ML GUIDE

RENT REVIEW for Landlords

Rent review is at the heart of commercial property

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ML GUIDE - RENT REVIEW FOR LANDLORDS

INTRODUCTION

I have written this ML Guide for landlords of shop and retail property, but the principles apply to all types of business premises, such as offices, factories and warehouses, leisure property, and so on.

However, business tenancy rent review law does not apply to agricultural tenancies, residential lettings (but where the residential letting is not separate from the business premises - for example, a shop with a residential flat included in the shop tenancy and let as a whole would be subject to business tenancy law, but not in respect of the flat only), fishing and mineral rights, licences, [provided they are not tenancies - simply calling a document a licence doesn't mean it necessarily is one], and tenancies-at-will.

I hope you will enjoy reading and find the information useful. If you have any questions, or need more explanation, then please contact me.

PLEASE NOTE

All the information and comment in this ML Guide is for general information and assistance only and is not intended a substitute for specific advice. Also, all the information is believed accurate in June 2011 and relates to the law in England and Wales only.

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1.0 INTRODUCTION

1.1 The shop property market comprises landlords, (including developers), owner-occupiers, tenants and licensees. Tenancy is also known by the legal term 'lease', but, strictly, lease is the document, whereas tenancy is the nature of the occupancy. A difference exists between a tenancy and a licence: in outline, the main difference is whether the occupant has exclusive possession. Calling a document a licence does not make it one.

1.2 A letting is the act of transferring the use of the property to someone in exchange for rent, usually a sum of money. The relationship of landlord and tenant is created by a contract expressed or implied, whereby one person that is possessed with an interest in real property - usually called the landlord or lessor - confers on another person - usually called the tenant or lessee - the right to exclusive possession of the premises or some part of it for a period of time which is definite or can be made definite by either party, usually in consideration of a periodical payment of rent either in money or its equivalent.

1.3 Under s2 of the Law of Property (Miscellaneous Provisions) Act 1989, a contract "for the sale or other disposition of an interest in land" must a) be in writing, b) incorporate all the terms that the parties have expressly agreed in one document or, where contracts are to be exchanged, in each document; and c) be signed by or on behalf of each party. A failure to satisfy those requirements will mean there is no contract at all between the parties.

1.3.1 s2 of the Law of Property (Miscellaneous Provisions) Act 1989 excludes a contract to grant a short lease as defined in section 54(2) of the Law of property Act 1925. The following requirements must be satisfied: a) the lease is not in writing, b) the lease takes effect in possession for a term not exceeding three years; and c) the lease is at the best rent that can reasonably be obtained without taking a fine (premium).

1.4 The capital value of shop property is often substantial so, if landlords did not let but only sold outright, then tenants might not be able to afford to set up shop. A tenancy can be more tax-efficient, because rent is categorised as a business expense. In the past, tenant-attitude was respectful, sometimes fearful, but nowadays many retailers think landlords should expect to be treated like any other supplier. In fact, the landlord and tenant relationship is completely different. Unlike other suppliers with whom a retailer does business, and whose interests are aligned, and where the retailer may be able to dictate terms, a landlord is under no such obligation, and the interests of landlord and tenant are often diametrically opposed: in other words, tenants invariably want less, whereas landlords will want more.

1.5 For a tenant, a shop or a commercial property for retail use is a physical place in or from which the tenant can run its business. How a tenant wants to run its business, the style and mode, pricing, and so on, is largely a matter of choice. Some retailers, such as operators of large supermarkets and restaurants, trade in isolation, relying upon their own initiatives to generate trade, but most retailers depend upon the existence of other retailers nearby: sharing footfall (pedestrian flow) so as to cash in on the goodwill of the shopping community.

1.6 A retailer makes money out of the difference between how much it costs in total for the retailer to pay its suppliers for products and services and the total resale price of those items to the customer. In outline, a financial overview of trading accounts might show gross turnover (exclusive of VAT), cost of sales, operating and overhead costs, net profit before tax. Level of turnover and/or the number of shops is not necessarily indicative of the level of profit, there are many variables; and for multiple retailers with economy of scale, many branches may under-perform as profitable outlets in their own right, their only function to get trade discounts from bulk buying. Regardless of the type of business, for any retailer a shop is a marketing tool: a means by which the retailer can offer for sale its choice of products and services to customers in the retailer's target market. So, to a tenant, the locality, the trading position, characteristics of the property, terms of the tenancy, the calibre of other retailers nearby and prospects for the locality are important factors.

1.7 The retailer aim is to maximise profit margin, but that margin will vary depending upon the cost of sales and the cost of the place where sales are transacted. Cost of sales includes raw materials, shipping and freight, marketing, pricing, and so on. Cost of place includes the total property cost commitment and the overheads of the business, such as staff wages, and so on. Total property costs include rent, business rates, water rates, building insurance, repairs, decoration, any service charge, and the other terms of the tenancy.

1.8 Unlike other suppliers with whom a retailer does business, the relationship between landlord and tenant hinges upon a lease. A lease is a legally-binding document that records the agreed terms and conditions upon which the property is let by the landlord to the tenant. A lease is a commercial contract, meaning the parties are deemed to know what they are doing. The term of a tenancy can often last for years, during which anything can happen: although many retailers are more interested in signing up so they can start trading as soon as possible, ensuring the wording and phrasing in tenancy documents properly records the intention because the consequences of getting it wrong with a business tenancy can be horrendous.

1.8.1 When a new tenancy is granted, the onus is on the landlord's side to draft the document and on the tenant to approve. When landlords are content to leave the wording of the lease to their solicitors without involving a rent review surveyor, there is a risk that the drafting precedents slavishly used by solicitors may not be appropriate for the particular circumstances. Frequently, I am asked to advise on the implications where the landlord's or tenant's interpretation of a word or phrase in the lease differs from what the tenant or landlord had in mind. Also, there are practical aspects when drafting a rent review clause that might seem okay on the face of it at the time, but can have an adverse effect on the landlord's position.

1.9 Retailers are in the retail business, landlords in the property business. In essence, business is about helping people in exchange for money: business is not an extension of social services! The profit margin for a landlord is the performance of the investment. Investment is about becoming better off, so what you buy, when you buy it, how much you pay, whether you have a mortgage, costs during ownership, and when you sell (even if you never sell, the property would still have a market value), will affect your investment. Performance is measured by either capital growth or rental growth, or both. The investment is not just the property itself, but also the effect on the value of the property of the terms of the tenancy upon which the premises are let.

1.10 The landlord owns the property: that is all. The trading prospects, the state of the market that the tenant's business serves, how well the actual tenant is faring, are immaterial. The tenant's circumstances are only relevant in so far as whether the landlord would expect rent on time and other terms of the tenancy to be honoured. Otherwise, the only relevant factors are the terms and provisions of the lease.

1.10.1 There is an ideology that the landlord and tenant relationship should be a partnership, sharing the ups-and-downs together. However, a landlord generally has no say in the operational side of the tenant's business, so it doesn't follow that property costs are to blame, as many retailers claim, so much as retailers coming unstuck in times of change as a result of operational difficulties, and/or personal life-style expenditure.

1.11 When the shop is offered to let in the open market, the landlord will have an asking rent, but the rent the tenant agrees is likely to be whatever the tenant can afford, based on the tenant's projected figures for the running of its business. Few tenants care about the wider long-term consequences of their business plans and most are single-minded. Some retailers deliberately pay top rents to ingratiate themselves with landlords, whilst others agree what they can afford at the time, expecting future rent reviews to also be based upon affordability.

1.12 The moment the lease is completed, affordability and business tenancy law part company. At rent review, it is assumed the actual tenant can afford, pro-rata, the same as everyone else, because the object of a review is to enable the landlord to receive the market rent at the review date (or valuation date if different), and for the tenant to ensure it is not paying any more or less. Hence, a rent review is for the benefit of both parties.

1.13 However, because the premises cannot be offered to let in the market with vacant possession, because the actual tenant has a tenancy, the lease will contain guidelines for how the rent is to be valued if the premises were available to let. At rent review, the valuation approach is objective. In business tenancy law, a rent review is not about how much the actual landlord might want, or what the actual tenant could afford, but what the lease says about how the rent is to be arrived at. Rent is the product of the terms of the tenancy upon which the premises are let. One cannot say 'this is the rent for the premises' without also stating, knowing or defining the terms upon which the premises are or would be let. Unless the lease says otherwise, the approach is to calculate the rental value as if the premises were available to be let in the market between a hypothetical willing landlord and a hypothetical willing tenant on a tenancy containing whatever terms and conditions are specified in the review guidelines, subject to shop rental valuation and business tenancy law.

