FRUSTRATION OF LEASES – THE HAZARDS OF CONTRACTUALISATION¹

Warren Barr, Lecturer, School of Law, University of Liverpool

The introduction of the doctrine of frustration to leases by the House of Lords in *National Carriers Limited* v *Panalpina (Northern) Limited* ² has been well documented³, and is symptomatic of an increasing tendency throughout the common law world to emphasise the contractual nature of the lease over the proprietary aspect⁴. However, frustrating a lease remains a possibility rather than a reality for British landlords and tenants, as, at the time of writing, a lease has yet to be terminated by frustration. In the nineteen years since *Panalpina*, the question of frustration has arisen only twice in reported cases⁵, and the discussion was *obiter* in both.

The task facing any member of the judiciary faced with an actionable leasehold frustration is not an enviable one, as the boundaries of frustration have yet to be set; so much so that no judicial consideration has been given to the actual mechanics by which frustration will terminate a lease. It will be shown that there are a number of potential hazards in this area, which may undermine the operation of the doctrine in landlord-tenant law, and that the doctrine may not operate as expected by their Lordships in *Panalpina*. It will be submitted that the solution to many of these dangers, in the absence of statutory intervention, lies in the dual device of viewing the lease as primarily a property relationship and applying a sub-species of frustration which allows for lawful excuse for non-performance of covenants. Contractualisation of the lease is to be resisted.

¹ This article is not concerned with issues arising out of privatisation, in which the term "contractualisation" is used in a general sense. The term is employed here to describe the "sea change" in legal thinking concerning the legal principles regulating the term of years, from traditional property to general contractual principles.

² [1981] 2 AC 45.

³ See, for example, Treitel, *Frustration and Force Majeure* (1994); Wilkinson. "Frustration of Leases" (1981) 131 NLJ 189.

⁴ This process is known as the 'contractualisation' of leases. It is trite law that a lease has a duality of legal character, as it is both a contract and grants an estate in land, yet, as will be discussed *infra*, in modern practice the contractual covenants are often viewed by the parties as more significant than the estate interest. This has lead to the application of contractual principles to the regulation of the landlord and tenant relationship. For a succinct and balanced discussion of this phenomenon at home and abroad see Bright and Gilbert, *The Nature of Tenancies* (1995) pp 69-120.

⁵ Holbeck Hall Hotel Ltd v Scarborough BC [1997] 2 EGLR 213, where no ruling was obtained on whether a business tenancy was ended by frustration when coastal erosion caused the demised building to fall into the sea. See also Prince v Robinson (1999) 31 HLR 89, in which frustration was mentioned in a case relating to a Rent Act protected tenancy, which was decided on other grounds.

THE APPLICATION OF FRUSTRATION TO LEASES

In the years before *Panalpina*, frustration was held inapplicable to leases, as the lease granted an estate, and this conveyance of the legal estate was the essence of the bargain agreed between landlord and tenant, so that was not affected by most supervening events. A typical example is *London & Northern Estates Co v Schlesinger*⁶, where an Austrian defendant who claimed that his lease of a flat had been discharged by frustration of purpose in 1914, because he had been prohibited from residing there as an alien enemy, was denied relief as Lush J considered that:

"It is not correct to speak of this tenancy agreement as a contract and nothing more. A term of years was created by it and vested in the appellant, and I can see no reason for saying that because this order disqualified him from personally residing in the flat, it affected the chattel interest which was vested in him by virtue of the agreement. In my opinion, it is vested in him still".

This reasoning may have been technically compelling, but on first reading it does not accord with the modern reality of many lettings by lease. It is undeniable that in many commercial and residential leases, it is the leasehold covenants entered into by the parties which are considered to be of paramount importance. It is the covenants which regulate the use of the demised property and impose obligations on the parties; the grant of an estate may be viewed as largely incidental to the parties' purposes.

This viewpoint, whatever the merits, clearly impressed their Lordships in *National Carriers Limited* v *Panalpina (Northern) Limited* ⁸, in which they held, Lord Russell dissenting, that while a lease would "hardly ever" be discharged by frustration, there was no authority "to erect a total barrier inscribed 'You shall not pass'" ¹⁰. The majority rejected the argument that the conveyance of the estate was the essence of the bargain between landlord and tenant, asserting that such a proposition ignored the commercial realities underlying the transaction:

"However much weight one may give to the fact that a lease creates an estate in land in favour of the lessee, in truth it is by no means always in that estate in land in which the lessee is interested. In many cases he is interested only in the accompanying contractual right to use that which is demised to

⁶ [1916] 1 KB 20.

Ibid at 24; subsequently approved by Earl of Reading CJ in Whitehall Court Ltd v Ettlinger [1920] 1 KB 681 at 686, where he too denied relief to a dispossessed tenant of flats as he could "see no reason why the chattel interest which was vested in the tenant by virtue of the two leases was affected merely because he was personally prevented from residing in the flats". The same reasoning was also in evidence in both the Court of Appeal's decision in Matthew v Curling [1922] 2 AC 180 (CA) per Bankes LJ and Younger LJ. The House of Lords decided the appeal on different grounds, but did not doubt the opinion of the lower court.

