Ponsford and others v HMS Aerosols Ltd [1978] 2 All ER 837

HOUSE OF LORDS

LORD WILBERFORCE, VISCOUNT DILHORNE, LORD SALMON, LORD FRASER OF TULLYBELTON AND LORD KEITH OF KINKEL

3, 4 MAY, 29 JUNE 1978

Landlord and tenant - Rent - Review - Reasonable rent - Improvements made to demised premises - Rent to be the higher of existing rent or a 'reasonable rent for the demised premises' - Improvements made pursuant to landlord's licence and at tenant's expense - Improvements becoming part of demised premises - Whether improvements to be taken into account in assessing 'reasonable rent for the demised premises'.

In 1968 the landlord's predecessors in title granted to the tenants a lease of a factory for a term of 21 years. For the first seven years of the term the rent was to be £ 9,000 and for the second and third seven years of the term it was to be the higher of £ 9,000 or such sum as should be 'assessed as a reasonable rent for the demised premises for the appropriate period'. If the parties failed to agree on the assessment of the rent, the assessment was to be made by an independent surveyor appointed by them. In 1969 the premises were burnt down. They were rebuilt by the landlords from the proceeds of the fire insurance on the premises but, pursuant to a licence granted by the landlords, incorporated substantial improvements costing £ 31,780 paid for by the tenants. It was common ground that once the improvements had been made they formed part of the demised premises. When the rent came to be reviewed for the second seven year period the tenants claimed that in assessing a 'reasonable' rent no account should be taken of the improvements which they had paid for. The Court of Appeal held that since the improvements were included in the demised premises they were to be taken into account in assessing the rent. The tenants appealed to the House of Lords contending that on the true construction of the rent review clause a 'reasonable' rent meant a rent which was reasonable between the parties.

Held (Lord Wilberforce and Lord Salmon dissenting) - The appeal would be dismissed because on the true construction of the lease what the tenants were required to pay rent for was the 'demised premises', which included the improvements they had paid for. An independent surveyor assessing the rent would therefore be required to assess a reasonable rent for the premises, not what would be a reasonable rent for the tenants to pay. A reasonable rent for the premises would be that based on market value without reference to the particular parties or how the premises were built and paid for (see p 842 *f* to *h*, p 843 *g*, p 847 *b* and *e* to *g*, p 848 *f*, p 849 *b* to *f* and p 850 *b* to *d*, post).

Cuff v J & F Stone Property Co Ltd p 833, ante approved.

John Kay Ltd v Kay [1952] 1 All ER 813 distinguished.

Decision of the Court of Appeal [1977] 3 All ER 651 affirmed.

Notes

For the nature and reservation of rent, see 23 *Halsbury's Laws* (3rd Edn) 536-543, paras 1193-1201.

Cases referred to in opinions

Cuff v J & F Stone Property Co Ltd p 833, ante.

Kay (John) Ltd v Kay [1952] 1 All ER 813, [1952] 2 QB 258, CA, 31(2) *Digest* (Reissue) 936, *7688*.

United Scientific Holdings Ltd v Burnley Borough Council, Cheapside Land Development Co Ltd v Messels Service Co [1977] 2 All ER 62, [1977] 2 WLR 806, 75 LGR 407, HL.

Appeal

This was an appeal by HMS Aerosols Ltd ('the tenants') by leave of the Court of Appeal against the decision of the court ([1977] 3 All ER 651, [1977] 1 WLR 1029) (Cairns LJ and Sir Gordon Willmer, Roskill LJ dissenting) on 8 February 1977 allowing an appeal by Ian Reginald Ponsford, Peter Philip Rough and Edward John Posey ('the landlords'), suing as trustees of the G M Posey Voluntary Settlement, against the judgment of Whitford J given on 3 February 1976 whereby he made a declaration that on the true construction of a lease dated 19 August 1968 made between the landlords and Fieldhouse (Uneeda) Ltd, the tenants' predecessors in title, the reasonable rent for the second and third periods of the lease was a rent that was to be assessed without regard to any effect on rent of certain improvements which had been carried out at the tenants' expense. The facts are set out in the opinion of Viscount Dilhorne.

Peter Millett QC and Michael Rich for the tenants.

Leolin Price QC and Bruce Coles for the landlords.

Their Lordships took time for consideration

29 June 1978. The following opinions were delivered.

LORD WILBERFORCE.

My Lords, this case concerns the interpretation of a rent review clause, and is one of impression. Of the four judges who have considered it, two favour one interpretation, two another. Your Lordships are, unfortunately, also divided in view.

The clause is contained in a lease of industrial premises for 21 years from 24 June 1968 at an initial rent for the first seven years of £ 9,000 per annum. For the second and third seven years of the term it is to be £ 9,000 'or such sum whichever be the higher as shall be assessed as a reasonable rent for the demised premises for the appropriate period'. There follow provisions for fixing this reasonable rent by an independent surveyor.

Soon after the granting of the lease the buildings were burnt down. The landlords, having received insurance money, undertook to reconstruct them, but at the same time the tenants desired to make some improvements. They applied to the landlords for a licence, and on 14 November 1969 this was granted by a formal document under seal. It contained this clause:

> '3. IT IS HEREBY AGREED and declared that all the [tenants'] covenants and conditions contained in the Lease which are now applicable to the premises demised thereby shall continue to be applicable to the same when and as altered and shall extend to all additions which may be made thereto in the course of such alterations.'

