SCOTTISH LAW COMMISSION

(SCOT. LAW COM. No. 75)

IRRITANCIES IN LEASES

REPORT ON A REFERENCE UNDER SECTION 3(1)(*e*)
OF THE LAW COMMISSIONS ACT 1965

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SCOTTISH LAW COMMISSION

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Report on a reference under Section 3(1)(*e*) of the Law Commissions Act 1965

To: The Right Honourable George Younger, M.P.
Her Majesty's Secretary of State for Scotland

We have the honour to submit our Report on Irritancies in Leases

(*Signed*) PETER MAXWELL, *Chairman*
R. D. D. BERTRAM
E. M. CLIVE
JOHN MURRAY
C. G. B. NICHOLSON

R. EADIE, *Secretary*
19 November 1982

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CHAPTER 1

INTRODUCTION

1.1 In *Dorchester Studios (Glasgow) Limited* v. *Stone and Another*,[1] the House of Lords refused to allow an irritancy,[2] incurred by the tenant's failure to pay an instalment of rent on the due date required under the lease, to be purged[3] by an offer of payment of the arrears in full made shortly after that date and before action to enforce the irritancy was brought. Although he had no doubt that it was a well established doctrine of the law of Scotland that a conventional irritancy of the kind in question could not be purged after it had been incurred, Lord Kilbrandon recommended that the doctrine be re-examined by the Scottish Law Commission from the policy point of view.[4]

On 21 September 1976 the Commission received from your predecessor a reference under section 3(1)(*e*) of the Law Commissions Act 1965 in the following terms:

> "Without prejudice to the Commission's freedom to offer advice on any possibilities of reform of this branch of the law I should be glad if the Commission would in the light of *Dorchester Studios (Glasgow) Limited* v. *Stone and Another* and the observations made in the judgments in that case consider and advise on the operation of irritancy clauses in leases of commercial and industrial property (including leases of land for commercial or industrial development) and on related matters."

1.2 There was a wide response to our Consultative Memorandum No. 52 on Irritancies in leases,[5] comments being received from legal bodies and from a number of experienced practitioners, from landlords both in the private and public sectors and from academic commentators.[6] We are most grateful to all those who commented and in particular to those who gave us the benefit of their practical experience in an area whose development has derived in modern times not from case law or statute but from responses by practitioners to practical needs.[7]

Scope of proposals

1.3 We interpreted our reference as being restricted to leases of heritable property, including, as one of the related matters referred to in the reference,

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[1]1975 S.C. (H.L.) 56.

[2]"Irritancy" means annulment or termination. The word is, however, commonly used to denote an event specified in a lease as justifying termination. Thus where a lease contains a provision for termination in the event of non-payment of rent, such non-payment may itself be described as an "irritancy", and the clause in which the provision is made is described as an "irritancy clause". An irritancy can be enforced only by the party aggrieved by the contravention of a stipulation in the lease. It cannot be used by a defaulting tenant as a means of terminating his obligations under the lease.

[3]The "purging" of an irritancy denotes the remedying of the act or omission which has constituted the irritancy.

[4]1975 S.C. (H.L.) 56 at p. 67; see also Lord Fraser of Tullybelton at p. 73.

[5]Published in April 1981 and referred to in this Report as "the consultative memorandum".

[6]The consultative memorandum was also discussed in two Articles by Mr. A. I. Phillips in the Journal of the Law Society of Scotland (June and August 1981). In a further Article in the same Journal (January 1982) Mr. Phillips published the results of an informal survey which he had made of recent instances of enforcement of irritancies in leases.

[7]See para. 3.4 below.

the law of irritancies as it applies to agricultural leases. We also decided that any proposals we made should apply to leases of game and sporting rights, leases of minerals and leases of timber, provided in each case that the transaction was truly one of lease rather than one of sale or licence. We did not, however, consider that our proposals should apply to small landholders, statutory small tenants, crofters or cottars, whose statutory rights, although superimposed on rights enjoyed under leases, are truly rights *sui generis*. Accordingly, the recommendations in this Report do not extend to such holdings of land. Nor do they apply to leases of residential property.

1.4 We considered that our reference was directed at the operation of conventional irritancy clauses, and the references to irritancies in this Report therefore denote irritancies which have, like the irritancy for late payment of rent in *Dorchester Studios*, been agreed upon by the parties themselves as part of the contract of lease. In the consultative memorandum, however, we drew attention to the fact that proposals for reform of the law in this area might not be comprehensive in effect unless they could apply both to termination in reliance on an express provision of a lease and to termination in reliance on the general law relating to breach of contract. Our recommendations in this Report are therefore expressed to extend not only to cases where a conventional irritancy arises, but also to cases where the relevant default either constitutes, or is deemed by some provision in the lease to constitute, a material breach of the contract of lease.[1]

Summary of contents

1.5 In Chapter 2 of this Report we describe the existing law and the criticisms made of it. We then set out in Chapter 3 the factors which in our view should influence law reform in the area and in Chapter 4 our main recommendations for reform. In Chapter 5 we discuss, in the light of comments made on consultation, the proposals which we made in the consultative memorandum in relation to the effect of irritancies on third parties. In Chapter 6 we discuss some related matters and in Chapter 7 we make further recommendations as to the scope of our main recommendations.

[1]Such statutory irritancies as exist permit purgation and are not therefore dealt with in this Report.

CHAPTER 2

THE PRESENT LAW

Characteristics of irritancy clauses

2.1 The law leaves the parties to a lease free to stipulate for such conventional irritancies as they think fit, the only factor limiting their choice being the requirement that their stipulations must themselves be lawful. As we pointed out in the consultative memorandum, conventional irritancy clauses in commercial leases are likely to disclose the following characteristics:

(1) The events identified as sufficient to entitle the landlord to irritate the lease may not be limited to breaches by the tenant of his obligations under the lease itself (such as obligations to pay rent and other periodical sums,[1] or to observe the undertakings imposed on the tenant under the lease in regard to the subjects of let), but are likely to extend to extraneous occurrences such as the alteration of the financial or commercial status of the tenant, or his insolvency.

(2) No distinction is likely to be drawn, in respect of the events mentioned in the irritancy clause, between events which are, and events which are not, prejudicial or materially prejudicial to the landlord. The landlord is likely to be entitled to apply the sanction of irritancy to any breach by the tenant of his obligations under the lease, however minor or inadvertent that breach may be.

(3) No entitlement may be conferred on the tenant—particularly if the lease was settled at a time before the *Dorchester Studios* decision—to receive either prior warning from the landlord of an impending irritancy or a prior opportunity to remedy a remediable irritancy within a given period.[2] The enforcement of an irritancy for the non-payment of rent, for example, may not be expressed to be conditional upon the landlord serving a prior demand for payment.

Enforcement of irritancy clauses

2.2 In the consultative memorandum, we pointed out that although the law was solely concerned with the literal effect of the provisions of an irritancy clause, it was not to be assumed that all landlords would make it their invariable practice to enforce irritancy clauses to the letter. Comments on consultation have reinforced our view that practical considerations, quite apart from reasonableness on the part of landlords, do often act as a restraint on the rigorous application of irritancy clauses. Indeed the facts in *Dorchester Studios* are themselves an illustration of such self-imposed restraint on the part of a landlord: in that case, the landlords gave prior warning to the tenants (although they do not appear to have been obliged to do so under the lease) of the requirement to pay the rent on the due date. Mitigation by the landlord of the rigour of irritancy clauses is, however, a matter for his discretion. It

[1]Such as, for example, insurance premiums, service charges, rates or other similar impositions.

[2]The relevant clauses in the style of full repairing and insuring lease prepared by the Styles Committee of the Law Society of Scotland (which were settled after the decision in *Dorchester Studios*) do make enforcement of irritancy conditional upon the tenant having had an opportunity to remedy a breach of the obligation within a reasonable period after request by the landlord.

cannot be relied on by the tenant, nor by any third party such as a sub-tenant, secured creditor, or trustee in bankruptcy of a tenant whose rights derive from the tenant's own rights.

2.3 In *Dorchester Studios*, the House of Lords had no hesitation in re-affirming what they described as the well-established rule of Scots law that an irritancy clause, however harsh its effect, must fall to be enforced literally in accordance with its terms.[1] Lord Kilbrandon doubted whether such a rule accorded with the needs of social policy, but was in no doubt that the law of Scotland enabled a landlord to irritate a lease by reference to a breach of an irritancy clause regardless of questions of actual prejudice to the landlord.[2] Lord Fraser recognised that the rule could result in a lease being irritated by reason of one day's delay in paying rent. He did not, however, consider that it was unfair in principle to hold a landlord and tenant exactly to their contractual bargain in that way, provided that oppressive use of the irritancy was not in point.[3]

2.4 On that basis, the House of Lords rejected in *Dorchester Studios* any argument that a belated payment of the rent could, by removing the financial prejudice occasioned to the landlord, excuse the tenant from the irritancy of the lease incurred upon the failure to pay on the due date specified under the lease. The "distinctive Scottish common law doctrine" of irritancy, as the House of Lords saw it, enabled the landlord to enforce an unambiguously expressed irritancy, so that it was irrelevant to enquire whether the default occasioning the irritancy had in fact been remedied or whether such enforcement could have been contemplated by the parties.