1.13.1 For a multiple retailer, total property costs could be approximately 12%-14% of turnover, whereas to an independent or local trader with one or two shops the percentage might be 45%-50%. For many tenants, the only way their businesses can remain profitable is when their costs *are* below the going rate. Costs below the going rate are a form of subsidy. Customer demand is polarising, so with the gap widening between retailers that have what customers want and those that do not, tenants not on the receiving end of profitable demand are likely to be struggling for survival. In such cases, the tenant's reaction to a proposed increase is likely to be emotive, either expressed fiercely or in silence. It is common for a tenant to be unresponsive to communications and often the only way to whirr a tenant into action is to initiate dispute resolution procedure.

1.13.2 Since a tenant's failure to adapt its business style to changing reality cannot possibly be something for which the landlord should be expected to share responsibility, a landlord that adopts an accommodating attitude at rent review (and on tenancy renewal), by focussing on the business for which the tenant *chooses* to use the premises, can get stuck with a dud tenant; the investment under-performing for the wrong reasons. By allowing wider consequences into the on-going relationship between landlord and tenant, negotiations are likely to become personal and subjective, and undermine the objective criteria at rent review: namely the hypothetical tenant. In other words, because no tenant would willingly agree more than they can afford, the landlord may have to refer the review to 'arbitration' merely to have the revised rent resolved.

1.14 For landlords that prefer or can afford to be accommodating, one question is whether a tenant should be helped to survive the error of the tenant's ways. Something shop-tenants are good at is making pronouncements about the market as a whole as if their own subjective experience should be considered the only barometer of consumer behaviour. The world does not owe retailers a living and customers make up their own minds where to shop, for whatever reason. Perhaps because retailing is one of the largest employers, many retailers feel the sector should be a sort of level playing field for all, regardless of the state of the economy. In practice, it creates problems for successful retailers when landlords interfere with market forces by subsidising unprofitable businesses because that can prolong competition artificially.

1.15 In the same way tenants can get retailing wrong, so too can landlords as regards investment in shop property through not appreciating the implications of the terms of the tenancy, the effect of business tenancy law and/or rental valuation, and/or not understanding retailer market trends. Successful investment in shop property requires wits about you: what and when to buy and sell, to whom to let the premises, to whether to hang on to the existing tenant come-what-may or aim take a chance in the market. The shop property market is dynamic, rents fluctuate with supply and demand, and the date of a review may make a difference, as can the terms of the tenancy. It is not enough to think that, because you own a shop property, someone somewhere is bound to want to rent it; it can be a mistake to assume that because the shop is let to a multiple retailer that tenant would remain in occupation or want to renew the tenancy; and it is wrong to think that just because the lease contains upward-only rent reviews, or if there has been no increase for years, the rent has to go up.

1.15.1 Where a landlord has inherited a shop investment, or where the landlord was itself previously an owner-occupier retailer and let the premises in conjunction with sale of the business as a going-concern, factors that affect rental and capital growth are the same as if the property were bought afresh. Also, whereas generally a tenant can afford to pay more for the freehold than anyone else, since the tenant could dispose of its businesses as a going-concern assuming that business depends upon being attached to the particular property, whether the property would be worth buying or keeping as an investment depends upon the same criteria for appraisal as if it were being considered by an investor.

1.16 In practice, a particular tenant's occupancy of the premises, style of business and choice of products and services offered for sale, reflects the prevailing business plan of that particular tenant. If for whatever reason that plan should change then that could affect the tenant's need for the premises. It is rare for a landlord to be privy to what is happening behind-the-scenes of a tenant's plan: it is not necessary for a tenant to disclose or communicate its intention in advance. Therefore, the market value of the property can differ from the value of the investment, because the identity of the tenant and/or the terms of the tenancy can change and/or the interpretation of the terms of tenancy can change, whereas the location and position of the property is fixed.

1.17 Whilst the criteria for successful investment in shop property revolves around practicalities and prospects, the world of rent review does not. Rent review revolves around a series of hypotheses, two of which are that 1) the existence of a market is assumed and 2) someone somewhere would want to lease the premises and it is not necessary to identify that someone. Although many people (particularly the media) think that whatever is happening in the "real world" (wherever that is!) is bound to affect the rent review, fact is that at rent review a completely different mind-set is required. Unlike a lease expiry/renewal, where at the end of the contractual term the tenant can quit the premises or may be in a position to dictate terms should the landlord not want to lose that particular tenant, at rent review no such bargaining-power applies. The actual tenant cannot dictate terms as such, because, provided there is nothing in the terms of the tenancy otherwise, not only is the actual tenant not the only tenant in the market, but also it is not necessary for those other tenants to be identified. It is not necessary to prove the existence of demand because that is built-in to the hypothesis.

1.18 There is another important factor to bear in mind. Since the premises are let to the tenant, not to the tenant's (choice of) business, and because rent is payable regardless of the profitability of the tenant's business, the assumption is that the tenant is of independent financial means, and not dependent upon the availability of finance or borrowing from banks and lenders. Therefore, the ability of the tenant to afford the revised rent on review is irrelevant to the rent review itself. Where it could be relevant is in the practicalities to the landlord of obtaining the rent payable *after* the review has been agreed or ascertained. Although many landlords think no point in squeezing every penny in rent out of the tenant, that is a matter for landlord's discretion and nothing to do with the review itself. In my opinion, any discretion by the landlord as to the amount payable should be exercised *after* the review is agreed or ascertained: to do so before on the basis of perception of the tenant's claims and pleas could do the landlord disservice.

2.0 RENT REVIEW - PRINCIPLES

2.1 When a shop property is offered to let in the open market, the landlord's asking rent will be based on an estimated rent in the market for the premises, having regard to the size, layout and trading position. The landlord is in control. If a tenant is unwilling to offer what the landlord would accept then the tenant cannot force the landlord to agree. The tenant goes elsewhere, the landlord looks for another tenant.

2.2 When the parties (landlord and tenant (with or without involving advisers) agree outline terms in principle, subject to contract, the onus is on the landlord (advisers) to draft the wording of the lease, and on the tenant (advisers) to approve. There is no standard form of business tenancy generally, so all the terms and conditions can be worded from scratch, although solicitors generally use precedents, often slavishly. [A precedent is a legal case establishing a principle or rule of law that a court or other judicial body may use when deciding subsequent cases with similar issues or facts.] Precedents are great time-savers, but they can create problems. The main reason for a problem arising is that whereas the duration (or term) of a tenancy will often last for years, the wording is fixed at the commencement of the term and cannot be changed except by rectification (involving the original parties) or by mutual agreement. If either or both parties and/or solicitors (and surveyors) are inexperienced and/or if a precedent were overturned by subsequent events and/or rulings, including changes in the law, there is potential for the intention of the original parties to be interpreted differently, often resulting in a substantial saving for the tenant or considerably more for the landlord.

2.2.1 A property is an asset that can be bought, mortgaged, sold and transferred, and the tenant may be permitted to assign the tenancy or sub-let the premises. As time passes, the landlord and tenant and respective successors in title can differ from those parties to whom the lease was granted originally. If the original lease were poorly drafted or phrasing ambiguous then the successors in title could be stuck with that wording or phrasing. Similarly, any variations to the tenancy, such as licences to assign, underlet, alter and change the use, can also affect the interpretation and enforcement of the terms of the tenancy.

2.3 Experienced landlords and tenants will usually involve rent review surveyors to assist the respective solicitors. The surveyor must have a in-depth understanding of business tenancy law and rental valuation. At rent review (and on lease expiry/renewal) the terms and provisions of the lease will affect the rent.

2.4 In the market, rent is a product: it does not occur naturally, as in "this is the rent for the premises". To value rent, all terms and conditions of the tenancy must be known, stated in advance or defined. But, since the rent on a new letting is often agreed *before* the lease is drafted and approved, it is possible for a completed lease to contain terms and conditions that could produce a different rent to what was agreed. The test of efficacy is whether the rent would be the same if there were a review on the same date as the term commencement.

2.4.1 Whether it should surely be possible to cover all eventualities in advance when drafting and/or approving a lease, the answer is no. Many landlords, tenants, solicitors and surveyors have fixed ideas on the wording of leases, and may even have their own requirements and terminology. Wording and phrasing can be fashionable, creating during and designed for a particular time of the market. And, whilst possible to speculate, it is impossible to predict the future with any certainty.

