OUTER HOUSE, COURT OF SESSION

2020 CSOH 86

CA102/19

OPINION OF LORD ERICHT

In the cause

3639 LIMITED

Pursuer

against

RENFREWSHIRE COUNCIL

Defender

Pursuer: Lindsay QC; Addleshaw Goddard LLP
Defender: Dean of Faculty, Paterson; Ledingham Chalmers LLP

23 September 2020

Introduction

[1] The pursuer was the head landlord and the defender was the head tenant of a shopping centre. The head lease provided that the rent payable by the tenant to the landlord was the higher of £7210 or 16% of the Rack Rental Income. One of the sub-tenants renounced its sublease to the pursuer, paying a surrender premium in order to do so. An element of the surrender premium related to future rent. Other elements of the premium related to service charges, rates dilapidations and insurance premia. The defender claimed that it was entitled to 16% of the rent element of the premium. This was disputed by the

pursuer on the basis that the rent element of the premium was not rent and did not fall within the definition of Rack Rental Income.

The contractual position under the head lease dated 8 November 1972 and 18 January 1973 (the "Original Lease")

[2] The defender, a local authority, entered into a lease, as landlord, with Score Property Developments Limited, as tenant, of land in Johnstone. In terms of condition ONE of the lease, the tenant was obliged to erect on the ground within four years from the date of entry buildings comprising a supermarket and shops and/or offices. The tenant was obliged to repair, maintain and insure the buildings. Condition EIGHT was in the following terms:

> "In the event of the rack rental income exigible from the whole subjects (subject to deduction, if applicable as aforementioned) exceeding at any time or times during the period from Whitsunday Nineteen hundred and seventy four to the date of completion of all the first lettings the sum of Thirty thousand eight hundred and fifty pounds (£30,850) per annum, then the ground rental of Seven thousand pounds per annum otherwise payable for that period shall be increased by one-half (50%) of such excess with effect as and from the second half-yearly term date succeeding the date of such excess. In the event of the gross floor area of the buildings to be contained within the whole subjects exceeding by one-tenth (10%) or more the estimated floor area of Thirty two thousand square feet or thereby, then the Tenants shall, prior to appointment in accordance with the immediately preceding provision of any additional rental attributable to any such increase in floor area, deduct from such additional rent such sum as shall be equivalent to Nineteen Two-hundredths (9.5%) of the cost of developing such additional floor area including fees and interest thereon, all as the same may be certified by the Parties' Surveyors. On completion of all the first lettings, the annual ground rent then payable, calculated in accordance with the immediately foregoing provisions, shall be expressed as a fixed proportion of the total rack rental income then exigible from the whole subjects and thereafter with the effect as and from the second half-yearly term date succeeding the date of final completion of the first lettings the annual ground rent payable in hereof shall (subject to the foregoing provisions relative to a minimum therefor) be calculated at the second half-yearly term date aforesaid and at each and every half-yearly term of payment subsequent thereto throughout the duration of this Lease by reference to this proportion (which is to remain constant throughout the duration of this Lease) of the total rack rental income exigible from the whole subjects at the half-yearly term immediately preceding the relative term of payment and in regard to rent income and increases referred to it is understood and agreed that the Tenants shall provide

the Landlords with certified statements of the rack rental income at the terms of Whitsunday and Martinmas in each year."

[3] Condition THREE was in the following terms:

"The Tenants bind themselves to insure and keep insured the whole buildings and others contained within the whole subjects in the joint names of the parties with an Insurance Company to be selected by the Tenants and approved by the Landlords (which approval will not be unreasonably withheld) against loss or damage by fire, aircraft, explosion, and impact for such sum as shall represent the full reinstatement value of the buildings from time to time with the addition of a sum equal to Two years' rack rent of the whole subjects. In the event of any damage or destruction by way of the insured risks so as to render the whole subjects or any part thereof unfit for occupation and use, the tenancy shall not be terminated but the ground rent or a fair proportion thereof as may be agreed between the Landlords and the Tenants having regard to the nature and extent of the damage or, failing agreement, as may be determined by the arbiter hereinafter mentioned, shall be suspended until the whole subjects shall again be rendered fit for occupation and use. Further the Landlords bind themselves to concur in the application of all such sums as may arise from claims under such insurance in or towards the repair or reinstatement of the whole subjects."

