IN THE MATTER OF STRADBROKE HEALTH CENTRE

ADVICE

1 By a lease dated 8 November 1996 ("the Lease") Stradbroke Parish Council ("The Council") demised certain premises to the Stradbroke Health Trust ("the Trust") for a term of around 50 years[1]. The parcels clause[2] provides that the property demised was "all that piece of land situate adjacent to Wilby Road in the Parish of Stradbroke Suffolk as the same is delineated and edged red on the plan annexed hereto ("the Premises")". The plan shows no building within the edging, probably because the HC had not by the time it was drawn up, been built.

2 The matter comes to me because the parties are in dispute as to the proper interpretation of the rent review clause in the Lease, which provides, so far as is material, for the rent to be certified by a valuer "as the fair market rent of the premises with vacant possession … but disregarding any effect on it of the considerations specified in paragraphs (a) (b) and (c) of Section 34(1) of the Landlord and Tenant Act 1954 as amended by the Law of Property Act 1969." ("the RR Clause"). In essence, it is the Trust's position that the reference in the RR Clause to 'the premises' means that only the land is to be valued. By contrast, the Council contends that the land and the buildings standing on it ought to be valued. In default of agreement as to the rent, the parties have appointed Mr Alex Stefanovic as an expert valuer to determine it. In turn, he has instructed me to advise him as to the

[1] The precise term length is not immediately clear on the face of the Lease, since it is expressed in terms indicating an intention that the Lease would already have been extant before 1 April 1996. I do not need to resolve this issue for the purposes of my Advice.
[2] Clause 1

proper construction of the RR Clause in respect of the property to be valued.

THE LAW AND THE SCOPE OF THE RELEVANT / ADMISSIBLE EVIDENCE

3 It will I hope help the parties for me to set out some of the key legal principles involved in a case such as this.

4 Fundamentally, the process of construing a document is an attempt to identify the intentions of the parties. However, that is a process undertaken on an objective basis; the parties' actual subjective intentions are inadmissible. The Court looks at the document and tries, in the light of the admissible background factual matrix against which the document was agreed, to ascertain its meaning. Where, as here, the Court is faced with a document that is to be registered on a public register (a lease of this length was subject to compulsory registration), the background evidence that is available is much more restricted. In *Cherry Tree Investments v Landmain*, the Court of Appeal held that a mistaken omission from a registered charge could not be corrected by construing it in the light of a facility letter that preceded it. Lewison LJ said:

> *"The reasonable reader's background knowledge would, of course, include the knowledge that the charge would be registered in a publicly accessible register upon which third parties might be expected to rely. In other words a publicly registered document is addressed to anyone who wishes to inspect it. His knowledge would include the knowledge that in so far as documents or copy documents were retained by the registrar they were to be taken as containing all material terms, and that a person inspecting the register could not call for originals. The reasonable reader would also understand that the parties had a*

choice about what they put into the public domain and what they kept private. He would conclude that matters which the parties chose to keep private should not influence the parts of the bargain that they chose to make public. There is, in my judgment, a real difference between allowing the physical features of the land in question to influence the interpretation of a transfer or conveyance (which we do) and allowing the terms of collateral documents to do the same (which we should not). Land is (almost) invariably registered with general boundaries only, so the register is not conclusive about the precise boundaries of what is transferred. Moreover, physical features are, after all, capable of being seen by anyone contemplating dealing with the land and who takes the trouble to inspect. But a third party contemplating dealing with the land has no access to collateral documents."

5 Two points arise from the foregoing, which can conveniently be dealt with at the outset. First, the submissions / evidence put forward by both parties as to their subjective intentions are inadmissible and cannot be taken into account when it comes to construing the Lease. Second, the contemporaneous collateral documentation adduced by the parties – in particular the correspondence and Feasibility Study – would not have been things which 3rd parties could reasonably have been supposed to know about[3].

