



Commercial leases and side letters - A binding arrangement?

I WILL IF YOU WILL

The 2017 case of *Vivienne Westwood Limited v Conduit Street Development Limited* has highlighted the difficulties which might arise from 'side letter' arrangements. Typically, a Landlord wishing to attract and keep a tenant (particularly if they are a well-known brand or 'name') might seek to offer an inducement to enter into the lease. In this particular case the headline rent under the lease was £110K pa with rent reviews in the 5th and 10th years. On completing the lease, the Landlord agreed in a side letter that the tenant should pay a reduced rent of £90K pa at the outset and increasing to £100K pa after the 5th year. On the basis that the rent review went ahead, any increase would be capped at £125K.

THE SMALL PRINT

It was agreed that the arrangement was personal to the tenant, and would cease if the lease was assigned, and would not amount to a variation of the lease. The letter also provided that in the event of any breach of the terms of the agreement or lease, the Landlord had the option to terminate the agreement, and the rents expressed in the lease would be immediately payable as if the agreement had never existed. [The editor comments that such terms are fairly typical].

ALL GOOD THINGS COME TO AN END?

During the first 5 years of the term, the interest of the Landlord changed hands 3 times. 4 months after the first review date, the then Landlord claimed rent at £125K and the tenant paid such rent, but then defaulted on the next quarter rent. When the Landlord purported to terminate the arrangement due to the failure to pay the rent, the tenant paid the outstanding quarter. The Landlord determined the rent at the review date as £232,500.00 pa. Was the Landlord entitled to terminate the arrangement and then claim the much greater rent from the tenant?

PENALTY DECISION

On an application to the High Court, the Court had to determine if the arrangement was enforceable by the Landlord or whether it breached the rules preventing a Landlord from imposing an unlawful penalty on his tenant. A penalty will arise if a provision imposes a detriment on a party in breach of a primary obligation and which is out of all proportion to any legitimate interest in the performance of the obligation.

NO NEED FOR A VIDEO REF

The High Court had no difficulty in deciding that the effect of termination of the side letter amounted to a penalty for the following reasons:

- The side letter, although not varying the lease, had the effect of amending the tenant's primary obligation to pay rent at the reduced rate
- As a result of the termination, the rental liability would be retrospective as the rent would be payable as if the agreement had never existed
- The Landlord had the ability to terminate the agreement in respect of any breach no matter how trivial
- The Landlord had other remedies for late payment of rent and breaches, including interest recovery of costs and damages
- The arrangement between the Landlord and Tenant was regarded as a substantial term struck between the parties such that the Tenant was happy to enter into the lease
- The amounts payable by way of increased rent from the rent commencement date were out of all proportion to the nature of the breach

As a result, the Landlord was unable to rely on the termination provision in the side letter.

A NEW SIDE ORDER?

It is clear from this decision that side letters to commercial leases will need to be thoroughly scrutinised to ensure that the termination provisions do not give rise to an unenforceable penalty arrangement. In particular, Landlords will need to be wary of any change to a Tenant's primary obligations, and the nature of the consequences which might flow from a termination.

For more information please contact me.

David Barrett

Contact



David Barrett

Associate

Tel **01273 403243**

Email

**david.barrett@
adamsandremers.com**

Further Help & Advice

Lewes

Trinity House, School Hill,
Lewes, Sussex, BN7 2NN

Tel 01273 480616

Fax 01273 480618

DX 3100 Lewes1

Email **lewes@adams-remers.co.uk**

London

Commonwealth House,
55-58 Pall Mall, London, SW1Y 5JH

Tel 020 7024 3600

Fax 020 7839 5244

DX 140545 Piccadilly 5

Email **london@adams-remers.co.uk**