[4] Condition SIX was in the following terms:

"If at any time during the currency of this Lease the Tenants (which expression shall not in the context of this particular condition be deemed to include sub-tenants total or partial) shall (after receipt of written notice to their Registered Office) allow a half-year's rent to be in arrear for three months or shall (after receipt of written notice as aforesaid) in any other respect fail to comply with or shall contravene any of the conditions, provisions or restrictions hereinbefore contained or referred to or shall go into liquidation (otherwise than for the purpose of reconstruction or amalgamation) or in the event of this Lease having been assigned to an individual or to a partnership if he or they shall become notour bankrupt, then and in any of these events the Landlords at their option by notice in writing may bring this Lease to an end reserving nevertheless the Landlord's claim to all rents due or accrued and in respect of any breach of the conditions of this Lease."

[5] The Original Lease was varied by a Deed of Agreement, Variation and Assignation among the defender, Score Property Developments Limited and Norwich Union Insurance Group (Pensions Management) Limited dated 8 November 1972 and 18 January 1973 and 4 January 1974 ("the Deed of Variation"). In terms of the Deed of Variation, the interest of Score Property Developments Limited as tenant was assigned to Norwich Union Insurance

Group (Pensions Management) Limited. The Original Lease as varied by the Deed of Variation is hereafter referred to as "the Head Lease".

[6] The Deed of Variation made various amendments to the Original Lease. In particular the original condition EIGHT was renumbered as condition NINE and amended so that it read as follows:

> "In the event of the rack rental income as hereinafter defined exigible from the whole subjects (subject to deduction, if applicable as aforementioned) exceeding at any time or times during the period from Whitsunday between hundred and seventy four to the date of completion of all the first lettings the sum of Thirty thousand eight hundred and fifty pounds (£30,850) per annum, for that period shall be increased by one-half (50%) of such excess with effect as and from the second half-yearly term date succeeding the date of such excess. In the event of the gross floor area of the buildings to be contained within the whole subjects exceeding by one-tenth (10%) or more the estimated floor area of Thirty two thousand square feet or thereby, then the Tenants shall, prior to appointment in accordance with the immediately preceding provision of any additional rental attributable to any such increase in floor area, deduct from such additional rent such sum as shall be equivalent to Nineteen Two-hundredths (9.5%) of the cost of developing such additional floor area including fees and interest thereon, all as the same may be certified by the Parties' Surveyors. On completion of all the first lettings, the annual ground rent then payable, calculated in accordance with the immediately foregoing provisions, shall be expressed as a fixed proportion of the total rack rental income then exigible from the whole subjects and thereafter with the effect as and from the second half-yearly term date aforesaid and at each and every half-yearly term of payment subsequent thereto throughout the duration of this Lease by reference to this proportion (which is to remain constant throughout the duration of this Lease) of the total rack rental income exigible from the whole subjects at the half-yearly term immediately preceding the relative term of payment and in regard to rent income and increases referred to it is understood and agreed that the Tenants shall provide the Landlords with certified statements of the rack rental income at the terms of Whitsunday and Martinmas in each year. In this Condition the "rack rental income" means the rents (excluding all income from service charges and for replacement and renewal of apparatus, machinery and equipment by way of depreciation) which the Tenants (meaning here the said Score Property Developments Limited or their successors in the right of occupancy under this Lease or their sub-tenant of the whole subjects) are entitled to receive from their several sub-tenants"

[7] Around the beginning of February 2019, the various interests under the lease structure were held as follows. The landlord under the Head Lease was the defender. The tenant under the Head Lease was Alwyd Limited. There were various subleases to various

shops. In particular the supermarket unit was sublet as a Co-op supermarket (the "Co-op Sublease"). The sub-tenant's title under the Co-op Sublease was held by a Co-op entity, namely a property partnership called Rochpion Properties (4) llp. The Co-op Sublease was for a term of 63 years expiring in July 2037 at an annual rental of £268,000. The supermarket unit had in turn been sub-subleased by Rochpion Properties (4) llp to a charity, RAMH by a sublease dated 20 July 2016 and 16 August 2016 (the "Charity Sub-sub-lease"). The rent under the Charity Sub-sub-lease was £1 per annum.