Development of the common law

2.5 The present characteristics of the distinctive Scottish common law doctrine have to a large extent been imposed by judicial developments since the mid 19th century and it is arguable that those judicial developments have made the law on irritancies in leases harsher in effect than it need have been.[4] An indication of the broader and more flexible way in which the law might have developed can be found in *Hannan* v. *Henderson*,[5] where Lord Deas expressed the view that enforcement of a conventional irritancy should be "based on a fair and reasonable stipulation looking to the terms of the contract and the whole circumstances of the case". The law relating to feu contracts also illustrates how the law of irritancies can operate in a more flexible way than it does in relation to contracts of lease. In the case of feu

[1]The interest which the case excited may seem surprising in the light of the fact that the House of Lords reaffirmed existing authorities, some of which were relatively recent, e.g. *McDouall's Trs.* v. *MacLeod* 1949 S.C. 593, *Lucas's Exrs.* v. *Demarco* 1968 S.L.T. 89. The case was, however, the first one to obtain wide publicity after the drafting of commercial leases had developed as a recognised specialist technique, and this may explain the vigour with which it was discussed in comparison with the preceding cases.

[2]1975 S.C. (H.L.) 56 at p.67.

[3]1975 S.C. (H.L.) 56 at p. 72. See paras. 2.6–2.9 for the circumstances which may constitute such "oppressive" use.

[4]In his article "Breach of Contract" in 1979 Juridical Review, Dr. W. W. McBryde suggests that the present law on irritancies is largely "a result of too strict an interpretation of the decision in *Stewart* v. *Watson* (1864) 2M. 1414".

[5](1879) 7R 380. The case was concerned with the application of a conventional irritancy clause in a contract of co-partnery.

contracts, it was established in the 19th century cases[1] that the proper objective of an irritancy was to operate as a compulsitor for the performance of the vassal's obligations and that, in contrast to the position under a lease, the purging of a default after its occurrence achieved the object of the irritancy clause. There are, as we point out below,[2] distinctions between feudal tenure and commercial leasing contracts, but the discrepancy in the judicial view between the objectives of irritancies in feus and leases is nevertheless significant.

Abuse or oppressive use of irritancies

2.6 The literal enforcement of an irritancy clause was stated in *Dorchester Studios* to be subject to one qualification: namely, the equitable power of the court to relieve a tenant in cases of abuse or oppressive use of an irritancy.[3] The authorities, however, disclose that the Scottish courts have interpreted oppressive use or abuse in an extremely narrow way in the context of irritancy of leases.

2.7 The narrow basis of that interpretation is perhaps most clearly identified in *Lucas's Exrs.* v. *Demarco*.[4] In that case, Lord Guthrie stated that "oppression", in this context, inferred impropriety of conduct on the part of the landlord and that "abuse of irritancy" could not be established unless the landlord had invoked the terms of the contract to procure an unfair consequence. Hence, the act of enforcing an irritancy clause could not in itself be oppressive unless surrounding circumstances made it so.[5] This equiparation of oppression and impropriety may serve to explain why we have found no reported cases in which it has successfully been argued that enforcement of an irritancy has been oppressive.[6] A commentator on *Dorchester Studios* observed in relation to the power to relieve from oppressive use of irritancy that, "although the equitable power has been acknowledged to be waiting in the wings, in all of the modern cases it has never been allowed on stage to affect the action".[7] The restricted scope of the common law power has been emphasised in two cases[8] decided since *Dorchester Studios* and we think that the present interpretation of oppression makes it likely that the power will seldom, if ever, be exercised.

Irritancy and penalty clauses

2.8 Whilst irritancy clauses and penalty clauses are similar in their effect, they can be distinguished in law. The distinction, as Gloag explains it, is that under an irritancy clause the party "loses only the rights which belong to him solely under the contract which, *ex hypothesi*, he has failed to implement";

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[1]E.g. by Lord Kinnear in *Cassels* v. *Lamb* (1885) 12 R. 722 at p. 777.

[2]See paras. 3.3–3.5.

[3]1975 S.C. (H.L.) 56 at pp. 71 and 72.

[4]1968 S.L.T. 89.

[5]1968 S.L.T. 89 at p. 96.

[6]We understand that there has been at least one arbitration in which an arbiter has found in favour of a tenant on the basis that the landlord's attempt to irritate a lease was oppressive. The landlord in question abandoned his appeal against the arbiter's decision.

[7]Journal of the Law Society of Scotland, January 1976, p. 5.

[8]*Forth Homes Ltd.* v. *Williamson* (Sheriff Principal O'Brien 3 July 1978 unreported) and *H.M.V. Fields Properties Ltd.* v. *Skirt'N'Slack Centre of London Ltd.* 1982 S.L.T. 477. In the first case the irritancy resulted from a tenant's being one day late in the payment of rent.

whereas in a penalty clause the party "is deprived of property or money to which he has a title independently of that contract".[1] It must be noted, moreover, that the law relating to penalty clauses may be restricted in its operation to those instances where the penalty is incurred for an actual breach of contract whereas irritancies may arise as a result of extraneous events such as supervening insolvency of the tenant.[2]

The need for reform

2.9 It will be seen, therefore, that the risks inherent in an irritancy clause which is not suitably qualified in the tenant's interest, as it may not be, are risks against which, in the absence of circumstances which amount to "oppression", no protection can be expected from the common law. The common law does not for example require, as a precondition of the enforcement of such an irritancy clause, that warning be given to the tenant of the occurrence of any of the events referred to in it, or that an opportunity be given to the tenant to remedy, if he can, any relevant breach of his obligations. Nor can a tenant hope to succeed in any argument that enforcement of an irritancy clause is rendered oppressive by reason merely of that lack of warning or opportunity to remedy or of the triviality of the breach. Thus, in the consultative memorandum, we identified the basic defect of the existing law as being that it could operate in a way which would effectively penalise a tenant; for example, by enabling a landlord to take immediate advantage of an irritancy so as to terminate the lease, notwithstanding that the irritancy could have been used, without material prejudice to the landlord, as a compulsitor for the remedying of the relevant breach.

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[1]Gloag, *Contract*, 2nd edition, p. 664.

[2]See *Granor Finance Ltd.* v. *Liquidator of Eastore Ltd.* 1974 S.L.T. 296.

CHAPTER 3

FACTORS INFLUENCING REFORM

3.1 It was generally agreed on consultation that the present law was subject to the criticism that it could operate to penalise a tenant and that reasonable landlords would share the view that the law should not operate penally. At the same time, however, those consulted strongly emphasised, as we had done, that any judgment as to whether the enforcement of an irritancy could properly be described as penal must have proper regard to the particular incidents of the relation between a landlord and a tenant, in other words to what Lord Deas referred to in *Hannan* v. *Henderson* as the "terms of the contract and the whole circumstances of the case".[1]

Respect for contractual terms

3.2 In *Dorchester Studios* itself, Lord Fraser was at pains to emphasise the contractual basis of commercial leasing and the need to insist on performance of contractual terms.[2] In the consultative memorandum, we were similarly anxious to emphasise that proposals to ensure that contracts of lease could not be terminated by irritancy in a penal way must be devised on a basis consistent with the requirement that contractual terms fall to be observed by the parties to the contract. The importance of respect for the contractual terms has since been robustly re-affirmed by the House of Lords in a recent case dealing with the analogous problem of the circumstances in which a right under a common form charter-party clause to withdraw a vessel from hire may be exercised on a default by the hirer.[3] We have therefore taken into account as a general policy consideration the need to recognise, in devising arrangements to provide relief from irritancy, the distinction drawn by Lord Justice-Clerk Thomson between "lubricating the working of a contract and altering its terms".[4]

Irritancy as a special remedy

3.3 It was, however, suggested by some commentators on consultation that we might not have given sufficient weight to certain particular characteristics of the contract between a landlord and a tenant which affected the nature of irritancy as a remedy for default by a tenant. For example, it was emphasised to us, and we think fairly, that irritancy was a remedy specifically designed so that an owner of land could ensure that the land was restored to his

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[1](1879) 7 R. 380 at p. 383.

[2]1975 S.C. (H.L.) 56 at pp. 70–72.

