Wedlake Bell

QUARTERLY IN ADVANCE

SPRING 2023

NEWS AND VIEWS FROM OUR REAL ESTATE TEAM

IN THIS ISSUE

CAUTIOUS CASH – WHAT IF MY TENANT IS SANCTIONED?

Perplexed by property law? Our Professional Support Lawyer Gemma Cook is here to answer your most pressing questions

If a landlord has a sanctioned tenant, it cannot receive rent, enforce tenant covenants or forfeit the lease without taking further steps. It may also need to consider its obligations to its own lenders and investors.

The UK government brought in various measures to restrict the use of assets because of the Russian invasion of Ukraine. The measures are known as the sanctions regime and the regime casts a net wider than just the sanctioned person.

I am not sanctioned, how can the sanctions apply to me?

Those not on the list of sanctioned people might still see the consequences of the sanctions regime. All UK nationals and legal entities, wherever they are in the world, and all individuals and legal entities operating within the UK must comply with the UK sanctions regime. In the context of property, the most likely sanction to apply would be a financial sanction such as an asset freeze.

An asset freeze might be imposed on a tenant, whether existing or prospective. If a tenant were to be a sanctioned person, the tenant must not deal with its assets and they must not be made available to, or for the benefit of, the tenant. In short, the law restricts **anyone** from:

- making funds or 'economic resources' available, directly, or indirectly, to or for the benefit of, an individual or entity on the sanctions list. 'Economic resources' are widely defined and specifically include property; and
- dealing with funds or 'economic resources' owned or controlled by an individual or entity on the sanctions list, or a person acting on behalf of an individual or entity on the sanctions list.

So in a landlord and tenant relationship, landlords are susceptible to breaching the sanctions regime because payment of rent to the landlord by a sanctioned tenant may be unlawful due to the receipt of the frozen funds. Even making legitimate payments to the tenant (such as a refund of service charge at the end of the service charge year) could be caught.

What does this mean for a landlord?

The landlord is in a difficult position because, as a matter of contract law, it wants (and is due) the rental payments under its lease with the sanctioned tenant but:

- can a landlord forfeit for repayment of rent? Most likely, yes in certain circumstances, but does the landlord want to regain possession in a difficult market. It is also possible that the landlord seeking to forfeit would be 'dealing' with the tenant's property and this may be restricted under the terms of the sanction;
- what if a landlord has a financial loan secured upon the property? A lack of rental income might put the landlord in breach of its lending terms and also, affect its ability to repay the loan. Having a sanctioned tenant in the landlord's building could be enough of itself to trigger a default under the landlord's loan terms;
- a sanctioned tenant might make a landlord fall foul of its own ethical, social and governance agenda;
- the landlord will be worried to protect the integrity of the building. The sanctioned tenant might be prohibited from paying for utilities, security, and other essential building services; and/or
- what if the sanctioned tenant continues to pay the rents? Ironically, this is not the windfall everyone might hope. The receipt of the rent could still be a breach of the sanctions regime.

So what can a landlord do?

Specific licences

The OFSI, part of the Treasury, handles asset freezes, restrictions on making funds available, and/or economic resources available to or for the benefit of designated persons either directly or indirectly. The OFSI publishes a list of people who are subject to financial sanctions. The first step is to check whether a party, such as the tenant, is a designated person according to that list.

In certain circumstances, a landlord can request that the tenant apply for a licence (or apply for one itself) from the OFSI to enable payments to continue to be made to the landlord.

There is no guarantee that the OFSI will grant a licence and a licence may take some time to be granted. The OFSI can issue a licence only where there are legal grounds to do so. If the OFSI grants a licence, then it would authorise payments that would otherwise be prohibited by the sanctions regime.

General licences

There are also general licences, which are not applied for by a particular person, but rather, apply for the public. For example, a general licence was made to allow the payment of insurance and reinsurance premiums and broker commissions relating to the provision of insurance to UK properties. Under this general licence, UK insurers who are registered with the Financial Conduct Authority may receive funds (which would otherwise be sanctioned) and UK institutions may process those payments.

Any other options?

It is likely that any option is likely to require a consent from the OFSI. For example:

- **Appoint a receiver**: The English Courts have a discretionary jurisdiction to appoint a receiver under the Senior Courts Act 1981. A court may look favourably on such an appointment where the appointment is to preserve property from some danger threatening it. The appointment would allow the receiver to manage the property on behalf of the tenant but even the appointment is likely to also need an OFSI licence;

- **Recover rents from undertenants**: Commercial rent arrears recovery ("**CRAR**") is a method of enforcement to recover rent arrears relating to commercial property. Under CRAR there is an ability for a landlord to require an undertenant to pay the rent that it owes directly to the landlord rather than the intermediate tenant. This could be seen as dealing with the sanctioned tenant's assets and an OFSI licence may be required; and/or

- **Possession of tenant's goods**: CRAR also allows a landlord to instruct an enforcement agent to take control of a tenant's goods and sell them in order to recover an equivalent value to the rent arrears. The sale of tenant's goods is likely to be deemed to be dealing their 'economic resources' and therefore, require a licence from the OFSI.

What are the consequences of breaching the sanctions regime?

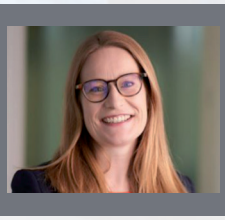
In short:

- financial penalties;
- reputational damage; and/or
- a prison sentence.

These can apply to the landlord because of the receipt or dealing with funds or assets. The OFSI can impose monetary penalties on any person who breaches financial sanctions. The maximum penalty is the greater of (a) £1,000,000 and (b) 50% of the estimated value of the economic resources involved in the transaction.