2.4.2 A solution to prediction is to introduce the best of both worlds, by enabling the parties to choose between one set of criteria and another, or one procedure over another. For example, with dispute resolution procedure, the landlord could elect for referral to arbitration or an independent expert. However, unless the consequences of choice are carefully worded, the aim may be undermined: for example, enabling an independent expert to determine responsibility for costs can back-fire on the landlord.

2.5 Each shop property is unique, even if the only difference is slight; also all landlords and tenants are different, so too are their advisers; also there is no standard form of lease and wording in use generally. All those differences make a difference: so, because rent is a product of the lease and the lease the product of the landlord and tenant and the property itself, a unique set of circumstances is created for each shop property.

2.6 Although the terms of the tenancy entered into by the original/first landlord and tenant are subjective, having taken into account the wider consequences for those parties, the operation, interpretation and enforcement of the tenancy during the term (and sometimes beyond) is subject to the strictures and objectivity of business tenancy law, regardless of the wider consequences for either party. Business tenancy law is a combination of legislation, case-law precedent, and rental valuation practice.

2.6.1 Although unrepresented landlords and/or tenants could draw comparison and make valuation and technical adjustments, in business tenancy law valuation surveyor opinion is preferred. Apart from shop property technical know-how, another main reason is emotional detachment. It is considered difficult if not impossible for the actual landlord or actual tenant of a shop property to decide objectively what rent should be agreed when that landlord or tenant is likely to be affected by the wider consequences of a decision.

2.6.2 In principle, the surveyor's opinion ought be derived from getting a feel for the market and thereafter if need be casting around for evidence. In practice, many surveyors value back-to-front. Instead of relying on a feel for the market, they skip that art and go straight to the science of 'comparable evidence'. Basing opinion on what already exists can often lead to difficulties, as I shall explain later.

2.7 Comparable evidence is what other landlords and other tenants have agreed for other premises of a similar nature on similar terms of tenancy. For evidence to be comparable, it may not have to be the same: differences can be adjusted or allowed for using valuation techniques and methodology. (Having said that, there is case-law to suggest that comparable evidence ought to be same in all respect as the premises in question.)

2.8 The quality of the evidence derived from the various ways in which rent can be fixed in terms of the weight which can be attached to it when forming opinions of value will depend upon the circumstances of each case. *All other things being equal,* the descending order of weight is:

(a) Open market lettings;
(b) Agreements between valuers at arms-length upon lease renewal or rent review;
(c) Determination by independent expert (including a PACT independent expert at lease renewal);
(d) An arbitrator's award (including a PACT arbitrator in respect of a lease renewal);
(e) Determination by the court under Part II of the Landlord and Tenant Act 1954.
(f) Hearsay. Although hearsay evidence is now generally admissible in civil proceedings this does not alter the weight to be attached to it. The quality of such evidence can however be enhanced through technical procedures such as Civil Evidence Act notices.

2.8.1 Inexperienced surveyors tend to use the descending order above as an exhaustive rule rather than a guide. However, in some markets, evidence may emerge that cannot conveniently be categorised, and which will nevertheless be relevant and probative.

2.8.2 Many surveyors consider evidence involving unrepresented parties to be unreliable unless in the opinion of the surveyor the parties are considered to have sufficient experience of the review process. In my opinion, there is no reason to dismiss as a matter of course an agreement involving unrepresented or partially represented parties: each situation should be considered on its merits.

2.8.2.1 Arbitrator's award and court determination carry less weight because such rents depend upon the evidence presented at the time.

2.8.3 What is known as "reliable evidence" may be hard to come by. Reliable evidence is generally considered to be the product of both landlord and tenant each represented by experienced surveyors, and better still, independent expert determination. Apart from the fact lease agreements between landlords and tenants are confidential, it is not compulsory to be helpful and many landlords and tenants do not want to get involved. Even so, many transactions are publicised in the media, landlords thrive on confidential information and surveyors and retailers tend to help one another, so evidence is available to professional participants.

2.9 Except for compliance with business tenancy law and the review guidelines, there is no set formula or logic for what the rent on review would or must be. Supply and demand is forever changing, and with thousands of landlords and tenants, every single lease different, and rental agreements for all manner of reasons, the market is in a constant state of flux. Unless the rent review is index-linked, there is no reason for the market rent to keep pace with inflation.

2.9.1 Regardless of the evidence, the market for the premises is not being tested, because a new lease from the landlord is not available. At rent review, because the premises are let, whether or not occupied, the market cannot be tested to completion because there is a tenancy already. Offering a property to let that is already let could be done, but there is no way of knowing whether any rental offer would convert from 'subject to contract' to unconditional completion without surrendering the existing tenancy beforehand.

2.9.1.2 To quote from case-law, "second best are rent reviews which are negotiated between valuers, because although their aim is to achieve the same end-result of deciding what the market rent is, their decision is not tested by the market; their decision, their agreement, is based on their conclusions about what the market would decide. Negotiated settlements therefore can be unreliable because of the possibility of error piled on error. They need. . . an occasional window of reality provided by open market decisions".

2.9.1.3 Because many surveyors value to front, and/or do not emotionally detach from their client's instruction, the feel that their opinion is supposed to be based upon may be bias in favour of the instructing party, or their personal sympathies. Sometimes the only way to obtain the market rent in accordance with the terms of the tenancy is to present reasoning to someone with no vested interest in the consequences.

3.0 RENT REVIEW - CLAUSE

3.1 Generally, a rent review clause comprises six elements: 1) the date and/or intervals for the review, 2), what has to be done and by whom to start the review, 3) the guidelines for valuing the rent, 5) the procedure for resolving disputes, and 6) what happens after the rent is agreed or ascertained.

3.1.2 A difference exists between the date of the lease and the date of commencement of the tenancy. The date of the lease is when the document was completed. The date of commencement of the term, which may be the same as the date of the lease, is normally the date from when the tenancy starts, also whence rent review intervals run, unless stated in the lease. The term commencement date may be on or before or after the date of the lease. The rent commencement date is also variable depending upon terms of the tenancy.

3.1.2.1 If when the lease was signed the parties forgot to fill in the actual review dates, or where dates in the lease and counterpart lease differ, then it would be necessary to look to the pre-lease negotiations or reach an acceptable conclusion. In any event, for purpose of rent rent review, it is important to have the original completed lease, or a copy of that completed lease. A draft unsigned lease is not good enough.

3.1.3 The review date may not be same as the valuation date and/or the review rent payment date, although often it is. In my experience, a valuation date and/or payment date may differ because that is what the parties wanted on grant of tenancy, or as a result of the timing of the notice to implement the review process.

3.2 Generally, unless otherwise stated in the lease, the revised rent will be back-dated to the review date, regardless of when the revised rent is agreed or ascertained.

3.3 Many tenancies contain what are commonly known as "upward-only" rent reviews. An "upward-only" rent review does not mean the rent must necessarily go up, simply the rent payable *after* the review has been agreed or ascertained cannot be less than the rent payable beforehand, (subject to the terms of the agreement

pertaining to that rent payable beforehand). Actually, there is no such thing as an "upward-only" rent review, because, strictly, the basis only applies to rent payable, as distinct from valuation of the market rent. There is no reason why a landlord or tenant should not agree the market rent or have it ascertained at a lower figure , even though the actual rent payable after the review would remain unchanged.

3.3.1 On the plus side, "upward-only" reviews maintain at least the same sum of rent payable to the landlord throughout the term of tenancy, and encourage the landlord to grant a longer term than otherwise so as to provide the tenant with the security of a longer term of tenancy. The disadvantages are that a) tenants dislike the idea that landlords should receive at least the same rent throughout the term or remaining term of the tenancy when the market rent at a subsequent review date might be lower, and b) because the rent payable would not fall, the property could be overrented, thereby affecting the capital value of the investment.

3.3.1.2 Incidentally, where an existing tenancy contains "upward only" rent reviews and on expiry of that tenancy the tenant renews per Landlord and Tenant Act 1954, and even if it were agreed the renewal tenancy would also contain "upward-only" rent reviews, the initial rent payable at the start of the renewal tenancy would be the market rent, and that may not be the same as the rent payable before expiry.

3.4 Since there is no standard form of business tenancy generally, and every lease is different, there are no set guidelines for rent review. Each lease contains guidelines of its own. The wording of guidelines may be clear, vague or ambiguous depending upon the skill of the draftsman and the experience of the parties and advisers when the tenancy was granted (or varied subsequently).