[3]*Awilco* v. *Fulvia* (otherwise referred to in this Report as *The Chikuma*) [1981] 1 W.L.R. 314 at p. 322 where Lord Bridge defined the courts' proper aim, in construing common form clauses in contracts, as being "to produce a result such that in any given situation both parties seeking legal advice as to their rights and obligations can expect the same clear and confident answer from their advisers and neither will be tempted to embark on long and expensive litigation in the belief that victory depends on winning the sympathy of the court". The analogy between the termination of contracts for the hire of land and the termination of contracts for the hiring of vessels was noted in *Forth Homes Ltd.* v. *Williamson* (Sheriff Principal O'Brien unreported 3 July, 1978) and was also noted by Professor Black in his comments on the consultative memorandum.

[4]*McDouall's Trs.* v. *MacLeod* 1949 S.C. 593 at p. 602.

possession in circumstances where a tenant had become unable, through commercial failure or otherwise, to perform his obligations as possessor, and that it was important to appreciate that a landlord had an interest as owner and not merely as collector of rent. One of our consultees observed that the landlord may, in many cases, have a real interest to ensure that the land is physically occupied and used and even used in a particular manner. It was similarly emphasised to us that the peremptory nature of irritancy reflected the legitimate interest of the landlord in ensuring that he could have a timeous remedy avoiding the real prejudice which would arise if the repossession of the land were to be delayed by lengthy procedures.

General considerations

3.4 Two other more general considerations have weighed with us in the light of comments made on consultation. Stress was placed by legal practitioners on the fact that the law in relation to commercial leasing had not been developed to any significant extent either by statute or by case law.[1] We think it is important in considering how the law in this area may be reformed to bear in mind that a tradition of active judicial intervention in matters affecting landlords and tenants such as has characterised English law has had no counterpart in Scotland. Hence no traditional experience would be available in this area if legislation were to confer wide "equitable" discretions upon the courts. Stress was also placed by practitioners on the circumstances surrounding the negotiation of contracts of lease. In the consultative memorandum we referred to a view expressed that commercial leases might effectively be dictated to tenants as *contrats d'adhésion*, without any real opportunity for tenants to modify the landlord's terms. This view of commercial leases was vigorously disputed by many of the professional advisers who commented on the consultative memorandum. They contended, on the basis of their own experience, that provisions for a tenant's protection on the lines of the model clauses of the Law Society of Scotland Styles Committee would, in fact, normally be conceded if the tenant's advisers requested their insertion. They further commented that legislative arrangement should not be imposed merely in order to provide a solution which a tenant's professional advisers had failed to provide in negotiating the lease.

Conclusions

3.5 The considerations referred to above have influenced our approach to the reform of the law of irritancies in the following ways:

(1) Our emphasis on the contractual basis of leasing has led us to be cautious of the argument that, since leasehold tenure has largely replaced feudal tenure in the commercial property area, it follows that the law on the irritancy of leases should be harmonised with the law on the irritancy of feus. The latter is a point of reference for the former, but it seems to us that it cannot be more than that if the essential nature of a lease as a continuing contract is to be respected.

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[1]The undeveloped nature of the case law is perhaps not surprising if account is taken of the fact that disputes under commercial leases are commonly referred to arbitration rather than to the courts. Our recommendations are therefore expressed in a way which takes account of the likelihood that they will fall to be applied by arbiters as well as by courts.

(2) We think it necessary in devising any procedures which involve the courts to ensure that the relevant procedures are ones which are not likely to result in undue delay or to impose an undue burden on the court in judging matters of commercial import.

(3) We have thought it right to be cautious about devising legislative procedures which would operate in circumstances where a similar result could be expected to be achieved in a more practical way by negotiation between the relevant parties.[1]

3.6 Our characterisation of commercial leases as being in essence contracts for the hiring of land explains why, in this context, we draw no distinction between different categories of commercial lease. It is obvious that the commercial consequences of an irritancy of a ground lease may differ markedly from the consequences of an irritancy of a lease where a full market rent is being paid. However, as we noted on consultation, the legal principles involved do not differ between the two cases. It should also be noted that, even if it were relevant to draw a distinction between different categories of lease, it might be extremely difficult to reflect the distinction in a satisfactory way in statutory language. The categories are not closed nor are they mutually exclusive.

[1]The Article in the Journal of the Law Society of Scotland (January 1976), referred to in para. 2.7 above, which criticised the state of the law following the decision in *Dorchester Studios* emphasised the responsibility of professional advisers to make provision for the relevant contingencies when drafting leases.

CHAPTER 4

MAIN PROPOSALS FOR REFORM

Statutory notice procedure

4.1 In the consultative memorandum, we took the view that protection against the enforcement of irritancies in a penal way would require to be conferred by an appropriate statutory provision. It did not appear to us that protection could be left to depend upon the negotiation of suitable clauses by tenants' professional advisers for insertion in the relevant contracts of lease. It was argued by many landlords' advisers on consultation that protection ought, in fact, to be capable of being achieved through the negotiation of appropriate provisions in leases, since landlords would not normally resist the inclusion of protective clauses requiring a "notice to remedy" procedure to be observed before the enforcement of an irritancy. This argument, however, was advanced against the background that tenants' advisers were alert, largely because of the decision in *Dorchester Studios* itself, to the need to negotiate appropriate protection for their clients against the danger of unqualified irritancy clauses. Even if it could be assumed that such negotiation would in normal cases ensure the insertion of suitable provisions (such as the Law Society of Scotland Styles Committee's Model Clauses) in individual leases, there would remain the problem of traditional "unqualified" irritancy clauses, whether inserted in leases before or after the decision in *Dorchester Studios*. We were also doubtful in the consultative memorandum about the possibility of any development of the existing equitable powers of the courts to grant relief from irritancies of an oppressive kind. As we have mentioned above, there have been observations in two cases since the consultative memorandum was published which have emphasised the severe limitations which constrain the courts' present powers to grant relief.[1]

4.2 The kind of statutory provision which we originally envisaged for application to all events justifying termination of a lease would have made enforcement of irritancies conditional upon the landlord having given the tenant prior notice requiring the relevant breach of the lease (if remediable) to be remedied within a reasonable time. Our object in devising such a notice, or ultimatum, procedure was to ensure that, where the possibility of remedy existed, the irritancy clause in the lease would act as a compulsitor for the taking of remedial action and not as a means whereby a landlord could take immediate advantage of the breach so as to procure an opportunistic termination of the tenancy. We envisaged that the procedure would operate in all cases of remediable breach by a tenant; that the relevant legislation would prescribe an appropriate, fixed time limit for the taking of remedial action is cases where the breach consisted in a failure to make punctual payment of money; and that in the case of other types of breach procedures would require to be devised to enable an appropriate remedial period to be agreed between the parties, or otherwise determined in the event of their failure to agree. We suggested, for that purpose, that the landlord would require to fix what he regarded as a reasonable period and that the tenant

[1] See para. 2.7.

would be entitled to apply to the court to resolve any dispute between the landlord and himself, either as to the reasonableness of that period or as to the facts surrounding the breach.

MONETARY BREACHES

Recommendations

4.3 We remain of the view that in cases of default by a tenant in the making of monetary payments (whether of rent or otherwise), where a minimum period for remedy of the default can be prescribed by legislation, a statutory procedure of the kind we originally envisaged is the most appropriate means for protecting the tenant. We have given careful consideration, in the light of consultation, to what the prescribed period should be and have come to the view that the relevant notice should specify a period of not less than 14 days from the date of its service. **We therefore recommend that, where there is default in the making of a monetary payment under a lease, the landlord should not be entitled to rely on such default as grounds for termination of the lease unless he has given the tenant written notice specifying a period of not less than 14 days for the remedying of the default in payment and stating that, unless the default is remedied within the period specified, irritancy may result.** (Recommendation 1) Cases may occur where days of grace for payment are permitted, under the lease or otherwise, and the period of grace would not expire until after the end of the 14-day minimum period for remedy under the notice procedure. **We therefore recommend that, where the 14-day minimum period would expire before the end of such days of grace, the period to be specified in the notice should be not less than the unexpired balance of the days of grace.** (Recommendation 2) **We also recommend that notices should be served by recorded delivery, but that the notice procedure should not apply where the tenant has no address for service in the United Kingdom known to the landlord.** (Recommendation 3) We have considered whether legislation should enable the notice to be given before the due date for the payment in question, but have concluded that it should not be given until after the due date has passed. We think it is undesirable that statutory notices threatening irritancy should be given before there has been any default.

Application to material breaches of contract

4.4 As we explain in paragraph 7.2 below, we intend that the notice procedure which we have recommended should apply in those circumstances where the default in payment either constitutes, or is deemed by the parties to constitute, a material breach of the contract of lease, as well as when such failure is the subject of an express irritancy provision.