Action points for landlords

- Check whether a tenant is on the UK sanctions list as a designated person. It is important to note that if an entity or individual is designated, the sanction also applies to any entities (meaning a body of persons corporate or unincorporated or any organisation or association or combination of persons) that are owned or controlled, directly or indirectly, by a designated person. Those entities may not appear on the UK sanctions list. This works by deeming any assets held by such entities to be owned by the designated person.
- Undertake thorough Know Your Client (KYC) processes on any prospective tenant and carrying out a repeat exercise regularly during any continuing relationship.
- If a landlord becomes aware that a tenant is a designated person, advice should be sought immediately. The nature of the sanction will be considered and, if appropriate a report may need to be made to the OFSI.
- If a landlord thinks it may have breached a sanction, again, a report may need to be made to the OFSI.



GEMMA COOK
Professional Support Lawyer
T: +44 (0)20 7406 1603
E: gcook@wedlakebell.com

ESCHEATED OUT OF YOUR PROPERTY?

In the recent High Court case of *Dixon v The Crown Estate Commissioners [2022] EWHC 3256 (Ch)*, two former shareholders of a dissolved company were deemed to have an equitable interest in the dissolved company's properties, despite the properties having escheated to the Crown Estate.

What does escheat mean?

Escheat is a remnant of feudal law which is based on the assumptions that (a) all land in England is held by the Crown and at some point in the past the Crown granted that land to a feudal tenant in chief and (b) no land can be ownerless. Therefore if the interest in land granted comes to an end, then the land will revert to the Crown and be known as 'bona vacantia' (literally, "ownerless goods").

The Crown can then opt to disclaim such bona vacantia if it considers that it would not be effective for the Crown to sell it, or that owning the relevant property would be risky (for example if the land is contaminated). A disclaimer by the Crown means that the property is treated as if it never passed to the Crown as bona vacantia at all. Instead, it 'escheats' to the Crown Estate, which is a different part of the Crown as the ultimate owner of all land.

What happened in Dixon?

The two claimants in this case owned a property development company and the company owned two properties in Stanley and Carlisle. One of the claimants wished to retire and move abroad, therefore together, the claimants decided to wind up the company and the two properties were to be assigned to each of them prior to the company being wound up. The claimants believed that the company's accountant had given effect to their instructions when in fact, the advisors had not wound the company up or transferred the properties. In the mistaken belief the company had no assets they applied for the company to be struck off the Register of Companies and the company was dissolved in 2010. The claimants had paid tax in relation to the distributions to them and subsequently on rent they received personally from the properties. However in late 2020, the claimants realised that none of the formalities for winding-up the company had taken place and the two properties were still registered in the name of the company at the Land Registry.

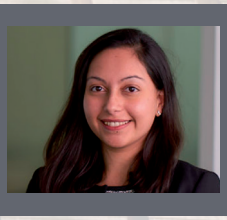
If a company governed by the Companies Act 2006 is dissolved then section 1012 of the Companies Act 2006 provides that all of its property will vest in the Crown as bona vacantia. In this case, the Treasury Solicitor disclaimed the two properties, after which the legal title to each property vested in the Crown Estate Commissioners for the Crown Estate.

KEY POINTS

- **A decision of conscience, the claimants were not to lose their properties due to a failure on the part of their advisors.**
- **They had acted to their detriment by paying taxes on the properties interests that they thought they had on the fair assumption that the properties had been transferred to them.**
- **No windfall for the Crown Estate in this case but a useful example of how a historic concept can apply to modern life.**

However, the Judge deemed the company to have held the properties on trust for the claimants at the time of dissolution, through proprietary estoppel. Proprietary estoppel refers to the equitable jurisdiction of the court to interfere in cases where the assertion of legal rights would be unconscionable. The court granted an order vesting the properties in the two claimants under section 44(ii)(c) of the Trustee Act 1925 or alternatively under section 181 of the Law of Property Act 1925.

The Judge held that it would be unconscionable for the Crown Estate Commissioners to deny the claimants' ownership of the properties and making of vesting orders in favour of the claimants in respect of each of the properties would be consistent with the interests of justice as otherwise the Crown Estate would receive a windfall. The failure to transfer the properties out of the company before it was struck off and dissolved was a clear mistake which the making of vesting orders in favour of the claimants would correct.



ANKITA SAHADEV
Solicitor
T: +44 (0)20 7395 3081
E: asahadev@wedlakebell.com

EXISTING HIGHER RISK BUILDINGS – COMPULSORY REGISTRATION OPENS 6 APRIL 2023

The mandatory registration of existing occupied higher risk buildings ("**HRBs**") with the new Building Safety Regulator will open on 6 April 2023 with a 6-month period to complete registration. The Government estimates that some 13,000 buildings will require registration, but the precise number is unknown. The registration needs to be done by the "principal accountable person" (as defined by the Building Safety Act ("**BSA**")) itself, this will usually be the party responsible for repairing the common parts of a building ("**PAP**").

The regulations relating to the registration of HRBs are known as the Higher Risk Building (Key Building Information etc) (England) Regulations 2023 ("**Regulations**") which will apply in England (Wales, Scotland and Northern Ireland will have their own regulations). Essentially, an HRB is a building over 18 metres or comprising seven or more storeys and with two or more residential units. The height of a building is measured from ground level to the top floor surface of the top floor. Storeys completely below ground level and ones purely for roof-top plant or machinery are to be ignored in counting the number of storeys. Any mezzanine level is a storey if its internal floor area is at least half of the internal floor area of the largest story in the building not below ground level.

Certain existing buildings are to be excluded from the definition of HRBs for registration purposes, namely hotels, "secure residential institutions" (e.g. prisons), military premises, hospitals and care homes.

Key building information (as set out in the Regulations) in relation to the registration must be submitted in electronic form by the PAP or a person authorised on its behalf, within 28 days of registration. This information is quite extensive including details of materials used in construction and for older buildings may take some time to gather. It will therefore be sensible to have it ready at the time of registration or at least to be confident that it will be available within 28 days of registration. Any subsequent changes to the supplied information must be submitted within 28 days

You can sign up for information about and details of registration ***here***. If any legal advice is required about whether your building(s) need to be registered, please contact a partner in our construction team.