3.5 The actual lease will contains terms and conditions for operation and enforcement of the tenancy between the actual landlord and actual tenant. The function of the review guidelines is to provide the notional terms of a replicate tenancy to be granted as if the premises were available to let in the market. In practice, the guidelines may be worded and phrased so as to enable either landlord or tenant to obtain a greater or lesser rent than the terms and conditions of the actual tenancy would support. For example, where the actual tenancy restricts use of the premises the guidelines for the replicate tenancy might not contain a restriction.

3.5.1 Amongst fairly standard terminology are the phrases 'willing landlord/lessor' and 'willing tenant/lessee'; matters to be assumed could include the premises being fit and ready for immediate occupation and use, the assumed Use Class even though the permitted use might differ; matters to be disregarded might include any effect on rent of the tenant's occupation of the premises, any effect of rent of any improvements carried out by the tenant other than in pursuance of an obligation to the landlord, any goodwill attaching to the premises by reason of the tenant's occupation, and any effect on rent of any licences. [The definition of 'willing' is enshrined in business tenancy law: basically, the landlord and the tenant are abstractions, hypothetical parties.]

3.5.2 Unrepresented parties/inexperienced advisers will often go straight to the amount of rent, and may not even bother to read the lease, but experienced surveyors start with the review guidelines. Ignoring the guidelines can prove a big mistake because, as I have said, rent is the product of the terms of the tenancy, and how the parties chose to define the various components for valuing the market rent are important.

3.5.3 Inexperience tends to read wording literally, but thinking that may not enough. For purpose of rent review and valuation, the literal meaning of words and/or phrases is not always applicable so should not be taken for granted. Words have precise neutral meanings, but connotations (positive or negative) can be attached, so interpretations can vary depending upon the party's agenda. In business tenancy law most of the words and phrases in connection with rent review have been considered by the courts. [In my law library, I have thousands of case-law judgements and articles on strategy at rent review and lease renewal.)

3.5.3.1 Interpretation of the construction of tenancy contracts is fashionable: nowadays, it is a presumption in favour of reality, but the court could be reluctant to rewrite a contract merely because it produces an unusual commercial outcome. Furthermore, it may not be a question of ascertaining what the original parties intended, so much as the effect on rent of what was agreed. All in all, another reason to use my rent review specialist services is to avail of in-depth of understanding of the interpretation of wording and phrasing.

4.0 RENT REVIEW PROCESS

4.0 In outline, the rent review process comprises five stages:

1) Implementation
2) Agreeing the rent - Negotiations
3) Dispute resolution and procedure - Referral
4) Recording the agreement
5) Payment of the revised rent

4.1 Implementation

4.1.1 Implementation of a rent review includes how long before the review date the procedure should be started, whether notice should be served and if so then when, by what means and where, and by and on whom.

4.1.2 How long before depends upon the wording in the lease. There is no statutory period of notice. Starting too far ahead might lead to hardly anything happening until much nearer the time. Too close to the review date is likely to mean negotiations continuing well past the review date.

4.1.3 Whether the review is started by the landlord or the tenant depends upon the actual lease. In modern leases, there is a tendency for either party to have the right to start. Where only the landlord can start the review but does not, it is possible, per case-law, for a tenant to force the landlord into doing so, failing which the landlord's right to review would be lost. If the tenant has the right to start the review but waits for the landlord to make the first move, then the tenant cannot usually successfully claim the right to review would be lost if the landlord takes no action.

4.1.4 Subject to whether time is of the essence or implied, it may not be necessary to implement the review around the time of the review date. An outstanding review where no action has been taken will leave the tenant in a state of uncertainty and present the landlord with an opportunity to capitalise should the tenant make a request or application, for example, to assign the tenancy, or sub-let. Whether a review could be said to be abandoned if no action were taken is not necessarily so. In case-law, the right to implement a review some 13 years old was upheld. Tenants well-versed in rent review will normally do whatever they can to avoid a review remaining outstanding because of the problems that could arise otherwise.

4.1.5 On starting a review, there are practicalities to consider. When intended to instruct a surveyor, it is sensible to do so at least six to nine months before the review date. That will enable the surveyor to inspect the premises, monitor the locality for evidence, and enable the surveyor to provide advice for the proposal. It is unusual for a review to be agreed or ascertained before a review date and may be ill-advisable. Negotiations can and do take time, at least they do if you want the best deal, and a proposal or agreement reached way ahead of the valuation date could be wrong if the market changes . When landlords have a go at doing the review themselves, only instructing a surveyor if they come up against resistance, such landlords will often inflate the proposal because they expect the tenant to make a counter-offer. Simple bartering may not work because most tenants nowadays are likely to claim no increase. Also, inflating the proposal can cause problems for a surveyor subsequently instructed because it can affect credibility.

4.1.6 Where the lease requires a notice to be served to implement the review, the period of notice may be stated in the lease, in which case it might be necessary to comply with the terms of the tenancy. There is no statutory form of notice, as at lease expiry/renewal, but the notice should be in writing.

4.1.7 Generally, a lease will contain requirements for the service of notices, and usually by recorded or special delivery. Service by hand may be possible, but I do not advise that unless delivered to the tenant personally and a receipt obtained on delivery. Service by electronic means including fax is not advisable: many tenants have statements on their emails and websites refusing to accept the service of notices by email; and fax machines can be unreliable. The advantage of recorded delivery/special delivery for notices is both proof of posting and tracking of delivery. Use of recorded delivery is enshrined in business tenancy law.

4.1.8 Where notice is to be served is important. It may be necessary to serve notice on the tenant at a different address to the premises, or for notice to be addressed to a particular person in the company. Again, the lease will provide details. Where there are no specific details, notice should be served either on the tenant at its last known address or registered office, with a copy to the premises, (and/or agents), or to the premises, with a copy to the last known address or registered office (and/or agents) where applicable.

4.1.8.1 Provided the notice has been served in accordance with the tenancy, it may not be necessary for the notice to have been received by the tenant for the notice to be enforceable. Also, any mistakes in the notice that would not be reasonably considered misleading to a recipient might not render the notice invalid.

4.1.9 Depending on the requirements of the lease, the notice may or not require a rent to be specified. If not necessary to specify a rent, then I recommend serving notice to operate the review (if notice to operate the review were required), and a separate letter (it can be sent in the same envelope as the notice) containing the proposal. Where a rent is to be specified, it may not have to be the market rent per the guidelines: a margin for negotiation can be included. However, where the procedure requires a rent to be specified, the wording of the notice must be in a form that is capable of acceptance: the notice must not be marked 'subject to contract' and/or 'without prejudice' because that would invalidate the notice. Only when not necessary to specify a rent can 'subject to contract' and/or 'without prejudice' be used. Even so, in business tenancy law, one must careful when and when not to use 'without prejudice'. In outline, a proposal 'without prejudice' can be accepted. It is doubtful whether 'subject to contract' has any efficacy in the context of a rent review in a tenancy already in force.

4.1.10 It is an established principle that time is not of the essence for a rent review unless stated in the lease, or there is a contra-indication in the express words or in the interrelation between the rent review clause itself and other clauses or in the surrounding circumstances. (For example, a break-clause at the review date; and the word "shall" could mean time is of the essence.) Even so, the timing of a notice may be critical. Where the lease states time is of the essence, that can mean loss of right to review if notice were not served correctly. Although time of the essence for the landlord's notice is less common nowadays, the lease may require the tenant to serve a counter-notice within a specified period, failing which the rent in the landlord's notice would be binding.

4.1.11 Where the review guidelines do not require a rent proposal, simply the parties are to agree the rent within a stated time, failing which the dispute resolution procedure would be implemented, tenants often try to reason a proposal be made or else there is nothing to discuss. I consider that a non-starter: there is nothing to stop the tenant, or the landlord for that matter, starting negotiations without a proposal. The objective is to agree the market rent, per the review guidelines, and that can be done without having to be told in advance what the landlord or tenant would have in mind.

4.1.12 Where the lease requires the tenant to serve a counter-notice within a specified period of time, the mode of service, and the wording of the counter-notice must comply with the requirements in the lease, or else the counter-notice could be invalid.

4.1.13 When the tenant acknowledges the notice or opening letter, or where a surveyor acknowledges on behalf of the tenant, it is prudent to ensure the person responding or the surveyor's client is the legal tenant before commencing negotiations. It is common for members of the tenant's family or associates to act like they are the tenant, or for the surveyor to think acting for the legal tenant only to discover not; or for the tenancy to have passed to another party without the landlord's consent or knowledge. Years ago, when the Government made it financially attractive for unincorporated businesses to incorporate, many sole proprietors and partnerships incorporated without assigning the tenancy, often assuming wrongly no need to do so.

