



Greening Make Good Australia



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Foreword

The built environment is one of the most critical areas in which we can reduce mankind's impact on our environment. RICS, being the world's largest property and construction organisation, has the obligation of using its reach and influence to bring about the changes that are needed.

RICS has produced this Guide to Greening Make Good to assist the property industry in reducing waste at lease end through valuing the materials used and trying to avoid waste through planning, agreement, sharing responsibility and ensuring that the parties that will do the work will do so in an environmentally acceptable manner.

It is hoped that this document has started a process that will reduce the huge amount of waste from Make Good. RICS welcomes feedback so that industry comments can be used to evolve Greening Make Good into a system that meets high environmental standards and further reduces waste and damage to the environment.

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Disclaimer

This is a guide only. It is not intended to be an instruction manual, nor a detailed step by step process which must be followed, but rather a guide to encouraging the process of 'Make Good' to be less wasteful and less environmentally damaging. This guide does not provide legal advice and is general in nature. You are advised to take legal advice from a professionally qualified legal advisor.

Contents

1. Introduction	3
2. Tenants' Make Good Obligations and Landlord's Rights	4
3. Repair Covenants and Make Good	4
4. Who Should Carry Out The Works?	5
5. Recognising and Factoring in Competing interests	5
6. Guidance to Tenants to Minimise Make Good	6
6.1 Assessing the Premises Before Signing a Lease	
6.2 Planning Your Fit Out	
7. Make Good – New Approaches	7
7.1 Agreement of Make Good at Lease Commencement	
7.2 What is the Best Environmental Approach for New Leases?	
8. Greening Make Good Advantages	8
8.1 Landlord	
8.2 Tenant	
8.3 Issues to Address	
9. Using a Make Good Deed at Lease End to Reduce Cost and Waste	9
9.1 Preparing a Make Good claim	
9.2 Make Good Deed	
9.3 Advantages of the Make Good Deed	
9.4 Disadvantages of the Make Good Deed	
10. Appendix 1 – Green Make Good Deed	11
11. References	13

1 Introduction

Make Good, or Dilapidations as it is also known, refers to the process at the end of a commercial property lease where the tenant is required to hand back the premises they are vacating in a particular condition that is established by the terms of the lease. To date this has usually involved physical works such as the demolition of partitions and built in furniture and the stripping out of services, followed by the reinstatement of the original fittings, fixtures and finishes. The standard to which the tenant is required to Make Good often includes the term "Subject to Fair Wear and Tear" meaning that the finishes may be worn and this reflects the situation that the tenant has paid for the right to use the premises and can leave the premises in a 'used' condition.

Generally, when the vacating tenant has left, the premises will not be in 'as new' condition and therefore the landlord may decide to redecorate, replace worn carpet, and carry out other works to bring the premises to a condition where it will be attractive to prospective tenants.

When the new, incoming tenant takes occupation they may well remove sections of new ceiling and flooring, repaint recently painted walls and adjust services for their own requirements.

The amount of waste caused between one tenant terminating and another starting their own occupancy is unacceptable. The waste being in:

- cost
- time
- labour
- materials, including their embodied energy.

Works can be carried out by the vacating tenant. Alternatively if the landlord accepts, the tenant may provide a monetary settlement.

It should be noted that just because costs were incurred when materials were installed as part of a fit out, this does not mean that they have Value, Value is determined by the amount another party will pay for

the fit out items. (If they cost to remove they will have negative value, no matter how much they cost in the first place).

Every case will be different. An example of improvement is where a tenant can improve the standard lighting by installing commercial office tube light fittings that are energy efficient and are able to be zoned and separately switched.

It is a requirement of most leases to carry out alteration works with landlord's approval and, at the time of seeking their approval, agree that the works would be an improvement and therefore will not require removal (and the old equipment reinstalled) at the termination of the lease.

FOOT NOTE: In reading this text readers should also refer to the RICS publication Best Practice Guidance Notes In Relation to Make Good Works 2004.

Tenants' Make Good Obligations and Landlord's Rights 2

“ promotes the avoidance of unnecessary waste by adopting a Green Make Good approach ”

The obligations of the tenant and the rights of the landlord regarding repair and Make Good are invariably covered contractually in the lease.

Where the lease does not include some form of covenant by the tenant to repair and Make Good, the obligations on the tenant are to be found in the common law relating to waste. A repair obligation is almost always expressed in a lease and therefore there is no need to detail the common law regarding waste in this publication.