SARAH ELLIOTT
Partner
T: +44 (0)20 7395 3192
E: selliott@wedlakebell.com

BTR BOOM

As a firm we are seeing a huge increase in activity in the build to rent ("**BTR**") development sector. BTR is not a 'new kid on the block'. It has been around for a while. However, in recent times it has caught the eye of some very substantial investors who are pouring money into it. At a time when there are so many uncertainties in the real estate world, it is encouraging and interesting to see such a boom. So what is all the fuss about?

What is BTR and just how big is it?

As the name suggests, a BTR development is a development of homes that are developed and built specifically for rental rather than for sale. Although part of the private rented sector ("**PRS**"), BTR distinguishes itself by offering good quality, energy efficient homes with longer term tenancies at more predictable rents in booming locations and with easy access to local amenities and infrastructure. The developments are professionally managed and tenants usually have enhanced communal facilities and social spaces, such as a gym, residents lounges, roof gardens and guest rooms for hire, with some developments offering 24/7 concierge services, childcare and car hire.

BTR emerged as a result of the Government's Montague Review of the rental sector in 2012. The review's main focus was to lower rental costs through increasing rental supply and encouraging institutional investors into the market whilst at the same time improving standards. Just over ten years on it is certainly a success story.

Since 2012 over £30bn has been invested into the BTR sector and research data from the British Property Federation ("**BPF**") shows that there are now over 242,500 BTR homes in the UK which are either completed, under construction or in planning. Many more are on the way and it isn't just the private sector that is getting on board – a significant proportion of local authorities and other affordable housing providers now have BTR in their housing pipelines. The BPF is currently predicting that the sector will be worth £170bn by 2032.

Why is it so attractive to investors?

There are many reasons but some of the key factors are:

Demand: This has continued to increase over the last decade and is expected to continue its upward trajectory. Higher mortgage rates have led to an affordability squeeze in the sales market keeping aspiring first time buyers in the rental market for longer. In addition, a lack of good quality housing in the PRS sector is being exacerbated by buy-to-let landlords continuing to withdraw from the market due to more stringent requirements and less friendly tax policies.
Scale: BTR facilitates large scale investment with each development delivering anything from 50 to several hundred homes. This leads to economies of scale resulting in enhanced rental yields.
Speed: BTR developments can be built faster than other developments which often rely on sales revenue from early units to fund construction of later units. Units can also be filled very quickly.
Security: Tenants are encouraged to stay for longer term lets which gives increased security and the potential for fewer void periods.
Other income: Investors may benefit from other income streams through creation of retail, entertainment and office space within the BTR development.

Isn't it just for city centres?

Developers and investors initially focused on apartment blocks (multi-family homes ("**MFH**")) for young professionals in London and other major cities. These developments do remain in high demand but those original customers have grown up and may want different things; they may have families of their own and/or require more or different types of space. BTR providers have grown with their customers, diversifying their offering and looking to attract a much wider customer base. As a result there has been a shift in emphasis and we are seeing a huge rise in single family homes ("**SFH**") – essentially houses rather than flats/apartments – which are cheaper to deliver than MFH as they are less complex. However SFH developments necessarily need larger areas of land. Rather than being limited to the cities a whole raft of the UK is now available for investors.

KEY POINTS

- **BTR is one of the fastest growing sectors. The BPF is currently predicting that the sector will be worth £170bn by 2032.**
- **The developments are growing with their customers. We are seeing a shift in the location and nature of developments, such as a move to single family homes within the BTR offering.**
- **Tenants and investors are mutually interested in the sustainability of developments leading to a real desire to incorporate sustainable design principles and renewable energy technologies in BTR schemes.**

What impact will the Building Safety Act have on BTR?

The Building Safety Act ("**BSA**") was introduced in response to the Grenfell Tower tragedy with the purpose of securing the safety of people in or about buildings and improving building standards. The BSA is likely to have a significant impact on the design and construction of new BTR developments by placing greater accountability on building owners and developers for the safety and quality of their product. Requirements will be more stringent for higher rise developments and it may be some time until the industry really understands all the implications of the BSA, particularly as secondary legislation with the detail of many of the requirements is still awaited. The proposed Government gateways have the potential to cause delay at various points during design and development and it will be interesting to see how BTR developers and investors agree to deal with these risks. BTR investors usually look to pass as much risk to the BTR developers as possible but this may be unviable for some developers and contribute, at least in the short term, to more investment in low rise SFH rather than high rise MFH.

What about sustainability?

Most BTR investors now require an EPC rating of a 'B' as a minimum with net zero homes being the ultimate goal. Tenants are also increasingly interested in energy savings that can be achieved with well-designed BTR homes. As many BTR operators pride themselves on providing a 'customer experience' and not just a place to live and as investors have a long term interest in their units, there is a real desire to incorporate sustainable design principles and renewable energy technologies in BTR schemes.

What is next?

Although the BTR sector is unlikely to be completely immune to the ebb and flow of market conditions, the sheer scale of the developments gives BTR operators a real advantage. It is clearly here to stay. The big question is how quickly the BTR sector can grow to meet the demand – we need continued investment, realistic Government targets and Government funding together with advances in technology to continue the evolution of this booming sector. Watch this space…

Wedlake Bell has advised on a variety of BTR schemes. We have enjoyed being at the forefront of BTR; drafting and negotiating innovative documentation on behalf of house builder clients and working alongside some of the largest institutional investors in the sector.

SARAH ELLIOTT
Partner
T: +44 (0)20 7395 3192
E: selliott@wedlakebell.com

RACHEL WALBOURN
Partner
T: +44 (0)20 7406 1635
E: rwalbourn@wedlakebell.com

TATE THAT: WHEN IS A VIEWING PLATFORM AN INTRUSION OR NUISANCE?

The recent Supreme Court case of *Fearn & others v Board of Trustees of the Tate Gallery* has brought the ancient principles of nuisance under the spotlight. The decision has made headlines on all news channels, not just the legal press.

Facts

The claimants owned flats in a building next to the Tate Gallery (and its associated viewing platform) with floor to ceiling windows and views across London. The flat owners claimed that they were under constant scrutiny in their homes from visitors to the Tate's viewing gallery, which included people taking photographers of them in their flats and with some even using binoculars to take a closer look inside their homes.