The improvements, including I understand the construction of a new bay, and the

installation of sprinkler equipment and a central heating system, were carried out at a cost of about £ 32,000, which sum was paid by the tenants.

Now, at the end of the first seven years, the question which arises is this: on what basis is the independent surveyor to fix the reasonable rent? It is not disputed that he must fix that rent for the premises as improved: they are now 'the demised premises'. But can he take into account the fact that the improvements have been paid for by the tenants? The answer depends solely on the construction of the words 'a reasonable rent for the demised premises'.

Many arguments great and small have been used by either side. I start by discarding some which, for my part, I find inconclusive or unhelpful.

1. The landlords, and the majority judges in the Court of Appeal, place great reliance on the words 'for the demised premises'. They show, it is said, that the surveyor only has to look at the premises and value them as they are: he cannot consider anything else. For my part I find these words neither conclusive, nor even indicative. They state the obvious. What else could the rent be for? The question is not what the rent is payable for but on what basis the surveyor is to fix it, on the market value, the rack rent value or (whatever this means) on the basis of what is reasonable.

2. The clause, it is said, prescribes merely 'a reasonable rent'. If the surveyor were to consider other matters than the visible character of the premises it would say 'reasonable in all the circumstances'. A distinction is thus made between this clause and the statutory provision considered by the Court of Appeal in *John Kay Ltd v Kay* in which it was held that the words 'such rent ... as the court in all the circumstances thinks reasonable' gave to the court a wide discretion. I cannot find the least substance in this argument. The word reasonable has no abstract or absolute meaning: it only has significance when related to a set of facts. What is reasonable in some circumstances, may be unreasonable in others. I find no difference between the two expressions.

3. It is said that if the tenants had wished to protect themselves against paying rent based on the improvements, they could (and should) have done so when the licence was granted. I do not agree. If the review clause has the meaning for which they contend there was no need for them to do so. If it bears the opposite meaning, they lose their case. The question which is right remains to be decided.

4. It is said that the tenants' argument involves reading the clause as if it said 'a reasonable rent for the tenants to pay' and that there is no justification for reading in the latter words. I do not follow this argument. There is no need on the tenants' argument, to read in any words. The rent which has to be fixed is a rent payable by these tenants under this lease which has 14 years to run and which may be renewed thereafter. It is not a rent (to follow the words of s 34 of the Landlord and Tenant Act 1954) at which the holding might reasonably be expected to be let in the open market by a willing lessor. The contrast in language is plain; the landlords' contention, indeed, is that the words mean just that, which, in my opinion, they cannot do.

I turn to arguments of substance. The clause exists and must be interpreted in the context of this lease and of what the parties must have been aware of at the time they agreed to it. They must have known the following: 1. That a tenant has the right to make improvements subject to the landlord's approval which cannot be unreasonably withheld. A landlord cannot as a condition of granting approval demand an increased rent. The landlords here did not of course do so in 1969. 2. If, when the lease expires, the tenant is in a position to call for a new lease, the rent then payable must be fixed without regard to the improvements (Landlord and Tenant Acts 1954 to 1969). 3. If, when the lease expires, the tenant goes out, he may be entitled to compensation in respect of the improvements to the extent to which they add to the letting value.

These facts would be known to any surveyor called on to fix a reasonable rent.

In the light of this, one has to ask: would a rent, taking into account the physical existence of the improvements and nothing more, be a reasonable rent? The answer to this is surely negative. It is not reasonable: (a) for a tenant who has spent £ 32,000, at an interest cost of maybe £ 3,200 per annum, to pay rent on the product of this expenditure for the rest of the term, even if he gets some compensation at the end of the lease; (b) for a tenant, who on a renewed lease would pay rent on a basis which disregarded the improvements, to pay rent during the current lease on a basis which did not disregard them; (c) for a landlord, who could not exact an increased rent on licensing the improvements, to obtain one at a later date by use of the rent review clause, the purpose of such a clause being to adjust the rent for inflation and market changes.

If, at the present time, the landlords were to say to the tenants 'We are asking you to pay an increased rent which, of course, takes account of the improvements you have made to our premises' the tenants would surely say 'That is most unreasonable'. And conversely, if the tenants were to say 'We offer to pay you an increased rent taking into account inflation since 1968, the rise or fall in market demand, and the fact that we paid for the improvements made in 1969' the landlords would surely say 'Fair enough'.

If the meaning of 'reasonable' is not such as to admit the considerations to which I have referred, I must ask what its meaning is or what the 'reasonable rent' referred to in the clause is. The answer given to this is that the rent is the market rent. Then, when the question is asked why, if this is so, the clause does not so state, the answer given is that the word reasonable is put in so as to exclude a freak rent which some extraordinary tenant might offer. I must say that I find this a very lame argument. A market rent (or a rack rent) is one thing; a reasonable rent is another. A reasonable market rent is a hybrid which I cannot understand, and the clause, understandably, does not use these words.

