CONFLICTING COVENANTS

REVISITING *DUVAL V 11-13 RANDOLPH CRESCENT*

What happens when a landlord:

a. On the one hand, gives Tenant A a licence to do something which would otherwise be a breach of Tenant A's lease, but;

b. On the other hand, is under an obligation to Tenant B to enforce the covenants in Tenant 1's lease?

This conflict has the potential to arise frequently. Indeed, I recently advised in a similar matter regarding permitted use. It is a little surprising therefore that the question has only recently been considered in the Supreme Court. Answering the question requires a rigorous consideration of how to interpret leases. The thought process is a useful one to go through, as it informs how we should go about reading leases generally, and how implied terms may appear to plug any gaps.

The question was answered in *Duval v 11-13 Randolph Crescent Ltd* [2020] 2 WLR 1167, which will have some important wider implications when interpreting leases. In this note I will be focussing on how the Court came to its decision and what those wider implications are.

THE BACKGROUND

I shall refer to the Respondent landlord as L, the Appellant tenant as T, and the third party tenant as T2.

L owned a block of 9 flats. T and T2 were leaseholders. All leases had the same terms ["the Lease"].

There were three clauses in play which created the potential for conflict.

First, as with most leases, the Lease included absolute prohibitions which prevented tenants from doing certain things. One of these was a prohibition against cutting, maiming or injuring the structure of the premises ["the Absolute Prohibition"]. As its name implies, the Lease did not expressly give L the ability to authorise any breach of the Absolute Prohibition.

Second, as is common, the Lease included qualified prohibitions. One was in relation to altering, improving or adding to the premises. However, unlike the Absolute Prohibition, the Lease expressly provided that tenants could obtain L's consent – not to be unreasonably refused – in order to carry out such works as would otherwise be a breach ["the Qualified Prohibition"]

Third, there was an obligation on L to:

a. Ensure that every other lease in the block included terms of a similar nature to the Absolute Prohibition and the Qualified Prohibition; and

b. Enforce the Absolute Prohibition and the Qualified Prohibition against other tenants subject to:

   i. A tenant requesting such enforcement; and

   ii. That tenant paying (and, beforehand, providing security for) L's costs of that enforcement on a full indemnity basis.

   ["the Enforcement Obligation"]

I have set out the full wording of the Absolute Prohibition, the Qualified Prohibition and the Enforcement Obligation in the attached Appendix.

The relevant facts were as follows:

a. T2 asked L for permission to carry out works to her flat. These were substantial works;

b. Some of the works involved cutting into the loadbearing walls;

c. Some of the other tenants objected to the plans, and L refused permission;

d. T2's builders then presented the plans again to L, who relented and granted permission;

e. T issued a claim seeking a declaration that L could not lawfully grant permission, as to do so would breach the Enforcement Obligation.

THE DECISION OF THE SUPREME COURT

It was common ground before the Supreme Court that a landlord was entitled to authorise any breach of a lease, notwithstanding the fact that the Absolute Prohibition did not provide for such permission. This set the foundation for the on which the decision was built.

Therefore the Court started by considering the express provisions of the Lease -this is where the decision may have some wider implications.

The Court of Appeal (and indeed the Parties) had approached the contents of the Absolute Prohibition and the Qualified Prohibition as follows:

a. Whilst a piece of work may be caught by either Prohibition, the two had to be mutually exclusive;

b. Some work may have fallen into the Qualified Prohibition without falling into the Absolute Prohibition, but not vice versa;

c. As soon as a piece of work was capable of falling within the Absolute Prohibition, it ceased to be covered by the Qualified Prohibition.

d. By way of example, replacing a hanging pendant light with a ceiling floodlight would probably fall solely within the Qualified Prohibition, because it did not involve cutting, maiming or injuring the ceiling (but would be an alteration). However, installing a new floodlight which required the ceiling or walls to be cut into for wiring purposes would immediately push the matter into the Absolute Prohibition.

The Supreme Court decided that this was not the proper interpretation of the Prohibitions. It was an undesirable interpretation because extremely minor and routine works, such as a simple re-wiring job, may fall within the Absolute Prohibition. Importantly, although L could of course grant permission to breach the Absolute Prohibition, there was absolutely no requirement for L to act reasonably in granting such permission (unlike as regards the Qualified Prohibition). Thus it could prove a significant hindrance to tenants who would naturally be looking to carry out routine works over the lifetime of their lease.

Rather, the Supreme Court interpreted the two Prohibitions as being on a spectrum, rather than being binary. A piece of work would fall at one end or the other depending on how substantial it was. If it was more routine, it would fall within the Qualified Prohibition. If it was more destructive, it would fall within the Absolute Prohibition. Whether a wall or ceiling was technically cut was not the test.

This is an important reminder that contractual terms need to be read together. If the terms of a lease create an identifiable scheme, there is scope to argue points of interpretation that would be unavailable if the terms were considered in isolation. *Duval* is a very good, practical example of that.

Insofar as the appeal was concerned, the difference between the Absolute Prohibition and the Qualified Prohibition was not of immediate relevance. No-one was saying that T2's substantial works plan could be characterised as anything less than a breach of the Absolute Prohibition. However, the importance of the Prohibitions would reveal itself later.

It was the Enforcement Obligation which took centre stage in the appeal. T needed to show that L was prevented by the Enforcement Obligation from giving a licence to T2 to carry out the works.