The claimants brought a claim in nuisance, sought an injunction, and claimed to protect their rights of privacy afforded by the European Convention of Human Rights.

KEY POINTS

- **Visual intrusion can be a nuisance**
- **The "ordinary use of land" is privileged so it is never a nuisance even if it severely harms the amenity of neighbouring land. It must be a substantial interference with the ordinary use of the claimant's land. The use as a viewing gallery is manifestly very particular and an exceptional use of land. This should ease the concern for developers. Whilst they will need to consider the impact of this judgment, the construction of a building is not a nuisance but it is in fact how such a building is used that could cause the nuisance.**
- **It is not a defence that the claimant came to the nuisance. It was not relevant to the court's decision whether the flats were built/purchased before or after the viewing gallery started to be used.**

Decision

Their claims were rejected by the High Court who put the onus back on to the claimants by saying the viewing platform was not a nuisance as the claimants could put up curtains and blinds to protect themselves from intrusion from the viewing platform. The Court of Appeal also rejected their claims on the basis that the law did not and should not recognise overlooking and visual intrusion as an actionable nuisance.

In February 2023, after a six year long battle, the Supreme Court overturned (and heavily criticised) the judgments of the lower courts in what will arguably now become the starting point for any claim in nuisance for decades to come.

Their Lordships held that whilst the law may not have recognised this form of visual intrusion as a nuisance before, the categories of nuisance are not closed and the intrusion on the claimants in their own homes was "much like being on display in a zoo". The unusual circumstances of this case meant the decision turned on the question of what was the "ordinary use" of the Tate Gallery. The Supreme Court held that the use of other parts of the gallery building that also overlooked the claimants' flats, for purposes such as offices and restaurants, would not constitute a nuisance as they were ordinary uses of a gallery. However, the express encouragement for visitors to use the viewing platform for the purpose of looking out (and therefore into the claimants' flats) was not ordinary for the use of an art gallery and therefore, it caused a nuisance.

We now await to see what remedy is awarded to the claimants after their hard fought battle.

This judgment puts a socially progressive principle right at the heart of nuisance and emphasises the rule of "give and take". Going forward, it will be interesting to see how this newly highlighted principle will apply in a world of CCTV, social media and seemly ever increasing scrutiny.

LUCY DODDS
Solicitor
T: +44 (0)20 7395 3157
E: ldodds@wedlakebell.com

UNEARTHING CONTAMINATED LAND

The Contaminated Land Regime ("**Regime**") governs the remediation of contaminated land in England and Wales and came into force on 1 April 2000. Over twenty years later, the Environment Act 1995 and the Environmental Protection Act 1990 ("**EPA**") remain the key pieces of legislation.

What is contaminated land?

Under the EPA, land is 'contaminated land' if it appears to the local authority to be in a contaminated condition because there is:

- significant (or a significant possibility of) harm being caused; or
- pollution (or a significant possibility) of controlled waters.

If a local authority suspects that there is contaminated land, it must establish a 'significant pollution linkage' by identifying all of the following:

- Contaminant – the most common; contaminants are arsenic, lead and benzo(a)pyrene, but contaminants can also include oil, pesticides and asbestos;
- Pathway – this can include, air, earth, soil and running water; and
- Receptor – this is typically humans.

Remediation

If there is a risk of significant harm, and a significant pollution linkage, the local authority has a duty to require remediation of the site.

Some contaminated land can be considered a 'special site', which means that the responsibility for remediation of the contamination will be passed from the local authority to the Environment Agency. Special sites can include land within a nuclear site, land involving the manufacture of explosives and land owned or occupied by the Ministry of Defence.

All 'interested persons' must be notified of the contamination, which usually includes the owner and any occupiers of the contaminated land. A 'remediation notice' will be served on every 'appropriate person', specifying what they must do within a set timeframe. The 'appropriate person' can be either a Class A person (meaning the original polluter), or a Class B person (meaning the current owner or occupier of the land even if they didn't cause the pollution) if the original polluter cannot be found or identified.

Liability

The general principle is 'polluter pays' and so a Class A person(s) would have the primary responsibility for remediation.

Liability will be apportioned between all 'appropriate persons' if there is more than one person in the polluting class. For Class A persons, the authority will consider the area, length of time in ownership or occupation, and whether there was a reasonable opportunity to remedy the contamination. For Class B persons, their interest in the capital value of the land will be considered.

However, DEFRA's Contaminated Land Statutory Guidance outlines a number of exclusions for both Class A and Class B persons. For example, a Class A person can transfer its liability under the Regime to another person if the Class A person provides sufficient information about the contamination. This is how a seller often seeks to transfer liability to a buyer in a sale contract.

Sanctions

Failure to comply with a remediation notice is an offence resulting in a fine (in addition to the expensive clean-up cost) and the relevant authority may seek an injunction to force compliance with the notice. Company directors also can be held personally liable for environmental contamination.

KEY POINTS

- **Prior to acquiring a property it is important to consider whether contamination may be present by instructing an environmental survey.**
- **An owner or occupier can be liable for remediation works even if they did not cause the contamination.**
- **The level of environmental survey required will depend on the type, location and current or former use of the land.**
- **Express contractual provisions can be used to transfer liabilities from one party to another and/or specifically require one party to carry out remediation works.**

PHILIP SLEGG
Solicitor
T: +44 (0)20 7406 1655
E: pslegg@wedlakebell.com

DUVAL – DO WE NEED TO WORRY?

In May 2020, the Supreme Court ('**SC**') handed down its judgment in the case of *Duval v 11-13 Randolph Crescent Ltd [2020] UKSC 18*. The decision raises interesting points in practice for parties that are looking to obtain or grant consent to alteration works in commercial and residential leasehold properties. This article analyses the potential consequences for landlords, property owners, and developers operating in the commercial property sphere.

Background

The final decision centred around the interpretation of mutual enforceability clauses, qualified versus absolute covenants.

The case related to a single block residential building, separated into nine individual flats, each let under a 125 year long lease on similar terms. The landlord, 11-13 Randolph Crescent Limited, was a freehold company owned by the respondent, Dr Duval, and the other tenants in the building.