⁸ [1981] 2 AC 45.

⁹ *Ibid* at 52H *per* Lord Hailsham.

¹⁰ *Ibid* at 59F *per* Lord Wilberforce.

him by the lease, and the estate in land which he acquires has little or no meaning for him". 11

The dictum of Laskin J in the Canadian case of *Highway Properties Limited* v *Kelly, Douglas & Co Limited* ¹², which warned against separating leases from other commercial contracts, was also considered highly persuasive:

"It is no longer sensible to pretend that a commercial lease, such as the one before the court, is simply a conveyance and not also a contract. It is equally untenable to persist in denying resort to the full armoury of remedies ordinarily available to redress repudiation of covenants, merely because the covenants may be associated with an estate in land."

Their Lordships involved themselves in an extensive review of previous authority and considered the arguments against the application of frustration to leases. They were struck by the commercial situations in which frustration had been held to apply, which they felt were analogous to the concept of the lease, namely demise charters of ships¹³, agreements for leases¹⁴ and licences to occupy land¹⁵. Accordingly, to "place leases of land beyond a firm line of exclusion seems to involve anomalies, to invite fine distinctions, or at least to produce perplexities."¹⁶

Lord Simon said, in relation to demise charters of ships:

"On the other hand, to deny the application of the doctrine would create an anomalous distinction between the charter of a ship by demise. . . and a demise of land: compare, for example, a short lease of an oil storage tank and a demise charter for the same term of an oil tanker of a peculiar class to serve such a storage tank, and a supervening event then frustrating the demise charter and equally affecting the use of the oil storage tank. Again, a time charter has much in common with a service tenancy of furnished accommodation . . . But most strikingly of all is the fact that the doctrine of frustration undoubtedly applies to a licence to occupy land . . ."¹⁷.

A further argument put before their Lordships was that a lease, like a contract for the sale of land, vested a legal estate in the tenant on conveyance. It followed, therefore, that as property owner the tenant was in the same position as a freeholder in bearing the risk of any subsequent destruction or event affecting the land¹⁸. Lord Simon, in rejecting this

¹¹ *Ibid* at 76C per Lord Roskill.

^{12 17} DLR (3d) 710 at 721, a case dealing with the application of repudiatory breach to leases.

¹³ See Blane Steamships Ltd v Minister of Transport [1951] 2 KB 965.

¹⁴ See Denny, Mott & Dickinson Ltd v James Fraser Ltd [1944] AC 265 (HL).

¹⁵ See *Krell* v *Henry* [1903] 2 KB 740.

¹⁶ Panalpina op cit at 57E per Lord Wilberforce

¹⁷ Ibid at 64E/F

¹⁸ See Paine v Meller (1801) 6 Ves 349, where after a contract for the sale of land had been agreed it was held not to be capable of discharge, even though the premises were destroyed before the completion of the conveyance as the risk of

submission, refused to view a lease and a contract for the sale as analogous concepts:

"Moreover, the sale of land is a false analogy. A fully executed contract cannot be frustrated; and a sale of land is characteristically such a contract. But a lease is partly executory: rights and obligations remain outstanding on both sides throughout its currency. Even a partly executed contract is susceptible of frustration in so far as it remains executory: there are many such cases in the books."

Having dispensed with the arguments against the applicability of frustration to leases, their Lordships turned to the question of its operation. Lord Hailsham considered that the operation of frustration, by means of an implied term in the lease to cover supervening events, was not problematic as leases generally contained provisions allowing them to be terminated before the term date:

"... Seeing that the instrument as a rule expressly provides for the lease being determined at the option of the lessor upon the happening of certain specified events, I see no logical absurdity in implying a term that it shall be determined absolutely on the happening of other events — namely, those which in an ordinary contract would work frustration." ²⁰

The Lordships also opined that the introduction of the doctrine would not open the floodgates to litigation since it would rarely be successful and be rarely used:

"It is the difference immortalised in *H.M.S. Pinafore* between "never" and "hardly ever," . . . though. . . the doctrine [is] applicable in principle to leases, the cases in which it could properly be applied must be extremely rare."²¹

It is submitted that this decision is regrettable, for a number of reasons. Their Lordships were so intent in holding that frustration would be applicable to leases, no doubt in what they believed to be the interests of justice, that they failed to give due consideration to whether it *should* apply to leases. They saw the contractualisation of the lease as a universal panacea for the problems created by supervening change in this area. In doing so, they failed to properly consider the method by which frustration could destroy the lease, and indeed if it was possible for it to do so. Indeed, their reasoning is much less compelling than it at first appears.

such events had passed to the purchaser as owner of the land. In this case the equitable proprietary interest vested in the purchaser was sufficient to identify him as purchaser.

¹⁹ *Ibid* at 68D.

²⁰ Panalpina op cit at 55E, approving a dictum of Aitken LJ (dissenting) in Matthew v Curling [1922] 2 AC 180 at 199.