In support of their argument the landlords and the majority in the Court of Appeal appeal to a judgment of Megarry J in *Cuff v J & F Stone Property Co Ltd* (Page 833, ante). The actual decision in that case could not be supported except on the basis of a concession made by counsel in the case which was plainly wrong. But reliance was, naturally, having regard to its source, placed on the reasoning of Megarry J. I hope I do justice to it by summarising it in this way: to allow the surveyor to explore questions of who paid for the improvements would be to embark on an uncharted sea of what

might be moral and ethical considerations, such as might interest a philosopher or a theologian but could not be part of a valuation process. And the tenants' contention involves other difficulties: what would happen if the improvements were paid for not by the tenants but by a subsidiary or related company? I am not impressed by these latter difficulties: if such payments were made they must surely be on account of or on behalf of the tenants and taken into account as such. And that to take them into account is a normal process of valuation is surely shown by the terms of s 34 of the 1954 Act which requires a market rent to be fixed, there being disregarded any effect on rent of any improvement carried out by the tenant. 'Disregards' of this kind are part of the daily work of surveyors, which they can and do carry out without assuming the mantle of other callings.

My Lords, clear words may sometimes force the courts into solutions which are unjust and in such cases the court cannot rewrite the contract. This is not such a case: in my opinion logic and justice point in the same, not opposite, directions. I cannot attribute any meaning to 'reasonable rent' in this context than one which takes into account (or disregards) what any landlord, any tenant, any surveyor would consider it reasonable to take into account (or disregard). In this case the surveyor should disregard any effect on rent of improvements carried out (viz paid for) by the tenants.

I agree with the judgment of Roskill LJ and would allow the appeal.

VISCOUNT DILHORNE.

My Lords, by a lease dated 19 August 1968 the land-lords' predecessors in title leased to the tenants a factory at Barking for a term of 21 years from 24 June 1968 at a yearly rent of £ 9,000 during the first seven years of the term and during the second and third seven years of the term at a rent of £ 9,000 'or such sum whichever be the higher as shall be assessed as a reasonable rent for the demised premises for the appropriate period'.

The lease made provision for the reasonable rent for the demised premises for those periods to be agreed between the parties, and, if they failed to agree, for it to be assessed by an independent surveyor appointed by them. If they failed to agree on a surveyor, it provided for his appointment by the President of the Royal Institution of Chartered Surveyors.

The factory buildings were destroyed by fire. They were rebuilt with the use of the insurance moneys with improvements wanted and paid for by the tenants who obtained a licence dated 14 November 1969 from the landlords to make them. These improvements included the addition of a bay to the factory and the installation of central heating. They cost £ 31,780.

It is common ground that the improvements made by the tenants formed part of the demised premises and the question on which there has been and is much division of judicial opinion is whether when assessing a reasonable rent for the demised premises regard should be had to the fact that the improvements were paid for by the tenants. If in consequence of them the rent was assessed at a higher figure than it would otherwise have been, the tenants say that is not fair. They should not, they say, be required to pay rent on account of expenditure they had made on their landlords' property. They point out that if the lease had been for only seven years and they had been granted a new tenancy by order of the court under Part II of the Landlord and Tenant Act 1954, as amended by the Law of Property Act 1969, and the rent for that tenancy fell to be determined by the court the effect of the improvements on the rent for which the holding might reasonably be expected to be let in the open market by a willing lessor would have had to be disregarded (s 34 of the 1954

Act). It would be highly anomalous that they should have to pay a higher rent on a review under the lease they had for the second and, it may be, for the third periods of seven years than that which they would have had to pay on the grant of a new lease under the 1954 Act. What, they say, has to be determined on a review of the rent is what is a reasonable rent for them to pay for the demised premises and they contend that it would not be reasonable to require them to pay anything on account of the improvements they had made.

Our task can indeed be simply stated. It is just to decide the meaning of the words 'assessed as a reasonable rent for the demised premises'. Their meaning is not altered or affected by the fact that in 1969 Parliament decided that in assessing the rent of a new tenancy granted under the 1954 Act the effect of improvements such as those made in this case was to be disregarded. Landlords and tenants are usually advised by lawyers on the terms of leases. 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. A precedent which could be adapted is in s 34 of the 1954 Act. In the absence of any such express provision as Parliament thought it necessary to include in s 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 tenants was to be disregarded.

If it be thought to be unfair, as Parliament clearly thought it unfair, that a tenant should pay a rent which reflected the value of the improvements made by him, that is no ground for interpreting the words in question as the tenants contend. It is not for us to rewrite the lease. It may be that the parties in 1968 did not consider what was to be the effect on the assessment of the rent if the tenants made improvements.

One does not know but just as I see no ground for supposing that they did consider it, I see no ground for concluding, if they did consider it, that the landlords agreed that the effect of improvements should be excluded.

Rent review provisions are now commonly included in leases at the instance of landlords to give them some protection against inflation. If they were not included, landlords might only be disposed to let for a shorter term. Their object is to secure that in real terms the rent payable does not fall below that initially agreed on. It was not disputed in this case that that is their main object. In the present case and in many others provision is made for the assessment to be made by an independent surveyor. What is he to do? Surely it is to assess what rent the demised premises would command if let on the terms of the lease and for the period the assessed rent is to cover at the time the assessment falls to be made. That rent may depend to some extent on local factors such as deterioration of the neighbourhood. In assessing it, the surveyor will be assessing the reasonable rent that others, not just the sitting tenant, would be prepared to pay for the use and occupation of the premises. He will not consider the tenant's position separately.