In 2015, Mrs Winfield, one of the tenants, wanted to carry out works to her flat. The proposed works included the removal of a section of an internal load-bearing structural wall, which was absolutely prohibited under her lease.

The landlord was willing to grant consent to the works, however, Dr Duval objected. In December 2015 and February 2016, Dr Duval requested that the landlord secure an undertaking from Mrs Winfield not to act in contravention of a clause prohibiting structural works by cutting or maiming any of the load-bearing or structural walls within her flat. On both occasions, Dr Duval agreed to indemnify the landlord if legal action became necessary.

In May 2016, Dr Duval began proceedings against the landlord, seeking a declaration that the landlord did not possess the power to permit Mrs Winfield to carry out structural works to her flat.

Leasehold models for enforcement of covenants

The enforcement of covenants by leaseholders differs on a case-by-case basis, but there are generally three models that apply.

Model 1: The first model, which is most prevalent in the commercial property sphere, sees the landlord control the enforcement of covenants for each tenant.

Model 2: Contrastingly, a letting scheme is often used in the residential property sector. Under a letting scheme, each tenant covenants directly with all other tenants, with an intention for mutual enforceability of each covenant.

Model 3: The third model operates as a middle-ground between the former models. Here, there is no letting scheme, and the leasehold tenants cannot sue each other directly for breaches of covenant. However, tenants can request that the landlord takes action against a fellow tenant upon certain conditions being met, such as the payment of costs and the provision of security for such costs, just as Dr Duval did.

The relevant lease clauses

So what are the relevant lease clauses, what do they mean, and what is the relationship between them?

The first clause was concerned with alterations, improvements and additions. It stated that a tenant cannot undertake works to their property without permission from their landlord. This is a qualified covenant. In the absence of express drafting, it is implied under statute that such consent from the landlord cannot be unreasonably withheld.

KEY POINTS

- **Mutual enforceability provisions may become obstructive to proposed alteration works.**
- **Previous landlord discretion surrounding alteration works may now require greater thought.**
- **There is uncertainty as to how this case will impact landlords in the commercial property sector, but it may result in potentially reduced development opportunities for tenants.**
- **The power wielded by tenants could increase, and more varied options may need to be considered by landlords to solve alteration works being blocked by dissenting tenants.**

The second clause was:
"Not to commit or permit or suffer any waste spoil or destruction in or upon the Demised Premises nor cut maim or injure or suffer to be cut maimed or injured any roof wall or ceiling within or enclosing the Demised Premises…"

Contrastingly, this is an absolute covenant, which means a complete ban on a particular activity. Common absolute covenants include prohibitions against subletting the premises, structural works, keeping pets at the premises, and running a business from the premises for instance.

This case highlights the relationship between these two types of clauses. The absolute prohibition of the second clause did not extend to routine repairs, renovations, and alterations, these are covered by the qualified covenant. Consequently, routine works and alterations would not impinge on the other lessees or adversely affect the structure.

The last relevant clause was the mutual enforcement clause, the clause on which this case was decided. The clause points to the prohibitions above and precludes the landlord from granting a licence to any lessee to do anything that would otherwise amount to a breach of an absolute covenant in that lessee's lease. Whilst the clause does not expressly state that the landlord cannot grant consent to the works, it was found to be implied.

The decision

The SC confirmed that where a lease contains an absolute covenant, a requirement for all tenant leases to be granted in substantially the same form, and a mutual enforceability covenant obligating the landlord to enforce such covenants upon request, then the landlord would be in breach if they give consent to another tenant to carry out works in breach of an absolute covenant. The SC argued that it would be "uncommercial and incoherent" to suggest that a dissenting tenant's enforcement request could be overlooked by the landlord.

Application to commercial properties

The impact of this case on a commercial property is yet to be fully appreciated in practice. If a landlord is approached by tenants who wish to undertake prohibited alteration works that require landlord consent, any of the following could apply:

- A landlord could be mandated by way of an injunction to take enforcement action against a breaching tenant, requiring them to reinstate such work.
- Recently issued licences for works may be open for challenge due to the 12-year limitation period in which to bring a claim for breaches of covenants. Damages may be minimal, but nuisance claims could be significant.
- A landlord, property owner and/or developer alike could face uncertainty, which could be enough to reduce and/or hinder development opportunities.
- Its application may extend to qualified covenants that are not complied with; for instance, a landlord will not be able to grant retrospective consent to works performed in breach of any covenants requiring a landlord's prior approval.

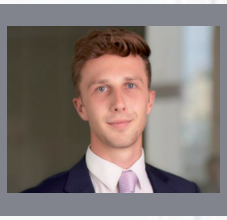
The potential challenges are varied, and there is no reason why the mutual enforceability clause could not be applied to other situations where absolute covenants prohibit certain types of flooring, signage, and usage for instance. Where landlords have previously shown discretion around such matters, they may now be more cautious.

Commercial Solutions

But is it all doom and gloom for landlords who find themselves in a position where they are happy to grant consent to alteration works to be performed by a leaseholder, but a separate leaseholder is objecting to the proposed works as per their mutual enforceability covenant? The following proposed solutions present options for landlords to consider to resolve this potential issue:

- Decline to grant consent to the works.
- Re-seek consent from all the affected tenants.
- Grant consent to the works in the form of a licence and suffer the potential damages which could be minimal, should all the tenants not consent.
- Grant consent to the works on grounds that the landlord is protected against claims by other tenants, for example, by requiring an indemnity from the tenant, and granting consent on the condition that the tenant reinstates the premises in the event of a compliant for breach of the mutual enforceability clause.
- Formally vary the relevant lease, as opposed to granting a licence, on the premise that the landlord is 'enforcing the lease'.
- Make an application to the Lands Tribunal under Section 84 of the Law of Property Act 1925, which allows the modification or discharge of a restrictive covenant. This option is a possibility if the lease was granted for a term of more than 40 years, and at least 25 years have expired.

