Break Clauses

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Introduction

1. Beginning his judgment eight months ago in GKN Aerospace Services Ltd v Duncan Investments Ltd [2020] EWHC 3719 (Ch), Fancourt J's first words were: "*This is yet another case about the exercise of a break option in a lease*". In the last few years, we have seen no signs of a slackening in the flow of disputed break clause cases coming before the courts. The reasons are obvious: there is little standardisation in the wording of such clauses, allowing landlords to insert apparently innocuous wording that contains traps for the tenant, and the increased focus that recent authorities have brought to bear upon break clauses is often too late for those tenants for whom the trap has already been sprung.

2. Although the decided cases treat with all aspects of break clauses, including the attempts made on behalf of tenants to comply, often vainly, with notice requirements and stringent conditions precedent, this paper concentrates upon the following commonly-encountered grey areas: (1) the vacant possession requirement; (2) the obligation to reinstate; and (3) any obligation to remove chattels and tenant's fixtures.

A brief recap

3. The typical (tenant's) break clause will contain all or some of the following ingredients:

   (1) various requirements as to form, mode and timing of the notice of intention to terminate the lease

(2) a requirement that the tenant should, "up to" or "by" the putative termination date have complied with its covenants;

(3) a requirement that the tenant should deliver up vacant possession of the premises on the break date.

4. I covered the first of these ingredients (the notice requirements) in a paper I delivered to the White Paper Conference Company Commercial Property Leases Conference in 2016. In this paper, I turn to the third – the vacant possession requirement – but bring in two commonly-found compliance requirements (the second ingredient), examining how these impact upon vacant possession.

5. The common theme that emerges from the many authorities on the topic is that break clause stipulations must be strictly complied with. Perhaps the most succinct warning was given by Lloyd LJ in Legal & General Assurance Company Ltd v Expeditors International (UK) Ltd [2007] 2 P&CR 10:

> "It is common ground that, in general, conditions attached to a break clause, as with any other option provision, must be strictly complied with, so that even a day's delay in giving vacant possession or a shortfall in the payment of rent of a few pounds would be fatal."

6. The decided cases reviewed in this paper show that it is common for the vacant possession requirement – ostensibly simple to comply with – not to be satisfied in practice.

Meaning of "vacant possession"

7. In NYK Logistics (UK) Limited v Ibrend Estates BV [2011] 2 P&CR 9, a break clause case with which I deal in more detail below, Rimer LJ said:

> "The concept of 'vacant possession' in the present context is not, I consider, complicated. It means what it does in every domestic and commercial sale in which there is an obligation to give 'vacant possession' on completion. It means that at the moment that 'vacant possession' is required to be given, the property is empty of people and that the purchaser is able to assume and enjoy immediate and exclusive possession, occupation and control of it. It must also be empty of chattels, although the obligation in this respect is likely only to be breached if any chattels left in the property substantially prevent or interfere with the enjoyment of the right of possession of a substantial part of the property."

8. This summary conceals three ingredients, referred to in later authorities as "the trilogy". This was perhaps best explained by Nugee J in paragraph 39 of his judgment in Goldman Sachs International v Procession House Trustee Ltd [2018] L&TR 28:

> "… what the obligation to give vacant possession normally requires is threefold. That is to return the premises to the landlord free of, or vacant of: first, people; secondly, chattels (subject to the decision of the Court of Appeal in Cumberland Consolidated Holdings Ltd v Ireland [1946] KB 264, which is to the effect that a party is only in breach of the obligation to give vacant possession by leaving chattels on the property if the physical impediment substantially prevents or interferes with the enjoyment of the right of possession of a substantial part of the property); and, thirdly, legal interest. So, a person does not comply with the obligation to give vacant possession if it is subject to a legal right in somebody else to take possession. That trilogy of people, chattels, and interest, … I accept accurately reflects the general law of vacant possession."

9. The third ingredient is a simple matter of fact: has the tenant terminated any third party rights over the premises by the break date? The first and second ingredients of the trilogy give rise to much more complex questions, which I examine by reference to the decided cases.

Ingredient (1): free of people

10. In Legal & General Assurance Society Limited v Expeditors International UK Limited [2007] 1 P&CR 5[1], Lewison J said:

> "If [the tenant] is actually using the property for purposes of his own otherwise than de minimis, he will be held not to have given vacant possession."

11. This ingredient ought in principle to be the easiest to satisfy, since it is solely in the tenant's power to accomplish. In practice, however, its satisfaction often gives rise to dispute. Three situations call for special mention.

