Browne Jacobson

Monosolar IQ Ltd v Woden Park Ltd [2020] EWHC 1407 (Ch)

The court generously comes to a tenant's aid when interpreting an index-linked rent review clause.

01 July 2020

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Facts

The tenant (M) held a lease of land for 25 years and six months to develop a solar energy farm at an initial rent of £15,000 per annum. The lease had a tenant's break right at any time on giving six months' prior notice.

The rent payable under the lease was subject to annual reviews to reflect increases in the Retail Prices Index (RPI). The relevant clause provided that the revised rent would be calculated according to the following formula:

Rent payable prior to the Review Date x	Revised Index Figure (RIF)
	Base Index Figure (BIF)

BIF was the RPI for the month two months before the start of the lease term and RIF was the RPI for the month two months before the relevant review date.

M accepted that, read literally, the way the indexation clause was drafted meant that, on the first anniversary of the lease, the rent was to be increased by the RPI increase over the first year of the term. However, on the second anniversary, the revised rent was to be increased again by the aggregate RPI increase over the first and second years of the term and, on the third anniversary, that further revised rent was to be further increased by the aggregate RPI increase over the first, second and third years of the term - and so on. Applying this cumulative formula, one set of figures put forward by M suggested that the rent could escalate to more than £76m per annum by year 25 of the term.

Issues

1. Was it clear that the indexation clause in the lease was a mistake?

2. If so, was it clear what the indexation clause in the lease should have said?

Decision

1. The terms of the indexation clause were unorthodox and were not in use as a standard commercial precedent. They purported to use an index that was a measure of inflation to determine the amount of the annual increase (or decrease) in rent, but in a way that did not increase (or decrease) the rent according to the way that the index was intended to operate, nor according to any measure of inflation in the preceding year (save in the case of the first rent review). The increases in rent produced were irrational and arbitrary and bore no relation to the increase (if any) in the index during the year since the previous review date.

The conclusion that a person intending to buy the lease would reach was that the indexation clause had to have been a drafting mistake. It did not matter that M had a rolling break right available if the rent were to escalate unacceptably as this might require M to dismantle its apparatus, reinstate the land and write off costs significantly earlier than planned.

2. There were clear indicators in the lease that what had been intended had been the application of the RPI to the rent currently payable on an annual and cumulative basis (i.e. the indexation would be by reference to the increase (or decrease) in the RPI over the previous year only, not over the entire expired part of the lease term). The court therefore made a declaration accordingly as to the true construction of the indexation clause.

Points to note/consider

1. In many ways M was fortunate here. The court felt able to distinguish this case from the Supreme Court decision in Arnold v Britton and others [2015] UKSC 36 (where, memorably, the Supreme Court refused to help tenants of holiday chalets stuck with fixed £90 service charges which were subject to compounded 10% increases every three years for the duration of their 99 year leases). This was on the basis that the leases in that 2015 case were granted at a time of high inflation in the 1970s and 80s (so there was nothing irrational or arbitrary about the increases, even if they did produce harsh results later in the lease terms). It was also significant that the lease in this case expressly stated that the rent was to be reviewed to reflect increases in the cost of living. However, other tenants may not be so lucky.

   The case is therefore a reminder of how careful you need to be where a lease (or indeed any commercial contract) contains a mathematical formula for calculating payments and costs. It is a sensible precaution for such a formula to be double-checked by a colleague to ensure that it operates as the parties intended. Where the formula is particularly complex, worked examples within the body of the document should also be considered.

2. There are generally two ways of calculating annual index-linked rent reviews. One way is to start each time with the initial rent payable and apply increases in the index since the start of the lease to that initial figure. Alternatively, you can start each time with the rent currently payable and apply increases in the index over the last year to that current figure. The problem with the lease as drafted in this case was that, from a tenant's perspective, you had the worst of both worlds (starting with the current rent but applying to it increases in the index since the start of the lease).

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