Leases vary in what is required by a tenant by way of Make Good at the end of the term. Sometimes, there is no requirement to remove fit out and Make Good (for instance, because the tenant took the premises as fitted out space). However, more commonly, the landlord will require the tenant to carry out some Make Good work. At the extreme, the tenant will be required to remove all of the partitioning and fit out, and put the premises back to base building configuration.

It is the view of RICS that the object of a well constructed Make Good clause in a lease is the overriding principle that neither party shall gain an advantage at the termination of the lease. In this publication RICS promotes the avoidance of unnecessary waste by adopting a Green Make Good approach.

3 Repair Covenants and Make Good

Invariably, all leases have a general repair covenant, which applies throughout the lease and at the end of the term (that is the tenant must yield up the premises in a state of repair consistent with its obligation to keep the premises in good repair). Therefore, the repair covenant is relevant to the Make Good obligation.

The tenant should ensure that there are three important qualifications to the repair obligation, as this is relevant to the Make Good at the end of the lease. These are:

- the tenant should not be responsible for fair wear and tear;
- the tenant's obligation to repair must be with regard to the condition of the premises at the commencement of the lease; and
- the tenant should not be responsible for structural repairs or replacements.

Given that tenants should ensure that the lease does not require them to return the premises in any better condition than at commencement of the lease, they should take steps to record the condition of the property at commencement. It is good practice for the landlord and the tenant to sign off on a condition report at the commencement of the lease.

In the context of the repair obligation, in New South Wales and Queensland there is a statutory maximum on recovery of damages by the landlord. This is set out in Section 133A of the Conveyancing Act 1919 NSW and Section 112 of the Property Law Act 1974 QLD.

That is, the landlord cannot recover damages that are greater than the amount by which the breach diminishes the value of the “reversion” (i.e. the value of the property as is established in the lease). For instance, if the tenant breached the repair covenant, and the cost of putting the premises into the state of repair that the tenant ought to have kept them, exceeds the reduction in value of the property, the landlord can only claim for the reduction in value. Also, as a result of those sections, the landlord cannot claim for damages for breach of the covenant to leave the premises in repair at the end of the lease where the premises are to be demolished or structurally changed in a way that makes the repairs valueless. This may also include refurbishment. For example, if it is the landlord's intention to replace a ceiling as part of a refurbishment following the end of the lease, the landlord cannot claim for repairs to the old ceiling that it is their intention to replace.

Who Should Carry Out The Works? 4

“ The landlord is generally in a better position, environmentally and strategically, to manage the Make Good works ”

The tenant is usually concentrating on their move to new premises and may not have skills or experience in property related matters.

Most landlords are used to managing building works and generally have a high standard of environmental requirements for building works.

Landlords can increase the scope of works to upgrade or refurbish the premises to new standards.

There is always a risk that the landlord will reject the standard of work carried out by the tenant.

5 Recognising and Factoring in Competing Interests

In many instances an incoming tenant wanting to improve the environmental performance of their premises may be keen to install energy efficient fixtures and systems. However, there is often a disincentive as the landlord may require them to be removed and the old system reinstated to match the remainder of the building which has old and inefficient fittings and equipment.

In these cases, particularly where landlords or their agents and consultants are trying to maximise the amount obtained from the tenant at the end of the lease - which usually maximises the waste caused - the tenant has to factor in:

1. the cost of the new equipment they installed;
2. the costs of its removal;
3. the reinstatement of the old equipment at the end of the lease.

This can make the business case for installing environmentally efficient equipment hard to make work, particularly with a trend to short term and flexible leases where the tenant has a limited time to recover expenditure.

Guidance to Tenants to Minimise Make Good

6

It is suggested that to reduce the need to Make Good for environmental initiatives tenants should do the following:

6.1 Assessing the Premises Before Signing a Lease

- When assessing the premises prior to signing a lease establish if there are finishes or services that you would wish to alter when you undertake your fit out.
- Discuss proposed changes with the landlord. You may be able to reach agreement to share some costs, particularly if the equipment you wish to have in the premises would be seen as an improvement.
- Seek to agree that these improvements will be excluded from Make Good claims. Make sure the lease term is long enough or contains lease options for any improvements and changes to bring positive returns.

6.2 Planning Your Fit Out

Minimise the impact of your fit out on the base building:

- Try to avoid removing or replacing base landlord's equipment such as flooring and ceilings.
- Use systems that are free standing where possible so that their fixings do not damage the base building.
- The more open plan your fit out the less changes to the building services.
- Consider wireless data systems, they dramatically reduce the cabling waste and you can take them with you.
- Lease integrated fit out. That is, where the tenant installs the ceiling and carpet to suit their needs, which are likely to have continuing use. The rent

should be adjusted accordingly to factor in the lower costs to the landlord (or other appropriate concession provided to the tenant). The lease should record the agreement that if a suitable quality of ceiling (or carpet) is installed, it will not need to be removed at the lease end.