²¹ *Ibid* at 52H.

IS THERE A NEED FOR FRUSTRATION IN LANDLORD-TENANT LAW?

It is clear that there may be exceptional circumstances where frustration or a similar, more adaptable right might make sense. *Matthew* v *Curling*²², for example, is a very exceptional set of facts in which it might be felt that the tenant was treated harshly. The tenant had covenanted, *inter alia*, to insure the demised premises, and to expend the insurance money on rebuilding if the demised premises were destroyed by fire at any time during the currency of the term. The demised premises were requisitioned by military authorities and subsequently destroyed by fire. The tenant was held liable to pay rent and reinstate the premises. The tenant was unable to make use of the existing legislation for compensation due to a technicality and it appears that the insurance company also refused to make a payment on this basis. The tenant was therefore put to considerable expense to rebuild premises which had been destroyed through no fault of his own, and which he had no right to occupy.

It is doubtful, however, that frustration would improve the lot of the tenant in this situation, since the term had a reasonable amount of time left to run. In *Panalpina* itself, the length of the disruption set against the length of the term was important in the finding that the lease in that case had not been frustrated – five years out of a ten year term was not considered sufficient interruption. A right to vary the terms of the agreement or to abate the rent would be more satisfactory, since the tenant may wish to retain his proprietary asset. If the rental obligation is suspended while the reinstatement was to take place, this would relieve the burden on the tenant. This is not possible with frustration. It must also be remembered that this particular set of facts is unlikely to arise again, being so exceptional. Modern compensatory legislation is also generally better drafted and benefits from being drafted to remedy a particular wrong or meet a particular set of needs.

It must also be considered that, especially in the commercial sphere, landlords and tenants are usually better advised than most contractual parties, and may well have allocated the risk of certain supervening events by either express covenants allowing for termination, or by insurance means. The presence of notices to quit might also allow the parties to terminate the transaction and escape, without the need for frustration. Nevertheless, such clauses are not universal, especially in residential leases where the balance of power usually lies firmly with the landlord.

The application of frustration to leases may be limited by an even more fundamental issue than those already outlined. In most cases of frustration, the plea of a tenant or landlord will be that the purpose of the transaction has been frustrated. Although English law was the first to recognise frustration of purpose in the case of *Krell* v *Henry*, Treitel²³ opines that the courts have been very reluctant to apply it since. Broadly, pleading frustration of purpose will not succeed, unless some common object agreed between the

²² [1922] 2 AC 180.

²³ Treitel Frustration and Force Majeure passim.

parties has been radically altered²⁴. Even if this is successful, the court will not discharge the contract if some other contractual purpose may be performed, provided that purpose is not wholly trivial. In *London & Northern Estates Company* v *Schlesinger*, for example, the fact that the tenant could not reside in the premises would not have been a sufficient ground to discharge the contract, as he would still have been able to assign or sub-let his interest to someone who could. It is submitted that their Lordships in *Panalpina* may have confused the position in English law with that under American law. Lord Wilberforce cited a passage from *Corbin, Contracts* with approval:

"Many short-term leases have been made, in which the purpose of the lessee was to conduct a liquor saloon, a purpose known to the lessor and one which gave to the premises a large part of its rental value. Then followed the enactment of a. . . prohibitory law preventing the use of the premises for the expected purpose. . . The prohibition law. . . frustrates the purpose of using the premises for a liquor saloon in the reasonable hope of pecuniary profit. . . "25.

It is submitted that under the English law of frustration, unless perhaps the lease contained a user covenant restricting the use of the premises to the particular use prohibited or made it otherwise unachievable, there would be no frustration of purpose in a similar situation, as the premises would be available for some other purpose.

Hence, frustration will, as their Lordships opine, probably operate only in the rarest of circumstances. This makes the introduction of the doctrine all the more objectionable, when one considers the difficulties which may arise in cases where the doctrine operates.

HAZARDS OF FRUSTRATION

1. Frustration discharges a contract automatically

The effect of frustration is to bring about the automatic discharge of the contract in question from the time it was frustrated²⁶. The doctrine is not discretionary and may be pleaded by any party to the contract²⁷. This may promote rather than suppress injustice, as it has a special venom when applied to the landlord and tenant relationship. Termination may occur where the tenant does not himself wish to raise the plea of frustration and is happy to continue paying the rent notwithstanding the events which have occurred, but the landlord wants the property back. The landlord has, in effect, an additional right akin to forfeiture, without the fetters of relief against the action.

²⁴ See, for example, Conigrex SARL v Tradex Export SA [1983] 1 Lloyd's Rep 250 at 253

²⁵ Corbin Vol 6 (1951) s1356, cited in Panalpina op cit at 59A/B.

An exception to this rule is where the contractual obligation is severable, part may be discharged and part remain in force – See *The Nema* [1982] AC 724 (HL).

²⁷ See Hirji Mulji v Cheong Yue SS Co Ltd [1926] AC 497, PC.