[8] In February 2019, the pursuer acquired Alwyd's interest as tenant under the Head Lease at a price of £3,760,000. The date of entry was 13 February 2019. The acquisition was effected by an assignation between Alwyd Limited and the pursuer dated 7 February 2019.

[9] The Co-op then renounced its sublease of the supermarket unit with effect from 13 February 2019. The renunciation was given effect by a Deed of Renunciation ("the Renunciation") by Rochpion Properties (4) llp in favour of the pursuer dated 11 February 2019 and 19 February 2019.

[10] The consideration for the Renunciation was a payment by Rochpion Properties (4) llp to the pursuer of a premium of £4,250,000. The pursuer's position was that an unquantified element of the premium related to the sub-tenants renunciation of its obligations to pay future rent, and that the other unquantified elements within the Premium related to the sub-tenant's renunciation of its obligations relating to service charges, rates liability, dilapidations and insurance premia.

[11] The practical effect of the Renunciation (leaving aside for the moment the premium which is the subject of this dispute) was that instead of receiving 16% of an annual rent from the Co-op of £268,000 for the remaining 18 years of the Co-op Sub-lease, the defender would receive 16% of an annual rent from the charity of £1.

[12] On 28 March 2019 the pursuer sought the defender's consent to an assignation of the tenant's interest in the Head Lease. The proposed assignee was Strathcarron Estates (Johnstone) Limited ("Strathcarron"). The defender did not consent, on the grounds firstly that payment was due to the defender as the rental element of the premium fell within "rack rental income", and secondly in relation to the covenant of Strathcarron.

Procedural history

[13] The pursuer raised a commercial action seeking declarator that the defender had unreasonably withheld its consent to the proposed assignation in favour of Strathcarron, and an order ordaining the defender to consent.

[14] The defender counterclaimed seeking declarator that in terms of the Head Lease:

> "(i) the part of the premium paid to the pursuer by the Co-op in lieu of rent forgone (the 'rental premium') is Rack Rental Income in terms of the Head Lease; and (ii) the pursuer's certification of the Rack Rental Income at 15 May 2019 should include the rental premium."

The defender also sought decree ordaining the pursuer to certify to the defender the amount of the Rack Rental Income at 15 May 2019.

[15] The pursuer subsequently abandoned the principal action, due to uncertainty as to whether the assignation to Strathcarron would proceed in the light of the disruption to the retail market caused by Covid-19. The case proceeded in respect of the counterclaim only, and called before me for debate. The debate was conducted remotely by Webex in view of Covid-19 restrictions.

Submissions for the pursuer

[16] Senior counsel for the pursuer invited me to sustain the pursuer's second plea-in-law in the answers to the counterclaim and grant decree of absolvitor, failing which sustain its first plea-in-law and dismiss the counterclaim.

[17] Counsel submitted that the correct interpretation of the Head Lease was that no part of the premium paid by the Co-op to the pursuer should be included in the calculation of Rack Rental Income regardless of whether or not any element of the Premium was attributable to future rent. The Premium was not "rents" for the purposes of condition NINE of the Head Lease as varied, and therefore was not to be taken into account when quantifying the Rack Rental Income.

[18] There was no dispute between the parties as to the law on contractual interpretation, and in that regard counsel referred me in particular to *Ardmair Bay Holdings Limited* v *Craig* [2020] SLT 549 at paras [47] to [49], *Rainy Sky SA* v *Kookmin Bank Co Limited* [2011] 1 WLR 2900 at paras [19] and [23] and *Arnold* v *Britton* [2015] AC 1627 at paras [20] and [77].

[19] Senior counsel referred to the following factors.

(a) rents

[20] Counsel submitted that the parties chose to use the word "rents" rather than general words such as payments or monies. The Oxford English Dictionary, and the common law definition of rent (Bells Dictionary page 910), specify that rent is for the use of land. Payments made in respect of non-occupation of leased premises are not for the use of the premises and are not rent (*Standard Life Assurance Company* v *Greycoat Devonshire Square Limited* [2001] L&TR 290 at paras [11], [12] and [16]). No part of the capital premium could

be classified as "rent" because the Premium was paid as consideration for non-occupation of the supermarket.