The Supreme Court broadly agreed with the Court of Appeal that the Enforcement Obligation was a contingent obligation. On its face, the Enforcement Obligation only arose if both a request had been made by a tenant and that the tenant had provided security for any costs which might arise. The Supreme Court proceeded on the factual basis that that contingency had not been created by T in this case.

However, the Court then moved on to consider any relevant implied terms. The Court considered that there was a general rule that, where a contingent obligation existed, the party bound by the obligation could not take steps to prevent the contingency from arising..

Having considered various authorities on the source of this rule, the Court decided that it operated as an implied term, and not as some free-standing rule of law. Whether such an implied term arose was now governed by the guidance from *M&S v BNP Paribas* [2016] AC 742 and the principles of business efficacy.

The Court considered the following points to determine that there was such an implied term:

a. The leases were lengthy with substantial premiums, with each tenant taking the view that they held a valuable asset in the lease;

b. Each tenant would know that, over the lifetime of the lease, it was inevitable that both repair and modernising works would be carried out to the other flats;

c. However, tenants would also assume that routine improvements would not impact on the other tenants or alter the wider structure or fabric of the building, and as such they could expect that L would readily grant permission for such routine works;

d. The tenants would have appreciated the desirability for L to retain the common parts and the structure of the building itself.

Against that factual matrix, the Court determined that tenants had an expectation that they could rely on the Enforcement Obligation. The Court decided that the Lease would not achieve business coherency if L could simply put himself beyond the reach of the Enforcement Obligation by granting a licence. Therefore, it was an implied term that L could not create a situation whereby the contingency within the Enforcement Obligation could not arise.

This meant that, by granting the licence to T2, L was in breach of the Enforcement Obligation, notwithstanding the factual finding that T had not triggered the contingency.

L raised an argument against this conclusion, which brings us back to the interpretation of the Prohibitions. L's argument was that if a piece of work fell under the Absolute Prohibition, every single other tenant would be able to hold L and the applying tenant to ransom. This was not conducive to a

block with so many long leases, and presumably not what any of the parties envision when the leases were formed.

The Court's response to that argument was to reiterate its finding on the proper interpretation of the Prohibitions. By placing the Absolute Prohibition and the Qualified Prohibition on a spectrum, tenants would not be able to block routine works. Presumably this consideration would operate in reverse as well – the ability of tenants to block works using the Enforcement Obligation be taken into account when determining whether a proposed work met the threshold of the Absolute Prohibition.

WIDER IMPLICATIONS

The following points come out of the Court's decision:

a. Where we have linked covenants, like the Absolute Prohibition and the Qualified Prohibition, be prepared to see them on a spectrum rather than mutually exclusive. Note that this may stretch the natural interpretation of the words to breaking point. This will undoubtedly create disputes, such as:

    i. In claims for declarations that a landlord has unreasonably refused consent for works. Tenants may decide to bring such a claim in circumstances where the landlord assumed the proposed works fell within an absolute prohibition, and so had not acted reasonably in refusing consent (or responding at all within a reasonable period). The Court would need to determine which side of the line the breach fell;

    ii. In situations where a landlord provided some wide, blanket consent in relation to a qualified prohibition, only for a tenant to commence works which the landlord assumed would fall squarely within an absolute prohibition. A subsequent injunction application may be defended on the basis that the un-authorised works actually fell within the blanket consent.

b. It is good to know that the rule which stops parties from preventing contingent obligations from arising flows from implied terms, and is subject to the usual rules on implied terms;

c. Generally, the way that terms like the Enforcement Obligation operate is interesting. The Supreme Court was satisfied that it would not create any absurd situations in this case because of the way it

interpreted the Absolute Prohibition and the Qualified Prohibition. However, conceivably there may be a block of flats, with an enforcement obligation, where all non-decorative works (or changes of use, or keeping of animals etc) were absolutely prohibited. A set of disgruntled tenants could make life very difficult for each other by relying on this case.

CONCLUSION

Along with the wider implications set out above, this is a useful case generally because it shows how the Court grapples with tricky and conflicting lease terms.

Whilst all cases of interpretation rely on the construction of a specific and unique contract, it will be a brave judge who departs from the Supreme Court's conclusions in similar leases.

David Nuttall

ST IVES CHAMBERS

6th July 2020

APPENDIX

Cl 2.6 – The Qualified Prohibition:

"Not without the previous written consent of the landlord to erect any structure pipe partition wire or post upon the demised premises nor make or suffer to be made any alteration or improvement in or addition to the demised premises."

Cl 2.7 – The Absolute Prohibition:

"Not to commit or permit or suffer any waste spoil or destruction in or upon the demised premises nor cut maim or injure or suffer to be cut maimed or injured any roof wall or ceiling within or enclosing the demised premises or any sewers drains pipes radiators ventilators wires and cables therein and not to obstruct but leave accessible at all times all casings or coverings of conduits serving the demised premises and other parts of the building."

Cl 3.19 – The Enforcement Obligation:

"every lease of a residential unit in the building hereafter granted by the landlord at a premium shall contain regulations to be observed by the tenant thereof in similar terms to those contained in the fifth schedule hereto and also covenants of a similar nature to those contained in clauses 2 and 3 of this lease AND at the request of the tenant and subject to payment by the tenant of (and provision beforehand of security for) the costs of the landlord on a complete indemnity basis to enforce any covenants entered into with the landlord by a tenant of any residential unit in the building of a similar nature to those contained in clause 2 of this lease."