Default interest, persistent late payers and short leases

4.5 We do not think it is necessary, in view of the relatively short period for the making good of the default in payment of money, to make legislative provision for the payment of default interest. If, however, interest has been stipulated for under the lease, then such contractual interest would require to be added to any payment made after the due date and within the period specified in the notice. Similarly, we do not think, having regard to the time which would be required for any relevant court application, that there would be any practical purpose served in enabling landlords to apply to the court

for dispensation from the need to give 14 days' notice to persistent late payers. Nor do we think that very short leases need to be excluded from the scope of the notice procedure, given that resort to irritancy without notice would be of limited value in such cases, taking into account the time required to obtain any necessary decree against the defaulting tenant.

Incidental benefit

4.6 The introduction of a notice procedure in respect of the payment of rent and other sums should have the incidental effect of remedying a situation to which our attention was drawn on consultation. This is the situation which arises, following a change in landlord, in cases where irritancy can result from a failure to make payment to a landlord who has not intimated his address and identity.

NON-MONETARY BREACHES

Notice procedure inappropriate

4.7 In the preceding paragraphs we have been concerned with cases where the default in question relates solely to the punctual payment of a sum of money. Different considerations may apply in cases where the default consists in a failure to comply with an obligation *ad factum praestandum*, such as a failure to observe an undertaking to repair or maintain the subjects of let. We have come to the view, in the light both of comments made to us on consultation and of our own further reflections, that a notice procedure could not be guaranteed to work in an appropriate way in the case of breaches of obligations of that kind, where the time reasonably required to remedy the consequences of the breach would necessarily depend upon the individual circumstances and could not be prescribed in a general way by statute.

Protracted disputes

4.8 We envisaged in the consultative memorandum that, in the absence of agreement between the parties, the courts would have had to determine what constituted a reasonable remedial period. Anxieties were expressed on consultation that procedures to resolve disputes of that kind between the parties might become protracted, and it was pointed out that a landlord would inevitably be prejudiced by the lapse of time involved, even in those cases where his view as to the reasonable remedial period ultimately prevailed. We believe that irritancy should not lose its characteristic as a speedy and efficient means whereby a landlord may recover possession in the event of a tenant's default and we think that a notice procedure which applied to breaches generally might have that result.

Further defects

4.9 Two further defects are likely to attach to any procedure which depends upon a remedial period being given to a tenant who has defaulted in a non-monetary obligation so as to enable him to remedy the breach. First, if the period requires to be of such length as to give a reasonable opportunity for the remedial action to be completed by the tenant, the length of time granted may assist the tenant at the expense of the landlord. Moreover, any divergence between the interests of the landlord and the tenant as regards

what is a reasonable period for remedial action is likely to be specially marked in those cases where the tenant may be said to have been culpable in allowing the effects of a breach to accumulate, so that a correspondingly longer time is required to remedy the breach. Second, circumstances may arise in which the nature of the breach itself is such as to invite dispute as to the extent to which it is properly to be regarded as a remediable breach or not. For example, in the case of an obligation to maintain subjects of let in good order and repair, "fair wear and tear excepted", dispute could arise as to the extent to which the need for remedial action was to be apportioned between the relevant default by the tenant and the effects of such fair wear and tear. The example may also be taken of a lease with a prohibition against sub-letting or parting with possession. If the subjects were to be sub-let or left unoccupied, would an irremediable breach be regarded as having arisen by reason of that sub-letting or parting with possession as such? Or could a tenant fairly argue that termination by him of the sub-let or the resumption of occupancy by him should be regarded as having remedied the situation?

A wider equitable power

4.10 We have sought, therefore, to devise a rule which can operate to prevent penal enforcement of irritancies in a way which will avoid the possibility of protracted proceedings at a preliminary stage. We think that this can best be achieved if the general equitable power presently available to the court to relieve a tenant from an "oppressive" use of an irritancy can be reformulated so as to be freed of its existing limitations. At the same time, however, it should not be extended into a broad discretion, which could invite tenants to seek the sympathy of a court or arbiter in cases where the enforcement was not in the penal category.[1] Put shortly, the object of any new formulation of the existing equitable power to relieve must be to preserve that power as a residual power only, but as a residual power which can be expected to be applied in practice in cases which clearly justify such application. Moreover, we do not consider that the proposed new formulation should be extended so as to afford protection in circumstances other than termination on the grounds of an act or omission of the tenant, or a change in the tenant's circumstances (such as the loss of a licence or supervening insolvency). It should not, for example, apply in cases where termination is occasioned either by the expiry of a stipulated period of time or by resumption by the landlord of part of the subjects let. It is also conceivable that a commercial lease may contain provisions entitling the landlord to terminate the lease if there is a breach of an obligation owed to the landlord by a person other than the tenant, or if some specified event occurs which is wholly unrelated to any act or omission by the tenant or to the tenant's own circumstances. We do not think that legislation should extend to protect tenants from acceptance of termination provisions of that kind.

The fair and reasonable landlord

4.11 We have given careful thought to the devising of appropriate provisions to achieve the above criteria. We think it is essential that the ultimate enforceability of an irritancy must be judged by reference to a standard which

[1]See e.g. Lord Bridge's observation in *The Chikuma* [1981] 1 W.L.R. 314 referred to in para. 3.2 above.

is broad and objective, and which can in its practical application reflect those particular factors which are applicable to contracts of lease. Existing legislation dealing with the termination of agricultural leases provides a precedent for such a statutory standard. The legislative provisions which enable the Scottish Land Court to withhold consent to the operation of a notice to quit refer to that power being exercisable in those circumstances where "a fair and reasonable landlord would not insist on possession".[1] We think that this criterion of the "fair and reasonable landlord" could be used in relation to commercial leases generally as a criterion by which to judge whether insistence on an irritancy was penal in its effect. Consultation has led us to believe that there is clear understanding amongst landlords and their advisers as to what a fair and reasonable landlord would and would not insist upon in relation to the negotiation of an irritancy provision and we think that there would be a similar understanding as to the limits of fairness and reasonableness in relation to the enforcement of such provisions.

Further considerations

4.12 We think that a basic standard of the kind we envisage would require to be supplemented in three ways. First, the basic criterion of the fair and reasonable landlord must be so expressed as to relate to what such a landlord would have insisted upon as regards enforcement of his rights in the particular circumstances of the case. Second, it should be made clear that the relevant unfairness and unreasonableness may reside in the manner of enforcement, as for example where the landlord has not afforded such reasonable opportunity to remedy a breach as would have been afforded by a fair and reasonable landlord, taking into account the time and economic cost involved. Third, the statutory provisions should make it clear that the basic criterion is to be applied not to the parties' agreement to the inclusion of the particular irritancy provision in the lease—however rigorous that provision may be—but only to the reliance placed on the provision in particular circumstances.

Recommendation

4.13 **We recommend, therefore, that the existing power of the courts to grant equitable relief from the enforcement of an irritancy in oppressive circumstances should be recast as a statutory provision to the effect that a landlord shall not be entitled to rely (other than in cases of default in making a monetary payment) on an act or omission by the tenant or on a change in the tenant's circumstances as grounds for terminating the lease if, in all the circumstances of the case, no fair and reasonable landlord would have sought so to rely.** (Recommendation 4) In consonance with a general recommendation which we make below,[2] the statutory rule should apply not only to cases where the enforcement takes the form of reliance on an irritancy clause but also to cases where the landlord seeks to rely on the fact that the tenant's act or omission or a change in his circumstances is, or is deemed by the parties to be, a material breach of the contract of lease.

Residual Power

4.14 We believe that if the existing common law power to grant relief against oppression were reformulated in this way, it would provide a workable and

[1]Proviso to S. 26(1) of the Agricultural Holdings (Scotland) Act 1949.
[2]See para. 7.2.

acceptable basis for the protection of tenants from the termination of leases in conditions which can properly be described as penal or oppressive. We do not think that a statutory relieving provision of the kind we recommend would give rise to the danger against which the House of Lords warned in *The Chikuma,*[1] namely the encouragement of tenants to embark on litigation simply in the hope of winning sympathy from the court. We think that it would be seen as a means by which relief could be obtained only in those residual cases where it was truly justified. We give examples below of the kind of residual case which we have in mind.