This is not a theoretical problem. In *John Lewis Properties plc* v *Viscount Chelsea*²⁸, the tenants wished to put forward an argument, based on *dicta* in *Bailey* v *De Crespigny*²⁹, that they had a lawful excuse for the nonperformance of a building covenant in their lease due to supervening events. The landlord threatened to counter-claim that the entire lease had been frustrated, on the basis that the requirements necessary to prove a lawful excuse would also have been sufficient to prove frustration of the covenant, which would have ended the whole of the lease. It is highly questionable whether such a claim would have met with any success. Nevertheless, the tenants, who risked losing the whole of their property asset, withdrew the argument. The landlord was effectively able to use the consequences of frustration as a bullying tactic against the tenants.

This unconscionable use of frustration may be especially worrying for tenants who hold as business tenants under the provisions of the Landlord and Tenant Act 1954. It may, without appropriate judicial care, allow the landlord to deprive the tenant of his entitlement to a new tenancy agreement as of right, in cases where the tenant would have merely wished an excuse for non-performance of the affected covenant, or to have paid the rent rather than lose his asset. It is true that the tenant in that situation would be able to agree a new tenancy with the landlord. However, the resulting tenancy would be on less favourable terms than a tenancy as of right, because in the latter situation the court can fix the terms if the parties themselves cannot agree on them, which gives a basis for negotiation between the parties.

2. Frustration is inflexible, and is less effective than other methods of dealing with supervening events

Frustration does not allow for the abatement of the rental obligation or the variation of the terms of the lease. Accordingly, where the premises are destroyed or rendered uninhabitable and the obligation is on the landlord to repair, frustration offers no solution to the tenant having to continue to pay the full rent because he will still have the legal estate, nor will it force landlords to renegotiate single-user clauses. It offers one solution and one solution only: the dissolution of the legal relationship between the parties.

In stark contrast, where a statute covers the supervening event the remedies offered are infinitely superior to those at common law. An excellent example is the Landlord and Tenant (War Damage) Act 1939. Where damage has been caused by war, section 1 of the 1939 Act relieves the tenant from any obligation to perform any repairing covenants in the lease. Moreover, there is no problem with the tenant having to pay rent for premises he does not wish to use. Section 4 gives the tenant the power to choose between disclaiming the lease or retaining it. If he chooses the latter option, as for example where the lease is highly profitable and is still of useful duration, he has to reinstate the premises, though he will not be required to pay rent until he has done so.

²⁸ [1994] 67 P & CR 120

²⁹ (1869) LR 4 QB 180, which suggests that it may be possible to suspend a single covenant in a lease, or have the frustrating event act as a lawful excuse for the non-performance of the covenant. This situation, including the *John Lewis* case, is discussed, *infra*.

Sensible interpretation of legislation can stop it being used to the advantage of a particular party. In *Cussack-Smith* v *London Corporation*³⁰, the ultimate tenants by virtue of Town Planning legislation, tried to secure the use of the demised estate without paying rent. They served a notice on the landlord under the Landlord and Tenant (War Damage) Act 1939 that they intended to retain the lease, although they knew that the plot could not in fact be so developed. Stable J held that the service of the notice was a nullity, as this is not what the legislature could have intended when drafting the Act.

3. Frustration may not be able to bring about the termination of the estate

Perhaps the most significant concern is the question of how frustration will dismantle the leasehold tenancy. The position will depend upon the application, or otherwise, of the Law Reform (Frustrated Contracts) Act 1943. It might be thought that there could be no reason for holding the Act inapplicable to the lease. However, in *Pioneer Shipping Limited* v *B.T.P. Trioxide Limited* ³¹, it was held inapplicable to voyage charter parties, which their Lordships in *Panalpina* considered to be analogous to leases, and the language of the Act does not seem appropriate to the landlord and tenant relationship. Both positions are clearly worthy of consideration.

If the Act does not apply, E O Walford summarises the position succinctly:

- ". . . frustration of the lease would produce the following result: -
- (a) The lessee would retain the benefit of the term granted by the lease, for it is now well settled that frustration does not entitle either party to recover any benefit properly acquired by the other party pursuant to the contract prior to the date of the frustrating event. . .
- (b) Although the lessee would retain the benefit of the lease he would not be liable to pay any rent becoming due during the remainder of the term.
- (c) The lessee would also be discharged from liability to perform any other obligations due to be performed after. . . the frustrating event."³²

The reason in this situation that the estate would remain vested in the tenant is that a party is not entitled to recover properly accrued benefits unless there has been a total failure of consideration³³, which there will not have been in the case of a lease, as the tenant will have had the benefit of the estate and suffered the detriment of paying rent.

³⁰ [1956] QB 1308.

³¹ [1980] 3 All ER 117

^{32 &}quot;Impossibility and Property Law" [1941] 57 LQR 339.

³³ Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd [1943] AC 32, where there had been a total failure of consideration because the buyers never received delivery of the products ordered in the contract due to the interference of a supervening event after the contract had been agreed but before delivery.