These are just some of the issues and solutions presented by the Duval case. In practice, it is likely that more will come to fruition.



ALEX PAINTING
Trainee Solicitor
T: +44 (0)20 3697 7402
E: apainting@wedlakebell.com

TEN THINGS TO CONSIDER WHEN LETTING A RESTAURANT

If you are a landlord who has a food and beverage (F&B) premises in your portfolio, or you are a prospective tenant who has found a site that is the perfect location for a restaurant, what are the top ten things you should consider? Here are our thoughts:

1. **Permitted Use** – firstly, does the premises have the correct permitted use for planning purposes? Put simply, will the local authority allow a F&B business to operate there? If so, does the permission suit the type of F&B business intended to operate from there? A permission for a premises to sell hot food takeaways (a "sui generis" permission) is different to a permission to sell food and drink for consumption mostly on the premises (Class E(b)). Putting in one table by the counter would not turn a takeaway into a restaurant but adding ten tables might incur the wrath of the local authority.
2. **Kitchen extraction systems** – a key part of the F&B fit out is the kitchen, and an important part of that kitchen is ensuring adequate ventilation and extraction of things like steam and cooking odours. An issue to get ahead of if the premises will require an external duct or extractor as these units often require access to the exterior of the premises to discharge the air.
   If the premises are only part of the building, it is likely that the demise will be an 'internal only' demise. This will mean that a tenant will need the landlord's consent (and any superior landlord's consent) to carry out alterations to the structure and/or exterior of the building. This can be dealt with in a 'fit out licence'. Some landlords may be more reticent to allow structural alterations, or the building may have certain restrictions on it – for example, a listed building which is prohibited from having certain works carried out on it to preserve the history of the building.
3. **Noise, smell, and nuisance** – as popular as a restaurant may be with its clientele, you may find that neighbours, whether residential or commercial, are less supportive. The lease may have permitted hours of use to ensure that patrons are not leaving too late at night, or that the sounds of clanking bottles or a busy kitchen do not disturb a good night's sleep. Most F&B leases usually have prohibitions on causing a nuisance or annoyance to any neighbouring property, including noise, fumes, or smells.
4. **Seating Licences** – is the premises adjacent to some open space that would be simply perfect for customers to spill out onto on a summer night? A few tables outside, some space heaters in the winter? If you are planning to use outdoor space, it is crucial to make sure that there is either a) the right for the tenant to use it in the lease or b) that space is included in the premises (check the demise plan). If the open space belongs to the landlord, they may grant a separate seating licence to allow seating to be set up out there. If the land belongs to the Council (for example a wide pavement outside a busy city pub) then it may require a 'pavement licence' to place removable furniture over the pavement as part of the public highway.
5. **Premises Licences** – sticking with licences. Will alcohol be served at the premises? Will live or recorded music be played? Most people are aware that a premises licence from the local Council is required to serve alcohol (and it is a crime to serve alcohol without one), but the premises will also require a 'PPL PRS' licence if there is going to be live music or recorded music played – the cost of such a licence will depend on the venue and how the music is used.
6. **1954 Act Renewal** – does the lease grant the tenant 'security of tenure'? This antiquated phrase gives the automatic right for the tenant to renew a lease on similar terms on expiry. If it does not have security of tenure, at the end of the term the landlord can ask the tenant to vacate and any goodwill or local following from the location may be lost. Some purpose-built developments will always insist on excluding security of tenure to keep control of their investments going forward – but this should be discussed at Heads of Terms stage.
7. **Break clause** – when entering into a lease, the tenant covenants to pay the landlord the quarterly rent until such time as the lease ends, or they can 'assign' their obligations to another company. A break clause allows the tenant to exit the lease on a pre-agreed date, subject to mutually agreed conditions. The starting position from a tenant perspective should be that if they have given the landlord enough written notice, are not in arrears of annual rent, and have removed any undertenants or third-party occupiers from the premises on the break date, then they will have successfully operated the break clause and are free to go.

8. **Turnover rent** – the landlord or their agent may suggest that the lease include turnover rent. This allows the landlord to charge the tenant a percentage of their turnover as rent. This may seem attractive in principle because if an F&B business is performing poorly then surely the turnover goes down and so does the rent? Most landlords will insist on a 'higher of' calculation, so the tenant either pays a) the basic agreed rent or b) the turnover rent, if that is higher. Turnover rent is particularly popular in retail and F&B because it (in theory) promotes a collaborative approach between landlord and tenant. If the landlord keeps the shopping centre or development in good repair and attractive to customers, then the tenant's turnover should increase and the landlord shares in the profits and both parties share the hit of any downturn in the industry.
9. **Rent free** – as the name suggests, this is an initial period where rent is zero in order assist the tenant with fitting out the premises and to assist the tenant to bed in during those difficult opening months. The number of months (or years!) will depend upon bargaining positions, the desirability of the location and the tenant's financial history, but do not be afraid to discuss either reduced rent or free rent.
10. **Repair** – the premises may currently be stripped back to shell. This blank canvas can be thrilling, but the parties need to take into consideration what the tenant will have to hand back to the landlord on the expiry of the lease. All the bespoke fit out may have to be pulled out to return the premises to the shell received on day one, at great cost to the tenant. At the end of the lease, the landlord will expect their premises to be returned in good repair and condition, to allow them to quickly re-let to a new tenant. It may be worth limiting the tenant repair obligation with a photographic 'schedule of condition' – this is a set of photos to be attached to the lease, which ensures the tenant only must hand back the keys with the premises in the state shown in the photos.

KEY POINTS

- **Negotiate – ensure that any financial points such as rent frees, break clauses, turnover rent or schedule of condition are agreed up front in the Heads of Terms.**
- **Fit out – agree fit out in advance. Will the tenant's extraction system aggravate the neighbours with fumes and noise? What state does the tenant need to hand the property back in?**
- **Licensing – does the premises require an outdoor seating licence? A premises licence for alcohol? A music licence? A gambling licence? All these licences require time and effort and should be sorted as early as possible in the transaction.**

ROB MCKELLAR
Associate
T: +44 (0)20 7674 0515
E: rmckellar@wedlakebell.com

PAY NOW, ARGUE LATER ABOUT SERVICE CHARGE DEMANDS

A recent Supreme Court decision dealt with the interpretation of a standard commercial service charge provision. Landlords and tenants will be interested in the Court's finding that a certification provision in a service charge created a "pay now, argue later" position rather than allowing the landlord to treat the certification of a financial year's service charge as conclusive.