6 Pausing here, the exclusion of the correspondence and the Feasibility Study is a matter which is beneficial to the Trust in this dispute. While I accept they are not totally unambiguous, in my view they definitely point towards the parties *subjectively* intending that more than a mere ground rent would be payable in the future. Despite that being my

[3] See also *Attorney General of Belize v Belize Telecom Ltd* [2009] 2 All ER 1127 and *Cosmetic Warriors v Gerrie* [2015] EWHC 3718

impression, I do not take account of it when assessing the meaning of the Lease on an objective basis.

7 In addition, the parties' subsequent dealings / correspondence are not admissible as to the meaning of the Lease either.

8 As such, while I have read all of the material supplied to me, the majority of it is, in fact, irrelevant to the task which I am asked to perform.

9 I should add at this stage that I have seen a point was taken at the end of December 2018 as to whether without prejudice material ought to have been included in the papers. Without taking a view as to whether that is correct, it concerns the 2016 rent review and as such, given what I have set out above, it is not relevant for my considerations so I would not be taking it into account anyway.

10 Returning to the legal position, certain general propositions about rent reviews are stated in Woodfall: Landlord & Tenant[4]:

> *"In construing a rent review clause, and in particular those parts of it that prescribe the basis of valuation, three fundamental principles must be borne in mind. First, the general purpose of a rent review clause is to keep the rent in line with current property values having regard to the current value of money, and not to provide either the landlord or the tenant with a windfall based upon an artificial basis of valuation. Secondly, as with any valuation, the valuer should adhere as closely as possible to reality and depart from it only when and to the extent that the rent review clause so requires, either expressly or by necessary implication. Thirdly, the overriding objective of a rent review clause*

[4] Para 8.027

is to arrive at an up to date rent, and the literal construction of a rent review clause may have to be sacrificed to achieve this result.

However, this is not to say that there is any presumption that the rent payable under a rent review clause should always be a market rent or that a rent review clause should always produce an increase in the rent.

The presumption of reality may have to give way to clear words in a lease, and the courts recognise that it is common for landlords to attempt to manipulate reality in order to achieve a higher rent. Similarly, where the words of a disregard are clear, the court will give effect to it, even though the result may not seem commercially sensible"

11 Woodfall continues, at paragraph 8.030:

"Normally the property to be valued is the demised property. However, there is nothing to prevent the parties from fixing the rent by reference to a hypothetical building, and this is sometimes done where the actual building has been modified or adapted to suit the particular needs of the actual tenant or is otherwise difficult to compare with buildings generally.

As a general rule, the property must be valued in the physical condition in which it stood on the valuation date, without regard to how it got into that condition."

12 In *Ponsford v H.M.S. Aerosols* [1978] 3 W.L.R. 241, the House of Lords considered a dispute over whether a tenant's improvements fell to be disregarded. Viscount Dilhorne said this:

"In the absence of any such express provision as Parliament thought it necessary to include in section 34, I do not think that one is entitled to conclude that by the use of the words 'assessed as a reasonable rent for the demised premises' the parties were seeking to express their agreement that in

assessing the rent, the effect of improvements made by the lessees was to be disregarded.

If the parties to this lease had agreed that the effect of improvements was to be disregarded in assessing the rent, that could easily have been stated and if that had been agreed, I expect it would have been … In the absence of any such express provision as Parliament thought it necessary to include in section 34, I do not think that one is entitled to conclude that by the use of the words "assessed as a reasonable rent for the demised premises" the parties were seeking to express their agreement that in assessing the rent the effect of improvements made by the lessees was to be disregarded."

12 In the same case, Lord Fraser said the following, referring to the general proposition of law that anything affixed to the land (such as a building) is treated as the land:

"The premises would have included the improvements without express provision to that effect, on the principle that anything made part of the premises by the tenants enures to the landlord"

13 *Goh Eng Wah v Yap Phooi Yin* [1988] 2 EGLR 148 concerned the demise of land on which the tenants built a cinema at their own expense. Lord Templeman said:

"By well-established principles, that rent would issue out of the land including any buildings from time to time on the land and would prima facie be referable to the value of the land plus buildings."