4.1.13.1 Although on expiry of a tenancy the Landlord and Tenant Act 1954 enables statutory notice to be served to identify occupants of the premises, there is no statutory obligation at rent review so the only way to be sure the tenant is whomsoever they say they are is to check carefully.

4.2 Agreeing the Rent - Negotiations

4.2 The landlord and tenant relationship hinges on a legally-binding document and rent review is function of tenancy management. Rent review is not about what the tenant would agree if it were were the landlord; per case-law: "it is not good for a tenant to say what is good for a landlord". There is no right or wrong way to negotiate a rent review, any more than there is a right or wrong way to negotiate anything. It all depends upon the circumstances and the parties involved. However, credibility is important, so regard must be had for shop rental valuation practice and business tenancy law. The main differences between negotiating a rent review and other types of negotiation is that compromise may not be such a good idea, and the tenant may not care about a jot about your circumstances. Some tenants, especially multiple retailers, get quite precious and protective about their shops and may think that whatever they want is what the landlord should agree.

4.2.1 Many surveyors think that where a landlord wants an increase it is up to the landlord to justify with evidence, but that is incorrect. A review is for the benefit of both parties so, rather than confrontation, I reason the parties should co-operate by contributing to the objective: namely, to agree the market rent pursuant to the review guidelines, or identify differences in opinion in connection with the dispute resolution procedure.

4.2.2 Review guidelines often state a period of time for agreement, failing which the dispute resolution procedure may be implemented but, provided time is not the essence, the literal timetable can be usually be ignored or extended by agreement. Whilst, in theory, there is nothing to prevent a review being agreed within the time-frame suggested if the landlord or tenant were amenable to the figure, in practice, rent review often takes a long time to conclude. Partly that may be a reflection of how busy are the parties and/or their respective surveyors, but often it is to do with pace of negotiation and need to carefully consider all possibilities. Generally, the timing of a rent-review is independent of the timing of other negotiations and transactions underway in the locality that may have a bearing on the review. In other words, it is not that a review cannot be concluded one way or the other in a relatively short time, but simply it may not be wise or prudent to do so.

4.2.2.1 Some landlords prefer to reach agreement sooner than later to avoid a build-up of back-rent, assuming an increase. Many tenants do not keep money in readiness so often request to pay back-rent in installments. Whether the landlord should be accommodating is a matter for landlord discretion.

4.2.3 In principle, there is no reason to negotiate at all. If a proposal were made and the tenant does not agree, or the tenant makes it clear from the start it considers no increase is justified, then there is no point in discussing the matter further. The logical step is to implement the dispute resolution procedure. Often, particularly with multiple retailers, the representing surveyors will write to the landlord to say that in their opinion and/or the tenant's opinion there should be no increase and would the landlord agree by signing a memorandum. As a gambit, such communications are often successful because many landlords assume that because the tenant is represented the surveyor's opinion is likely to be correct, so no point in arguing. It may also not be worth-while: since most surveyors charge, in my opinion, disproportionately for negotiating rent reviews it may not be worth pursuing the review at all, depending upon how much it would cost you. As for the state of the market, it is important to obtain surveyor opinion on the merits of the review rather than rely on media comment. (Media comment is too general: it is impossible to conclude whether there is any scope for increase without first considering the terms of the tenancy and the nature of the premises.) Some landlords commission surveyor reports on rental value but, in my opinion, that can be a waste of money. Often, valuation points can be overlooked and/or further evidence arise during negotiations which was not available when a preliminary report is prepared. And frankly nothing ventured, nothing gained. (Where I am instructed, I provide a preliminary report for the proposal as part of my service and at no extra charge.)

4.2.4 The nature and tone of negotiations may be friendly and amenable, or confrontational and hostile, depending upon the parties, their experience and personal preferences. There may be a lot at stake at rent review (every £500 a year increase can add approximately £5000 to the capital value of the investment; and wider consequences include opportunity for playing power-games and enhancing the reputation of advisers), so negotiations differ from the sort of negotiation where there is a desire for everyone to be happy. Generally, rent review negotiations are about one party winning, the other party losing. Generally, an unrepresented tenant will reason affordability or economical rent. "Unrepresented" includes tenants that negotiate themselves and/or through their solicitors or accountants. Neither solicitors nor accountants may be said to be rent review negotiators in the proper objective sense, because such advisers are on their client's side and generally only communicate their client's wishes. Depending upon the client's personality, surveyors too can be prone to supporting their respective's client's views on what should be communicated.

4.2.4.1 When the tenant is represented, a first consideration is by whom. The nature of the tenant's surveyor's experience and ability to manage expectations can make a difference to the outcome. Multiple retailers either handle the review in-house where they have an estates/property department, and/or instruct external niche-surveyors, regional or national firms/companies of surveyors but that does not necessarily make the actual surveyor dealing with the matter any good. Whether negotiations are handled by the same person or firm of surveyors throughout is up to the tenant. In larger surveying firms and retailers where employees come and go with regularity, it is not unusual for different people to be involved along the way. When you are up against someone whose reputation precedes them that is only daunting if you have little or no experience - it has been said of me by an auctioneer that if I were acting for the tenant then the investor could forget any idea of getting more rent! Small tenants, generally, tend to use local estate agents/surveyors, but again it all depends upon the experience of the actual surveyor involved with the matter. To an outsider, there may be no rhyme or reason for the whereabouts of the surveyor in relation to the client or the premises. Over the years, I have probably dealt with most if not all of the national and regional firms of surveyors, at all levels of the organisation from senior partners/directors down to juniors: all I can tell you is that the manner of negotiation and the possible outcome very much depend upon the experience of the actual surveyor dealing with the matter.

4.2.5 When you instruct a surveyor, really, it is best to leave the surveyor to their own devices. Frankly, it can become tiresome to have to explain ins-and-outs, and subtleties. Progress reports can be provided. In my case, whether acting for landlords or tenants, I am generally entrusted with virtual autonomy which means I am free to agree what I like without necessarily having to obtain client's instructions at every stage; and for some clients I am authorised to make binding decisions. Generally, the more experienced or senior the surveyor the less the client is likely to get directly involved in how the surveyor is conducting the negotiations. (NB: paragraph 4.2.10)

4.2.6 Although a review to market rent should be just that, the tenant's surveyor will not necessarily want to pursue that line of thought because any surveyor worth their salt will aim to beat the going rate. Advantages to such surveyors include a delighted client, advantages to tenants in paying less than market rent include budgeting and marketability of the tenancy. The point is at during negotiations, the tenant and/or the tenant's surveyor will want to achieve the lowest rent possible.

4.2.6.1 Negotiation requires an understanding of landlord-and-tenant psychology. What I am about to say may not be the case nowadays with retailers scrutinising property costs to the nth degree but it used to be thought that where a large firm of surveyors was acting and because such firms are accustomed to substantial fees their surveyors were not bothered about trying to save every penny. In any event, because of the effect of fees to surveyors cost-time expediency can enter the thinking. For example, if it would cost the tenant a disproportionate amount to persist, the tenant might consider it cheaper to agree some increase so as to avoid extra costs. However, since a landlord is unlikely to be privy to how much the tenant is paying its surveyor one should not assume that because the tenant has a surveyor the tenant would concede.

4.2.6.2 Some landlords have this idea that when surveyors are acting for tenants the tenant could be persuaded to agree more if the landlord were to circumvent the surveyor. Sometimes that is the case but invariably the tenant will consult the surveyor before agreeing anything with the landlord. With relatively low levels of rent and where the tenant is a local shopkeeper or where the landlord is used to dealing with the tenant's managing director, it may be possible to negotiate direct with the tenant by proposing an increase based on inflation, even though there is no link between inflation and market rent. With the cost-implications of instructing a surveyor the tenant may not consider arguing worthwhile. Over the years I have noticed a trend whereby landlords prefer to deal direct with small tenants, and only instruct surveyors where the tenant is a multiple retailer or large company. Generally, an unrepresented landlord trying to negotiate direct with a multiple retailer (or that retailer's surveyor) is likely to meet resistance nowadays as a matter of course.

4.2.7 Of the many ploys during negotiations, probably the most successful is to prey on fear of extra costs. The ploy is commonly used where the landlord is a private investor and the tenant a multiple retailer/bank, or large company. Although the dispute resolution procedure is intended for use in the event the parties are unable agree if all else fails, a good way to force agreement is to raise the possibility of extra costs. The ploy is used to persuade the other side to concede, rather than incur the extra costs.