The facts

The case was *Sara & Hossein Asset Holdings Limited v Blacks Outdoor Retail Limited* [2023]. The retail chain Blacks had received a service charge bill which was more than 700% higher than the previous year. Blacks had not paid the quarterly on account instalments of the estimated service charge. The lease contained a provision stating that the landlord was to provide the tenant "as soon as practicable after such total cost and the sum payable by the tenant shall have been ascertained a certificate as to the amount of the total cost and the sum payable by the tenant and in the absence of manifest or mathematical error or fraud such certificate shall be conclusive".

The landlord argued that the clause did what it appeared to do at face value and it allowed the landlord to certify both the total costs of its expenses and the sum of service charge payable by Blacks. Blacks was permitted defences in that if there was manifest or mathematical error or fraud then Blacks could challenge the service charge. Blacks had not sought to use these permitted defences. Instead, Blacks argued that whilst the certificate could be conclusive as to the amount of expenditure that the landlord had incurred, it could not be conclusive as to Blacks' actual liability for service charge. The landlord should not be allowed to be "judge in his own cause".

The findings

The judge at first instance had agreed with Blacks that the certificate was conclusive as to accounting matters and the amount of the costs incurred but was not conclusive as to the question of whether the costs themselves fell within the scope of the service charge provisions of the lease and whether they could be properly recovered through the service charge. The judge at first appeal agreed with this analysis.

The Court of Appeal disagreed. It found that the clause could be clearly and plainly understood and the effect was that the certificate was conclusive as to the amount of the total cost and the sum payable by the tenant. There was no express term which distinguished the sum payable by the tenant from its liability under the lease. The Court of Appeal held therefore that the landlord was entitled to summary judgment on its claim for unpaid service charges. The Court found that the lease provisions were successful in limiting the tenant's ability to resist payment. The landlord needed the regular cashflow coming from a conclusive service charge regime for it to provide the services.

The decision of the Supreme Court was to find a third way between the landlord's argument that the service charge was a "pay now, argue never" (apart from the permitted defences) regime and Blacks' argument that it was an "argue now, pay later" regime. The Supreme Court's interpretation was that the provision was a "pay now, argue later" clause. The certificate was conclusive as to the landlord's claim, and the tenant had to pay it as the landlord was entitled to summary judgment for any failure to pay. However, Blacks could subsequently raise any arguable counterclaim if it was able to establish one.

The Supreme Court argued that the lease contained several provisions that would have been inconsistent with an ability of the landlord to be a judge in its own cause, for example the obligation on the landlord to provide the services in accordance with the principles of good estate management, the tenant only being liable for a fair and reasonable proportion of the overall expenditure, and the right to inspect the landlord's receipts and invoices.

Analysis

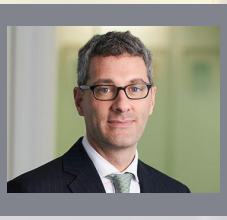
The judgment is a mixed bag for landlords and tenants. The good news for landlords is that in dealing with clauses like this, then in the absence of a tenant raising an argument that there has been manifest error or fraud, summary judgment should be available to a landlord making a claim for unpaid sums. This will be a quick way for the landlord to recover monies which will help the landlord with its cashflow. Tenants will not be able to engineer leverage by withholding payment to negotiate discounts. They will not be able to raise frivolous claims. They will have to pay and then consider carefully as to whether they can establish a counterclaim.

For tenants there is the good news that even if any issues do not amount to there being "manifest errors", the tenant will still have a right to counterclaim later against the landlord if they wish to challenge elements of the service charge which have been passed on to them. Whether the tenant can challenge will depend on the precise wording of the service charge provisions within the lease. The landlord will not simply be able to put anything through the service charge without fear of any comeback.

Finally, this case is of interest from a legal perspective as the majority in the Supreme Court were prepared to interpret the lease in a highly "purposive" way. There was a dissenting judgment from one of the judges who said that the other judges' interpretation was not supported by the actual language of the clause itself. Lord Briggs thought that the correct interpretation was that the clause was a "pay now, argue never" regime where if the tenant could not use one of the permitted defences the landlord's certificate was conclusive as to both the total of the landlord's costs and the sum payable by the tenant. He said that the majority's interpretation was not open to the Court as it had not been advanced by either party and the Court was required "to choose between genuinely available constructions, rather than mending the parties' bargain". The judges were moving away from the actual wording of the lease and reaching a commercial interpretation based on reading the lease as a whole. This is not the usual way that Courts interpret contractual documents and it will be interesting to see if it sets a precedent.

KEY POINTS

- **Landlords may wish to seek less ambiguous wording in future leases so that it is clear that the certification of the service charge is truly conclusive as to the tenant's liability.**
- **Tenants will wish to try to water down any wording about certification being conclusive.**
- **Tenants with similar wording in their leases are in practice going to have to pay up or risk summary judgment.**
- **They may however be able to raise any claims even after paying.**



BEN DUNBAR
Senior Associate
T: +44 (0)20 7406 1699
E: bdunbar@wedlakebell.com

WHAT IS A SECTION 106 AGREEMENT?

A local planning authority ("**LPA**") can mitigate a development's impact by making the grant of planning permission conditional on the completion of an agreement with, or a unilateral undertaking from, the landowner and/or developer. These agreements / undertakings (collectively known as '**planning obligations**') are made under section 106 of the Town and Country Planning Act 1990 ("**TCPA**"), and hence commonly referred to as 'section 106 agreements'.

So what can a planning obligation secure?