12. First, because the successful operation of a break clause is often linked to satisfaction of the condition covenants in the lease (repair being the obvious example), and because the tenant will have been trying to extract maximum beneficial use from the premises, compliance with the covenants is usually left to the last minute. The result is that contractors may often be found

[1] The decision subsequently went to appeal, but not on this point.

toiling away at the last remedial works on the break date itself, with the works needing some time for their completion. Such circumstances give the judge an easy means of deciding that vacant possession was not available, as happened in the NYK case. In paragraph 49 of his judgment, Rimer LJ said:

> "…so far as I can see, it had done nothing by [the break date] to manifest that it was giving up possession. It had offered to return the keys, but had not done so. It maintained on and after 4th April exactly the same control of the warehouse that it had maintained on and before 3rd April. It remained in occupation of it on and after 4th April in the like manner as it had on 3rd April; and it manifested that occupation by bringing its workmen to the warehouse on 6th April in order to continue with the [works of repair which it was obliged to do on delivery up]. Quite apart from NYK's continued occupation of the warehouse, its carrying out of those works was itself a further trespass to Ibrend's property. On NYK's case that it had terminated the lease on 3rd April, it had no right to carry out such works."

13. Secondly, the tenant may still have stores or equipment in the premises which it is in the process of moving elsewhere, as happened in the Legal & General case, and for which purpose it will have retained the keys to the premises. The break date in that case was 30 December 2004. The landlord's agent inspected the premises on the following day, and found an employee of the tenant sweeping the units, and supervising the removal of a couple of lorry loads of pallets and discarded garment rails. On January 4 or 5 2005, the tenant's assistant warehouse manager cleared up rubbish on the site and loaded a few pallets on to a truck. Lewison J summarised this activity as follows:

> "45. On the day after the break date, … the tenant was still expecting lorries to arrive and take away material that the tenant had left behind and wanted to remove, the photographs still show the tenant in active control of the warehouses which it was using, in part, for storage of materials that it wished to take elsewhere. The tenant's employee, Mr Tulip, was still on site for that purpose. After that time the units were still locked and the landlord was not able to get into Unit 15 with keys of its own
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> 47. … given the retention of all the keys by the tenant, the presence on the site of at least one of the tenant's employees, the continuing use of the warehouse for storage of materials which remained useful to the tenant and the arrival of vehicles to collect them, the landlord could not have occupied the warehouses without difficulty on December 31, 2004 and Unit 15 was locked for many days thereafter.

> 48. Had this been the decisive point I would have held that the tenant had failed to give vacant possession on December 30, 2004."

14. Thirdly, where the landlord is being uncooperative about receiving the keys from the tenant (as happens surprisingly often in practice), the tenant will naturally be concerned lest the premises be broken into and vandalised or occupied around the break date, and will therefore institute security patrols and caretaking to guard against that. However, if it goes further, and installs security measures on the premises themselves, then it is asking for trouble. In John Laing Construction Ltd v Amber Pass Ltd [2004] 2 EGLR 128, Robert Hildyard QC, sitting as a Deputy High Court Judge, upheld the tenant's arguments that its security measures, in the form of the retention of keys and the installation of removable concrete blocks, did not in fact negate the delivery of vacant possession – but it would be imprudent for tenants to rely upon such a beneficial outcome, given the doubt expressed by Lewison J as to the judge's reasoning in the Legal & General case.

Ingredient (2): free of chattels

15. In paragraph 42 of his judgment in the Legal & General case, Lewison J said of this ingredient:

> "The second test looks at the physical condition of the property from the perspective of the person to whom vacant possession must be given. If that physical condition is such that there is a substantial impediment to his use of the property, or a substantial part of it, then vacant possession will not have been given. As the Court of Appeal said in the Cumberland case, that is likely to be satisfied only in exceptional circumstances."

16. In practice, however, there are a number of examples of cases where the landlord has succeeded in relation to this ingredient. Three will suffice for today's purposes.

17. First, in Secretary of State for Communities and Local Government v South Essex College of Further and Higher Education [2016] PLSCS 249, having given its break notice, the tenant moved out of the premises, leaving them locked and alarmed, and left behind some freestanding partitioning, two reception desks, and a quantity of chattels, including computer screens, a photocopier which was still paid for and owned by the defendant with a sign left on the top of it saying "do not move", a box of student files which defendant was under a statutory obligation to preserve for audit purposes, and a certain quantity of cabling, wiring, trunking and electrical sockets relating to the IT equipment that had formerly been there and relating to the telephone system.