4.2.7.1 Generally, the extra cost of referral (to arbitrator or independent expert, depending upon which method is stated in the lease) includes the additional fees payable to the party's surveyor and any other advisers, the costs and fees charged by the appointed third party, the application fee to the Royal Institution of Chartered Surveyors for making the appointment, and the tenant's costs. There is no set scale of charges for arbitration or independent expert and the hourly rate and minimum payable varies from surveyor to surveyor. Nowadays, between £200 an hour and to around £375 an hour is the norm. The prospect of at least £3500 exclusive of VAT and disbursements payable to the arbitrator or independent expert may be enough to deter, and that is before the RICS application fee, extra fees payable to your surveyor, or the possibility of having to pay the tenant's costs as well. As to whether landlord and tenant would share the costs of referral proceedings, I shall explain later.

4.2.7.2 Threat of referral will only work as a ploy if the tenant or landlord were fearful of the prospect. A common mistake beloved of unrepresented landlords is to try to persuade the tenant to agree so as to avoid costs of involving a surveyor, but when the tenant takes advice of an experienced surveyor the landlord's stance is considered a sign of weakness. Consequently, in attempt to break an impasse in negotiations, there is no point in a landlord instructing his surveyor to inform the tenant that the review would be referred to 'arbitration' only to find the tenant amenable to the prospect. The only way to test the water is to apply the extra costs procedure, either by making a Calderbank offer or making application to the RICS, or a combination of both. I explain later.

4.2.7.3 Where a tenant is unresponsive to communications, the only way to force the pace is to initiate the dispute resolution procedure. Initiating procedure does not necessarily mean having to go all the way. There are several steps that can taken before there is no stopping. The first step is to make the application to the RICS; next to wait for the identity of the appointed surveyor to be released, the third step is to request the appointed surveyor to take no action so as to enable negotiations to be continued; next to request the appointed surveyor to issue draft timetable for conduct of the matter subject to agreement by the parties; the fifth step is to ask for the agreed timetable to be issued as formal directions. All those steps and any others that might be taken where opportunity arises can be done in parallel with negotiations. Any proposals for amicable settlement can be on condition the tenant pays at least half of the RICS fee and appointed surveyor's costs.

4.2.8 During negotiations, there may be any number of proposals and counter-proposals but provided none of the offers are in a form capable of acceptance the possibilities to reach agreement can be explored. In my experience, landlord attitudes fall into two categories: some after every penny they can get, others more accommodating. Those after every penny are usually indifferent to the wider consequences for the tenant so tenant's letting off steam will cut no ice. Others may not be as tough or demanding, but that doesn't mean they have to be generous. There is no entitlement to any 'sitting-tenant' discount.

4.2.9 A distinction exists between the rent another landlord nearby might charge or another tenant might be paying, and the market rent. Different landlords and different tenants think differently. For whatever reason another landlord is not charging as much as it could, or a nearby tenant paying a lot less, that does not mean having to accept the same value pro-rata. Although such evidence might support a lower rent for the tenant, the dispute resolution procedure might be beneficial because the overriding factor is not what someone else has agreed for different premises, but what your premises on your tenancy would let for in the market.

4.2.10 Where the landlord is negotiating direct, the landlord can decide whether and when to accept the tenant's offer. When the landlord instructs a surveyor, negotiations will reach the stage where the surveyor thinks far enough. In theory, every offer should be reported to the client but I doubt many surveyors would do so - I know I don't - because unless the offer would receive the surveyor's recommendation presumably the client is content to be guided by the surveyor. The surveyor is not usually able to accept the tenant's (final) offer without obtaining the landlord's instructions. Generally, surveyors can only advise and recommend: it is up to the client to decide. Assuming the client accepts the recommendation, and assuming the tenant likewise of its surveyor, negotiations are concluded in principle, thereafter the agreement in writing, usually a memorandum.

4.3 Dispute Resolution and Procedure - Referral

4.3.1 During negotiations, the valuation approach is often both subjective and objective: in other words, the wider consequences for both landlord and tenant play their respective parts. On referral to arbitration or independent expert, the valuation approach is completely objective. The psychological implication of referral is loss of control of the process of rent review. Losing control may be beneficial. Since, in business tenancy law, a landlord is not obliged to propose a rent strictly in accordance with the review guidelines, referral of the market rent to someone with no vested interest in the consequences could result in a greater rent than the landlord's original proposal, or more than how much the landlord might have accepted beforehand. The tenant using the dispute procedure to attain a lower rent than the landlord would have agreed can backfire. Conversely, the tenant's offer to avoid referral might not be bettered by objective determination of the market rent. Therefore, given the extra costs, risks and uncertainty, the challenge when considering the dispute resolution procedure is whether referral would be worthwhile.

4.3.2 The object of referral is for the rent on review to be fixed independently and impartially. Although the phrase "going to arbitration" is commonly used, in fact there two different methods of referral - Independent Expert and Arbitrator - each with its own technical characteristics and legal requirements.

4.3.3 An Independent Expert is an individual, normally a chartered surveyor, whose Determination of rent the parties have covenanted to accept. Basically, a Determination is a valuation, an informed opinion. Because a Determination is an opinion the Independent Expert is free to make up his own mind as to the rent, regardless of what the parties might themselves opine. With a Determination, there no right of appeal as such, but an Independent Expert may be sued for negligence.

4.3.4 An arbitrator is a person(s), whose Award of rent is binding on the parties. An arbitrator is a quasi-judicial appointment, whose powers are derived from Arbitration Act 1996. Unlike an Independent Expert, an arbitrator is bound by the rules of evidence, so can only make up his own mind at or within the extremes of evidence presented during proceedings. Because an Award is not a valuation in the usual sense, an arbitrator cannot be sued for negligence; the only appeal on a point of law, or misconduct by the arbitrator.

4.3.5 Long ago, it was usual for surveyors when acting as negotiators for the parties to continue in that role on referral. However, as a result of surveyors doing just that in the witness box in court in connection with tenancy renewals, the court has laid down rules for surveyors acting in the capacity of expert witness. Compliance with the rules includes the primary duty of the expert witness to the court regardless of the instructing party. There are a number of tests the surveyor must satisfy, one of which is that the expert witness surveyor's opinion of rent would be the same if acting for the other party. In consequence, the RICS, wanting to comply with the law, has introduced a mandatory practice statement and guidance note ("PS") for chartered surveyors at rent review, but instead of limiting the mandatory requirements to arbitration, the PS also applies where the rent is to be determined by an Independent Expert. I am not going into much detail here, the subject would occupy a ML Guide in itself, but, basically, what has happened is that chartered surveyors are no longer allowed to act as negotiators on referral, but must choose between acting as expert witness or advocate or a combination of both roles, provided they make it clear in what capacity they are acting for evidence and their opinions.

4.3.5.1 In practice, the PS obliges chartered surveyors to act as purists on referral, even though that goes against the grain of realism for many surveyors. The argument against the PS is that the client reasonably expects the surveyor to continue to be on the client's side throughout, and not be free to make up his own mind about the rent regardless of the client's instructions. For my part, not being a chartered surveyor, I am not bound by the PS, but I am subject to the court's rules. Consequently, thanks to the PS, I find myself in the advantageous position when acting for the landlord (or a tenant for that matter) is being able to act as advocate and able to use the gamut of my knowledge and the forces of persuasion to influence the outcome. [I act in the capacity of expert witness surveyor only where my expertise on rental value is beyond reproach.]

4.3.5.2 For the most part, chartered surveyors are inclined to act in the capacity of expert witness at rent review referral: traditionally, advocacy is seen as acting in the client's best interests to the exclusion of all else, but actually that is incorrect. Using my specialist knowledge of rent review and study of advocacy, I have developed a method of acting as advocate at rent review referral and that I have used successfully on every occasion. [I am aware that non-clients, their advisers and chartered surveyors are likely to read this ML Guide!]

4.3.6 In ML Guide "Arbitration at Rent Review: The Landlord's Perspective" (MLG2), I explain the procedure so am not going to repeat it here. Suffice it to say that because many Independent Experts prefer not to have to do everything themselves, but invite input from the parties/surveyors, leaving it all to the Independent Expert is not a good idea. The advantage to the landlord and/or the tenant in themselves each instructing their own surveyor to represent their respective interests is to ensure the Independent Expert takes account of everything that the party's surveyor considers relevant to the review. With arbitration, it is also a mistake to leave it to the Arbitrator to decide because whilst the arbitrator can be helpful the rules of evidence and the nature of arbitral proceedings make it difficult if not impossible for the arbitrator to be particularly flexible.