He then considered whether there was anything in the language of the lease which displaced that construction, but concluded that the parties

intended that the rent to be fixed by the arbitrator should include them. He continued:

> *"… if the parties intended that the rent fixed by an arbitrator should ignore the buildings on the land, they should and would have given express instructions to the arbitrator for that purpose. In the absence of any such express instructions in the lease, then whatever the parties may in their heart of hearts have intended, the lease on its true construction does not authorise any deviation from the usual rule and it follows that the rent must be fixed by reference to the land and the buildings thereon."*

14 *Braid v Walsall MBC* (1999) 78 P. & C.R. 94 was a decision of the Court of Appeal in which the Court first endorsed the principle that, in construing a rent review provision there is a prima facie assumption that the parties intended that the premises should be valued as at the rent review date, that is to say together with any buildings situated thereon at that date. Sir Christopher at 102 then went on to say this:

> *"Nevertheless, all the authorities which established that proposition recognise that it is open to the parties to a lease to agree that the valuer shall assess the rent on the basis that, notwithstanding reality, the land is still undeveloped. And though Lord Templeman in Goh v Yap and some other similar dicta have referred to the need for 'express' instructions to negative the general rule, I do not think it could be or has been argued that this means that the lease has to include words which specifically and in terms [provide] that buildings shall not be taken into account in the valuation. All it means is that the lease must give a very clear indication of a contrary intention, if it is to negative the general rule."*

15 In *Sheerness Steel v Medway Ports Authority* [1992] EGLR 133, the rent review clause expressly provided for the disregard of certain

improvements, that is buildings standing on the premises. It said nothing about any other kind of improvements. The question was whether the valuation should take into account extensive earth moving operations by which the tenant had improved the property at his own expense. The Court of Appeal decided that the express exclusion of buildings and certain other provisions in the lease made it clear that only the buildings were to be disregarded[5].

16 Finally, In *Ipswich Town Football Club v Ipswich Borough Council* [1988] 2 EGLR 146 the Vice-Chancellor decided that the terms of the rent review clause in that lease required the buildings to be disregarded. The lease to the football club distinguished in many places between what it called "the sports ground" and the buildings and erections upon it. The rent review clause required a determination of the rental value of the "sports ground" and the Vice-Chancellor concluded that this meant only the unimproved land. This was a case in which the *prima facie* rule of construction was rebutted by the particular language of the instrument.

ANALYSIS

17 There is immediate appeal in the Trust's arguments. The parcels clause defines "the Premises" as a "piece of land"[6], while the RR Clause refers to the property to be valued as "the premises". Although that term is not capitalised in the RR Clause, I think that is likely to be a slip and nothing can be taken from it. Thus, the simple argument runs, the RR Clause requires the land itself, and no more, to be valued.

[5] See also *Laura Investment v Havering LBC* [1992] 1 EGLR 155
[6] The fact the front page of the Lease also refers to it being a "lease relating to land at Wilby Road" does not add anything more to the parcels clause

18 I also note that elsewhere in the Lease, distinctions appear to be drawn between the land on the one hand, and buildings erected on it, on the other (see, for example, clauses 2(1), 2(2), 2(11), 2(12), and 2(13)).

19 The use of distinctions between the land and buildings was a key feature in the *Ipswich FC* case, where the Court ended up deciding that only the land was to be valued.

20 The Trust also gains support from the proposition that, in general, it is considered unlikely that tenants will be keen to have agreed to pay for both a building's construction, and reviewed rent based on the enhanced value created by that building[7].

21 However, while on the face of the Lease, the parcels expressly referred only to land, in fact by the time the Lease was executed, the Health Centre ("HC") had already been built and was in use. Its existence is part of the admissible factual matrix. Quite plainly, given its existence, it was intended to be demised by the Council to the Trust. As noted above, as a matter of law, buildings are considered to be part and parcel of the land. Accordingly, on this basis, the reference to the land *in the parcels clause at least* must be taken as meaning the HC too.

22 If the RR Clause is to be read consistently with the parcels clause, both references to the 'premises' would therefore have to be taken as including the HC. They do not *have* to be so construed, so the question is whether, on the facts of this case, they should.

