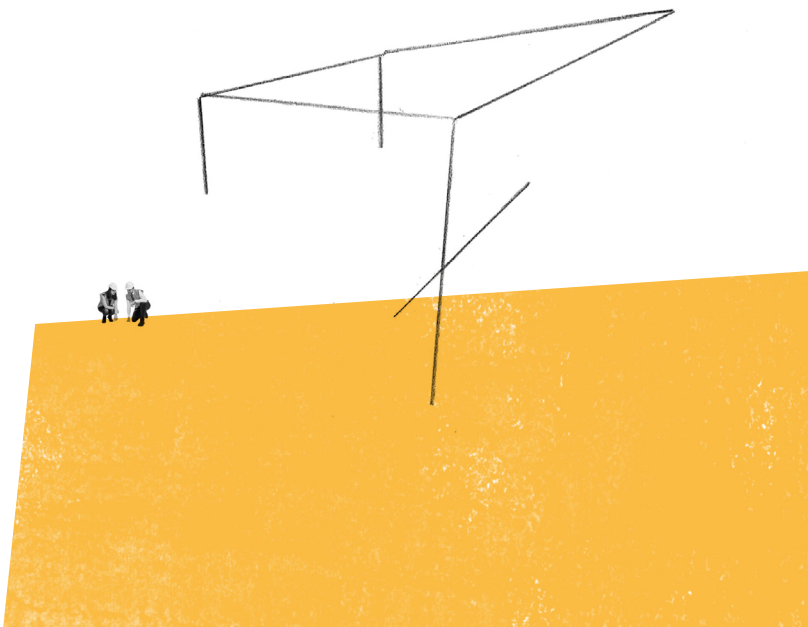
Occupiers should be aware of the extent of dilapidations work they may be liable to undertake in line with their lease obligations. This can be a complicated assessment - it is therefore normal for a landlord to engage a chartered building surveyor, experienced in the field of dilapidations, to advise them.

Occupiers then have a decision to make: undertake the works or agree a financial settlement in lieu. There are various 'pros' and 'cons' of each option - an occupiers' surveyor can advise on those as each set of circumstances are unique. However, agreeing a financial settlement does provide more certainty and allows occupiers to occupy the premises up until expiry without the disturbance of works. In our experience only a third of occupiers elect to carry out the works, with two thirds preferring the certainty of a financial settlement.

Unless occupiers have completed all the building work which the lease and any licences for alterations require of them, then occupiers should expect to receive a schedule of dilapidations from their landlords. A schedule of dilapidations lists the allegations, suggests remedial works and sometimes estimates the costs of the remedial works that the occupier has failed to address according to their lease covenants.

The schedule of dilapidations may be sent shortly before or shortly after the end of the lease term. If it is sent to occupiers before the end of the lease term, then the landlord may update it at the end of the lease to reflect any changes to the premises.

Even if the landlord does not send the occupier a schedule of dilapidations, the occupier still has potential dilapidations obligations and a chartered building surveyor can give advice as to the scope and potential cost of the obligations.





Property:
Sainsbury's Argos portfolio, UK
Client:
Sainsbury's Argos

**Saved client £100,000 on
landlord's original claim**

After lease expiry

Occupiers should receive a schedule of dilapidations and, within about 56 days after the end of the lease, also a quantified demand. However, occupiers should be aware that the landlord's entitlement to start a claim will not become legally time-barred for 6 or 12 years (depending on how the lease is signed) after expiry of the lease.

The quantified demand sets out what the landlord considers to be its likely overall loss as a consequence of the occupiers alleged breaches, including things like loss of rent and professional fees incurred. Because of other factors, such as market conditions and the landlord's future intentions for the property, the likely loss does not always equate to the cost of the works set out in the schedule of dilapidations.

The landlord or their surveyor should have endorsed the schedule of dilapidations to confirm that it is reasonable and reflects the landlord's intentions for the building. The landlord's intentions are important as it can have a significant impact on the value of the claim.

Occupiers are expected to respond to the schedule of dilapidations and/or quantified demand within 56 days of receipt. Occupier's responses (which should also be endorsed by their surveyors) normally take the form of a covering letter/email and a scott schedule. A scott schedule is an extended version of the schedule of dilapidations which allows space for the occupiers surveyor to comment on the content of the schedule of dilapidations.

Normally, the surveyors appointed by the landlord and occupier meet and can narrow the differences sufficiently to recommend a settlement figure to their respective clients. If such a settlement is not possible then there is a potential for alternative dispute resolution (ADR) or even litigation.

Importance of conduct and evidence

Dilapidations disputes can ultimately end up in the courtroom. It is therefore important for occupiers to protect their position in the event that the landlord eventually commences proceedings. The courts' expectations of landlord and occupiers conduct at lease end are set out in the Ministry of Justice's [dilapidations protocol](#).

Occupiers should always obtain early advice from their chartered building surveyors. Occupiers may be advised to make offers to settle at various stages, and should consider such advice carefully, as it may be referred to later in court.

Landlords should not, however, profit from dilapidations payments and so the amount set out in the quantified demand is sometimes lower than that in the schedule of dilapidations. This may be because of a number of reasons including:

- The landlord intends to redevelop the premises;
- The landlord intends to upgrade the premises;
- A new occupier wants the premises left as they are and the terms of the new lease don't prejudice the landlord.



Property:
Amazon, Dublin
Client:
Amazon Web Services

**Saved client 70% from
the original claim**

Common areas of dispute

Disputes can arise over:

- Whether the items identified by the landlord's surveyor are really a breach of the lease covenants.
- What repairs and other works will need to be undertaken?
- What constitutes an appropriate repair?
- What is an appropriate response for an occupier in repairing or renewing the elements that were in disrepair at the start of a lease?
- Whether any or all of the occupier's alterations to the building have to be reinstated.
- What needs to be redecorated or cleaned, with what materials and possibly in what colours?
- The circumstances under which an occupier can exercise a break clause (that is, ending the lease earlier than lease expiry) and whether an occupier has complied with the break clause conditions. Such conditions can be extremely onerous and therefore difficult to satisfy.
- The landlord's estimates of the cost of the remedial works in the schedule.
- The value by which a premises has been reduced as a result of it being in disrepair.
- The impact of any future redevelopment of the premises on the occupier's dilapidations liabilities.

Our specialist dispute resolution team can help manage and mitigate disputes that may arise. We are known for our deep technical knowledge, our practical experience and our thorough approach in resolving a great range of property dispute cases during the past two decades.

We also continue to be supported by tier 1 ranked real estate KC Nicholas Dowding, making us the only UK real estate advisor with in-house legal counsel.



Need advice?

As market leaders in this specialist field our highly experienced team has offered advice to both landlords and occupiers across all property sectors for many years.

1345 instructions per year

Retail

Acting for tenant:

£8.02 psf

Average saving from original landlord claim:

72%



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Office

Acting for tenant:

£9.18 psf

Average saving from original landlord claim:

68%



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Industrial and logistics

Acting for tenant:

£4.70 psf

Average saving from original landlord claim:

55%



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