TFTI

A TUFFIN FERRABY TAYLOR WHITE PAPER

NEIL GILBERT, JUNE 2013

HAMMERSMATCH PROPERTIES V. SAINT-GOBAIN 2013

THIS TERMINAL DILAPIDATIONS CASE REITERATES THE NEED FOR EARLY AND ROBUST VALUATION-BASED EVIDENCE

TFTI

HAMMERSMATCH PROPERTIES V SAINT-GOBAIN 2013

These proceedings, brought before the High Court in May 2013, reiterate the appropriate measure of and remedy for disrepair, whilst also bringing into sharp focus the need for robust valuation based evidence.

The case concerns a terminal claim for dilapidations relating to a large1930s industrial and office premises known as the Norton Building in Welwyn Garden City. The defendants, Saint-Gobain Ceramics and Plastics Limited (tenant) and Saint-Gobain Abrasives Inc. (guarantor) were granted a fully repairing and insuring lease for a term of 25 years, which expired in December 2009.

Saint-Gobain's requirement for the entire site ceased soon after their tenancy commenced, and following a number of sub-tenancies, the building remained largely empty from 2003.Saint-Gobain, keen to be released from their liabilities under the lease, began investigating a possible surrender with the landlord, Hammersmatch in 1999. By 2002, the proposals had reached the point at which Hammersmatch had decided to apply for planning permission to convert part of the site to a health club with serviced offices above. The planning application was ultimately denied after numerous unsuccessful appeals. Thereafter, Saint-Gobain sought to secure further sub-tenants. By 2008, surrender was no longer viable.

In 2010, Hammersmatch made a claim for £6.8M, stating that its intentions were to undertake works detailed in the schedule of dilapidations. By 2011, dilapidations works had yet to commence. Hammersmatch cited difficulty in securing finance and requested an undertaking from Saint-Gobain to fund the works on a staged basis, but to no avail. Saint-Gobain disputed the business case for spending in excess of £5M, stating that there would be no demand, even in repair, for a building of this age and type. A reasonably minded landlord, it maintained, would not undertake such works. The parties had reached an impasse.

The hearing centred around two key issues: firstly, the extent of Saint-Gobain's alleged breaches of covenant and appropriate costs, and secondly, the application of the statutory limitation on damages.

The building surveyors had reached agreement over the building fabric related costs but the claim relating to the building services remained in dispute. Hammersmatch, for example had claimed for new boilers, and new lifts. Both had exceeded their design life and had not been properly maintained. However, the defendant's M&E engineer established that parts were still available, and the court, referring to the case of *Fluor Daniel Properties v Shortlands* [2001] held that age was not a prerequisite for replacement and found that two of the four boilers and all lifts could be repaired.

As result of previous agreements and the subsequent findings in court, the reasonable cost of the works that Saint-Gobain should have carried out were set at £2.4M plus professional fees. However, the foremost issue in this case was whether a statutory limitation should be applied under Section 18(1) of the Landlord and Tenant Act 1927.

The first limb of Section 18(1) provides that a claim for damages for a breach of covenant shall "in no case exceed the amount (if any) by which the value of the reversion (whether immediate or not) in the premises is diminished owing to the breach of such covenant". This puts a ceiling on the level of recoverable damages so that they cannot exceed the difference in the value of the property in and out of repair.

In making a case under s.18(1), the defendant's valuation expert assessed that the value of the premises was predominantly in the site itself, with only a small uplift in price applicable had the buildings been in repair. On this, the opposing parties were in major dispute. Hammersmatch considered that the buildings could be simply subdivided, and with limited cosmetic work, could be returned to full occupancy. The claimant considered that the difference in value between the buildings in and out of repair would be greater than the cost of repairs, and so, the cost of repairs should form the basis of a damages assessment.

TFTI

HAMMERSMATCH PROPERTIES V SAINT-GOBAIN 2013

Saint-Gobain's valuation expert, basing their submission on a single comparable site, assessed that the site had a value of £2.85M. It was concluded that as the building would be demolished it would theoretically have the same value in repair and out of repair. An uplift of £100k was applied, which it was thought a developer would pay if the buildings were in repair. The defendants therefore claimed that the diminution in value should not exceed £100k.

The claimant argued and asserted that the comparable site did have suitable correlation with the Norton Building for use in a valuation, and the £100k was a notional amount without factual basis. It was found that this particular comparable was not appropriate for the case, and the "finger in the wind" approach was dismissed. Instead, Hammermatch's valuation expert relied on a different calculation method, based on a residual valuation. The Judge accepted the defendant's site valuation of £2.1M.

It was concluded that the value in repair (£3.06M), would exceed the cost of putting the building in repair (£3.08M) including professional fees, financing costs and including a risk management allowance of 15%. Had such allowance been excluded, the cost of the works would have been less than the value of the site.

It was agreed that once the site value falls below the cost of repairs, the diminution in value is the difference between the site value and cost of repairs. The diminution in value was therefore set at £900k plus fees (relating to the preparation of the schedule), with interest to be added to the settlement.

It was confirmed that loss of rent is only recoverable as a claim for damages in connection with a breach of a repairing covenant. Since a statutory cap applied in this case, the claim for damages excluded consequential losses.

In contemplation of this case, consideration was given to a number of long established dilapidations principles:

1. A breach of covenant to keep in good repair and condition does not occur unless there is deterioration from a previous physical condition (Post Office v Aquarius Properties 1987).

2. The appropriate standard of repair must reflect the age, character, and locality of the premises (Proudfoot v Hart 1890). Furthermore, the obligation is not to return the premises to the same condition as at commencement (*Mason v TotalFinaElf UK* 2003).

3. Damages should be assessed by reference to the cost of repair, unless replacement would be cheaper (*Riverside Property Investments v Blackhawk Automotive* 2005 and *Carmel Southend Limited v Strachan and Henshaw Limited* 2007).

4. The fact that an element has exceeded its life expectancy is not in itself evidence of disrepair (Fluor Daniel Properties v Shortlands 2001).

5. The first limb of s.18 (1) applies when the cost of repair will exceed the value of the site. Specialist diminution advice should be sought early on to assess any impact.

6. Since a claim for loss of rent stems from a breach of the repairing covenant, the statutory limitation under s.18(1) applies.

7. The role of the dilapidations advisor is quite different from that of an expert witness and both sides should appoint suitably qualified advisors at each stage.