23 The Trust would be entitled to argue that the obvious intention of the parties when the lease was drafted was that the HC would not by then have been built (otherwise clause 2(1) would make no sense). That in

[7] See *Coors Holdings v Dow Properties* [2007] EWCA Civ 255

turn gives rise to a potential argument that the RR Clause was agreed at a time when 'the Premises' were not intended to encompass the HC.

24 That is a reasonable argument, but the counter is that the HC was envisaged from the outset – whether or not it was thought that it would already have been built by the start of the Lease. Once built, it would have formed part of the demised property regardless.

25 Moreover, the Lease does not consistently differentiate between the land and the HC. For example, while I have referred to certain clauses already which do appear to differentiate, clauses 2(4), 2(5), 2(6), 2(7), 2(8), 2(10), 2(14), 3(1), 3(2), 3(3), 4(1) and 5(1) do not. The key to the interpretation of the *Ipswich FC* lease in the tenant's favour was the consistency of differentiation[8].

26 The other point of relevance in *Ipswich FC's* case was that there, the parcels clause *expressly* referred to *both* the land and the buildings as part of the demise. The parcels clause gave a specific label to the land, and it was that label which was used in its rent review clause. That is not a feature of the case before me.

27 Another aspect of the *Ipswich FC* case was that the Court formed the view it was a very carefully drafted document[9]. I do not think that can be said for the Lease, which has numerous inconsistencies, refers to the HC works on the basis that they have not yet been completed, fails to include the HC on the plan, and makes a mess of the habendum[10].

28 I also note, although this is not a particularly strong point, that the Schedule containing the RR Clause is structured so as to provide for 2

[8] It was not 100% consistent, but the Court was able to dismiss any inconsistency as a drafting slip.
[9] Even allowing for the minor drafting slips
[10] The part dealing with the term

distinct periods – first, the period during which the Trust was repaying its borrowing, and then afterwards. Thus the periods are referable to the borrowing, not to the periods before, and after the HC was *built*. As was said in *Goh v Yap,* rent issues out of the land (including any buildings that are part of the land).

29 In terms of the context of the Lease, I have already mentioned the point about tenants not being expected to be willing to pay for the building's construction and then the enhanced rental value attributable to it. That is a legitimate point, but here I consider that it is not a *particularly* weighty factor. The Lease clearly aims to set up a balance between the interests of the Council and the Trust through the rent provisions. In recognition of the fact that the Trust had paid for the building, payment of the 'fair market rent' was to be deferred until after the borrowing had been repaid. No date was set for that to be done – an omission which was of course beneficial for the Trust. The concessionary rent during this period was just £1 pa. That is a very significant financial benefit for the Trust, and detriment to the Council, as compared with a full rent. It is also relevant to note that this was, essentially, a 50 year lease. Thus, while the Trust bore the expense of the HC, it would reap the benefits of occupation for a significant time.

30 Equally, the Trust would always have been in a position to generate income from the HC. Although I appreciate that in fact, both parties actually intended the Trust would sub-let to the doctors who would be running the HC, the documents expressing those intentions would not have been reasonably available to a third party so I have to discount them (and of course the subjective intentions themselves are not admissible). The Lease prohibits underletting (clause 2(5)), and that must form part of the material for me to consider. However, the

remainder of that clause seems to envisage that, at least unless / until 'some person or body were to succeed the Trust in managing the HC', the Trust would be 'managing it'. As the managers of the HC, it would presumably be in a position to generate income from the HC. Clause 5(2) also permits the assignment of the Lease to such a 'successor', who would themselves be able to generate income.

31 Thus it cannot be said, in my view, that the Trust's expenditure is so disproportionate that it lends much support to the Trust's argument that it cannot have been intended to pay a market rent for the HC. Taken in the round, the true position is more balanced than that.

32 What other indications are there in the Lease? An important part of the RR Clause is that dealing with disregards. A disregard refers to a matter which might otherwise be taken into account in the valuation process, but which the valuer is forbidden from relying upon. Of course, on the Trust's primary case, the HC would not fall to be taken into account anyway, as it claims it is not part of 'the Premises'.

