

**SUBMISSION
TO THE
MINISTER FOR JUSTICE, EQUALITY & LAW
REFORM**

**ON
UPWARD ONLY RENT REVIEW CLAUSES**

APRIL 2009

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OVERVIEW OF THE SOCIETY OF CHARTERED SURVEYORS

Dating back to 1895, the Society of Chartered Surveyors is the largest professional body in Ireland representing both the construction and property industries. The Society has strong links with the RICS which represents over 110,000 members across 120 countries worldwide and is one of the most internationally respected and high profile global standards and membership organisations for professionals involved in land, valuation, property, construction and environmental issues.

Representing over 2,200 qualified chartered surveyors and a further 1,000 probationers who are undergoing their assessment of professional competence in order to achieve the gold standard of chartered status, members of the Society are typically professionals employed in the land, property and construction markets through private practice, in central, regional and local government, in public agencies, in academic institutions, in business organisations and in non-governmental organisations.

Their broad areas of expertise include:

- Quantity Surveying
- Valuation Surveying
- Building Surveying
- Planning & Development
- Geomatics & Land surveying

Members' services are diverse and can include offering strategic advice on the economics, valuation, law, technology, finance and management in all aspects of the construction and property industry.

Accountable to both members and the public, the Society of Chartered Surveyors has six primary roles:

- Developing and promoting the diverse knowledge of the profession
- Maintaining the highest educational and professional standards
- Protecting consumers through strict codes of practice
- Providing expert advice on property and built environment issues
- Appointing arbitrators and independent experts in commercial rent review disputes
- To act as the State Registration Body for the title of Quantity and Building Surveyor under the Building Control Act, 2007

ROLE OF CHARTERED SURVEYORS IN COMMERCIAL RENT REVIEWS

The purpose of a rent review is to allow the rent to be adjusted to the current open market rent, i.e. the rent which would be agreed if the property was offered for letting with vacant possession on the rent review date on the basis of a specified lease.

Since the property is already let, the market rental value cannot be established by offering the property for letting with vacant possession. In practice, the lease provisions, and in particular the rent review clause, outlines the basis upon which the rent is to be reviewed. This is usually negotiated between two willing parties (the landlord and the tenant) and normally its structure and content is based upon the advice of both parties' legal and property advisors.

When a rent review is triggered, the normal practice is for the landlord and tenant to each instruct a separate Chartered Surveyor to act on their behalf and negotiate, based on their knowledge of the market and of recent rental transactions involving similar properties, a reasonable market rent which would have been agreed if the property had been able to be offered for letting with vacant possession in the open market. **It is important to note that Chartered Surveyors act for both landlords and tenants.** Whilst an expert knowledge of the market is critical, it is important that revised rents are fixed based upon the assumptions outlined in the lease and in particular the rent review clause.

To achieve the best result for his/her client, the chartered surveyor will need a number of specialist skills:

- Knowledge of the local market and all recent comparable transactions and an ability to analyse other, often complex, transactions to be able to compare them on a like for like basis with the subject premises.

- A detailed understanding of lease structures and typical lease wording together with an awareness of the latest case law and of the effect of different lease wording and assumptions on value.
- Good negotiating skills in order to reach an amicable settlement on behalf of the client whilst being cognisant of their professional duty to maintain professional standards.
- The necessary skills of assembly and analysis of the facts and the ability to present the case either in writing or orally when it is not possible to reach an agreed settlement and the matter has to be decided by a third party or by the court. Also, the ability to assess the advisability and viability of referring the issue to a third party and to advise the client accordingly.

It is important for a chartered surveyor to be instructed in good time by the client. The chartered surveyor will normally do an initial report at this stage with views on value together with advice as to whether the market is expected to weaken or strengthen in the near future. As the rent review date approaches, the initial report is normally updated. At the appropriate stage, the chartered surveyor will enter negotiations with the other side and keep the client fully informed of progress at all times.

In most cases, the matter will be settled amicably and the file can be closed. Where an amicable settlement is not possible, the matter may be referred to a third party.

In all cases, a lease will provide for a third party dispute resolution procedure whereby an Arbitrator or an Independent Expert is appointed to determine the revised rent after receiving representations from both parties. An arbitrator in

these circumstances acts in accordance with the provisions of the Arbitration Acts, 1954 - 2001.

The Society of Chartered Surveyors provides an important service to the rent review process by maintaining a panel of highly qualified Chartered Surveyors who are trained Arbitrators and/or Independent Experts. These Arbitrators and Independent Experts have the requisite relevant skills and experience to perform their functions to the highest standards. A minimum threshold of demonstrable and appropriate Continuing Professional Development over a five year period is also necessary to maintain membership of the panel.

Upon receipt of an application from either the landlord or the tenant, the President of the Society of Chartered Surveyors makes an appointment of either an Arbitrator or an Independent Expert (depending on the provisions in the lease) drawing from this panel. This is a proven effective means of resolving rent review disputes at reasonable cost and to the satisfaction of all parties.