18. The landlord submitted that the tenant did not give up possession for each and all of the following reasons: (1) because it did not manifest any objective intention to do so; (2) because it continued to make use of the premises by storing various items in them; and (3) because of the substantial impediment to, or interference with, a substantial part of the premises because of the continued presence on the premises of those items.

19. The judge (HHJ Dight in the Central London County Court) held that vacant possession had not been delivered up, in that: (1) the tenant had given neither the keys nor the alarm codes to the premises; (2) although the items left by the tenant on the premises were for the main part easily portable chattels, their presence had the result that the premises clearly had not been abandoned. Moreover (3), in order to be able to use the rooms in which the items had been left, the landlord would have to do works to remove the partitions, the desks, the trunking, the cabling and the sockets.

20. As the judge said:

> "There was no positive step taken by the defendant to demonstrate to the outside world that it had given up vacant possession of the property, whether they intended to do so or not. Their subjective intention is not the key issue, it is the objective manifestation of it. Going back to the factual common ground there was no correspondence saying they were giving up possession, no hand-over meeting, no delivery of keys or codes, items were left on the premises, including items that they continue to own. It was really, in my judgment, more akin to an abandonment of the premises rather than a delivery up of them.
> Moreover, by leaving the photocopier and the files in the room, the tenant continued to store goods there and was therefore continuing to make use of the premises after expiry of the break notice.
> Lastly, the landlord could not, if it wanted, occupy the premises without difficulty or objection; there was a substantial impediment to use of a substantial part of it. At the very least the partitions would have to be removed, what appear to be the relatively substantial desks would have to be removed, the photocopier and the other chattels, the trunking and cabling."

21. Secondly, in Riverside Park Ltd v NHS Property Services Ltd [2017] L&TR 12, a lease granted in 2008 for a term of ten years gave the tenant a right to terminate the term on September 24, 2013 on giving at least six months' notice to the landlord, provided that the notice would only be effective if the tenant gave vacant possession of the premises on or before that date. The premises comprised the first floor of a building that, when let,

was laid out as an open-plan work-space. Under the terms of a licence for alterations granted on the same date as the lease, the tenant's predecessor had installed demountable partitions to create a unique configuration of small office spaces.

22. Notice was given under the break clause and the tenant vacated the building, leaving behind the partitions, kitchen units, floor coverings, window blinds, an intruder alarm and water stand pipes ("the Works"). The tenant had also failed to return certain key fobs giving access to the building and to deactivate the intruder alarm system. The landlord brought proceedings for a declaration that the lease had not been terminated, on the ground that, by the presence of the Works, the tenant had not given vacant possession as required under the break clause. The tenant contended that, by operation of law or on the proper construction of the lease, the Works were tenant's fixtures that the tenant was not obliged to remove unless, under the terms of the licence, the landlord required reinstatement; alternatively that the presence of the Works did not substantially prevent or interfere with the enjoyment of the right to possession so as to negate vacant possession.

23. The judge, HH Judge Saffman sitting as a Judge of the High Court, held that the Works were all easily removable, and constituted chattels rather than fixtures which the tenant would have been entitled to leave behind.

24. As to the first test, the landlord was able to deactivate both the intruder alarm and the missing key fobs and neither matter indicated an intention by the tenant to assert a right to use the premises; rather it no longer had the relevant fobs and had left the alarm on by oversight. As to the second test, the partitions were an impediment that substantially prevented or interfered with the right of possession and deprived the landlord of the physical enjoyment of the premises. The landlord therefore established that vacant possession had not been given and accordingly exercise of the break clause was ineffective.

25. The Riverside Park decision conceals an important point, which Lewison J explained in the Legal & General case as follows:

> "The first question arising under this head is vacant possession of what? In this case vacant possession of the premises. The premises will, in my view, exclude anything that is not demised. This means first in case of Unit 15 it will exclude the yard and in the case of all the units it will exclude the grass verges. Items left in these areas may amount to a trespass for which damages are recoverable, but they do not affect compliance with the condition itself.

> Secondly, in my judgment the premises will include anything which in law has become part of the premises by annexation. A fixture installed by the tenant for the purposes of his trade becomes part of the premises as soon as it is installed, although the tenant retains a right to sever the fixture on termination of the tenancy. Whether something is a fixture depends on the degree and purpose of annexation; in each case looked at objectively. If something has become part of the premises by annexation, then it is part of a thing of which vacant possession has to be given. Its presence does not amount to an impediment to vacant possession itself."