(b) exclusions

[21] The definition of "rack rental income" excludes "income from service charges and for replacement and removal of apparatus, machinery and equipment by way of depreciation". Counsel submitted that these exclusions confirmed that a legalistic and narrow meaning should be given to 'rents' as they make clear that other periodic payments received from the sub-tenants in respect of services charges and dilapidations are not to be included in its definition of rents.

(c) entitled to receive

[22] Counsel drew attention to the words in the definition of Rack Rental Income "are entitled to receive from their several Sub-Tenants". He submitted that the use of the word "entitled" connoted a legal obligation to make payment rather than an *ex gratia* payment or one which involved the agreement of the sub-tenant.

[23] Counsel submitted that the pursuer was not "entitled" to receive the Premium from the sub-tenant in terms of the sublease. It was only with agreement of the sub-tenant that the Premium became payable and entitlement to demand payment was not the same as a sum which only becomes payable once parties have reached agreement after carrying out negotiations. In order to be classified as rent, the obligation to make payment must be in the lease in question, and not any collateral agreement (*Mann* v *Houston* [1957] SLT 89). The use of the word "entitled" under reference to "sub-tenants" supported the interpretation that

"Rack Rental Income" extended only to rent that the pursuer has a legal right to receive from the sub-tenants under the subleases, and did not extend to collateral agreements.

(d) use of "rent(s)" in other clauses of Head Lease

[24] Counsel submitted that the meaning given to "rent" in conditions THREE and SIX of the Head Lease and condition EIGHT of the original Head Lease supported the pursuer's interpretation of condition NINE.

(e) fundamental purpose of Head Lease

[25] Counsel submitted that the fundamental purpose of the Head Lease was that it was a 125 year ground lease which permitted the construction by the Tenant of a supermarket, shops and offices upon the ground let. Thereafter, the subletting and management of the supermarket, shops and offices was a matter exclusively for the tenant. The landlord played no role in the management and subletting of these premises. The landlord received an agreed "ground rent" or an agreed percentage of the Rack Rental Income if that was more than the agreed ground rent. Other than the agreed percentage, there were no other profit or loss sharing mechanisms in the Head Lease. As there was no mechanism for sharing the profits and losses associated with the subletting, nor any joint management of the premises, the Head Lease could not be viewed as being akin to a joint venture or a partnership. The court would not readily interpret a clause as entitling the landlord to participate in compensation awarded to the tenant for loss to his own interest (*Lewison's Drafting Business Leases*, Bignell, 8th Edition paragraph 6.20). The defender's proposed interpretation was inconsistent with the fundamental purpose by seeking to impose a general sharing of the

monies received by the sub-tenant rather than a more limited entitlement to a percentage of the Rack Rental Income.

(f) commercial common sense

[26] Counsel submitted that the defender's interpretation was not consistent with commercial common sense. Any reverse premium paid by the pursuer to persuade a new sub-tenant to enter in a sublease of the supermarket would be paid by the pursuer alone with no contribution from the defender. Any refitting of the supermarket would be at the pursuer's expense with no contribution being made by the defender. There would be unfairness if the defender received 16% of the Premium, made no contribution to the reverse Premium and fitting-out costs and received 16% of the rent. That could not have been the intention of the parties.

[27] In contrast, the pursuer's interpretation accorded with commercial common sense. The surrender of a sublease was part of the everyday management of the premises which is a matter exclusively for the tenant: all income and expenditure incurred in every day estate management is with the tenant alone. The landlord should not enjoy a share of income from estate management while avoiding any liability for its costs.

[28] Counsel further submitted that the commercial rationale for limiting the definition of rent to periodic payments was that these were clear and readily ascertainable, unlike capital sums payable as a premium. A premium may be composed of a number of distinct elements blended together and it may become impossible to identify what element of the capital sum was attributable to rent as opposed to service charges, dilapidations or compensation thus making quantification of the Rack Rental Income almost impossible. The pursuer's interpretation would result in the benefits to the landlord and tenant as may

reasonably be expected, avoiding an excessive or disproportionate burden on one party and resulting in commercial predictability (*Grove Investments Limited* v *Cape Building Products Limited* [2014] HOUS LR35 at para [11]).