It may be said that this is treating a reasonable rent for the demised premises as the rent obtainable on the open market and that the decision in *John Kay Ltd v Kay* shows this to be wrong. That was a decision on s 12 of the Leasehold Property (Temporary Provisions) Act 1951 which gave the court power to grant a tenancy 'at such rent and on such terms and conditions as the court in all the circumstances thinks reasonable', and it was held that that did not mean the rent which the property would fetch if offered in the open market as property to let. If the wording of this lease had been similar to that, the surveyor would in my opinion have been entitled, indeed would have been bound, to have regard to the particular circumstances of the tenant. I do not think that the decision in that case affords any support for the view that the task of the surveyor under the lease was not to assess what would be paid in rent for the use and occupation of the demised premises if offered to let on the open market. What significance then is to be attached to the word 'reasonable'? I think that it was included to give the surveyor some latitude. He might know that if the premises were to let, there was someone who would be prepared to offer an exceptionally high rent for their use. The use of the word 'reasonable' would enable him to disregard that.

The rent payable by the tenants will of course be rent for the demised premises, but as I see it the task of the surveyor is not to assess what would be a reasonable rent for the tenants to pay but what is a reasonable rent for the premises. That, when assessed, is payable by the tenants. If the effect of the improvements on the rent payable is to be disregarded, then

the tenants will not be paying a reasonable rent for the demised premises but a reasonable rent for the demised premises less the improvements; but it is recognised that the improvements are part of the demised premises. If the effect on the rent of the improvements is to be disregarded then in my opinion an express provision is required to effect that, as was necessary in the 1954 Act.

In *Cuff v J & F Stone Property Co Ltd* (Page 833, ante) Megarry J also had to consider a provision for the review of rent in a lease in all material respects similar to that under consideration in this case. He too had to consider the meaning of the words 'assessed as a reasonable rent for the demised premises'. In the course of his judgment, which I found illuminating and with which I respectfully entirely agree, he said (See p 836, ante): 'There is nothing save the expression "reasonable rent" to give colour to the view that anything save pure matters of valuation are to be considered' and:

> '... it seems to me to put an impossibly heavy burden on the word "reasonable" in this lease to say that it allows and requires the surveyor to explore questions of who paid for the improvements, and in appropriate cases to allow some discount for this, calculated on an unspecified basis.'

He held that (See p 836, ante)--

> 'the surveyor must take the premises as he finds them, and then determine what he considers to be a reasonable rent for those premises, regardless of who provided them or paid for them'.

Roskill LJ in his dissenting judgment in the present case attached great importance to the different factual background in that case. There the improvements had been made some 12 years before and so the phrase 'the demised premises' clearly included the improvements when the lease was executed. In the present case it is not disputed that 'demised premises' included the improvements made after the lease was executed and this being so I do not myself see that the fact that in *Cuff v J & F Stone Property Co Ltd* (Page 833, ante)the improvements were made before the lease was entered into affords any ground for distinguishing that case from this. In that case there had been a lease to J & F Stone Lighting and Radio Ltd and, on 3 March 1966 when the lease was expiring, the court made an order for the grant of a new lease. No doubt the rent fixed by the court disregarded the effect of the improvements but the defendants in the action tried by Megarry J were not the lessees in whose favour the court had made the order. It appears from Megarry J's judgment that the form of the lease they entered into was agreed between them and their landlords. Whether the rent review provision he had to consider was a term of the tenanc which the court ordered to be granted, the judgment does not reveal but it would not affect the meaning of the provision in my opinion if it was.

Roskill LJ also wondered whether Megarry J would have reached the same conclusion if it had not been conceded for the lessees that the improvements were not simply to be disregarded but I do not see any reason to suppose that Megarry J would have come to a different conclusion if that concession had not been made. Megarry J had to decide the meaning of the words used in the lease, as we have to do, and I do not see how the factual background or the concession to which I have referred can properly be considered as aids to the determination of the meaning of ordinary English words.

In my opinion Cairns LJ and Sir Gordon Willmer came to the right conclusion in this case and were it not for the division of opinion in this House, I would have been content simply to say that I agreed with them and Megarry J and with their reasoning.

In my opinion this appeal should be dismissed.

LORD SALMON.

My Lords, the relevant facts and the terms of the lease have been fully set out in the speech of my noble and learned friend, Lord Wilberforce, and I shall not repeat them in any detail. I would however emphasise that the lease was for a period of 21 years and provided for a rent of £ 9,000 a year reviewable in the seventh and 14th years of the term so that in the second and third seven year periods, the rent should be £ 9,000 a year 'or such sum whichever be the higher as shall be assessed as a reasonable rent for the demised premises'.