26. This reasoning explains why in the Riverside Park decision it was so critical for the landlord to be able to prove that the Works were not fixtures. Had they been, then the tenant would have succeeded in its contention that it had delivered up vacant possession of the premises – because the Works would have formed part of the premises, rather than possessions within them.

27. It is worth mentioning in this context another recent decision that turns upon the question whether items left in the premises by the tenant constituted tenant's fixtures, or formed part of the premises. In Dreams Ltd v Pavilion Property Trustees Ltd [2020] L & TR 22, a landlord and tenant entered into a deed allowing the tenant to surrender its lease on 25 April 2019. Clause 8 of the deed stated: "The surrender is with vacant possession". The tenant duly gave notice of its intention to surrender the lease. On the surrender date, it left in situ a mezzanine floor and lift. The landlord claimed that these were tenant's fixtures, and that their continued presence in the premises prevented the tenant from giving vacant possession, contrary to clause 8 of the deed.

28. The tenant issued proceedings seeking a declaration that the lease had been terminated. The court ordered a preliminary issue to be tried, namely whether, on the true construction of the deed, the tenant was obliged to give vacant possession before the landlord could be obliged to accept a surrender. It was assumed for the purpose of that issue that, by failing to remove the lift and mezzanine floor, the tenant had failed to provide vacant possession at the completion date. The tenant accepted that it was contractually obliged under cl.8 of the deed to give vacant possession, but submitted that this was not a condition precedent to the obligations of the landlord to complete the transaction. It submitted that a breach of clause 8 might have a range of effects, from the trivial to the serious, and for that reason, clear words would be required to make the obligation a condition precedent. The conditions to completion were instead expressly set out in clause 6 of the deed, which said nothing about vacant possession. The

tenant added that the court could give effect to a contractual obligation (not being a condition precedent) to give vacant possession by way of damages or by making any specific performance conditional on an order for compensation.

29. The landlord submitted that the obligation of the claimants to give vacant possession of the premises was a condition precedent to its obligation to complete the agreement to surrender. Relying on the general law, it contended that in sales of land the purchaser's duty to complete is conditional on the property being delivered with vacant possession where this has been promised in the contract. The parties deliberately adopted the usual form of a sale to convey an estate in land and did nothing to displace that general principle. The landlord did not say that failure to give vacant possession discharged it from its obligations under the deed, or that the tenant had repudiated the contract. It contended, rather, that it did not have to complete unless and until vacant possession was given.

30. Miles J resolved these competing arguments in favour of the landlord, holding that the obligation of the tenant to give vacant possession of the premises was indeed a condition precedent to the landlord's obligation to complete the agreement for surrender. The agreement was a contract for the conveyance of an estate in land, where customarily the purchaser's duty to complete is conditional on the property being delivered with vacant possession where this has been promised in the contract. The parties deliberately adopted the usual form of a sale to convey an estate in land and did nothing to displace that general principle. The landlord was therefore right to say that it did not have to complete unless and until vacant possession was given.

31. The preliminary issue having been determined in the landlord's favour, the remainder of the case, involving an investigation of the factual position whether the lift and mezzanine were tenant's fixtures which the tenant had to remove, and then a question of interpretation as to whether such a finding precludes and argument that the fixtures remained part of the premises, will presumably follow.

32. What these cases leave unresolved (although the question may arise in the Dreams case, should the litigation proceed that far) is what is the consequence where the tenant covenants to remove its fixtures, and does not. Can it be said in those circumstances that it has failed to deliver up vacant possession of the premises, because the fixtures which it has failed to remove constitute an impediment?

33. This question was considered but not resolved in the Goldman Sachs case. The tenant argued that a failure to remove its trade fixtures, did not mean that it was in breach of the obligation to give vacant possession. The tenant noted that this was contrary to the approach of the judge in the Riverside Park case, where he had said in paragraph 92 of his judgment that even if the Works constituted fixtures rather than chattels:

> "… I would have found that there was an obligation to remove them arising out of the fact that the licence to erect them had ceased to have effect and that their presence in the Premises on the date of purported termination of the Lease meant that vacant possession of the Premises was not given."

The tenant contended that this passage was obiter, and unreasoned.