[29] Counsel noted that the surrender of the sublease by the Co-op was a legitimate part of the management of the premises and there was no suggestion that it was an artificial transaction designed to improperly maximise the monies received by the tenant at the expense of the landlord. Accordingly, the circumstances were different from those in *Freehold and Leasehold Shop Properties Limited* v *Friends Provident Life Office* [1984] 271 EG 457.

[30] Counsel submitted that the language used in condition NINE was clear and unambiguous. The mere fact that a contractual arrangement has worked out badly for one of the parties is not a reason for departing from the natural language (*Arnold* v *Britton* at para [19]).

Submissions for the defender

[31] Senior counsel for the defender invited me to grant declarator in terms of the first conclusion of the counterclaim and fix a proof before answer to determine the remaining conclusions.

[32] There was no dispute between parties as to the principles of legal interpretation. Counsel however emphasised the passages in *Arnold* v *Britton* at para [15], *Wood* v *Capita Insurance Services* [2017] A.C. 1173 at paras [10] and [12] to [14] and counsel submitted that even on the pursuer's narrow textual analysis, the pursuer's contention was wrong. The definition referred to "and the rents which [the pursuer is] entitled to receive" from its sub-tenant. The pursuer was entitled to receive the rental premium. The definition did not constrain "rents" to those payable in terms of a sublease. The pursuer was entitled to

receive the rent under the Co-op sublease and equally entitled to receive the premium in discharge thereof. In agreeing the Renunciation, the pursuer became entitled to receive the rental premium in lieu of the rent they would have received had the sublease continued. *Mann* v *Houston* was distinguishable. If payments in lieu of rent were to be excluded, clear wording to that effect could have been included *(Global Port Services (Scotland) Limited* v *Global Energy (Holding Limited)* [2015] CSIH 42 at para [27]. The exclusions and the definition were not confined to periodic payments and included, for example, the tenant's repairing obligation. The objective meaning of the words used in the definition included both payments of rent and payments in lieu of rent such as the rental premium.

[33] Counsel further submitted that the Head Lease was a development lease. The parties were an economic partnership. Both the landlord and tenant were to participate in the investment, hence the rent (upon completion of the development and the first lettings) being calculated as a percentage of the Rack Rental Income (*Lewison's Drafting Business Leases,* paragraphs 6.19 to 6.21; *Freehold and Leasehold Shop Properties Limited* v *Friends Provident Life Office* at page 451). In that context a reasonable person would have understood the definition to include a payment in lieu of rent.

[34] Counsel further submitted that an analogy might be drawn with the prohibition on alienation of lands held under entail. The prohibition on alienation was applied to a grassum as it deprived the successor of rent to which he would otherwise be entitled (Bell's Dictionary, definition of "grassum" page 492, Green's Encyclopedia (1999) VII 502).

[35] Counsel further submitted that the common objective was to share in the spoils of the development (*Grove Investments Limited* v *Cape Building Products Limited* at paragraph 11). This was also emphasised by condition TEN which permitted the pursuer, at its sole discretion, to sublet individual units without obtaining consent from the defender.

[36] Counsel submitted that it made commercial common sense for the pursuer and defender to share in the rental income or any payment to be made in lieu thereof. The pursuer's construction made no commercial sense. It allowed the tenant to defeat the landlord's entitlement to a share in the rental income (via a premium or grassum). On the pursuer's argument, it would be open to the pursuer to enter into new subleases with a substantial grassum and a low rent.

[37] Counsel responded to the factors identified by the counsel for the pursuer as follows.

(a) rents

[38] The premium was not a payment for non-occupation, but a payment to be freed from the obligation to pay rent. In any event, the pursuer had accepted that part of the premium was referable to future rent. *Standard Life Assurance Company* v *Greycoat Devonshire Square Limited* was in the defender's favour.

(b) exclusions

[39] Counsel submitted that the exclusions were not of assistance as exclusions did not relate to income.

(c) entitled to receive

[40] Counsel submitted that the wording was "entitled to receive from their several sub-tenants" not entitled to be received under the sublease. The fact that the entitlement was in a separate deed did not divorce the payment from the necessary connection with the rent. The payment was made to escape obligations under the sublease including the obligation to pay rent for the balance of the term. The discharge of the rent was a payment of rent.

(d) use of "rent(s)" in other clauses of Head Lease

[41] Counsel submitted that the reference to rents in other clauses was not of assistance. Condition THREE related to insurance and SIX to urgency. Condition EIGHT in the Original Head Lease had been renumbered as condition NINE so was not another clause.

