HERBERT SMITH FREEHILLS

COURT OF APPEAL DISMISSES 'COVID DEFENCE' AGAINST CINEMA'S RENT ARREARS

07 September 2022 | London
Legal Briefings

The decision will be welcomed by landlords seeking recoveries but reminds tenants of their financial obligations

The Court of Appeal has dismissed appeals against the grant of summary judgment to commercial landlords for payment of accrued rent in two cases where the relevant premises (in each case operated as cinemas) had to be closed for extended periods due to Covid restrictions: *Bank of New York Mellon (International) Ltd v Cine-UK Ltd; London Trocadero (2015) LLP v Picturehouse Cinemas Ltd and others* [2022] EWCA Civ 1021.

The decision serves as a reminder of the high threshold for implying contractual terms, namely where it is necessary to give business efficacy or so obvious as to go without saying. As the court commented, the scope for implication is particularly limited where the contracts in question are detailed documents prepared by lawyers.

It also illustrates a claim based on unjust enrichment (such as here for total failure of consideration, or “failure of basis”) will not be available where this is inconsistent with the express terms of the contract.

The court rejected an argument that, as the restrictive legislation introduced to address the Covid pandemic was “unprecedented”, it was appropriate for the court to consider applying the law in a fresh light. Even if the legislation were unprecedented (which the court said was debateable) that was no reason to disregard or disapply fundamental principles of the law of contract or to extend the law of unjust enrichment beyond its proper bounds.

In light of its conclusion, the court found it unnecessary to decide the issues of whether, if the basis for the obligation to pay rent was the ability to lawfully use the premises as cinemas: (i) that basis did fail totally; and (ii) the obligation to pay rent could be apportioned so that there was a total failure of basis during the periods when the premises could not lawfully be used as cinemas. These questions had been decided *obiter* in favour of the defendants at first instance, but as they did not arise the Court of Appeal preferred to express no view. The court noted particularly the issue of apportionment was a "potentially complex one which is better decided in a case where it is critical to the determination of the issues on appeal and not merely *obiter*."

BACKGROUND

The background to the two underlying cases in these conjoined appeals is set out in our previous blog posts here and here.

In broad summary, in both cases the claimants were the landlords under leases for cinema premises and the defendants were tenants or guarantors under those leases. The claimants sought to recover arrears of rent for periods during which the premises were closed due to Covid restrictions.

The defendants argued that they were not liable for various reasons, including on the basis that: (i) terms should be implied into the leases to the effect that the obligations to pay rent were suspended during periods when the premises could not lawfully be used as cinemas; and/or (ii) there had been a total failure of consideration, or "failure of basis", in relation to such periods.

The High Court in both cases found that the defendants' arguments had no real prospect of success and accordingly granted the claimants summary judgment. The defendants appealed.

DECISION

The Court of Appeal dismissed the appeals in both cases. Sir Julian Flaux (Chancellor) gave the leading judgment, with which Snowden LJ and Sir Nicholas Patten agreed.

Implied terms

The court referred to the restatement and summary of the law on implication of terms in *Yoo Design Services Ltd v Iliv Realty Pte Ltd* [2021] EWCA Civ 560 (which itself relied on the leading authority of *Marks & Spencer Plc v BNP Paribas Securities Services* [2016] AC 742, considered here). The two tests for the implication of a term are that, on an objective assessment, the term is:

1. necessary to give business efficacy to the contract, in that the contract would lack commercial or practical coherence without it; or

2. so obvious as to go without saying.

The court found that none of the implied terms contended for in the either of these cases satisfied either the test of necessity or obviousness.

With regards to the test of necessity, the court noted that the leases "work perfectly well without the implied terms" and so there was no lack of commercial or practical coherence without them. The leases allocated the risk that the leased premises could not be lawfully operated as cinemas to the tenants in circumstances where, as in the present case, the rent cesser provisions (which suspended liability to pay rent in the case of physical damage or destruction rendering the premises unfit for occupation or use) did not apply.

As to the test of obviousness, the court found that the terms which were sought to be implied did not meet the requirements of the test. If the officious bystander had asked whether the parties intended that the rent obligations were to be suspended if the premises could not be used lawfully, the response would be "far from a testy 'of course' from both parties".

Referring to the comment of Carr LJ in *Yoo Design* that the test for implication is a stringent one, the court held that it was nowhere near satisfied in these cases. Further, the proposed terms would be inconsistent with the express terms of the leases, as they would reallocate the agreed allocation of risk, and so they could not be implied for that reason also.

Failure of basis

In considering the arguments on failure of basis (which is a species of unjust enrichment), the court began by noting the comments made by Carr LJ in *Dargamo Holdings Ltd v Avonwick Holding Ltd* [2021] EWCA Civ 1149 to the effect that it would be a very rare case in which such a case could be made out despite the existence and performance of a valid contract. One such exception, as identified in *Avonwick,* is where unjust enrichment fills a "gap" in a contract, such that a claim in unjust enrichment is complementary to and does not contradict the terms of the relevant contract.

The defendants argued that the common understanding or assumption that the premises could be used lawfully as cinemas was a fundamental basis for the obligation to pay rent, and that basis had failed. However, the court considered that the basis for the obligation to pay rent under the leases was the demise of the premises for a 35-year term and that the defendants' contention regarding the fundamental basis of the leases was inconsistent with the express terms of, and the allocation of risk under, the leases. The leases contained a careful contractual regime for the allocation of risk. This included the rent cesser provisions which were complete codes as to the circumstances in which the obligations to pay rent were to be suspended, namely where there was physical damage or destruction of the premises.

Therefore, there was no gap in the leases to be filled and no scope for the operation of the law of unjust enrichment.

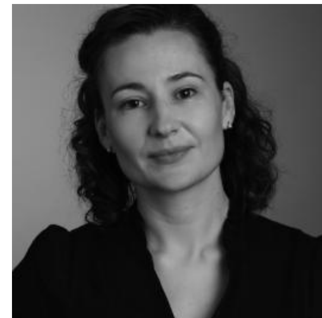
KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

MARTIN HEVEY
SENIOR ASSOCIATE, LONDON
+44 20 7466 2631
Martin.Hevey@hsf.com

STEVEN CHUA
ASSOCIATE, LONDON
+44 20 7466 2364
steven.chua@hsf.com

MATTHEW BONYE
PARTNER, LONDON
+44 20 7466 2162
Matthew.Bonye@hsf.com



SHANNA DAVISON
PROFESSIONAL SUPPORT LAWYER, LONDON
+44 20 7466 7561
shanna.davison@hsf.com

LEGAL NOTICE

The contents of this publication are for reference purposes only and may not be current as at the date of accessing this publication. They do not constitute legal advice and should not be relied upon as such. Specific legal advice about your specific circumstances should always be sought separately before taking any action based on this publication.

© Herbert Smith Freehills 2022

SUBSCRIBE TO STAY UP-TO-DATE WITH INSIGHTS, LEGAL UPDATES, EVENTS, AND MORE
Close

© HERBERT SMITH FREEHILLS LLP 2022