- If you propose to use materials that require the removal of landlord finishes, e.g. stone wall panelling, consider mounting it on panels that can be installed over the top of the base building finishes and later removed. You will also find that if you need to refurbish or revamp during the term of your lease you can simply lift them off and drop the new ones in place.
- Consider carpet tiles that can be mixed and matched to suit a changing office, and define reception and break out spaces through colour or pattern changes. Some carpet tile companies also commit to take back their product at the end of a lease. This works well if your fit out was shell and core.
- Remember that if you have a Make Good you need to allow an appropriate amount of time to complete the works.
- Always seek landlord permission for alteration works and bear in mind your liability for making good.
- Use second hand fit out to minimise environmental impact or seek premises where the previous tenants fitout remains and can be reused.



7 Make Good - New Approaches

7.1 Agreement of Make Good at Lease Commencement

In Make Good neither the landlord nor the tenant should profit. Make Good can be an uncertain process where the claim may cause the tenant unnecessary distraction when they are relocating their business. In many instances the tenant will not have made provision for the cost of Make Good.

From the landlord's point of view they usually want the premises available to lease as soon as possible with the minimum disruption and uncertainty as to quality, quantity and cost of work they will have to do. From an environmental point of view, having the tenant carry out Make Good by lease end without testing whether a potential new tenant can make use of the existing fit out is very wasteful. Any demolition and disposal of materials should be carried out to the highest possible environmental standards.

7.2 What is the Best Environmental Approach for New Leases?

Make Good works can be assessed at lease commencement. The lease will prescribe the extent of the Make Good work the tenant will be carrying out and the lease term is known (although there may be options to extend).

A sum of money can be agreed and can be a payment in addition to the rent through the first term of the lease or it could be calculated to arrive at an amount to be paid at the end of a lease. This would be set out in the lease.

To take this further, it is not unreasonable for the tenant to suggest that the lease also state that the tenant receive a credit (i.e. does not incur the total agreed sum) where the landlord is not required to carry out all of the work that the amount was set aside to cover. The tenant's argument for taking this approach is that this is both an environmentally sensible and a fair approach. In this scenario, the tenant will usually only know the amount of the saving when a new tenant is found.

Example 1: The tenant would relocate office equipment such as: computers, printers, copiers, filing cabinets (not built in), furniture (not built in), chairs, etc.

Example 2: The tenant would only relocate computers, printers, copiers.

“ Agreeing a cost of a Make Good at lease commencement will provide certainty for both parties ”

8.1 Landlord

- The landlord would have the responsibility of removing the fittings or furniture and would be better placed to carry out the works and any disposal to good environmental standards.
- The landlord would have the option of leasing the premises with some of the partitions and furniture in place, therefore saving waste.
- Certainty for the landlord on what they will have to do.

8.2 Tenant

- Knowledge that they will not be required to pay an undetermined amount for Make Good as they vacate.
- The tenant can occupy the premises right up to the last day of the lease, avoiding the need to allow time to carry out Make Good works.
- Agreeing a cost of a Make Good at lease commencement will provide certainty for both parties.

8.3 Issues to Address

- Alterations to the tenancy during the lease term could change the cost of Make Good.
- **Consider:** When seeking approval for alterations the landlord and tenant would agree if the cost of the making good could be affected by the changes, and if so by how much.
- The tenant exercises an option for a further term of the lease.
- **Consider:** The tenant would have met its obligations for Make Good and the additional payments specifically for Make Good would cease. Where the tenant agreed to provide a fixed sum at the end of the term, that same sum should continue to apply if the lease is extended by the exercise of an option on the basis of an appropriate indexation of the sum.

9 Using a Make Good Deed at Lease End to Reduce Cost and Waste

Where there is an existing lease and there has been no opportunity to utilise Environmental Performance clauses or determine a pre lease financial settlement, the parties to the lease can agree a “Green Make Good Deed” (Appendix 1).

It should be noted that the terms of the Green Make Good Deed will invariably be inconsistent with the terms of the existing lease. For instance, it is probably the case that the existing lease requires fit out to be removed by lease end. From a contractual point of view, the landlord is not under any obligation to agree to a Green Make Good Deed. Therefore, in cases where the landlord is reluctant, the tenant needs to “sell” the benefits of the Green Make Good Deed to the landlord well before the end of the lease. The landlord should be encouraged to commit to this course on the basis of corporate social responsibility.