(e) fundamental purpose of Head Lease

[42] Counsel submitted that the structure was not a joint venture or partnership in the strict legal sense but was a symbiotic relationship where the head landlord controlled the land, the head tenant contributed the building and developed then ran the business. Both the head landlord and the head tenant benefits from the rent. The head tenant gets a lion's share; it has the greater work to do and the greater risk to bear. It was an economic but not legal partnership (*Lewison's Drafting Business Leases* at paragraph 6.19). The danger of the head tenant cheating the head landlord should be dealt with by interpreting the contract to allow the premium to be construed as rent (*Freehold and Leasehold Shop Properties Limited*).

(f) commercial common sense

[43] Counsel submitted the wording of the lease was clear and there was no ambiguity and therefore it was not necessary to resort to common sense (*Global Port Services (Scotland) Limited*). In any event, on the pursuer's interpretation the commercial intent of the parties that rent would be shared would be defeated: by taking a premium and then a peppercorn rent the tenant could defeat the entire purpose of the Head Lease. On the defender's interpretation there was no unfairness arising out of the landlord not being required to pay the costs of an inducement or refit because that is what the parties had bargained for. On

the defender's interpretation, if a sublease was surrendered for a premium and then re-let at a substantial rent, both parties would benefit as the pursuer would get 84% of the premium and of the new rent.

Decision and discussion

[44] The effect of the Renunciation is that the sub-tenant's obligation under the Co-op Sublease to pay rent to the pursuer for the remaining 18 years of the lease has been replaced with an obligation on the sub-tenant to pay a lump sum to the pursuer in respect of the termination of the lease. The pursuer accepts that an unquantified element of the lump sum related to the sub-tenant's renunciation of its obligations to pay future rent.

[45] It has long been recognised that the payment by a tenant of a lump sum instead of periodical payments can be open to abuse.

[46] For example, under the law of entail there was a prohibition on taking a premium (or to use the traditional Scots law term, a grassum) rather than rent in a lease of entailed land. As Bell's Dictionary puts it:

> "GRASSUM; an anticipation of rent in a gross or lump sum, or a fine paid in consideration of a lease for a term of years. In questions with singular successors there is no limitation of the power to take grassums, only the rent must not be thereby diminished so as to be altogether elusory. In regard, however, to lands under entail, the heir in possession must administer the estate *secundum bonum et aequum* taking no more of the annually accruing rents and profits than he leaves to descend to his successors. Hence grassums, as being, in effect, anticipations of the future rents, to the prejudice of succeeding heirs, are held to be struck at by the prohibition against alienation."

[47] Another example can be found in relation to statutory protections of residential tenants. In *Samrose Properties Ltd* v *Gibbard* [1958] 1 WLR 235 a landlord was not prepared to let a residential property under a lease which was subject to the Rent Acts. The Rent Acts did not apply if the rent was less than two thirds of the rateable value. So the landlord let

the property for a premium of £35 and quarterly rent of £1, that rent being under two thirds of the rateable value. The court held that the sum of £35 paid by the tenant was commuted rent and that the reality of the matter was that the landlord had let the premises to the tenant for an annual rent of £39 and, accordingly, that the tenant was entitled to the protection of the Rent Acts.

[48] Another potential abuse was identified by the English Court of Appeal in *Freehold and Leasehold Shop Properties Limited* v *Friends Provident Life Office* [1984] 271 EG 451. That case concerned a development lease under which the head landlord was entitled to a percentage of the rack rental achieved by the head tenant from the sub-tenants. The issue before the court was interpretation of a rent review clause, the details of which need not concern us here. There was no provision in the head lease preventing the head tenant from subletting for a premium and a nominal rent, and there was brief discussion of this in the context of the commercial effects of the possible interpretations of the clause. Oliver LJ noted that one particular interpretation:

> "produces, or is capable of producing, very unsatisfactory results from the landlord's point of view if the tenant chooses to adopt a letting policy of granting terms at low rents in consideration of premiums."(p135B-C).

