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DILAPIDATIONS – ARE YOU PAYING TOO MUCH?

If you settle based on Cost of Works alone, then possibly.

The statutory (Diminished Value) cap – Section 18 in England & Wales, Section 65 in Ireland – exists for good reason. Quite simply, "cost" and "value" are not one and the same thing.

More often than not, the law of diminishing returns applies to "mending" second-hand properties. One reaches a point in objectively targeted expenditure beyond which one can keep on spending, but no more will be added to – or recovered in – value.

Dilapidations are of course negotiated by **building** surveyors, as their discipline is identifying breaches (of covenants to: Repair, Decorate and Reinstate) and negotiating the remedial pricing thereof. The best will get it to the lowest possible figure. Similarly, they will suggest obtaining a Diminution Valuation where they consider it might assist achieving lower still.

But the judgement as to whether or not the cap applies – whether the freehold reversionary **value** has been diminished by the same or a lower amount than the cost of the remedial works – is possibly best made by a **valuation** surveyor. Preferably one with open market transacting experience which informs that judgement.

Our website (currently being updated for relaunch in the New Year, along with *The Dilaps App*) shows CASE STUDIES and some of the myriad multiple retailers (CLIENTS) for whom we consistently secure lowest settlement figures in dilapidations in conjunction with their building surveyors.

For units in most, other than the best, **Shopping Centres**, the settlement should be at or about NIL, both because the unit with your old shopfit still in place can be let on a temporary, as well as longer term, basis and as the statutory cap is on the "freehold reversionary value", one slightly tatty shop is not likely to have any discernible impact on the value of the entire Shopping Centre, in respect of which it is an inextricable part.

For **department stores**, in addition to the rebuttals for those located in shopping centres as above, there is a powerful case these days that supersession (assumed under the First Limb, no matter what the Landlord's stance is under the Second Limb) will be substantial (if not total) as the property has to be evolved to an altogether different use.

For most **high street** shops, the following breaches which a building surveyor must price a remedy for, are unlikely to have any impact on freehold reversionary value:-

- Tatty upper floors – surplus and/or likely to be voided or converted to residential;

- Old shopfit – in weaker locations, this will assist and enable letting to temporary occupiers; in stronger locations, it will be lost i.e. become irrelevant in the "best bid";

- Tatty "back of house" – so long as safe and functional, some tattiness will not impact the best rental bid in the open market;

- Shrunken pointing, dirty/spalled brickwork etc. – These "issues can be exceptionally pricey to remedy (primarily due to access/scaffolding), yet are purely aesthetic, rather than structural, most of the time. Especially when these affect side or rear elevations, they are unlikely to be done in practice, notwithstanding the fact that a landlord will claim (and happily take) the price associated with this remedy.

Commonly, only exterior wind & watertight items "survive" to commensurately impact the otherwise full freehold reversionary value.

For **retail warehouses**, many are likely to be divided to create the smaller units more in demand these days, which is where the **valuer** can reasonably assume likely supersession, whether or not admitted by the Landlord. In any event, many items which are accepted as "breaches" to which prices must be attached by the **building** surveyor, do not impact **value** because of reasons such as being absorbed in the eventual new tenant's shopfit and corporate colours, or are just irrelevant to value in practice such as minor dents to side and rear cladding elevations, dirty roof sheets etc.

Lastly, it is often claimed that if your vacated unit has been re-let with only some, or no, works done but with a **Schedule of Condition**, this in some way evidences the landlord's "loss". In practice, however, it does not because:-

- The full open market rent is being secured, as if the property was in a condition in which a tenant would commit to a standard full repairing and insuring (FRI) lease. That is because the new tenant is being excluded from liability for repairing certain elements specified in the Schedule of Condition. The obligation is simply to hand back in no worse condition than as demised;

- Usually, the landlord is actually under no express obligation to fix any of these items excluded from the new tenant's obligations. As such, in practice, if and when elements do fail and cause, for example, water ingress, the tenant ends up having to repair them (by default) in any event;

- So long as the "new" tenant hands the property back in no worse state than demised, there is nothing to stop the landlord simply repeating the process all over again;

- By definition, the elements of disrepair excluded by virtue of the Schedule of Condition are not material to the new tenant's ability to occupy and fully enjoy the property;

- Indeed, unless it can be demonstrated that, on the balance of probabilities, the rent under the new letting subject to a schedule of condition was discounted to reflect the perceived "risk" to the new tenant of having to carry out repairs which it is excluded from having to do, but in respect of which the landlord has no express obligation to undertake, then no loss in value will actually exist in practice.

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