Application

4.15 First, the statutory relief could be applied to those cases for which the notice procedure proposed in the consultative memorandum was designed, namely cases where the landlord has taken advantage of a breach by the tenant of a provision of the lease to enforce an irritancy in circumstances where a reasonable landlord would not have done so without first giving a reasonable opportunity to the tenant to remedy the breach. It could also apply in cases where the landlord has, in fact, provided a prior opportunity to the tenant to remedy the breach, but that opportunity has been unreasonably inadequate. We believe, therefore, that the objectives which, in the consultative memorandum, we envisaged would be achieved by the notice procedure would be capable of being achieved through the application of the new relief, but without the accompanying risk of protracted disputes at a preliminary stage on questions arising out of the notice procedure. Our proposals are not intended to carry any implication, however, that relief should be available, regardless of the individual circumstances, in all cases where notice to remedy a default has not been given. We intend that the availability of relief must depend upon what is reasonable in the particular circumstances involved, and those circumstances could conceivably be such as to justify a reasonable landlord in withholding an opportunity to remedy. Thus for example, if a tenant had on previous occasions taken advantage of the landlord's willingness to allow a remedial period, or had taken advantage previously of the statutory provisions, those factors would constitute relevant "circumstances of the case" and could make it reasonable for the landlord to decline to allow another remedial period to the tenant. Again, in the case of an irritancy clause in respect of a failure to maintain subjects of let, the subjects might have been allowed to fall into disrepair to such an extent as to necessitate a long period for proper repair. In such circumstances, it might well be reasonable for a landlord to decline to allow an adequate time for remedy of the breach.

4.16 Second, the statutory relief which we propose could apply in cases where the tenant's breach of an obligation is irremediable, but is nevertheless of such a trivial nature that the enforcement of irritancy as a sanction for it cannot reasonably be justified. An example might be a failure to maintain some minor item under a lease which imposed a general maintenance obligation on the tenant. In such cases, as with remediable breaches, the application of the provisions would depend upon the whole circumstances of the case and the standards of a reasonable landlord. This would enable recognition to be given to the fact that a landlord may reasonably be justified in seeking the

[1] [1981] 1 W.L.R. 314.

sanction of irritancy notwithstanding that the breach occasioning the irritancy is not, in isolation, of major significance. There may be cases where the qualitative nature of the breach is such as to justify irritancy although in quantitative terms it might not appear to do so, as for example in the case of a breach, albeit for a short time only, of an obligation to keep premises occupied. The previous conduct of the parties may also be relevant in such cases.

GENERAL

Forum for resolution of disputes

4.17 We suggested in the consultative memorandum that the Lands Tribunal, rather than the courts, might be considered the appropriate body in which to resolve the kind of issues likely to arise out of the operation of a notice procedure. Comments on consultation, however, strongly supported the view that the sheriff court rather than the Lands Tribunal would be the appropriate forum for resolution of such issues. Our attention was also drawn to the fact that the sheriff court is the traditional forum in regard to ejections and removings and that the involvement of another tribunal in questions relating to termination of leases would lead to an inconvenient division between the termination proceedings and the removal proceedings. We found those arguments convincing and they have persuaded us that there is no need to consider displacing the jurisdiction of the sheriff court and Court of Session in relation to the statutory provisions which we now recommend.

Declarator of irritancy

4.18 We have mentioned above the link between irritancy and removing. In the consultative memorandum, we enquired whether there should be legislative provision to the effect that any action of extraordinary removing must be preceded by a declarator of irritancy. The general consensus of those who commented on this question was that no specific legislative provision was required. We therefore make no recommendation on the point.

Refusal to grant entry

4.19 Our recommendations are made on the basis that they should apply only to the enforcement of irritancies during the currency of a lease, that is, after entry has been taken. They are not intended to apply where a landlord terminates the right of a prospective tenant to take entry because of failure to make any payment due, or to fulfil any other condition, on or before the date of entry.

CHAPTER 5

IRRITANCIES AND THIRD PARTIES

5.1 The enforcement of an irritancy clause may have consequences for third parties whose rights derive from the rights of the tenant whose lease has been irritated. Unless the parties have provided otherwise by contract, or are able to negotiate alternative arrangements at the time, a sub-tenancy will cease to exist[1] if the head tenancy is irritated, and the rights of a secured creditor whose security subjects consist of a tenant's interest under a lease will cease to have any value when that interest is terminated. In the consultative memorandum we recognised that the enforcement of irritancies could create problems for such sub-tenants or creditors. We therefore sought comments on proposals which would have conferred a limited degree of formal protection on third party interests adversely affected as a consequence of an irritancy.

Proposals

5.2 The proposals which we advanced were of two kinds. First, we invited comments on a proposal that sub-tenants and creditors known to a landlord should have the same right as the tenant himself to receive notices from the landlord under the statutory notice procedure which we proposed.[2] Second, we invited comments as to whether a legislative arrangement should be made to protect third party interests, following an irritancy, by enabling the courts in certain circumstances to exercise a discretion to vest the tenant's interest in the third party, subject to appropriate conditions. We recognised that a court exercising such a discretion would require to give careful consideration to the position of the landlord before it required him to accept the third party in substitution for the previous tenant, and that, in cases where there was more than one sub-tenancy, the substitution by the court of a multiplicity of partial tenancies for a previous single tenancy of a whole property unit might not be a reasonable proposition under any conditions.

Notices to third parties

5.3 The proposal as to the entitlement of a known third party to receive notice from the landlord would have conferred a procedural protection only. Therefore, in the consultative memorandum, we envisaged that it might have to be linked to a sanction which would have had a substantive effect. The notice procedure which we recommend in this Report[3] is limited to notice in respect of default in monetary payments, and the notices which would fall to be given to third parties would correspondingly be limited. We have concluded, partly in response to consultation and partly as a result of further reflection, that a requirement to give such notices to third parties ought not to be imposed

[1]Nevertheless, a decree of removing solely against the principal tenant may not entitle the landlord to evict a sub-tenant who is in possession as of right and who has not received notice from the landlord or from the principal tenant. Nor can such a sub-tenant be dispossessed by an action of ejection.

[2]See para. 4.2 above.

[3]See para. 4.3 above.

by legislation. We sympathise with the general observation which was made by some consultees that the law should not seek to impose upon a landlord a duty, merely because there has been a default by his tenant, to give notices to third parties with whom he has no contractual connection. The duty to keep such third parties informed, it was argued, ought properly to fall upon the tenant and could quite practically be imposed upon the tenant by the third parties. We think also that there would be severe difficulties of a practical nature in ensuring the intimation by a landlord to his own successors of third party interests intimated to him. Accordingly, we have decided to make no recommendation for legislation on this point.

Transfer of tenant's interest

5.4 The proposal that the court should have a discretion to protect third party interests affected by the irritancy of a lease raised, even in its most limited form, issues of substantial importance. We have concluded, in the light of consultation, that it would not be desirable or practical at this stage to seek to impose any legislative procedures in this area to supplement the possibility, which always exists, of negotiated arrangement between the parties. We have reached this conclusion both in relation to sub-tenants and in relation to creditors. The basis of our conclusion, however, differs as between the two.

Sub-tenants

5.5 In the case of sub-tenants, we recognised in the consultative memorandum that a discretionary power conferred upon the courts to substitute a sub-tenant for the tenant, as the party contracting with the landlord, would require the courts to strike a delicate balance between the interests of the landlord and sub-tenant. We envisaged that in some circumstances this balance might be so difficult to achieve that it would effectively preclude the exercise of the discretion. The difficulties involved were emphasised on consultation, even by those who were not opposed as a matter of principle to giving some kind of formal protection to sub-tenants. We think, however, that two considerations of overriding importance make the introduction of a court discretion in this area impractical. The first relates to the extent to which any scheme could be made to apply to existing sub-tenancies; the second to the effect of any scheme on the attitude of landlords to the creation of sub-tenancies in the future.

Existing sub-tenancies

5.6 We do not think that any new scheme for the possible substitution of a sub-tenant in place of a head tenant whose lease has been irritated could be applied to sub-tenancies which have come into existence prior to the date of the relevant legislation. It was pointed out to us on consultation that a landlord, in accepting or agreeing to a sub-tenancy, might well have done so without regard to the financial standing of the sub-tenant. The landlord would continue to look to the financial standing of the head tenant alone for the performance of the latter's obligations under the head lease. It followed that the exercise of any court discretion as to substitution of the sub-tenant would involve the courts in requiring the landlord to accept as tenant a party whose financial standing could not be assumed to be acceptable to the landlord. It

was put to us, and we agree, that landlords could not be expected, as a matter of principle, to accept that possibility.

Future sub-tenancies

5.7 Any legislative scheme for the formal protection of sub-tenants would therefore require to be such as to apply only to sub-tenancies created after the date of the relevant legislation. It was suggested, however, that the very existence of legislation which could impose a tenancy relationship between a landlord and a sub-tenant might have the result that landlords would prohibit sub-tenancies, so as to avoid the risk of the courts' discretion being exercised in relation to them in the future. It must, we think, be recognised that legislation could not impose any limitation on a landlord's contractual freedom so to prohibit sub-tenancies. We have had to take into account, therefore, the possibility that the introduction of legislation to protect sub-tenants might have the undesirable result of encouraging such a prohibition and might paradoxically result in a reduction in the number of permitted sub-tenancies.