Griffiths LJ, stated:

> "it is easy to ascertain the intention of the parties at the time [the relevant clause] was drafted, bearing in mind the genesis of this lease. This lease clearly arose out of a joint venture between the landlord, who was supplying the land, and the developer, who was providing the money to put up a large office block. They agreed on the rent for the first part of the lease, and thereafter the agreement was that they would share the cake between them. The landlord was to have 17% of the rent that was coming in from the building and the tenants were to have the remainder, the larger slice of the cake. It seems to me that this clause is effective to give effect to an understandable commercial intention at the time that they entered into this joint venture. I am sure that, at that time, it never crossed their minds that the tenant might seek to cheat the landlord by charging peppercorn rents and taking premiums; and I, like my lord, believe that if he did resort to that sort of a tactic it might well be possible to construe this lease to defeat his intention." (p135 H-J)

[49] Another example is where a future income stream is stripped out as capital. In *Standard Life Assurance Company* v *Greycoat Devonshire Square Ltd* [2001] L & TR 290, a tenant accepted a premium from a subtenant for surrender of a sub-lease. The head landlord was entitled to a percentage of the "Gross Rents Payable." The issue before the court was whether the dilapidations element of the surrender premium fell within the definition of "Gross Rents Payable" and, perhaps not unsurprisingly, it was held that it did not. However Donaldson J was clear that "Gross Rents Payable" did include the rental element of the surrender premium:

> "15. Finally, a restriction to payments for occupation would permit the tenant to act directly contrary to the obvious commercial purpose of the contract. The landlord shares in the fortune, positive and negative, of the tenant as regards the rental income achievable by the latter from sub-leases, since the landlord is entitled to a margin of 24.0695 per cent thereof; if the sub-rental income declines, so does the additional rental payable to the landlord under the lease. Where the rent payable under a sub-lease is in excess of current market rates, the tenant may accept a premium for the surrender of the sub-lease - such a premium will, at least in part, reflect the fact that any new sub-lease to a third party would *ex hypothesi* be at a lower rent. A future income stream can thus be stripped out as capital. That would be at the expense of the landlord under the head lease, unless the premium received by the tenant for the surrender is itself covered by the words "Gross Rents Payable".
>
> 16. It was therefore not surprising that before me [counsel for the tenant] conceded, and in my judgment rightly conceded, that any construction of the words "Gross Rents Payable" which failed to include such a premium would be aberrant.....
>
> 20… Payments for occupation, fees or other payments payable for consent to additional user or a premium for the surrender of a sublease all to my mind fall on one side of the line, and are included in "Gross Rents Payable". (p295-7)

[50] It is not uncommon for commercial reasons for a tenant, or indeed a landlord, to wish to bring a lease to an end. The terms of any such renunciation will reflect commercial factors such as whether a tenant wishes to stop trading out of the premises, whether a landlord wishes to re-let to a different tenant, and the prevailing market conditions for the

retail sector at the particular time. In this case, the Co-op had decided that it no longer wished to trade out of the supermarket unit. Indeed by the time of the renunciation it had already ceased trading from the supermarket and sub-let the supermarket to a charity.

[51] In this case, the rent due by the pursuer to the defender in terms of the Head Lease, following variation, was:

> "Seven Thousand Two Hundred and Ten Pounds per annum or 16% of the rack rental income (as therein defined), whichever shall be the higher"

[52] The Rack Rental Income was defined in condition NINE as:

> "The rents (excluding all income from service charges and for replacement and removal of apparatus, machinery and equipment by way of depreciation) which the Tenants (meaning here the said Score Property Developments Limited or their successors in the right of occupancy under this Lease or their Sub-Tenant of the whole subjects) are entitled to receive from their several Sub-Tenants."

[53] The issue in this case is whether the rental element of the surrender premium falls within that definition of "Rack Rental Income".

[54] The pursuer's position is that the rental element of the premium does not constitute "rents". Rent is a payment for occupation: the premium was a payment for non-occupation. The effect of the pursuer's interpretation of the Head Lease is that the pursuer is entitled to 100% of the rental element of the premium.

[55] The pursuer founds on dictionary definitions of rent. The Oxford English Dictionary definition of "rent" is:

> "a tenant's regular payment to a landlord for the use of property or land".

Bells' *Dictionary & Digest* defines "rent" on page 910 in the following terms:

> "RENT; the consideration given to the landlord by a tenant for the use of the lands or subjects which he possesses under lease ..."