This appeal turns solely on the true meaning of the words 'a reasonable rent'. Considerable stress was laid by counsel for the landlords and the majority of the Court of Appeal on the words 'for the demised premises'. I am afraid that I do not

understand how those words can afford any real help in construing the words 'a reasonable rent' as used in the lease. After all, the rent fixed by the lease could hardly be a rent for anything other than the demised premises. Moreover, it is plain, as the landlords have always conceded, that when the demised premises were rebuilt, extended and improved after the fire which took place in the first year of the 21 year term, the cost of the extension and improvements (amounting to £ 31,780) was voluntarily paid by tenants. By a well established legal principle the extension and improvements became part of the demised premises, but this does not mean that in assessing a reasonable rent for the tenants to pay, it would be possible to increase the rent because of the additions and improvements to the landlords' premises which the tenants had made at their own expense.

The case for the landlords really turns on the argument (with which I disagree) that 'a reasonable rent' for the demised premises must mean the open market rent for the demised premises. If the parties had meant the open market rent they would, no doubt, have said so, as they usually do.

Two appeals were recently heard together in your Lordships' House, namely *United Scientific Holdings v Burnley Borough Council* and *Cheapside Land Development Co Ltd v Messels Service Co*. As appears from your Lordships' speeches, virtually every reported case relating to rent revision clauses was drawn to your Lordships' attention on the hearing of those appeals. I have again looked at these cases, and in each of them the rent revision clause clearly provides that the tenant shall pay the open market rent at the time of review or the original rent whichever should be the higher. If the provision in the present lease for revising the rent had been couched in similar terms, I would agree with the majority of the Court of Appeal. Had the parties agreed that the rent should be revised on the basis of open market value, the tenants would be bound by their agreement to accept a revision on that basis however unfair and unreasonable the result might turn out to be in the special circumstances of the case.

In the present case, however, the rent revision provision calls for the rent to be revised on the basis of 'a reasonable rent', which, for reasons I shall presently attempt to explain, can, and in this case does, mean something quite different from an open market rent. Although there may be cases in which a rent review clause has provided for review on the basis of a reasonable rent, I have been unable to discover any such case which has come before the courts other than the present case and *Cuff v J & F Stone Property Co Ltd* (Page 833, ante) to which I shall later return. One, if only one, of the reasons why the latter case was apparently thought not to be worth reporting at the time may have been that its rent revision clause may have seemed to be sui generis.

A lease constitutes a contract between a landlord and a tenant, binding them, their successors and assigns, under which it is agreed that the landlord shall let and the tenant shall rent premises on the terms set out in the lease. If the lease pro-

vides for a rent review, in the same terms as the lease under consideration, I am convinced that the surveyor who, in default of agreement between the parties, assesses the reasonable rent cannot do so in blinkers or in a vacuum. He necessarily must have regard to the relevant circumstances of the case. I know of no other method of deciding what 'reasonable' means in a contract, whether it be 'reasonable time', 'reasonable price' or 'reasonable rent'.

No doubt, in many cases, the reasonable rent will turn out to be the open market rent of the demised premises, but not always; certainly not, in my view, if the demised premises, as in the present case, have been extended and improved by the tenant at his own expense. It is well settled law that the extension and improvements enure for the benefit of the landlord, but not twice over, unless this has been expressly agreed by the tenant, as, for example, when the rent review clause provides that

the rent shall be reviewed to coincide with the open market rent at the date of the review. I imagine, however, that even in such a case, a tenant who proposed spending a substantial sum of money in making additions and improvements to the demised premises would, before carrying them out, if properly advised by his solicitors, normally insist on the landlord entering into an agreement that any increase in the open market rental of the premises caused by these additions and improvements should be disregarded in future rent reviews.

There is, however, no need to enter into a new agreement, if, as in the present case, the lease calls for 'a reasonable rent' to be assessed on the rent review, and means what, in my view, it says, not by implication, but expressly and plainly. Whether or not either party to the lease foresaw, at the time it was executed, all the relevant facts which existed at the date of the rent review is, to my mind, irrelevant. I agree entirely with Roskill LJ that the reviewed rent must be reasonable as between the parties to the lease, a reasonable rent for the landlords to accept and for the tenants to pay, having regard to all the relevant circumstances of the case existing at the date of the rent review.

I do not consider that the ordinary surveyor would have the slightest difficulty in assessing a reasonable rent on the basis I have indicated; indeed I think he would be astonished to be asked to assess it on any other basis. He would have been called in only because the landlords and the tenants were unable to agree between themselves what would be a reasonable rent for the tenants to pay during the next seven years. I do not know of any legal principle or sound authority which requires the surveyor, in assessing the reasonable rent, to shut his eyes to what any surveyor would regard as a vitally relevant factor, namely that the extensions and improvements to the demised premises had been paid for by the tenants out of their own pockets. He would recognise that the additions and improvements to the premises would, in all probability, enure to the benefit of the landlords when they recover possession of the premises and that, quite apart from a possible double benefit for the landlords, it would be most unreasonable for them to recover a higher rent from the tenants on account of additions and improvements which the tenants had made to the premises entirely at their own expense and with the landlords' consent.

I think that any competent and experienced surveyor would estimate the open market rent of the whole of the demised premises at the date of the review and, in fixing the reasonable rent, would discount from the open market rent that part of it attributable solely to the additions and improvements which had been made at the tenant's expense. This appears to me to accord with common sense and justice.