5.8 These considerations have persuaded us that no arrangements could be imposed by legislation in relation to sub-tenants which would be worthwhile, having regard to the scope for their application or the likelihood of their acceptability. The problem appears to us to be one which can properly be left to be resolved by contract or negotiation amongst the parties involved.

Tenants' creditors

5.9 A tenant's creditors will necessarily be adversely affected if his insolvency leads, as it may be expected to do, to the enforcement of an irritancy clause under the lease, unless special provision has been made in the lease in anticipation of the insolvency or unless an arrangement can be made with the landlord at the relevant time. Three separate categories of creditor may be distinguished in this context. First, there may be secured creditors whose security takes the form of a standard security over the tenant's interest under the lease. In their case, irritancy of the lease will terminate the tenant's interest, so that the security subjects will cease to exist. Second, there may be secured creditors whose security takes the form of a floating charge over the undertaking of a company which includes the interest of that company as a tenant under a lease. In their case, a receiver appointed following an insolvency will find that the tenant's interest has ceased to exist on the irritancy and has ceased to form part of the undertaking attached by the charge. Lastly, there may be unsecured creditors. In their case, the tenant's interest under the lease will, on termination by irritancy, cease to form part of the insolvent estate.

5.10 We sought comments in the consultative memorandum as to whether formal procedures ought to be available to creditors who did not succeed in negotiating suitable arrangements for their protection in such circumstances. The kind of formal procedure which we envisaged was the same as that envisaged for the protection of sub-tenants, namely a discretion in the courts to vest the tenant's interest in the affected creditor. We recognised that a serious commercial imbalance might arise if, say, a tenant's interest under a lease which could have been assigned at a substantial premium by the tenant were to be irritated on an insolvency, to the disadvantage of the creditors and

to the advantage of the landlord. It was agreed by consultees that such problems could certainly arise in practice. The example most commonly cited was the problem which would arise if the value of a landlord's reversionary interest had been substantially increased by the tenant's own expenditures on the subjects of let and the reversion to the landlord was accelerated by irritancy following the insolvency of the tenant. In such circumstances, it was pointed out, a lease which the tenant might have been able to assign at a substantial premium would cease to be capable of being turned to account by his trustee, liquidator or receiver and an adventitious benefit would be conferred on the landlord.

The W.S. Society scheme

5.11 The question arises as to whether, and by what means, it is appropriate for statute to intervene in such cases to provide protection for the interests of creditors. It was pointed out on consultation that creditors would not normally wish to take over the tenant's interest, but only to turn it to account, and that the most appropriate manner of protecting creditors would therefore be to enable them to exercise, in place of the tenant, any power available to the latter to assign the lease. The W.S. Society devised a helpful example of the form which such arrangements might take. They envisaged that, in the case of an insolvency, the standard security holder, trustee, liquidator or receiver would require to exercise an option within a short period (say one month) as to whether he wished an opportunity to assign the lease, assuming it was assignable; if he decided to assign, he would have a further relatively short period (say six months) in which to do so, having first obtained any requisite consent for the assignation from the landlord. The creditor (or the trustee, liquidator or receiver) would, however, by virtue of exercising the original option, require to assume all the obligations of the tenant under the lease (other than obligations to occupy the subjects of let) and would continue to be subject to those obligations either until he found a permitted assignee or until the landlord was successful in re-letting the subjects of let following a failure by the creditor to find an assignee within the permitted period. The assumption of such obligations by the creditor was seen as a necessary compensation to the landlord for waiver of the right to seek immediate repossession.

Constraints

5.12 The W.S. Society scheme illustrates the constraints to which any formal protection scheme might require to be subject in order to be acceptable to landlords. The price for enabling the creditor to exercise the tenant's ability to assign would be the assumption by the former of substantial obligations to the landlord, which might require to subsist for the remainder of the lease. We think, however, that a further difficulty would arise if it was desired to make such a protection scheme applicable to all cases of insolvency. The scheme assumes the existence, and the relevant date, of someone such as a receiver, trustee in bankruptcy or liquidator with whom the landlord can deal. In many cases, however, the irritancy may follow upon notour bankruptcy or diligence and so may occur at a date when there is no trustee, liquidator or receiver appointed and no certainty that one will ever be appointed. In such circumstances, the essential precondition of the existence of a responsible person with whom the landlord could deal would not exist.

General considerations

5.13 More general considerations have also persuaded us that the effect of an irritancy on the creditors of a tenant is not an appropriate area for legislative intervention. It was pointed out to us by several consultees that the blame for any unfair allocation of advantage and disadvantage between the landlord, on the one hand, and the creditors' interests, on the other, fell to be imputed not to any deficiency in the law of landlord and tenant, but rather to the failure of the advisers to make appropriate provision in the lease. It was put to us, for example, that no building lease ought to be settled on terms which would make it impossible for the tenant's interest to be turned to account, for the benefit of his creditors, following an insolvency and that, if statute were to intervene in this area, it would be operating to remedy an avoidable omission by professional advisers. We have reached the conclusion that the difficult situations which no doubt can arise in cases where an unqualified conventional irritancy clause has been included in a building lease, or in a lease of commercial property to whose value the tenant has added, are not such as to justify a statutory scheme for the protection of creditors. It is also relevant to bear in mind that the introduction of statutory arrangements to protect the interests of tenants with assignable interests under leases might result in landlords becoming less willing to grant assignable leases.

Receivership and irritancy

5.14 The Institute of Bankers in Scotland suggested to us, in their comments on the consultative memorandum, that the particular considerations applicable to receivership might be regarded as justifying special provisions, to prevent an irritancy operating to the disadvantage of a receiver in cases where the company in question had been a tenant under a lease which it could have assigned for value. This suggestion was prompted by the thought that the continuance of a business enterprise, which is one of the objectives of receivership, might be rendered impossible if possession of business premises were lost as a result of an irritancy occurring by virtue of the receiver's appointment. It is true that the distinction between receivership and liquidation as insolvency procedures has been emphasised in cases on receivership law,[1] but landlords who commented on the consultative memorandum did not appear to regard the right to repossession as any less necessary in the one case than in the other. For that reason, we think that if the relation of receivership to irritancy is to be considered it would be more appropriately considered in connection with the law relating to receivers, and not as a special case in the law of irritancy as such.

[1] *Lord Advocate* v. *Royal Bank of Scotland Ltd.* 1977 S.C. 155 and *Taylor, Petitioner* 1982 S.L.T. 172.

CHAPTER 6

MISCELLANEOUS MATTERS

6.1 In the consultative memorandum, we sought comments on two matters which might affect the ability of a landlord to enforce an irritancy although they did not arise in the context of the penal enforcement of irritancies. The first matter was the ability of a landlord to enforce an irritancy at a time when he was in breach of his own obligations as landlord under the lease. The second matter was the question whether acceptance of rent by a landlord should bar the enforcement of an irritancy for a breach of the lease known to him at the time the rent was accepted.

Principle of mutuality of obligations

6.2 We suggested in the consultative memorandum that the effect of a landlord's own breach on his ability to enforce an irritancy shoud not be the subject of legislative provision, but should depend upon the application of the principle of mutuality of obligations in the general law of contract. There is authority for the application of that principle to the particular case of a contract of lease[1] and, as we have mentioned above, we have been concerned to preserve, so far as practicable, the application of normal contract law principles to commercial leases. There was general agreement on consultation that a legislative statement of the principle was not required and we do not believe that anything in our proposals would affect its continued application. We therefore remain of the view that no provision should be made on this matter in any legislation to follow on this Report.

Irritancy and acceptance of rent

6.3 We also raised the question of whether legislation should clarify the circumstances in which a landlord's acceptance of rent from a tenant, in the knowledge that a breach of the lease had occurred, should preclude the landlord from subsequent resort to irritancy as the remedy for such breach. We did so against the background that the existing law in this area was unclear, but could result in unfairness to a tenant if his lease was irritated after prior acceptance of rent had led him to believe that his continued possession of the subjects of let was assured. We have come to the view, in the light both of comments on consultation and of further developments in the law,[2] that there is no need for legislative intervention in this area and that any attempt to devise a legislative formula might lead to the wrong results in some cases.

6.4 It was put to us by several consultees that legislation should not seek to establish a rule that acceptance of rent necessarily affects a landlord's ability to resort to irritancy as a remedy. It was strongly argued that a landlord should in principle be entitled, as it was put, "both to his rent and to his remedy" and that if the principle were otherwise a landlord who was involved

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[1] *Macnab of Macnab* v. *Willison* 1960 S.L.T. (Notes) 25.