This Green Make Good approach gives the landlord the opportunity to lease the space with fit out in place, without losing their right to require the tenant to pay for their Make Good obligations. If the landlord can find another tenant to use the space largely as it is fitted out there will be no value loss to them and the amount of waste reduction will be significant.

From the tenant’s point of view the worst case is full liability for their Make Good, the best case is that they will pay a greatly reduced amount.

The Deed recognises the obligations of a tenant to Make Good under a traditional lease arrangement but attempts to reuse the existing fit out for a future leasing opportunity.

A critical component of the Green Make Good Deed is the requirement on the tenant to lodge a bond or bank guarantee equal to the tenant’s full Make Good liability. The landlord then has an agreed time in which to market the space with the fit out remaining with the comfort of having limited exposure if the worst case transpires and a complete removal of the fit out is required.

NOTE: Green Building Council of Australia may award credit points under Green Star, for recycling of materials. Having outgoing tenant materials for use would benefit the landlord and the incoming tenants.

The use of a Green Make Good Deed has the potential to:

- reduce the cost of making good;
- save time for tenant and landlord;
- reduce waste of materials;
- reduce conflict in Make Good.

Since no physical Make Good will be undertaken prior to lease end, the tenant can occupy the space until the lease ends – as long as the Green Make Good Deed has been agreed and any financial bond lodged in advance of this date.



9.1 Preparing a Make Good Claim

An assessment of the tenant's liability should be prepared. You are referred to the RICS Best Practice Guidance Note for Make Good (2004) with regard to the steps required in the preparation of a Schedule of Make Good. Even if a formal Schedule is not required it is recommended that these steps are followed to ensure the legal obligations of the outgoing tenant are assessed and included in the Deed.

A Schedule of Make Good indicating the separate Make Good costs for each item relating to the applicable lease clauses is prepared and agreed between the parties. The total cost of the tenant's obligation has to be agreed in much the same way as a traditional Make Good. Remember that the value of the claim may not just be based on the actual Make Good work, it may also include items such as professional fees if these are applicable under the lease.

9.2 Make Good Deed

As described above the Green Make Good Deed promotes the concept of the landlord agreeing to market the property with the existing fit out in place with the aim of finding a new tenant who will take the premises with part or all of the existing fit out or subject to a minor upgrade. The parties should agree a period during which the landlord will attempt to lease the space with no, or limited, Make Good having been carried out. The outgoing tenant will provide a security equal to the full cost of the Make Good, which will be drawn on by the landlord if ultimately the entire fit out, or part of it, is not required by the incoming tenant.

9.3 Advantages of the Make Good Deed

- Reduced waste from minimising the "triple waste" of make good as an outgoing tenant Makes Good to its fit out, the landlord refurbishes it and the incoming tenant fits out, making changes;
- both parties have certainty regarding the maximum cost if the works are required to be undertaken;
- the landlord gets vacant possession at lease end and can start marketing the space quickly;
- the outgoing tenant can occupy until their lease expires, rather than having to allow a time for making good within the term of their lease;
- incoming tenants can save on fit out costs and are contributing to reduction of waste by reuse of existing ceilings, partitions, services; even workstations and tea rooms;
- the Deed is flexible and can be partially or wholly implemented depending on the needs of the incoming tenant;
- the landlord can still require Make Good to be carried out or paid for by the outgoing tenant for areas of work deemed necessary for marketing purposes (such as redecoration) although minimising waste would be encouraged to allow the incoming tenant to benefit from this.

9.4 Disadvantages of the Make Good Deed

- The tenant can have costs associated with a bank guarantee or bond wrapped up for a period of 6 months or more;
- an incoming tenant may not be able to use the existing tenancy fit out and so ultimately the outgoing tenant may have to pay maximum costs for their Make Good obligations;
- agents may need to rethink marketing strategies to market space with existing fit out or in need of works in an effort to reduce waste;
- there may be additional delays if the new tenant requires Make Good prior to commencing their fit out.