Nor am I discouraged in this view by the fact that s 34 of the Landlord and Tenant Act 1954 (as amended by the Law of Property Act 1969) provides:

> 'The rent payable under a tenancy granted by order of the court under this Part of this Act ... 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 carried out by the tenant or a predecessor in title of his] ... '

I refer to this section solely because the reason why Parliament made this provision is obviously because Parliament realised that it would be unreasonable for a tenant who, at his own expense, had made improvements to the demised premises to have his rent increased as a result of those improvements, and that it would be none the less unreasonable because the tenant might, at some future date, obtain some compensation for those improvements from the landlord under ss 1 and 2 of the Landlord and Tenant Act 1927.

I do not understand how in assessing a 'reasonable rent' a surveyor can be required to take an element into account which would make the rent unreasonable. Nor do I understand how the majority of the Court of Appeal, who recognised that the decision

at which they arrived with reluctance was unfair, could have regarded the rent which that decision produced as reasonable. This seems to me to be a contradiction in terms. As appears from their judgment they were however very much influenced by *Cuff v J & F Stone Property Co Ltd* (Page 833, ante). Before dealing with the authority, I must refer to one of the arguments on behalf of the landlords in support of their proposition that 'a reasonable rent' should be construed as necessarily having the same meaning as the open market rent. The argument was that the word 'reasonable' was introduced into the lease before the word 'rent' to give the surveyor some latitude (which he has in any event). It would enable the surveyor, so the argument ran, to disregard a freak rent which he knew that someone might be prepared to offer for the demised premises. This, in my respectful view, is a wholly untenable argument. No self-respecting surveyor would take into account a fantastically high or fantastically low rent in assessing an open market rent any more than he would do so in assessing a reasonable rent.

I will now deal shortly with *Cuff v J & F Stone Property Co Ltd* (Page 833, ante) which raised exactly the same question for consideration as the instant case. In my opinion, the decision in *Cuff's* (Page 833, ante) case was wrong and the grounds on which it was based are unsound for the reasons I have already indicated and which are as applicable to that case as they are to the present case. It is fair to say that in *Cuff's* (Page 833, ante) case, counsel for the tenant conceded that the improvements made at the tenant's expense could not be wholly disregarded by the surveyor in assessing 'a reasonable rent for the demised premises' under the rent revision clause. It may be that but for that unfortunate concession the judge might have come to a different conclusion. The judge said (See p 836, ante) in a passage quoted with approval by Cairns LJ ([1977] 3 All ER 651 at 656, [1977] 1 WLR 1029 at 1034, 1035):

> '... it seems to me to put an impossibly heavy burden on the word "reasonable" ... to say that it ... requires the surveyor to explore questions of who [had] paid for the improvements, and ... to allow some discount for this, calculated on an unspecified basis ... If one accepts to the full that "reasonable" means "right and fair", one may still say that it means "right and fair" in a valuation sense, without extending it to the whole range of moral and ethical considerations. I say nothing of the improbable case of a reasonable rent which is to be assessed not by a surveyor but by a philosopher or theologian; but I do say that ... a provision for a reasonable rent to be assessed by a surveyor ... will not cast the surveyor loose on uncharted and perhaps unchartable ethical seas such as these.'

To assess 'a reasonable rent' does not call for the surveyor to embark on uncharted or unchartable moral or ethical seas. All he has to take into consideration are the relevant business factors applying to the case. I cannot see that it would cast any burden on the surveyor to find out (as easily as the judge did) what additions and improvements the tenant had made to the demised premises at his own expense and then to assess a reasonable rent on the basis I explained earlier in this speech.

The following passage in the judgment in *Cuff's* case (See p 836, ante) was also quoted with approval by Cairns LJ ([1977] 3 All ER 651 at 656, [1977] 1 WLR 1029 at 1035): 'The question is not that of the rent "which it would be reasonable for the tenant to pay", but that of "a reasonable rent for the demised premises" ... ' I can see no difference between these two formulations. In my opinion, they both mean a rent which, in all the relevant circumstances, it would be reasonable for the tenant to pay and for the landlord to accept. It cannot, in my opinion, be reasonable to increase the

rent to be paid by the tenant because of the additions and improvements the tenant has made to the demised premises at his own expense. Any rent increased because of such additions and improvements could not, in my opinion, sensibly be

regarded as a 'reasonable rent' within the ordinary and natural meaning of those words.

My Lords, for the reasons I have indicated I would allow the appeal.

LORD FRASER OF TULLYBELTON.

My Lords, I need not repeat the facts of this case, as they have already been fully set out in the speech of my noble and learned friend, Viscount Dilhorne, with whose reasoning and conclusions I entirely agree.

The only question for decision in the appeal relates to the proper construction of a few words in the lease. The words occur in cl 1 which provides that, during the second and third seven year periods of the lease, the yearly rent shall be £ 9,000 'or such sum whichever shall be the higher as shall be assessed as a reasonable rent for the demised premises for the appropriate period ... ' There is no dispute that 'the demised premises', which originally meant the factory described in cl 1 of the lease, now mean the factory as rebuilt after the fire, including the improvements made at the expense of the tenants, with the approval of the landlords given in a licence dated 14 November 1969. 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 landlords, but provision to that effect was in fact made in cl 3 of the licence, which is in the following terms:

> 'IT IS HEREBY AGREED and declared that all the [tenants'] covenants and conditions contained in the Lease which are now applicable to the premises demised thereby shall continue to be applicable to the same when and as altered and shall extend to all additions which may be made thereto in the course of such alterations.'