[2] See para. 6.5 below.

in *bona fide* discussion with a tenant as to whether a breach of a lease had occurred would be inhibited from accepting rent during the negotiation period. We considered whether that principle could leave a tenant without a remedy in the kind of special cases which we had in mind. We have come to the view, however, that protection in appropriate cases should now be available either as a result of developments in the general law or as a result of the application of our own proposals relating to equitable relief from irritancies.

Recent developments

6.5 The developments in the general law derive from a recent affirmation by the House of Lords of the proposition that a party who seeks to argue that another party has abandoned a remedy against him need not show, as he would have to do if personal bar were relied on, that he has acted to his own prejudice in reliance on such abandonment.[1] That proposition has since been applied, in *Banks* v. *Mecca Bookmakers (Scotland) Ltd.*,[2] to the enforcement of a rent review in a commercial lease, with the result that acceptance by the landlord of rent at an unreviewed rate for two quarters following a review date was held, on the facts of the case, to infer abandonment by the landlord of his contractual right to review the rent for the remainder of the review period. The circumstances which will justify an inference of abandonment of a landlord's right to review the rent may clearly be very different from those which would justify an inference of abandonment of a right to irritate the lease. Nevertheless, the decision in *Banks* establishes the possibility that a tenant who might not be successful in a plea of personal bar against the landlord may nevertheless be able to argue, in appropriate circumstances, that the landlord has abandoned or waived his right to invoke an irritancy.[3] Apart from arguments based on abandonment or waiver of rights by a landlord, our own proposals for a reformulated equitable remedy against the oppressive use of an irritancy could also apply in those special cases where the circumstances surrounding the acceptance of rent in the knowledge of a breach were such as to render resort to the remedy of irritancy for that breach unreasonable to the tenant.

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[1] *Armia Ltd.* v. *Daejan Developments Ltd.* 1979 S.C. (H.L.) 56.

[2] 1982 S.L.T. 150.

[3] An argument based on personal bar was advanced on behalf of the tenant in *Forth Homes Ltd.* v. *Williamson* (Sheriff Principal O'Brien 3 July 1978 unreported) but failed because the tenant could not show that he had altered his position in reliance on the landlord's actions.

CHAPTER 7

SCOPE OF REFORM

7.1 In the consultative memorandum, we made three important proposals as to the scope of any legislation to reform the law on irritancies. First, we suggested that the reformed law should apply to the termination of a lease on the grounds of the tenant's material breach of contract. Second, we suggested that the reformed law should apply to leases entered into before as well as after the date of coming into force of the relevant legislation. Finally, we suggested that parties should not be permitted to exclude the application of the reformed law by contractual arrangement.

Application to tenant's material breach of contract

7.2 The first suggestion was made in order to ensure a systematic reform of the law, and met with general agreement on consultation. If the provisions for reform of the law were to apply only to the enforcement of conventional irritancies as such, then they might have an unduly limited effect if landlords were to rely on the tenant's material breach of contract, rather than on conventional irritancy clauses, as grounds for terminating leases. The possibility could also arise of certain circumstances being deemed to be material breaches of contract under a lease in order to facilitate such reliance. **We therefore recommend that the notice procedure and the new basis for relief from the penal enforcement of irritancy, recommended in paragraphs 4.3 and 4.13 respectively, should apply not only to cases where reliance is placed on a conventional irritancy clause but also to cases where reliance is placed on a breach of the contract which is or which, in terms of the contract, is deemed to be material.** (Recommendation 5)

Application to existing leases

7.3 With regard to our proposal that any amending legislation should apply in relation to leases entered into before as well as after the date of its introduction, it was generally accepted that it would not be helpful to enact legislation in this area unless it could apply to existing leases. On the other hand, we think that the legislation should not operate retrospectively where formal steps have been taken in respect of termination before its commencement date. **We therefore recommend, subject to the qualification mentioned below, that our recommendations should apply in relation to the termination of leases entered into before as well as on or after the commencement date of any implementing legislation. However, such legislation should not apply to termination by virtue of circumstances arising before the commencement date of the legislation if, prior to that date, the landlord has served written notice on the tenant of his intention to terminate by virtue thereof.** (Recommendation 6)

Prohibition of contracting out

7.4 With regard to our proposal that parties to leases should not be entitled to contract out of the relevant legislation, consultees generally accepted that

legislation in this area would be largely ineffective unless contracting out was prohibited. **We therefore recommend that parties should not be allowed to disapply the provisions of any legislation to follow on this Report, whether in the leases themselves or in ancillary documents.** (Recommendation 7)

Landlords' powers of resumption

7.5 Our recommendations are not intended to affect the exercise by landlords of such powers of resumption of part of the let subjects as may have been reserved to them under the lease.

SUMMARY OF RECOMMENDATIONS

1. A landlord should not be entitled to rely on a tenant's default in making any monetary payment due under a lease as a ground for termination of the lease unless he has served on the tenant written notice specifying a period of not less than 14 days for the remedying of the default and stating that irritancy may result if the default is not remedied within that period. (Paragraph 4.3; Clause 1(1), (2) and (3)(*a*).)

2. Where the 14-day minimum period would expire before the end of any days of grace for payment, whether permitted under the lease or otherwise, the period to be specified in the notice should be not less than the unexpired balance of the days of grace. (Paragraph 4.3; Clause 1(3)(*b*).)

3. Notices should be served by recorded delivery, but the notice procedure should not apply where the tenant has no address for service in the United Kingdom known to the landlord. (Paragraph 4.3; Clause 1(4) and (5).)

4. A landlord should not be entitled to rely on an act or omission by the tenant (other than a failure to make any monetary payment due under the lease) or on a change in the tenant's circumstances as a ground for termination of the lease if, in all the circumstances of the case, no fair and reasonable landlord would seek so to rely. (Paragraph 4.13; Clause 2(1).)

5. Recommendations 1–4 should apply not only where the landlord relies on a conventional irritancy clause for the purpose of termination but also where reliance is placed for that purpose on the fact that the tenant's default, act, omission or changed circumstances constitute a breach of contract which is, or which is deemed to be, material. (Paragraph 7.2; Clause 1(1)(*b*) and 2(1)(*b*).)

6. Any implementing legislation should apply to leases entered into before, on or after the commencement date of the legislation, except where termination results from circumstances which have arisen before such commencement date and the landlord has, prior to that date, given written notice of his intention to terminate the lease by virtue of those circumstances having arisen (Paragraph 7.3; Clause 3(1).)

7. Parties to leases should be prohibited from contracting out of any implementing legislation. (Paragraph 7.4; Clause 3(2).)

APPENDIX A

Irritancies in Leases (Scotland) Bill

ARRANGEMENT OF CLAUSES

Clause

DRAFT

OF A

BILL

TO

Restrict as respects Scotland the right of landlords to terminate certain leases in the event of a breach by tenants or of a change in their circumstances.

BE IT ENACTED by the Queen's most Excellent Majesty, by and with the advice and consent of the Lords Spiritual and Temporal, and Commons, in this present Parliament assembled, and by the authority of the same, as follows:—

Irritancy clauses etc. relating to monetary breaches.

1.—(1) A landlord shall not for the purpose of terminating a lease be entitled to rely—

(*a*) on a provision in the lease which purports to terminate it, or to enable the landlord to terminate it, in the event of a failure of the tenant to pay rent, or to make any other payment, on or before the due date therefor or such later date or within such period as may be provided for in the lease; or

(*b*) on the fact that such a failure is, or is deemed by a provision of the lease to be, a material breach of contract,

unless subsection (2) or (5) below applies.

(2) This subsection applies if—

(*a*) the landlord has, at any time after the payment mentioned in subsection (1) above has become due, served a notice on the tenant—

(i) requiring the tenant to make payment of the sum which he has failed to pay on the due date together with any interest accruing thereon in terms of the lease within a period specified in the notice; and

(ii) stating that, if the tenant does not comply with the requirement mentioned in sub-paragraph (i) above, the lease may be terminated; and

(*b*) the tenant has not complied with that requirement.

(3) The period to be specified in any such notice shall be not less than—

(*a*) a period of 14 days immediately following the service of the notice; or

(*b*) any period remaining between the service of the notice and the expiry of any time provided for in the lease or otherwise for the late payment of the sum which the tenant has failed to pay, if that remaining period is more than 14 days.