BACKGROUND & LEGAL FRAMEWORK OF RENT REVIEW CLAUSES IN COMMERCIAL LEASES

Modern commercial leases are a legal contract freely negotiated by two willing parties which impose considerable obligations on both. Leases negotiated between landlords and tenants are done so against this background more often now with the benefit of professional advice. The initial commercial terms are negotiated and agreed between Chartered Surveyors acting for the parties and thereafter, the lease document is negotiated and concluded, based on commercially acceptable terms, by solicitors acting for the respective parties. Chartered Surveyors provide advice during the negotiations in relation to the rent review clause in the lease, amongst other matters.

The ebbs and flows of supply and demand impact all commercial property sections to varying degrees. They also impact on the detailed terms within leases including rent, lease duration, repairing and insuring obligations, break clauses with various notice provisions, rent review provisions and other incentives offered by the landlord to the tenant. This list is by no means an exhaustive list.

Landlord & Tenant legislation provides for the periodic review of rents and it has become a well settled convention in commercial leases that rent reviews occur every five years.

Fundamentally, leases between landlords and tenants are contracts binding those parties, the detailed terms of which reflect the legal "bargain" that both parties find acceptable, normally having received professional advice - the motivation from the tenant to occupy space required for business and the requirement of the landlord for an economic return.

Given the legal context of a commercial lease, any interference in existing contracts could give rise to legal difficulties. The ultimate arbiter of the enforcement of any provision of a lease, including the rent review clause, can only be decided by a Court.

RENT REVIEW PROVISIONS

Market conditions and the relative strengths of landlords and tenants at the time of the negotiation of the lease provide for the nature of the rent review clause and whether or not an upward only rent review clause should be incorporated.

Landlord and Tenant Law (Woodfall, 4th Edition) notes that:

'an upwards only review may be one of two types. The clause may provide for the rent never to fall below the rent agreed at the start of the lease, but otherwise to fluctuate up or down according to changes in market value, or it may provide for the rent never to fall below that payable immediately before the review date'.

Thus, an upward only rent review clause does not necessarily mean that the rent will increase.

When agreeing the terms of a lease, both landlords and tenants tend to take a medium term view on the market generally.

The system of five yearly lock in rent clauses has allowed tenants some budget stability and protection in a rapidly rising market. Tenants were content to accept that the rent mightn't go up but at best would remain static. In return, a landlord accepted a relatively infrequent opportunity to increase rent and depending on when the rent review date fell, would be affected by the market at that date. Even in the event that the rent remained the same - which at that point

is effectively five years old - the landlord may have potentially missed growth opportunities in the intervening period.

ADDRESSING THE CURRENT CONCERNS

It is plain to see that the property market is in serious difficulty at the present time and in particular, the retail sector to varying degrees. The submissions from Retail Excellence give rise to legitimate concerns but represent only one perspective on the matter.

Alongside the difficulties facing some tenants, landlords must also deal with a different set of challenges, including:

- Purchase price of property
- Funding terms
- Fluctuating capital values
- Fluctuating interest rates

The majority of commercial property (retail, office, industrial) is owned by a variety of institutions and/or funds who have acquired the properties in order to generate rental income to pay pensions or dividends towards policies or shareholders.

Anecdotally, it is the experience of the members of the Society of Chartered Surveyors that landlords are already in fact adopting a flexible and realistic approach and are reaching agreement with tenants who have sought

- a deferral of rent,
- a reduced rent, or
- the payment of rent on a monthly basis

where difficulties are substantiated and such flexibilities are warranted.

The landlord must weigh up the commercial reality of losing a tenant against the tenants' consideration of his legal obligations under the agreement. Normally, these flexible arrangements are at variance with the terms of the lease that has been signed. Our members have advised that in the majority of cases landlords are agreeing some form of concession notwithstanding the terms of the lease, to assist the tenant in getting through the current economic difficulties, where such a flexibility is warranted. These negotiations are private and conducted on a one-to-one basis and normally include a confidentiality clause.

RECOMMENDATIONS

In keeping with the Minister for Justices' recent invitation to the Society to *'consider, in the context within which your organisation operates, how best you and your members might contribute towards ensuring that we continue to have a dynamic and vibrant retail sector which supports employment within the economy and which, at the same time, provides an appropriate return for those who have chosen to invest in this sector'*, the Society recommends the following:

- (1) That the Minister for Justice invites all stakeholders (Pension Funds, Private Investors, Financial Institutions, Tenants, and Professional Bodies involved in property) to come together to review the practice in commercial real estate leasing in Ireland. This group should also consider the experience in other EU countries.
- (2) That the Society immediately issues a communication to its members highlighting the contents of this submission. It should be noted that it is not possible for the Society to issue any instruction or recommendation to its members in light of the provisions of the Competition Act, 2002.
(Chartered Surveyors must also adhere to professional standards in the management of rent reviews for both landlords and tenants so as to observe the commercial terms of a lease and observe their duty of care to their client.)
- (3) That a member survey is immediately undertaken by the SCS to establish the true extent of landlord flexibilities in accommodating tenants generally in the context of rent reviews.