33 Here, the disregard relates to, so far as is material, to tenants' improvements other than under an obligation.

34 I note it has been said that the disregard in the Lease should not apply to the HC because cl. 2(1) of the Lease contains an obligation to build the HC. The problem with this argument is that the works were not done pursuant to that covenant, as they were done before the Lease was executed.

35 The specific disregard in the Lease is referable to s.34(1)(c) of the Landlord & Tenant Act 1954 (as amended). The full version of this provision in force at the time of the Lease was:

34(1) *The rent payable under a tenancy granted by order of the court under this Part of this Act shall be such as may be agreed between the landlord and the tenant or as, in default of such agreement, may be determined by the court to be that at which, having regard to the terms of the tenancy (other than those relating to rent), the holding might reasonably be expected to be let in the open market by a willing lessor, there being disregarded—*

…

(c) any effect on rent of an improvement to which this paragraph applies,

…

34(2) Paragraph (c) of the foregoing subsection applies to any improvement carried out by a person who at the time it was carried out was the tenant, but only if it was carried out otherwise than in pursuance of an obligation to his immediate landlord and either it was carried out during the current tenancy or the following conditions are satisfied, that is to say,—

(a) that it was completed not more than twenty-one years before the application for the new tenancy was made; and

(b) that the holding or any part of it affected by the improvement has at all times since the completion of the improvement been comprised in tenancies of the description specified in section 23(1) of this Act; and

(c) that at the termination of each of those tenancies the tenant did not quit.

(underlining added)

36 The first point that is striking about this is the question how it can be relevant, in its full terms, to a rent review, given that the underlined part is applicable only to lease renewals. In *Euston Centre Properties Ltd v H. & J. Wilson Ltd (1982) 262 E.G. 1079*, the High Court took the view that it was permissible to essentially ignore most of s.34(2). There, the Judge said the 'relevant' part was simply:

"The rent payable … shall be such as … may be determined … to be that at which … the holding might reasonably be expected to be let in the open market by a willing lessor, there being disregarded… (c) any effect on rent of an

improvement to which this paragraph applies… (2) Paragraph (c) of the foregoing subsection applies to any improvement carried out by a person who at the time it was carried out was the tenant, but only if it was carried out otherwise than in pursuance of an obligation to his immediate landlord …"

37 In *Euston* it was held, in effect, that where there is an express disregard relating to s.34(1) (as amended), an improvement carried out by the tenant before it became the tenant (eg while it was a mere licensee allowed in by the landlord to do some works), that improvement would not be disregarded, because it wasn't carried out by a person *"who at the time it was carried out was the tenant"*. Here, so far as I am aware, no one contends that the Trust was in occupation prior to the Lease *as a tenant*[11]. On that basis, its construction of the HC would not fall to be disregarded under s.34(1)(c).

38 Accordingly, I see no evidential basis for advising that the HC constituted an improvement to be disregarded within the meaning of the Lease.

39 That in turn leads to the argument, which was endorsed in *Ponsonby*, and *Sheerness Steel* that where, as here, a lease contains express disregards, matters which do not fall within them ought normally to be valued.

40 It may well be apparent, from reading this Advice so far, that my view of the Lease is that as a matter of the language used, the HC forms part of the Premises and ought to be valued. My view is fortified because it accords with the fundamental principles involved in cases of this nature, in particular those relating to the desirability to value property 'as it is'

[11] I have seen reference in the minutes to the Council arranging for a letter of consent to be written permitting the Trust to enter onto the land prior to the Lease being finalised. Entry pending negotiations for a lease does not usually give rise to a tenancy: *Javad v Aqil* [1991] WLR 1007

(the presumption of reality). It also recognises the principle, recognised in *Braid*, that a 'very clear indication' is needed in a lease if the general position (that all of the property is to be valued) is to be restricted. I just do not think that such contrary indications as there are, are clear enough.

41 **On balance therefore, although this is a difficult and complex case, I am of the view that the Premises, within the RR Clause, includes the HC and can therefore be taken into consideration by Mr Stefanovic when certifying the fair market rent.**

42 I advise accordingly. Please do not hesitate to contact me should anything further be required.

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12th of February 2019