(4) Any notice served under subsection (2) above shall be sent by recorded delivery and shall be sufficiently served if it is sent to the

EXPLANATORY NOTES

General

The Bill makes provision for two forms of protection for tenants against the penal enforcement of irritancies in leases. The first is a new "warning" or notice procedure applicable where a landlord seeks to terminate a lease on the basis of the tenant's failure to make any monetary payment due under the lease (see paragraphs 4.3–4.6). The second, which is applicable to all other conventional irritancies in leases, is a development of the courts' equitable power to grant relief from abuse or oppressive use of irritancies (see paragraphs 2.6–2.7 and 4.10–4.16). Both forms of protection are expressly designed to cover the possibility of termination resulting from the tenant's breach of a contractual term which is or which is deemed to be material as well as reliance by the landlord on a conventional irritancy clause (see paragraphs 4.4, 4.13 and 7.2). The Bill does not apply to leases of land used wholly or mainly for residential purposes or to crofts, the subjects of cottars and other holdings to which the Small Landholders (Scotland) Acts 1886 to 1931 apply (see paragraph 1.3).

Clause 1 implements Recommendations 1, 2, 3 and 5 and introduces a mandatory notice procedure in respect of termination based on the tenant's failure to make a monetary payment due under the lease (see paragraphs 4.3–4.6).

Subsection (1) applies the requirement to give notice to the tenant to the case where the landlord relies on a conventional irritancy clause for the purpose of termination (paragraph (*a*)) and to the case where the landlord relies on the tenant's material breach of contract for that purpose (paragraph (*b*)) (see paragraphs 4.4 and 7.2).

Subsection (2) sets out the details of the notice procedure and the need for a tenant to comply with any notice served in order to obtain protection. The matters to be stated in the notice are listed.

Subsection (3) states the minumum period for payment of arrears which is to be specified in the notice. Account is taken of the possibility of days of grace being permitted; the basis of calculation in such cases is set out in paragraph (*b*) (see also clause 1(1)(*a*) and paragraph 4.3).

Subsection (4) requires notices to be served by recorded delivery at an address (including an address for service) in the United Kingdom (see paragraph 4.3).

tenant's last business or residential address in the United Kingdom known to the landlord or to the last address in the United Kingdom provided to the landlord by the tenant for the purpose of such service.

(5) This subsection applies where the tenant does not have an address in the United Kingdom known to the landlord and has not provided an address in the United Kingdom to the landlord for the purpose of service.

Subsection (5) has the effect of exempting the landlord from the requirement to observe the notice procedure in those exceptional cases where the tenant has no known address for service in the United Kingdom (see paragraph 4.3).

Irritancy clauses etc. not relating to monetary breaches.

2.—(1) Subject to subsection (2) below, a landlord shall not for the purpose of terminating a lease be entitled to rely—

(*a*) on a provision in the lease which purports to terminate it, or to enable the landlord to terminate it, in the event of an act or omission by the tenant (other than such a failure as is mentioned in section 1(1)(*a*) of this Act) or of a change in the tenant's circumstances; or

(*b*) on the fact that such act or omission or change constitutes, or is deemed by a provision of the lease to constitute, a material breach of contract,

if in all the circumstances of the case a fair and reasonable landlord would not seek so to rely.

(2) No provision of a lease shall of itself, irrespective of the particular circumstances of the case, be held to be unenforceable by virtue of subsection (1) above.

(3) For the purposes of subsection (1) above,

"all the circumstances of the case" shall include, in a case where—

(*a*) an act or omission by the tenant or a change in the tenant's circumstances is alleged to constitute a breach of a provision of the lease or a breach of contract; and

(*b*) the alleged breach is capable of being remedied in reasonable time and at economic cost,

whether a reasonable opportunity has been afforded to the tenant to enable the breach to be remedied.

Clause 2 implements Recommendations 4 and 5 restricting landlords' powers of termination, in circumstances other than those covered in clause 1, by reference to the test of the fair and reasonable landlord. The test is based on the proviso to section 26(1) of the Agricultural Holdings (Scotland) Act 1949 (see paragraph 4.11).

Subsection (1) states the fair and reasonable landlord test and applies it to the case where the landlord relies on a conventional irritancy clause for the purpose of termination (paragraph (*a*)) and to the case where the landlord relies on the tenant's material breach of contract for that purpose (paragraph (*b*)). (See paragraphs 4.13 and 7.2.) The importance in practice of the phrase "in all the circumstances of the case" is illustrated in paragraphs 4.15 and 4.16.

Subsection (2) makes it clear that the validity of a conventional irritancy clause as such is not open to question. The fair and reasonable landlord test is applicable only to the particular circumstances in which a landlord seeks to rely on the clause (see paragraph 4.12).

Subsection (3) gives guidance as to how the fair and reasonable landlord test may be applied in circumstances which involve a remediable breach of the tenant's obligations under the lease. It is not intended to exclude the possibility that in certain circumstances it may be fair and reasonable for a landlord to resort to irritancy without offering the tenant an opportunity to remedy the relevant breach (see paragraph 4.15).

Transitional and supplementary provisions

3.—(1) Where circumstances have occurred before the commencement of this Act which would have entitled a landlord to terminate a lease in reliance on a provision in the lease or on the ground that the circumstances constituted a material breach of contract, but the landlord has not before such commencement given written notice to the tenant of his intention to terminate the lease in respect of those circumstances, he shall be entitled to terminate the lease in respect of those circumstances only in accordance with the provisions of this Act.

(2) Nothing in this Act shall apply in relation to any payment which has to be made, or any other condition which has to be fulfilled, before a tenant is entitled to entry under a lease.

(3) The parties to a lease shall not be entitled to disapply any provision of this Act from it.

Clause 3 contains supplementary provisions designed to ensure that the protection introduced by the Bill is fully effective and to clarify the type of situation to which it applies.

Subsection (1) implements Recommendation 6. It applies the substantive provisions of the Bill to all relevant leases (see the definition of "lease" in clause 4), regardless of their date (see paragraphs 4.1 and 7.3). However a saving is made for those cases where a landlord has, prior to the commencement date of the legislation, given notice to the tenant of his intention to terminate the lease, whether on the basis of a conventional irritancy clause or of the latter's breach of contract (see paragraph 7.3).

Subsection (2) restricts the application of the Bill to irritancy during the currency of a lease, by excluding from its scope any action by landlords in respect of conditions requiring to be fulfilled prior to entry being taken (see paragraph 4.19).

Subsection (3) implements Recommendation 7. It prevents contracting out of the new legislative provisions (see paragraph 7.4).

Definition of lease.

4.—(1) In this Act "lease" means a lease of land, whether entered into before or after the commencement of this Act, but does not include a lease of land—

(*a*) used wholly or mainly for residential purposes; or

(*b*) comprising a croft, the subject of a cottar or the holding of a landholder or a statutory small tenant.

(2) In subsection (1) above—

"cottar" has the same meaning as in section 28(4) of the Crofters (Scotland) Act 1955;

"croft" has the same meaning as in section 3 of the Crofters (Scotland) Act 1955; and

"holding", "landholder" and "statutory small tenant" have the same meanings as in the Small Landholders (Scotland) Acts 1886 to 1931.

Clause 4 defines "lease" in terms of the Commission's reference (see paragraph 1.3). Residential leases are the principal category of lease falling outwith the scope of the Bill.

Short title, commencement and extent.

5.—(1) This Act may be cited as the Irritancies in Leases (Scotland) Act 1983.

(2) This Act shall come into force at the end of the period of two months beginning with the day on which it is passed.

(3) This Act extends to Scotland only.

APPENDIX B

List of those who submitted written comments on Memorandum No. 52.

James T. Aitken, Assistant Secretary, North of Scotland Hydro-Electric Board
J. Alexander
C. A. J. Beckett, Chartered Surveyor
Professor Robert Black
William Brown, S.S.C.
James M. Burnett, Chartered Surveyor
Miss Barbara D. Clegg, Senior Solicitor, Renfrew District Council
E. Clucas, Depute Secretary and Legal Adviser, East Kilbride Development Corporation
Committee of Scottish Clearing Bankers
R. Craig Connal, Solicitor
Faculty of Law, University of Glasgow
W. T. Fraser, Solicitor
J. Hunter, Senior Town Clerk Depute, City of Glasgow District Council
Professor J. A. M. Inglis
Investment Protection Committee, British Insurance Association
Law Society of Scotland
W. O. Lunn, Solicitor to Strathclyde Regional Council
Ian J. Miller, Director of Law and Administration, Grampian Regional Council
Alexander B. Mitchell, Solicitor
John W. Morris, Secretary and Legal Adviser, Cumbernauld Development Corporation
W. H. Page, Chartered Surveyor
A. I. Phillips, Editor, "Journal of the Law Society of Scotland"
Roy Roxburgh, Solicitor
Scottish Development Agency
Scottish Law Agents Society
David Semple, Solicitor
P. C. Shanks, Secretary and Solicitor, Forth Ports Authority
Sheriffs' Association
Sheriffs Principal
Society of Writers to the Signet
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