This fortunate tenant would remain the recipient of the term, and would be at liberty to use it as he pleased, free from any contractual covenants he had entered into, until it was terminated by effluxion of time. The tenant's conduct could cause extreme damage to the value of the reversion, and the landlord may have to stand by, powerless, as he watched his reversion fall into ruin, or be gutted by fire. In the majority of cases, it would be cold comfort indeed that he too would be released from any obligations under the lease, especially since he would lose his right to any rental income from the premises³⁴.

The tenant may also be disadvantaged if frustration occurs. He might have paid a large premium for the lease, disguised as a once and for all service charge, because the landlord had covenanted to keep it in repair, which he will not now have the benefit of nor will the premium be returned to him.

This is a highly undesirable position, and it is suggested that their Lordships must have expected the Law Reform (Frustrated Contracts) Act 1943 to apply to leases. In essence, section 1(2) of the Act provides that all sums payable before the frustrating event cease to be payable; that sums already paid under the contract are recoverable; and that the court has discretionary powers to allow expenses incurred in the performance of the contract by the payee to be set off against the sums paid or payable.

If the lease is viewed simply as a contract, then the estate would come to an end and the landlord would get the demised premises back, as sums already paid are recoverable. Beyond that, however, the position is uncertain. As H M Wilkinson³⁵ points out:

"It is easy to say that the tenant must give up possession and can cease to pay rent but... what is the position of sub-lessees or of mortgagees? If a premium has been paid is it to be returned in full or will the court apportion it according to the length of time enjoyed by the tenant?... What if the tenant has improved the property and could claim a payment for enhancement from the landlord at the end of the term. Does an earlier frustrating event cancel his right to claim?".

Moreover, Jeffrey Price³⁶ asks what the position will be where the premises have been let at a rent higher than the market value. It seems that the landlord will be forced to disgorge the rent paid, and will only get the value in return (by way of set-off) which is therefore likely to be less.

It is submitted that there may be a more fundamental problem – namely, that even if the Law Reform (Frustrated Contracts) Act 1943 applies, there is a question whether frustration, as a contractual doctrine, can actually operate to bring about the destruction of the estate.

³⁴ It is submitted that this is only possible where the lease is viewed purely as a contract, since rent is a dual obligation, both contractual by covenant and proprietary as an incorporeal property right, which is an incident of the estate and compensation for the granting of the estate. The discharge of the contractual aspect will therefore not affect the proprietary obligation. See *infra* p 92.

 ^{(1981) 131} NLJ 189 at 191
"The Doctrine of Frustration and Leases" (1989) 10 JLH 90 at 103.

This is the suggestion that in the hybrid relationship of contract and property law which the lease represents, it is the property element which is the ascendant and governing aspect. This is so because the proprietary estate is the essential element which transforms an otherwise commercial contract into a lease; it is the defining element which separates the lease from a contractual licence to occupy and, being an interest limited in time, from ownership of the fee simple absolute. The estate describes the parcels of land demised, and the duration of the holding. The relational contract element, on the other hand, is a creative subsidiary which works within the discipline of the estate and regulates the use to which the parties may put the estate. Its lifetime is strictly co-extensive with that of the estate, and it may not destroy the estate. This is so, even though on the surface it may look to be of more importance than the proprietary aspect of the arrangement.

When a legal estate is vested in the tenant by the completion of the conveyance, what he receives is "a time in the land, or land for a time" 37. He has been given exclusive possession of the demised parcels of land in a unitary block of land, subject to a right in the landlord to get the land back and to compensation in the form of rent for the loss of his right to possess the parcels, called the reversion. Once the lease has run its course the estate is destroyed and the demised parcels are returned to the landlord. The concept of the estate is elastic enough to encapsulate the right of the landlord to get the parcels back at the fixed term date or at any other. Accordingly, where he has a right of forfeiture reserved to him for breach of covenant, it is inherent to the nature of the estate granted that it may be ended at any time. Similarly, where the tenant is given a "break" clause in a lease, which is exercised in the form of a notice to quit, it is not evidence of a contractual right bringing about the destruction of the estate: the right to get out of the lease at any time is inherent to the nature of the estate granted so that when it is exercised, it destroys the lease as if the term date had been reached. The right has also been granted by the landlord as holder of the reversion, since it is his right to give.

Therefore, it is suggested that the contractual doctrine of frustration when it applies to leases will discharge the contractual side of the relationship, not the estate which it has no power to do. It is not a matter of whether the lease is executed or executory, as their Lordships suggest in *Panalpina* – it is the simple proposition that only a right reserved in the time-fixing formula of the estate can successfully destroy it; the estate can survive the destruction of the contract. This has been recognised to an extent by the Australian judiciary in relation to a right to terminate the lease for repudiatory breach, which they have opined may only exist where there is a right to forfeiture³⁸.

In *Panalpina*, their Lordships had suggested that since a right to end the lease prematurely exists within many leases there is no logical absurdity in implying a right to end the lease by frustration. However, this misses the issue that in all other cases the right to terminate is linked to the nature of the estate granted and the right of the landlord to get back that which has been

³⁷ Walsingham's Case (1573) 2 Plowden 547 at 555.