The pursuer also founds on a passing comment in *Standard Life Assurance Co* v *Greycoat Devonshire Square Limited* that "While there is no doubt that "rent" connotes a payment for

occupation," (p294). However any force which such a passing comment by Donaldson J might have is negated by his later statement at p297 that a premium for the surrender of a sublease was included in Gross Rents Payable (see para [48] above).

[56] The logic of the pursuer's argument is that the rent is payment for future occupation, the rental element of the lump sum is not a payment for future occupation, therefore the rental element is not rent and does not form part of the Rack Rental Income.

[57] While that argument does have some attraction in its logical simplicity, what it fails to take into account is the contractual structure as a whole.

[58] The contractual structure here is that of a development lease. The landowner and a developer enter into contractual arrangements to share in the proceeds of the development of an area of land. The landowner provides the land. The developer develops the land into a shopping centre. Having done so, the developer transfers his interest to an institutional investor. The institutional investor manages the shopping centre and sublets the shop units. The landowner's share of the proceeds of development is a basic rent at a low level plus, more significantly, a percentage of the rental income achieved by the institutional investor in its management of the shopping centre. The landlord shares in the risk and reward of the development. His return is not through a substantial fixed rent from the institutional investor which is payable regardless of the success or failure of the institutional investor in subletting the shop-units. Instead the landlord shares in the highs and lows of whatever rental income is achieved from the sub-lets.

[59] In these circumstances, the common intention of the parties to the Head Lease is that the defender as landlord shares in the proceeds of the development of the shopping centre by receiving a percentage of the proceeds. The definition of "rack rental income" must be read in the light of that common intention. The pursuer's construction would defeat that

intention. It would permit the pursuer to keep all of the premium, notwithstanding that part of that premium represents future proceeds in which the defender would otherwise be entitled to participate. It would permit the pursuer to strip out a future income stream as capital. It cannot have been in the contemplation of the parties to the Head Lease that their common intention to share in the proceeds could be easily frustrated by the taking of the proceeds in a lump sum rather than periodical payments. In my opinion the reference to "rents" in the definition of "rack rental income" includes the element of the surrender premium which is attributable to rents which would have been payable had the renunciation not taken place.

[60] There is nothing in the detailed textual analysis of the Head Lease undertaken by the pursuer which demonstrates that the intention of the parties was other than set out above. It is not surprising that payments for service charges, dilapidations etc are excluded from rents: these are not part of the proceeds of the development to be shared between the landowner and the developer. The references to rents in Condition THREE and SIX refer to specific circumstances of insurance and default and are not incompatible with the rental element of a reverse premium being included in the definition of "Rack Rental Income". Condition 8 of the Original Lease is of no additional assistance in interpreting Condition 9 of the Head Lease as they are substantially the same condition, 8 having been renumbered as 9 in the Head Lease. The definition of "rack rental income" refers to rents which the head tenant is entitled to receive from sub-tenants, and does not limit such receipts to receipts under a sub-lease. The premium is not a voluntary or *ex gratia* payment: the Co-op would not have been relieved from the obligation to pay rent had it not entered into a legal obligation to pay a rental element of a lump sum instead of continuing to make periodic rent payments. *Mann* v *Houston* does not support the proposition which the pursuer seeks to

draw from it that rent must be in a lease and not in any collateral agreement. The reason the court in *Mann* v *Houston* held that the missives did not constitute a lease was not because a premium was in a separate document but because the missives specifically stated that no rent was payable.

[61] It makes no difference that the figure of the surrender premium was arrived at by the parties to the Renunciation Agreement on a broad brush basis without being quantified in detail. It is perfectly understandable that such an approach was taken in the commercial negotiation of the Renunciation Agreement. However, the fact that parties happen to have adopted a broad brush approach does not mean that the rental element of the premium cannot be quantified. This case will now proceed to proof on the quantification of the rental element and both the pursuer and defender have instructed expert evidence on that quantification.

Order

[62] I sustain the defender's second plea-in-law in the counterclaim and repel the pursuer's second plea-in-law in the answers to the counterclaim and grant declarator as sought in the first conclusion of the counterclaim. I shall put the case out by order for discussion of further procedure. I reserve all questions of expenses in the meantime.