The question therefore becomes what is meant by 'a reasonable rent' in the context, and the reference to the demised premises is relevant only as part of the context. In my opinion the words point unambiguously to the result contended for by the landlords, and they mean the reasonable rent assessed on an objective basis, without reference to the particular landlord or the particular tenant or to the history of how the premises came to be built or paid for. Regard must, of course, be had to the terms of the lease, because its provisions with regard to duration, responsibility for repairs and other matters may affect the rent, but their effect would be the same whoever the landlord or the tenant might be. It is true that the words 'for the demised premises' do not add anything new, because there is no doubt about the identity of the premises for which the rent is payable, but in my opinion the words are of importance because they emphasise that the assessment is to be made by reference to the premises and not by reference to wider considerations or to what would be reasonable between these particular landlords and tenants. I respectfully agree with Sir Gordon Willmer in the Court of Appeal, and with Megarry J in his opinion in *Cuff v J & F Stone Property Co Ltd*, (Page 833, ante) that the position might have been different if the lease had provided for the rent fixed on a review to be that 'which it would be reasonable for the tenants to pay'. The emphasis would then have been shifted to the circumstances affecting the particular tenants as in *John Kay Ltd v Kay*. But those are not the words we have to construe.

The whole weight of the tenant's case rests on the word 'reasonable'. It is said that if the rent were to be increased because of the improvements for which the tenants themselves have paid, that would be unfair and the rent would therefore not be reasonable. With all respect to those who think otherwise, that argument seems to me to be unsound for several reasons. In the first place the description of the rent as 'reasonable' is quite insufficient to displace the objective standard which in my

opinion is indicated by the clause as a whole. I think that the effect of the word 'reasonable' is to exclude any exceptional or freak rent that might have had to be taken into account if the clause had referred to the open market rent. In the second place, having regard to the provisions contained in ss 1 and 2 of the Landlord and Tenant Act 1927 for compensation to tenants in certain circumstances for improvements made by them, I am not satisfied that the result of the landlords' construction of the clause is so unfair as has been suggested. Those sections are not referred to in the judgments of any of the judges in the Court of Appeal and they may not have been present to the minds of Cairns LJ and Sir Gordon Willmer when they said ([1977] 3 All ER 651 at 656, 666, [1977] 1 WLR 1029 at 1035, 1040) that they reached their decision with regret. The possibility of compensation at the end of the lease may not be so satisfactory to the tenants as a lower rent during the remainder of the lease after the first review date, but it goes some way to meet their complaint. Thirdly, whether I am right or wrong in regarding the possibility of compensation under the 1927 Act as relevant, and even if the result may seem harsh or unfair from the tenants' point of view, I would not regard that as sufficient reason for departing from what seems to me to be the proper construction of the words used. The lease is an elaborate document and the tenants presumably took legal advice before entering into it. They are a business concern, able to look after their own interests, and there is nothing to suggest that they were misled or taken advantage of in any way. It is most unlikely that either party had this problem in mind when the terms of the lease were agreed. If the parties intended that the general law was to be varied by special provisions in favour of the tenants, the time to make such provisions would have been when the licence for improvements was granted by the landlords, but that was not done. The problem has therefore to be solved by reference to the lease alone; it contains no express provisions in favour of the tenants on this matter and in my opinion it cannot, without distortion, be construed as making such provisions by implication.

The meaning of the clause appears to me to be free from ambiguity, and I do not consider that your Lordships would be justified in giving it an artificial construction because of any apparent anomaly that may exist between it and s 34 of the Landlord and Tenant Act 1954. The effect of that section is that, when a new lease is granted under Part II of the 1954 Act, the rent is not liable to be increased because of improvements carried out by the tenant or his predecessors in title, but circumstances in which s 34 applies are not those in which the question arises here. It is not material for the present purpose.

I would dismiss the appeal.

LORD KEITH OF KINKEL.

My Lords, this appeal raises a short but very difficult question as to the proper construction of a rent review clause in a lease.

The lease is one on industrial premises for a term of 21 years from 26 June 1968. It provided for a yearly rent of £ 9,000 during the first seven years of the term and during the second and third seven years the sum of £ 9,000 'or such sum

whichever be the higher as shall be assessed as a reasonable rent for the demised premises'. That assessment was to be made, failing agreement between the parties, by an independent surveyor.

The particular problem to be resolved arises in this way. At an early stage in the life of the lease the tenants desired that, in the course of the reconstruction of the premises following a fire, certain improvements should be incorporated at their expense. The landlords granted a formal licence for these improvements dated 16 November 1969, which provided, inter alia, that --

> 'all the [tenants'] covenants and conditions contained in the Lease which are now applicable to the premises demised thereby shall continue to be applicable

> to the same when and as altered and shall extend to all additions which may be made thereto in the course of such alterations.'