³⁸ See Progressive Mailing v Tabali 57 ALR 609, see also see W Barr "Repudiation of Leases – A Fool's Paradise" at pp 331-334 in P Jackson and D Wilde (eds), Contemporary Property Law (1999).

granted. There is no proprietary basis for an implied term. It is a right of contract alone. This is different from the situation where the parties have inserted a *force majeure* clause. Such a clause would alter the *nature* of the estate granted to determine the estate on the specified event agreed between the parties to the lease. There is no contractual implication of a term in these circumstances.

It is submitted that their Lordships were, with respect, in error to hold that frustration could apply to a lease on property terms. The effect of frustration would be to destroy the contract, but the estate would remain vested in the tenant. The position would be the same as that already outlined where, under a purely contractual analysis, the Law Reform (Frustrated Contracts) Act 1943 does not apply, with one notable difference: the tenant would still be liable to pay the rent reserved in the lease.

This is due to the dual nature of the rental obligation. Traditionally, rent payments were viewed as compensation for the loss by the landlord of his right to possess the demised land, and were considered an incident of the estate in land. The penchant for contractualisation of the lease led to the view, expressed by Lord Diplock, that rent is contractual consideration, "a payment which a tenant is bound by his contract to pay to the landlord for the use of his land"³⁹.

Nevertheless, as Troman notes⁴⁰, though the latter view has overtaken the traditional view, it had not extinguished it. It is still common practice in the drafting of leases to include both a reservation of rent in the reddendum, which will include the words "yielding and paying" and an express covenant from the tenant to pay rent. It is submitted that the right to rent is in itself an incorporeal right of property which is reserved to the landlord. The covenant sets the amount, which is then imprinted on the incorporeal right which is itself attached to the estate. On this basis, when the contract is discharged, the rental obligation remains at the level set by the covenant for the duration of the term so long as the estate remains. The landlord may even be entitled to the remedy of distress, if the tenant refused to pay⁴¹.

4. Other problems with the reasoning in *Panalpina*

The reasoning of their Lordships is, with respect, difficult to defend on a conceptual basis, especially given the dangers illustrated with an actionable frustration.

It was suggested that the lease was executory since contractual covenants remained to be fulfilled throughout the duration of the term. It is submitted that this ignores the essential basic fact that the right of possession (and property) which the landlord gives to the tenant passes as a unitary block. The contractual covenants are completely separate and do not transform the lease into something it is not, since they are subject to the estate. This does not ignore the commercial realities of the leasehold transaction, indeed it gives effect to the ultimate commercial reality which is that the parties have agreed a lease not a licence, and as such the tenant has become the property

⁴¹ See *Bradsham* v *Pawley* [1980] 1 WLR 10.

³⁹ United Scientific Holdings Ltd v Burnley B C [1978] AC 904 at 935.

⁴⁰ S. Troman Commercial Leases (1987).

owner with the attendant disadvantages and benefits which that classification brings, which includes the realisation that the majority of supervening events will not alter the fact that they are property owners. Similarly, the risk inherent in property ownership does pass to the tenant, unless it is otherwise divested in the terms of the lease, since he is the owner:

"Under the bargain between lessor and lessee the land for the term has passed from the lessor to the lessee, with all its advantages and disadvantages. . . If a principle of achieving justice be anywhere at the root of the principle of frustration, I ask myself why should justice require that a useless site be returned to the lessor rather than remain the property of the lessee?"

The argument that simply because frustration applies to demise charters and agreements for leases it must apply to leases also lacks force. Demise charters and leases are not analogous concepts. The former is a complex, commercial hire-purchase arrangement, which grants a personal licence to use a ship, enforceable between the parties to the contract only. The lease grants a right of estate ownership, which may be bought and sold subject to any restrictions in the leasehold document imposed by the landlord as holder of the reversion. Land is not the same as a chattel – it is unique and irreplaceable. It is possible with the right materials to create more ships, it is not possible to create land. The courts have in the past realised that a distinction exists, and have held the doctrine applicable to one and not the other. By way of example, the principle of relief against a forfeiture action, applicable to leases, does not apply to a demise charter for a ship since the parties in that case do not enjoy proprietary or possessory rights, just a personal contract of services⁴³.

Similarly, there is no disparity in holding frustration applicable to an agreement for a lease, and not a legal lease. While it is trite law that an agreement for a lease confers an equitable estate in the prospective tenant, by virtue of the fact that it is specifically enforceable⁴⁴, this does not mean that an equitable estate and a legal estate are one and the same:

"The entitlements under an agreement for a lease are closely linked to the parties' entitlement to enforce the agreement by specific performance. Being an equitable remedy it is a discretionary remedy, and may be refused. . . The rule in *Walsh* v *Lonsdale* is *not* to be taken as destroying the difference between legal and equitable estates. The very basis of relief in the granting of specific performance is founded on the distinction between executory and executed contracts."⁴⁵

Since no legal estate has actually passed, there has as yet been no separation of the elements of the lease and it is simply a contract for the purposes of the application of contractual doctrine. This is illustrated in *Austerburry* v

⁴² Panalpina op cit per Lord Russell at 71C.