34. Nugee J dealt with this argument in paragraph 42 of his judgment as follows:

> "I do not propose to decide this question. I accept the ordinary meaning of what it is to give vacant possession in terms of the trilogy of people, chattels, or interests. I accept that one cannot find in HHJ Saffman's judgment in Riverside any real discussion of the point as to whether the conclusion that the works in question were fixtures which the tenant had to remove meant that the tenant was in breach of an obligation to give vacant possession – indeed, for all one knows from the judgment, the point may not have been argued at all and may have been conceded – but I do not regard it as necessary for the purposes of this case to resolve the question."

35. This question therefore remains unresolved. Until it is determined one way or another, the prudent course for the tenant will be to leave time before the putative break date: (a) to reach an agreement with its landlord as to what should be removed; and failing that (b) to remove that which it is obliged to remove, paying proper attention to whether items are fixtures (which it *may* have to remove, depending upon the answer to this question) or chattels (which it *will* have to remove irrespective of the answer to this question); but (c) being careful not to remove too much – which is the final issue to which I now turn.

The problem with removing too much

36. The second ingredient, just discussed, resolves into a question whether the tenant has removed *enough* of its possessions from the premises of which it is required to give vacant possession. Sometimes, however, the question

arises whether the tenant has removed *too much* – so that it cannot in fact deliver vacant possession of "the premises" at all.

37. This question arose in Capitol Park Leeds Plc v Global Radio Services Ltd (2020) EWHC 2750 (Ch). In that case, a lease contained a tenant's option to terminate on 12 November 2017, subject (among other things) to the tenant giving vacant possession of "the Premises" on that date. "The Premises" were defined to include: "all fixtures and fittings at the Premises whenever fixed, except those which are generally regarded as tenant's or trade fixtures and fittings, and all additions and improvements made to the Premises".

38. The tenant gave due notice, and returned the keys to the landlord on 12 November 2017. Prior to that date, in a bid to comply with a reinstatement obligation, the tenant had stripped out various features of the Premises (such as ceiling tiles, ventilation equipment, lighting, radiators and floor boxes), including some which had been demised by the landlord, rather than being installed by the tenant. The landlord therefore argued that the tenant had not in fact delivered up vacant possession of the Premises, on the footing that parts of the Premises had been removed. The tenant argued by contrast that the Lease was a living, breathing document, and that the identity of "the Premises" was to be gauged by reference to its actual composition from time to time.

39. Judge Benjamin Nolan QC, siting as a Judge of the High Court, held in favour of the landlord in these terms:

> "65. Both Counsel accept that the authorities do not address the situation here where the Property may have been left empty but devoid of essential fixtures and fittings, whether part of the base build or "additions and improvements made to the Premises".
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> 66. In my judgment, these were generically the sort of outcomes against which the Claimant was guarding when it drafted or adopted the definition of "the Premises". Moreover, it made commercial common sense so to guard. By including the words "all fixtures and fittings at the Premises whenever fixed (except Tenant's fixtures)" and "all additions and improvements made to the Premises", the Claimant was ensuring that a Tenant exercising its Break Option could not do so by handing back an empty shell of a building which was dysfunctional and unoccupiable.
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> 67. … the Defendant gave back considerably less than "the Premises" as defined in the Lease. It did not give vacant possession. In my view, this is an exceptional case and therefore the second test identified in Cumberland and in Legal & General is satisfied, namely that the physical condition of

the Property was such that there is a substantial impediment to the Landlord's use of the Property, or a substantial part of it."

Conclusions

40. These many recent cases demonstrate that where the tenant seeks to operate a break clause which is subject (as most of them are) to a vacant possession condition, it will often leave it too late to secure an orderly removal of all its kit from the premises. Where kit is left behind, this will be relevant to the question whether vacant possession has been delivered, in one or both of two ways.

41. First, it may constitute evidence that the tenant is still using the premises for its own purposes (as in NYK and Legal & General), and is therefore manifesting a claim to be in possession – no matter how much or how little is there.

42. Secondly, even if the tenant is not "using" the kit as such (like the bags of hardened cement in Cumberland), if the quantity of it is sufficiently substantial, that may yet amount to a failure to deliver up vacant possession, for the obvious reason that the kit will prevent the landlord using the premises itself.

43. The position may be complicated where there is an obligation (rather than a mere entitlement) on the tenant to remove its fixtures and fittings. If the tenant fails to do so, it will face an argument, as yet undecided, that the continued presence of the fixtures amounts to a failure to yield up possession, in the same way as a failure to remove chattels would have done. On the other hand, if the tenant attempts to comply, but removes too much, then it will fact the converse argument that, although it has delivered possession, it has actually failed to deliver possession of whole of the premises.

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