The improvements were duly carried out at a cost to the tenants of some £ 32,000. The question to be determined is whether, on a proper construction of the words I have quoted above, account is to be taken, in assessing a reasonable rent for the demised premises for the second period of seven years, of the circumstances that the improvements in question were paid for by the tenants.

At first impression the words 'reasonable rent for the demised premises' suggest that what has to be ascertained is simply the rent that is reasonable for the premises as such in their actual state, the situation being viewed entirely objectively. 'The demised premises' must mean the demised premises as improved, by virtue both of the ordinary law and of the passage I have quoted from the licence agreement. So on this view any contribution the improvements might have made to rental value would have to enter into the assessment.

It was however argued for the tenants that to proceed in that way would involve assessment of the rent on the basis of market value, whereas the lease provided for a different basis, namely that of a 'reasonable' rent. It was not maintained that the assessment should be made on the assumption that the improvements did not exist, but it was said that any assessment of a 'reasonable' rent could not ignore the fact that the improvements had been paid for by the tenants. Otherwise an unreasonable result would be reached which was unfair to the tenants, considering that the landlords had not contributed to any increase of rental value resulting from the improvements and that their capital value would enure to the landlords' benefit at the expiry of the lease.

It must be recognised, in my view, that, if the approach is to be a purely objective one, it is difficult to perceive any difference in meaning between 'a reasonable rent' and 'the market rent', and so there is force in the argument that if the parties had intended a purely objective assessment they would have used the latter expression, which is in common use in contexts such as this one. I am not impressed by the suggestion that the expression 'a reasonable rent' might have been used merely in order to exclude any freak or special rent that a prospective tenant might be prepared to pay, because I think that in estimating the market rent a valuer would proceed on the general level of rents for comparable premises without reference to any such freak or special rent. I regard it as a proper inference that when agreeing on the terms of the rent review clause the parties did not have present in their minds the situation which might arise by reason of the execution by the tenants of improvements, because I consider that if they had they would have made specific provision about the application of the clause to that situation. But whether or not that is correct the clause must have been envisaged as capable of operating in respect of the original unimproved premises. Would the surveyor then have reached any different result than if he had simply been instructed to ascertain the market rent? I would think not, because I am not able to envisage any circumstances which he would take into or leave out of account in one case but not in another. It may be, of course, that in the surveying profession 'a reasonable rent' is well known to bear a particular meaning distinct from that of 'the market rent', but there is no available material to indicate whether or not that is so. As it is, I consider that in either case the surveyor would have regard to the condition of the premises, the terms and provisions of the lease,

and the general level of rent for comparable premises in the same locality or in similar localities, and I would not expect any difference in the resulting assessment. Even if the difference of wording were intended to lead to a different approach to the rent review, it is to be expected that the different approach would be capable of application where there had been no improvements.

That being so in the normal case, does the difference of wording lead to a different result where the tenant has carried out improvements at his own expense? I think

it could do so only if there were grounds for inferring that the particular wording used here was used in contemplation of that particular situation, and, as I have already said, I do not consider that such grounds exist. Further, I cannot think that parties can have had in view the additional factor that any licence agreement for improvements would fail to make provision for the manner in which the improvements were to be dealt with on a rent review.

In my opinion the words 'a reasonable rent for the demised premises' simply mean 'the rent at which the demised premises might reasonably be expected to let'. Considering that the demised premises necessarily include the improvements, to arrive at a lower rent by reason that the tenants paid for the latter would in substance mean that a rent for part only of the demised premises was being assessed. The fact that the assessed rent leads to an unreasonable result as between the particular tenant and the particular landlord does not mean that it is not a reasonable rent for the premises. The unreasonable result is due to circumstances which were not in contemplation when the terms of the rent review clause were agreed, and which were therefore not expressly provided for. They might have been expressly provided for at the stage when the licence for the improvements came to be granted, but they were not. I consider that the construction which the tenants would place on the review clause involves a severe straining of the language used and is not the correct one. I therefore reach the conclusion that the decision of the majority of the Court of Appeal was right.

Reference was made in the course of the argument to a number of statutory provisions regulating, in certain circumstances, the relationship of landlord and tenant of business premises, in particular s 34 of the Landlord and Tenant Act 1954. Section 34 is of some significance, in my view, as indicating the need, when it is desired that certain matters (including improvements carried out by a tenant) should be disregarded in the assessment of a rent, to provide expressly for this. But apart from that I do consider that any of the provisions referred to are of assistance in resolving the present problem of construction.

Reference was also made to the decision of Megarry J in *Cuff v J & F Stone Property Ltd* (Page 833, ante), finding in favour of the landlords in circumstances closely akin to those of the instant case. While I should not be disposed to adopt the whole of the reasoning of the judge in that case, I agree with him that the expression 'reasonable rent' is to be read in a valuation sense, and that 'the surveyor must take the premises as he finds them, and then determine what he considers to be a reasonable rent for those premises, regardless of who provided them or paid for them' (See p 836, ante).

My Lords, for these reasons I would dismiss the appeal.

Appeal dismissed.

Solicitors: Tarlo Lyons & Aukin (for the tenants); Gamlens (for the landlords).