⁴³ See *The Scaptrade* [1983] 2 AC 694 at 702.

⁴⁴ Walsh v Lonsdale (1882) 21 Ch D 9.

⁴⁵ Robertson "Frustration of Leases: Who Bears The Risk?" (1982) 9 Syd L Rev 672.

Corporation of Oldham⁴⁶, where it was held that a landlord had no privity of estate to enforce obligations against an equitable assignee. Therefore, the contractual element is ascendant and may discharge the equitable estate. This is not so with the legal lease, where a full proprietary estate has been granted.

It remains to deal with the argument that the law should not draw a distinction between a lease and a licence in relation to the application of frustration. Lord Hailsham⁴⁷ opined that it would be anomalous if a lease of a holiday cottage were held not to be frustrated in circumstances where a licence of the same premises would be. The answer is simply that in the one case (lease) the tenant is the owner in law of the property, whereas in the other the occupier has a right to use the property. There is no anomaly. This might seem unnecessarily harsh and doctrinaire, but this article is not advocating that a tenant in such a situation should not have some remedy, just that frustration is not that remedy.

ALTERNATIVE METHODS OF DISCHARGE BY SUPERVENING EVENTS

Property law, as it stands, can deal with supervening destruction of the subject matter of the lease. This is because, quite simply, on a property based analysis, destruction of the estate by some vast convulsion of nature or by burial under the sea does not require any doctrine of frustration through impossibility to bring the tenant's obligations to an end. The destruction of the freehold reversion necessarily entails the end of the estate, which is a lesser interest granted out of it. In the words of Lord Russell⁴⁸:

"... of the total disappearance of the site... [as] a piece of terra firma... I would not need the intervention of the court to say that the term of years could not outlast the disappearance of its subject matter: the site would no longer have a freeholder lessor, and the obligation to pay rent, which issues out of the land, could not survive its substitution by the waves of the North Sea".

This is only so, of course, where the *parcels demised* cease to exist, not the buildings or other structures on those parcels. Thus, destruction of office premises on the demised land will not suffice by means of an earthquake or otherwise, since the parcels themselves will still exist. The *obiter dicta* in *Holbeck Hall Hotel Limited* v *Scarborough BC* add little of substance to this important point. What of other supervening events?

A COMMON LAW SOLUTION – PARTIAL FRUSTRATION?

It is suggested that many of the problems of supervening events may be dealt with satisfactorily by a principle developed in *John Lewis Properties Plc* v *Viscount Chelsea*⁴⁹, called "frustratory mitigation"⁵⁰, which it allows for the *de facto* suspension of contractual obligations, except rent.

⁴⁶ (1885) 29 Ch D 750.

⁴⁷ Panalpina op cit at 54G.

⁴⁸ *Ibid* at 71E.

⁴⁹ [1994] 67 P & CR 120.

The doctrine of frustratory mitigation arises from the judgment of Mummery J in *John Lewis Properties plc* v *Viscount Chelsea*⁵¹. John Lewis took three 999-year building leases from the landlords. The demised premises included the famous Mackmurdo building, and the leases contained covenants by John Lewis to demolish and redevelop the site in two phases, according to plans approved by the landlords. Before the second phase was completed, the Mackmurdo building was listed as a Grade II listed building. An application by John Lewis for listed building consent to build was withdrawn following an indication from the Council that it would not be granted. Viscount Chelsea, the person entitled to the reversion at the time of the action, sought to forfeit the lease for the failure of the tenants to carry out the building scheme.

In considering the landlord's claim for breach of covenant, Mummery J held that "there may exist lawful excuses for non-performance of building covenants short of full frustration" on the basis of *dicta* of Lord Russell in *Cricklewood*, where he said⁵³:

"It may well be that circumstances may arise during the currency of the term which render it difficult, or even impossible, for one party to carry out some of its obligations as landlord or tenant, circumstances which might afford a claim to damages for their breach, but the lease would remain. The estate in land would still be vested in the tenant".

After noting that in *Cricklewood*, the claim was for arrears of rent, and that no lawful excuse thus existed, he held that John Lewis had a lawful excuse in the instant case for failure to perform the building covenant. The effect of this lawful excuse was to suspend the covenant, not to discharge it:

There is no logical reason to believe that what may be applied to a building covenant may not be applied to any other covenant in a lease, except that to pay rent which is more than a mere covenant. Moreover, the existence of the doctrine is assured. In the nineteenth century case of *Bailey* v *De Crespigny*⁵⁴, a restrictive covenant entered into by the landlord not to permit building on a paddock adjoining the demised land, was discharged when the paddock was compulsorily acquired by a railway company. It is suggested that the current doctrine is really a development of that principle, which has evolved to the point that a covenant may *de facto* be held in abeyance, until such time as either the lease ends by effluxion of time or otherwise, or the covenant once again becomes capable of performance.