10 Appendix 1 – Green Make Good Deed

Date of Make Good Deed:	
Lessor:	
Lessee:	
Premises:	
Lease and Date of Lease:	The lease of the Premises between the Lessor and the Lessee dated XXX
Commencement Date:	
Termination Date:	
Make Good	Means any works in the nature of removal of fit out, restoration of services and redecoration that are required to be carried out by the lessee under the Lease at the termination of the Lease.
Security Amount	\$XXX [Note: this should be the Total Make Good Costs (including GST) as set out in the Make Good Table]
Security Period	XXX months from the expiry date of the Lease

- 1 This deed is in connection with the outstanding Make Good obligation of the Lessee at termination of the Lease and overrides the Lease to the extent of any inconsistency.
- 2 The Lessor has agreed not to insist on the Lessee carrying out any Make Good works as at the termination of the Lease and during the Security period on the terms set out in this deed.
- 3 The Lessor and the Lessee have agreed that for the purposes of this deed the amount required to carry out the Make Good works is \$XXX.
- 4 The Lessee must provide a cash bond, unconditional bank guarantee or other security ("Security") acceptable to the Lessor (acting reasonably) for the Security Amount to be held by the Lessor as security for the money (if any) expended on Make Good works by the Lessor in accordance with this deed.
- 5 If the Lessor secures another tenant for the Premises during the Security Period, then the following applies:
 - (a) If the new tenant agrees to fully utilise the existing fit out in the Premises, the Lessor will return the Security to the Lessee and releases the Lessee in full from the Lessee's Make Good obligations under the Lease; or
 - (b) If the new tenant agrees to utilise part of the existing fit out in the Premises, the Lessor will allow to the Lessee the costs saved from not having to carry out the relevant items of Make Good works with reference to the Make Good Table below. In that case, the Lessee must promptly on request pay to the Lessor the Total Make Good Costs (including GST) as set out in the Make Good Table less the allowances for cost saved with reference to the Make Good Table.
- 6 If the Lessor does not secure another tenant for the Premises during the Security Period, the Lessor must make the following election by written notice to the Lessee within 7 days after the end of the Security Period:
 - (a) notify the Lessee that the lessor will carry out the Make Good work; or
 - (b) return the Security to the Lessee, in which case the Lessor releases the Lessee in full from the Lessee's Make Good obligations under the Lease.
- 7 If the Lessor does not give a written notice of election as required by clause 6 within time, the lessor is taken to have elected to return the Security to the Lessee under clause 6(b).
- 8 If the Lessor makes the election under clause 6(a) to carry out the Make Good work, then the Lessee must promptly on request pay to the Lessor the actual costs (provided they are reasonable) of the specific Make Good works carried out and referred to in the Make Good Table to the maximum of the Security Amount. The Lessor cannot require payment until the work has been carried out and the costs have been substantiated.
- 9 If the Lessee is required to make a payment to the Lessor for partial Make Good undertaken under clause 5(b) or for the complete Make Good undertaken under clause 8, and the payment is not made within 7 days of the request by the lessor, the Lessor can apply the Security to rectify that breach.

Make Good Table

Make Good Liability		
Clause reference	Brief description of Obligation - Example Make Good clauses	
Lease clause reference	remove all tenant's property, workstations and built in units and make good.	\$
Lease clause reference	replace damaged ceiling tiles, make good to grid.	\$
	remove internal partitions and make good to disturbed surfaces.	\$
	redecorate in accordance with lease obligation to all usually painted surfaces including remaining wall, partitions, set plaster ceiling areas, joinery items etc.	\$
	thoroughly clean all areas.	\$
	reinstate all power, data and fire services within the tenancy space to suit original base building arrangement and supply certificate of compliance.	\$
	Professional fees for landlords agent to supervise works (if applicable in lease).	\$
	Total Make Good Costs	\$
	Plus Goods and Services Tax (10%)	\$
Note 1: These costs have been determined inclusive of contractor profit, margin and supervision.		

EXECUTED by THE LESSOR in accordance with section 127 of the Corporations Act 2001 (Cth):

Signature of Director

Signature of Director/Secretary

Name of Director [BLOCK LETTERS]

Name of Director [BLOCK LETTERS]

EXECUTED by THE LESSEE in accordance with section 127 of the Corporations Act 2001 (Cth):

Signature of Director

Signature of Director/Secretary

Name of Director [BLOCK LETTERS]

Name of Director [BLOCK LETTERS]

OR (where lessee is a natural person) SIGNED SEALED and DELIVERED by THE LESSEE in the presence of:

Signature of Witness

Signature Lessee

Name of Witness [BLOCK LETTERS]

Name of Lessee [BLOCK LETTERS]

11 References

RICS Best Practice Guidance Notes in Relation to Make Good Works (1st Edition), 2004

P F Smith, West and Smith's Law of Dilapidations (11th Edition), 2001, Estates Gazette London

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