4.3.7 In outline, proceedings for Determination and Award are often similar. The Independent Expert or Arbitrator will draft Directions for procedure and for agreement by the parties. Directions normally include a closing date for report/submission, a second date for reply/counter-submission, and where advocacy is involved a third date for further examination. The Independent Expert or Arbitrator will inspect the premises (and any comparables). Usually fees and costs payable to the Independent Expert or Arbitrator must be paid in full before the Determination is released or Award published. Those fees/costs are normally be paid by one or both parties equally in the first instance, depending upon the Directions. After the rent is disclosed, the Independent Expert or Arbitrator would invite further report/submission so as to provide a Final Determination or Award on costs.

4.3.7.1 With complex rent reviews at arbitration, others advisers, for example, solicitors and barristers, may take part, but generally referral to arbitration or independent expert ("the third party") is left to the parties' surveyors. Usually, reports/submissions are in writing, but oral evidence can be given. Usually, the third party will ask if a preliminary meeting should be held to agree procedure - sometimes such a meeting is the first time the parties/surveyors have met - but experienced surveyors tend to dispense with that need. It is no one page-letter: a typical report can run to around 10,000-20,000 words and take a day or more to prepare; counter-submission and so on can be just as lengthy and detailed; the paperwork can be voluminous.

4.3.7.2 To the inexperienced landlord, some of the comment in reports/submissions by the tenant/surveyor about the landlord/surveyor may come over as difficult to swallow, but for those of us regularly involved with referrals it is nothing personal. Generally, personal slights are to be avoided and in my opinion there is nothing to be gained from maligning the opponent - there is bound to be disagreement expressed: that was the reason for the dispute - but the objective is the market rent, pursuant to the review guidelines.

4.3.8 For referral costs, the wording in the tenancy is the starting point. Popular thinking that each party pays half the costs is a myth.

4.3.8.1 Where referral is to Arbitration, any agreement in the tenancy as to responsibility for costs is void under the Arbitration Act. Normally, costs follow the award - in other words, the winner can ask for costs - but there may be special circumstances, such as differences in interpretation of the terms of the tenancy, or technical valuation issues, that could only be explored after rental outcome is known, so the costs might be a lesser share.

4.3.8.2 An Independent Expert's authority is derived from the lease. When the lease states each party is to pay half the costs of the Independent Expert that is binding on the parties. The costs referred to in the lease may or may not include the application fee to the RICS. If not then unless otherwise agreed with the other party, the party making the application to the RICS might normally have to pay.

4.3.8.3 When the lease is silent on the Independent Expert's fees/costs then the Independent Expert is not at liberty to impose responsibility: the Independent Expert might offer to determine costs and invite the parties' comments on responsibility but, unless otherwise agreed with the other party, the party that made the application to the RICS could end up paying all the costs, per the undertaking on the RICS application.

4.3.8.4 Where the Lease authorises the Independent Expert to determine costs, or failing which each party is to pay half, the Independent Expert is not obliged to determine on costs. Even if an Independent Expert invites the parties' proposals on costs the Independent Expert is not obliged to agree with the proposals.

4.3.8.5 In some leases, the parties can agree between themselves an Independent Expert or arbitrator by appointing a surveyor of their choice without involving the RICS. Saving the RICS application fee, at present, £369.00 inclusive of VAT, may not be such a good idea. Although one takes pot-luck with applications to the RICS, at least the RICS panel surveyors are trained in the role expected of them. On occasions, I act as arbitrator provided there is no conflict of interest.

4.3.9 A Calderbank offer may protect costs. A Calderbank offer (from Calderbank v Calderbank 1975, involving a matrimonial dispute, but whose principle involving the protection of costs is now enshrined in business tenancy law) is an offer to settle a rent review so as to avoid costs (and risk) of referral. The offer letter is marked 'without prejudice save as to costs' because the offer cannot be disclosed during dispute resolution proceedings, but after the rental outcome is known it could be disclosed by the party that made the offer for purpose of deciding (either by agreement between the parties or failing that or by the Arbitrator or Independent Expert) which party is to be responsible for the costs of the proceedings.

4.3.9.1 The offer and conditions has a date/time-limit for acceptance, and those conditions could alter if the offer were not accepted by the specified date/time. Amongst the conditions, it is usual to require each party to be responsible for half of any costs for referral and otherwise bear its own costs, before the closing date for acceptance, and thereafter for offeree to pay all costs, also possibly the offeror's legal costs and surveyor's fees.

4.3.9.2 The rental offer does not have to be the correct rent per the review guidelines. A Calderbank is generally but not necessarily pitched at the lowest rent the offeror would accept to avoid referral. If accepted then there is no going back: the rent and conditions in the Calderbank would become binding on the parties.

4.3.9.3 Any number of Calderbank offers can be made and by either party and at any time (always provided some dispute). (Arguably there is no reason for a landlord to make a Calderbank offer, because the principle of Calderbank is for the tenant to induce the landlord to avoid costs. It can get complicated because the actionable status of the parties may not be defined as claimant and defendant.) If a Calderbank were not accepted and further Calderbank(s) made, that does not mean the previous Calderbank(s) is/are rejected. The period for acceptance is normally 14 days or thereabouts, but may be shorter depending on what is happening during negotiations or at the time the Calderbank is made. A Calderbank does not have to be made before the dispute procedure is started and may be made after the Arbitrator appointed or Independent Expert nominated, or around the directions, and before any closing date or before release/publication of the rent. Calderbank is not something to do lightly: it is a matter of tactics which is why a Calderbank is used as a negotiating ploy. Just because a Calderbank specifies a rent does not mean the offeror would not agree a different rent; but any negotiations whilst a Calderbank is in force must allow for the possibility that if agreement were reached at a different figure then the time limit for acceptance of the Calderbank could pass.

4.3.10 Although there is no statutory wording for a Calderbank, in my experience, the wording of the conditions in a Calderbank is sometimes incorrect. Arguably the amount of costs to be avoided should be stated/ estimated. It is only when the dispute resolution procedure is arbitration that, regardless of any requirements in the lease, the arbitrator has overriding jurisdiction on costs. Where referral is to Independent Expert the Independent Expert is not allowed to stray beyond the terms of the contract(tenancy). Consequently, a requirement in the Calderbank to pay all of the costs in connection with a referral to an Independent Expert including the offeror's surveyor's fees could be unenforceable.

4.3.11 It could be a mistake to draw the offeror's attention to an unenforceable condition because a revised Calderbank offer could be made. By not mentioning the point until a claim for costs is made it should be possible to successfully reason the Calderbank be considered in its entirety and not in part so should be void.

4.3.12 The date of Award or Determination will often be before the rent is known to the parties, because of the requirement to pay the fees/costs before the Award/Determination is published/released. The date of Determination may not be critical, but the date of Award could cause problems in the event of appeal. There is a time-limit for appeal against an Award and the grounds are limited to a point of law and misconduct. A court application would made and if the claim were successful the Award could be set aide and a new one required.

4.3.13 If the Independent Expert's Determination were challenged on the ground of negligence and taken to court and the claimant successful then the court could order a fresh determination, or the claim could be for damages, the difference between what the Determination and what rent should have been determined.

4.3.13.1 Although an Independent Expert can make up his own mind on rent, it is incumbent upon the Independent Expert to assume it is preferable to verify all information and to carry out all investigations that a reasonable surveyor acting as an independent expert might be expected to carry out together with and consider would assist in making the decision. Regardless of any report or submission by the parties, the Independent Expert is not bound by or limited to the representations and has a duty to assemble his own information.

4.3.14 In modern leases, there is often a requirement whereby in the event one party pays all the costs of of the arbitrator or Independent Expert in the first instance then that party can recover those costs from the other party. When drafting the lease, the landlord should ensure the right to recover includes half the fee to the RICS; also any costs and interest incurred if the payer has to borrow to pay the arbitrator or Independent Expert.

4.4 Recording the Agreement

4.4.1 After the rent is agreed in principle, the review should be documented, usually in a Memorandum. It could be be done by exchange of open correspondence, but a Memorandum is formal, and can be affixed to the Lease. When I prepare a Memorandum (no extra charge!), I ask both parties to sign both copies, date, so each party receives a complete Memorandum. It is not necessary for signatures to be witnessed. Although some leases include wording for the Memorandum, generally that can be ignored. In my opinion, information in the Memorandum must be correct: sloppy drafting, for example not bothering with the full names of the parties, and so on, or fanciful wording as if because it is a legal document it has be pompous is to be avoided.