Frustratory mitigation avoids many of the practical and conceptual difficulties which would plague an actionable frustration. It permits the suspension of the contractual obligations without the need to discharge the estate, which the contractual entity cannot do. Moreover, it recognises that rent may not be discharged, as it is an incident of the estate.

⁵³ [1945] AC 221 at 234.

⁵⁰ See Morgan "Suspending Leasehold Covenants: A Doctrine of "Frustratory Mitigation" "[1995] Conv 74.

⁵¹ [1993] 67 P & CR 120.

⁵² *Ibid* at 132.

⁵⁴ (1869) LR 4 QB 180.

The standard required for the operation of the doctrine is also lower than the high threshold required for a successful action of frustration of purpose. It operates in circumstances less than frustration, and therefore the length of the prohibition or impossibility seems not to be of concern. In *John Lewis*, the lease had well over nine hundred years left to run.

The simple fact that it may be possible to suspend a number of covenants gives it an advantage over frustration, which must bring the whole contract to an end automatically. It is also suggested that the operation of the doctrine is not automatic at the behest of one party, by the very nature of the fact that it must be proved as a lawful excuse. Since it does not involve the discharge of the lease, the problems of apportioning payments and the demised premises does not arise.

Jill Morgan⁵⁵ suggests that the suspension of the lease in its entirety, including that of the obligation to pay rent, would make good sense. It is suggested that this would be impossible, given the nature of the rental obligation as only the contractual right to rent would be discharged. This accordingly might appear to deprive the remedy of some of its utility, since it would not help the plight of the tenant awaiting the reinstatement of premises or indeed the unfortunate tenant in the *Curling* case. It is submitted that a general right to abate rent would harm the landlord's position, since in most cases all he wants from his tenant and the tenancy is a guaranteed rental income stream, especially since he has given ownership of the property to the tenant in one unitary block not in a continuously flowing right dependent on the payment of the rental obligation. Moreover, it is submitted that specific legislation gives sufficient rights to the parties when it is deemed necessary to subvert the general rights of property. The tenant must accept the bad aspects as well as the good in owning property.

A more significant failing, however, is that where the landlord or tenant actually do wish to end the lease, it gives them no method of doing so. Unless there is an express term in the lease, or a break clause, the parties will be forced to keep the lease on foot even if they do not want to. This is most likely to effect residential tenants, due to their weak bargaining position.

Nevertheless, it is suggested that the principle of frustratory mitigation can be viewed as an evolution of the doctrine of frustration in the area of landlord and tenant law under property principles. Giving due consideration to the peculiar practices and complexities of legal relationships and drafting differing rules for them does not necessarily lead to the law being compartmentalised. It may in fact lead to a rule which is one evolutionary step beyond the original.

STATUTE

It might also be possible to supplement the gaps in frustratory mitigation by statutory enactment. The Law Commission have deliberated on the issue of the effect of supervening events and have come up with a proposal for termination, which is based upon intention, in the sense that the "purpose for which the tenancy was granted can no longer be fulfilled in accordance with

⁵⁵ Op cit at n 51.

the intentions of the parties."⁵⁶ It has the advantage that it works within the existing property law structure, by utilising surrender as the means of terminating an estate for supervening difficulties. Matters have come no further in the thirty-two years since the proposal was tabled, so it is perhaps a pious hope to think that such statutory enactment is possible.

CONCLUSION

The doctrine of frustration is ill-suited to use in landlord and tenant law. It is limited by practice and by principle, and the remedies it provides are clumsy and as capable of creating injustice as they are of achieving justice. More attractive alternatives exist along a property law route, by suspension of particular covenants through frustratory mitigation, or by the possible enactment of a statutory right for the tenant to surrender the lease in cases in certain supervening circumstances. Landlords and tenants, particularly in commercial lettings, would be well advised to circumvent frustration by the use of express clauses relating to common supervening events, if they do not already do so.

On a more general level, it is difficult to avoid the conclusion that the introduction of principles of contract law to the landlord and tenant relationship was ill-considered. It illustrates the need, on the part of reformers (judicial or otherwise), to think through the implications of the introduction of contractual doctrines in the landlord-tenant relationship, rather than simply seeing property law as outdated and in need of replacement.

In a sense, the stable door is being closed after the horse has bolted. Frustration is a reality, in spite of the attendant problems associated with it, and the reasoning of their Lordships has been used as justification to introduce other contractual principles, such as repudiatory breach.⁵⁷ However, if a subsequent court is willing to revisit the reasoning in *Panalpina*, and recognise that the contractual doctrine of frustration can only discharge the contractual element of a lease, the hazards of contractualisation might yet be avoided in relation to frustration of leases.

Law Commission Working Paper No16 Working Paper Proposals Relating To Termination of Tenancies Vol 2 (1968) Proposal 12.00.

For a review of the attendant difficulties caused by this doctrine, see the article by the author in "Repudiation of Leases – A Fool's Paradise" at pp 331-334 in P Jackson and D Wilde (eds), Contemporary Property Law (1999).