

Rent review process helps to find middle ground

11 April 2010

The ongoing debate on the rent review process has generated a lot of heat without necessarily shedding much light on the subject.

For example, despite much hot air and many column inches being devoted to the topic, it would appear that quite a few of the contributors to the debate do not understand what an upward-only rent review clause actually is. So let's start there.

The first thing to understand is that the phrase "upward only" is something of a misnomer.

It means that the rent will not go down, but it does not mean that the rent will go up.

The majority of leases have a clause stating that if the new rent is lower than the rent passing prior to the review date, then rent will continue to be paid at the old rate. This is the "upward-only" clause.

Furthermore, despite the impression given by many, there was no statutory requirement that a lease contain such a clause. Each lease is a separate contract, freely negotiated between the parties that entered into it.

The Minister for Justice has introduced legislation prohibiting upward-only rent review clauses in leases signed after February 28, 2010.

This is a classic case of closing the stable door after the horse has bolted - the majority of leases signed in 2009 contained market review clauses where the rent could go up or down on review, and the legislation does not (nor can it) affect existing leases.

The minister has now convened a working group "to consider the operation of the current system for determining the rent payable on foot of a rent review clause, with particular emphasis on the arbitration process and the adequacy of information available to all parties and, if necessary, to make such recommendations for change as may seem appropriate".

The Society of Chartered Surveyors (SCS) welcomes the setting up of this group, having called for such action in a submission to the minister in April last year.

Contrary to the image that some parties have tried to portray, the SCS is neither a landlords' nor a tenants' organisation. Its members act for both groups, and also as arbitrators and independent experts.

The rent review process

The rent review process is usually triggered by a rent review notice that the landlord serves on the tenant. This notice may be required to specify a revised rent, or the landlord may do so subsequently.

The tenant is entitled to ask for the basis of this figure and request comparable evidence on which the figure is based.

Both parties or their representatives will then attempt to agree the revised rent. This will be based on market evidence generated from transactions on properties that can be compared to the property under review.

The following factors can impact on the level of rent:

*location

*market conditions at the review date

* property transactions that have taken place in the vicinity

* size and layout of the property

* length of lease and frequency of reviews

*unusual/onerous lease provisions or unduly severe service charge costs, etc.

If the revised rent cannot be agreed, the parties (usually the landlord, but sometimes the tenant) will seek the appointment of an independent expert or arbitrator to determine the rent.

There is much confusion about the roles of arbitrators and independent experts.

The role of the arbitrator, at its simplest, is to hear the evidence of both sides and make an award purely on the basis of the evidence.

The arbitration process is governed by statute (hitherto the Arbitration Acts 1954/1998). The Arbitration Act 2010 will apply to those arbitrations commenced after June 8, 2010.

The role of the independent expert differs from that of the arbitrator, in that the independent expert can make his or her own enquiries and consider matters not adduced in evidence when arriving at a decision. The independent expert can use their own knowledge in arriving at a decision.

Rent reviews tend to be regarded as adversarial - landlord and tenant are immediately polarised.

But the idea behind a review is that neither side should be disadvantaged. The landlord should be rewarded by receiving a rent that he might otherwise receive in the market had his property been vacant, while the tenant should not have to pay any more than one of his peers might have paid for the right to occupy that space at the review date.

The advantage for both sides is that the rent is fixed for a further five years, so that each knows their cash position for that period.

In the past, landlords have complained that when they had to review at a particular time in an economic cycle, they might have got a nil or very small increase, whereas two or three years later, the increase could have been more substantial.

Equally, from a tenant's perspective they may have a review at the height of a cycle and be saddled with a rent which is higher than it might be during the years following a downturn. Such is the situation at present, and the problems it is causing are very real in many cases.

Landlords will need to be very pragmatic in dealing with cases where tenants are genuinely unable to pay their rent.

A vacant building is of no use to any landlord. However, tenants looking for help from their landlord need to remember that the landlord may have little room for manoeuvre with, for example, the bank that holds the mortgage breathing down their neck.

It must be remembered that it is market evidence that determines the rent payable on a review.

The usual basis of the reviewed rent is what that property would command in the open market as between a "willing landlord" and a "willing tenant".

The best evidence that will be considered by an arbitrator or expert is the open market letting of similar

properties in an equivalent location. Other evidence to be considered, but carrying less weight, will be rent review evidence.

Evidence of other arbitrations or expert's awards will carry much less weight - it is the rents paid by their peers and the evidence presented that determines the rent payable on a review.

Can the process be improved?

By and large, the rent review process as currently constituted works, although there is always room for improvement.

One of the main difficulties in the review process, and one that has been highlighted in recent commentaries, is the difficulty caused by the existence of confidentiality clauses.

A letting may take place with a "headline" rent at a certain level, and this may be put forward as primary evidence.

However, there are options available to a tenant, including the right to discovery, if the landlord is the same for the property under review.

The SCS has called for the setting up of a national database, where basic information on all property transactions would be recorded. This would ensure more transparency in the whole rent review process.

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