4.4.2 The Award or Determination is evidence of the rent review so should kept with the Lease and Counterpart. Many landlords prefer to have the rent documented in a memorandum as well. Whether the memorandum should state the rent is agreed (as distinct from awarded or determined) is a moot-point, but to be less pedantic agreement could be akin to not challenging the award or determination.

4.4.3 The name of the legal Tenant must be shown correctly. With a limited company, its registered office and company number should be shown.

4.5.4 The effective date of agreement is the completion date on the Memorandum or in the event of referral the date of the Award or Determination.

4.5 Payment of the Revised Rent

4.5.1 Unless otherwise agreed, or stated in the tenancy, the revised rent is payable from and including the review date so is back-dated if agreed or ascertained after the review date.

4.5.2 Subject to the terms of the tenancy, the payable date may be either on demand, or within a few days of the agreement or ascertainment, or the quarter day or next payment date following the agreement date.

4.5.2.1 Per paragraph 4.5.4 above, the completion date for purpose of enforcement of back-rent payment is the date of Memorandum or the date of Award or Determination.

4.5.3 Modern leases are likely to contain provision for interest on the back-rent. The rate of interest will be stated in the lease and is unlikely to be as high as the interest if the rent were late. The interest would either be calculated on a daily basis (simple interest) or compounded and the lease should provide details.

4.5.3.1 When the lease is silent no interest is payable. However, if the rent review were referred to arbitration then the arbitrator could award interest if requested.

4.5.4 Assuming an increase, it may be the tenant cannot afford to pay the whole of the back-rent but would like to pay in installments. That is a matter for landlord discretion.

4.5.5 If the rent review is market rent unprotected by an upward-only cushion and the market rent is lower than previously payable then the landlord would have to repay any excess. Pending agreement or ascertainment, the tenant would not normally be at liberty to withhold the previously passing rent.

4.5.6 In some leases,there is provision for rent payable between the review/payment date and the agreement or ascertainment to be the passing rent times a multiplier; for example 1.5 * passing rent. The intention of such a provision was to cushion the impact of a likely increase.

4.5.7 The payment date for rent due is date of receipt of cleared funds by the landlord, or agent. Therefore, payment by cheque due on 24 June, for example, would require payment to be made at least 3 working days beforehand to ensure cleared funds on 24 June. Cheque dated 24 June would be late payment.

4.5.8 On completion, building insurance cover for loss of rent should be changed. At the start of the review, cover should be adjusted from the review date based on the estimated market rent because the revised rent would be back-dated.

5.0 SHOP MEASUREMENT

5.1 Very large shops, stores and purpose-built supermarkets, and unusual buildings, such as banks, restaurants, night-clubs, leisure uses, non-ground floor premises, and so on, may be valued on an overall basis but, with the majority of shops, the total ground floor area is normally divided into zones. Zoning is a method of comparing shops of different layouts, configuration, shapes and sizes with one another, so as to arrive at a common denominator. Each zone is allocated a capital letter, such as Zone A, Zone B, and so on.

5.2 Zone A is the most valuable, because it is at the front of the shop, and each subsequent zone is often halved-back, but the fraction is a matter of surveyor opinion. For example, part of Zone A might be A/2, Zone B might not all be A/2, Zone C could be A/6, or Zone D might be A/10, etc. Basement storage might be valued at A/10, first floor sales A/10-15 and storage A/12-A/25. For arithmetical ease, the net area of each zone is expressed as a single figure, known as the area in terms of Zone A, or ITZA for short.

5.3 Usually, each zone is 20'0"(6.1m) deep, but depths vary in some towns and streets – for example, 15'0" (4.57m), 25'0" (7.62m), 30'0"(9.14m). Normally, measurement is taken from the building line to built depth, ignoring shop fittings, wall linings and non-structural partitioning, but allowing for nibs, piers, columns, and structural walls. (Where the shop-front is set back from the building line, assumption is it could be brought forward, unless not.) Normally, ground floor space, unusable for sales, is regarded as ancillary. Basements and upper floors are usually measured overall and valued on actual or potential use, depending upon physical layout and the provisions of the lease. Subject to the terms of the tenancy, actual or potential value of structural improvements may also apply. (It does not follow that tenant's improvements would have to be disregarded.)

5.4 Residential accommodation is valued on its merits, usually by reference to the number of habitable rooms, rather than the floor area itself.

5.5 To devalue the comparable evidence, and for ease of arithmetic, actual rents are converted into what is known as the Zone-A rent: for example Zone-A £75. The Zone-A rent is the agreed rent net of any adjustments pertaining to the comparable, divided by ITZA.

5.6 To calculate the rent the agreed ITZA for the shop is multiplied by the Zone-A rent. However, although each rent is often agreed on the back of another agreement, every lease is different so each situation can involve a different set of circumstances and different approach to negotiations. An agreed rent may have a hidden story attached; in any event, it may be beneficial to apply another interpretation. The point is valuation is an art, not an exact science, and devaluation is a matter of opinion, so each piece of evidence is considered on its merits.

5.7 With residential accommodation, perhaps behind the shop or more commonly a flat or flats on upper floors, the standard approach is to estimate the rent as if the flat(s) were let on an assured shorthold tenancy ("AST") and make an allowance for management, etc. Many years ago, the Estates Gazette, the leading property magazine, published an article by a surveyor on how flats above shops should be valued at rent review. The article was fairly comprehensive, but what the surveyor overlooked is that when the review guideline assumption is a letting of the premises with vacant possession (as is the normal case) the flat would have to be in a much better state than the tenancy would necessarily require. In other words, to support the estimated rent, the overall state would have to be to a standard commensurate with a tenant's expectations. On numerous occasions, I have successfully reasoned the point at 'arbitration' and obtained a lower rent. Therefore, thinking the estimated rent net of discount would be the rental value is not necessarily so.

5.8 Where premises are sub-let on a business tenancy, an allowance may often be obtained for the management costs. In other words, just because the tenant is getting say £7500 a year from its sub-tenant does not mean the full amount would be payable at the rent review.

6.0 CONCLUSION

6.1 I have had it said to me that in explaining rent review, zoning and so on, landlords are dispensing with surveyors and negotiating direct with their tenants. Personally, I think that was always going to happen and is perhaps an inevitability. I am critical of surveyors charging disproportionally high fees and landlords are bound to shop around: fees and costs to advisers can affect performance of the investment. However, there is no getting away from the fact the rent review process is full of pitfalls for the unwary, and to the uninitiated a stressful experience. Furthermore, that larger landlords and experienced property investment companies and others continue to use rent review surveyors is testimony to professional and specialist skills.

6.2 Although shop rental valuation and business tenancy law work both ways, the system is often loaded in favour of the landlord. It is the landlord's property; and the tenant has security in not having to relocate frequently, vital when it takes time to establish a profitable business. The landlord is also spared the cost of re-letting frequently, and can avoid empty property rates. Reflecting the wider consequences during negotiations, many tenants assume a likelihood of settling at less than market rent through amicable agreement. Problems arise when the tenant's business loses its way (operational difficulties), and/or when the rent on review is or becomes uneconomical. Because different landlords have different investment policies and objectives and because the knock-on effect of comparable evidence can drive away from the trading position those retailers whose presence was the main attraction for a tenant wanting to open a shop there in the first place, an inflexible approach to premises management can mean the tenant becoming caught in a vicious circle of rising rents and a trading position in decline. Landlord hoping to minimise decline through a leniency at rent review is, in my opinion, not necessarily productive. The tenant benefits, of course, but whether rent by itself is enough to stop decline is rare. Usually, it is the popularity of the trading position with other retailers and customers that determines stability. Factors that can hit hard a new shopping centre and/or big retailers, including supermarkets, opening in or out of town, also radically alter the dynamics.

6.3 Something retailers are good at is selling and one thing many excel at is not paying anything like as much rent as the terms of tenancy would support. Frequently, multiple retailers and large companies are represented by surveyors whose job is to protect the tenant from the market. On referral, whether to arbitrator or independent expert, it is vital for the landlord's surveyor to be focussed on the guidelines for market rent, the terms and provisions of the tenant, shop rental valuation and business tenancy law. In 1975, I pioneered the idea of specialising in rent review. Nowadays, many of my ideas pervade popular thinking. Apart from expertise, you will have access to my experience, spanning more than 35 years, handling rent reviews for landlords and retailers, large and small, and dealing with properties from those in 100% prime trading positions in city centres to local shops in back-streets. Because I specialise, my fees are generally considered excellent value for money and, unlike most surveyors, I do not charge extra if a review has to go to 'arbitration'.

I look forward to hearing from you.

Michael Lever