Planning obligations are used by LPAs to secure various benefits, including affordable housing and financial contributions for infrastructure and the local community like schools and public open space. The TCPA allows their use specifically for the purposes of:

> *"(a) restricting the development or use of the land in any specified way;*
> *(b) requiring specified operations or activities to be carried out in, on, under or over the land;*
> *(c) requiring the land to be used in any specified way; or*
> *(d) requiring a sum or sums to be paid to the authority"*

The scope of their use is however restricted by the Community Infrastructure Levy Regulations 2010, which require them to be:

- necessary to make the development acceptable in planning terms;
- directly related to the development; and
- fairly and reasonably related in scale and kind to the development.

These requirements are repeated by the National Planning Policy Framework, and LPAs must consider whether otherwise unacceptable development could be made acceptable through the use of planning obligations, in line with the three tests. Planning obligations that do not meet these legal and policy requirements cannot be taken into account by an LPA (or by a planning inspector on appeal) in deciding whether planning permission should be granted, and could place the planning permission at risk of judicial review.

In appeal situations, it is important to include a clause that allows the planning inspector to decide if the obligations meet the tests so that any of them can be held to be ineffective if they do not – this enables an inspector to grant planning permission where they may otherwise have been unable to due to an offending obligation.

The recent case of *The University Hospitals of Leicester NHS Trust, R (On the Application Of) v Harborough District Council* [2023] EWHC 263 (Admin) highlights the constraints on the use of planning obligations. The LPA had rejected the NHS Trust's request for a s106 contribution of 'about £914,000' to meet a localised funding gap that it argued the new development would precipitate. The court agreed with the LPA that the development would not create a localised funding shortfall, so the requested contribution would not meet the tests. The case clarifies that planning obligations cannot be used to address wider systemic problems that are not created by a proposed development.

Who makes the obligations to the LPA?

Whilst the TCPA does not require all those with an interest in the land to be a party to a planning obligation, in most cases LPAs do insist that they are, including mortgagees. It is sometimes possible to persuade LPAs to relax this requirement, for example in the case of owners of short leases, if the LPA can be satisfied that sufficient interests are otherwise bound and the obligations are capable of being enforced. The case of *R (McLaren) v Woking Borough Council [2021] EWHC 698 (Admin)* is a useful reminder of that. It involved a claim for judicial review of a planning permission, one of the claimant's grounds being that they should have been included as a party to the associated planning obligation due to their interest in the land. That argument failed as the court held that there is no legal requirement for all interests in a site to be bound by a planning obligation.

Since planning obligations automatically bind any successor in title to the covenanting parties' interests in the development land, the responsibility to comply with any undischarged obligations, as well as the liability for any breaches, will pass to future owners and occupiers, and potentially also mortgagees. For this reason, planning obligations often exclude liability for owners/occupiers of individual homes, mortgagees and statutory undertakers.

KEY POINTS

- **The scope of planning obligations is strictly controlled by legislation.**
- **Proposed obligations should be checked against the three 'tests' to reduce the risk of a challenge to the planning permission.**
- **Planning obligations run with the land, meaning any undischarged obligation could pass to a future owner, occupier or bank.**
- **Any variation to a planning obligation must comply with strict formalities.**
- **If enacted the Levelling-up and Regeneration Bill could change the existing regime significantly.**

It is essential that all parties acquiring an interest in a property that is bound by a planning obligation check that it has been complied with and are fully aware of their potential future liabilities.

Can planning obligations be varied?

Planning obligations made under s.106 of the TCPA can only be varied or discharged by deed using the provisions of s106A of the TCPA. Again, LPAs usually require all those with an interest in the development land to be parties to the deed, which can be problematic where various parts of the land have been sold. There is no similar power to vary or discharge old 'section 52 agreements' – an application may need to be made to the Upper Tribunal (Lands Chamber) for a discharge or modification of a restrictive covenant to achieve that.

The TCPA is silent on the period in which undischarged obligations remain enforceable, so it is unclear if the 12-year time limit imposed by the Limitation Act 1980 applies to breaches of planning obligations, or if LPAs may enforce breaches beyond that limit.

Future changes

The government intends to overhaul the existing regimes for planning obligations and the Community Infrastructure Levy in favour of a new 'Infrastructure Levy' to be introduced by the Levelling-up and Regeneration Bill. It is anticipated that planning obligations will remain necessary, but with a reduced scope.

Provisions in the Environment Act 2021 come into force in November 2023 which will require all developments to deliver a net gain of at least 10% in biodiversity value, generating obligations that may be secured by a planning obligation, particularly where off-site provision is proposed.

BARTHOLOMEW PRESTON
Trainee Solicitor
T: +44 (0)20 3697 7404
E: bpreston@wedlakebell.com

REGISTER OF OVERSEAS ENTITIES... THE STORY CONTINUES

As readers are aware, the Economic Crime (Transparency and Enforcement) Act 2022 ("**Act**") brought into being the Register of Overseas Entities ("**Register**"). The provisions relating to the Register came into force in stages in August and September 2022 and the transitional period for initial registration ended on 31 January 2023.

KEY POINTS

- **If an overseas entity is to acquire a new interest in property at the Land Registry, it must be on the Register at the date of the application for registration at the Land Registry.**
- **If an overseas entity wants to deal with a property that is (or should be) registered at the Land Registry, it must be on the Register at the date of the disposition. This is a once and for all opportunity for compliance.**

Current status

The position now is that any overseas entity which is the registered proprietor of UK property acquired on or after 1 January 1999 must now be on the Register or have made an application to be on the Register prior to the end of the transitional period. Such an entity, and all its responsible officers, will have committed an offence under the Act if it has not. Furthermore, where an overseas entity disposed of all of its UK property prior to the end of the transitional period, but after 28 February 2022, there is an obligation to have made certain disclosures to Companies House. A failure to disclose constitutes an offence under the Act.

Some commentators have asserted that as many as 40% of the overseas entities which ought to have applied to be on the Register have failed to do so. It would seem that the prosecuting authorities are going to be busy!

The logjam

We have concerns that the speed (or lack of) with which the Land Registry deals with applications to register property transactions may mean, on a strict interpretation of the Act, that offences will have been committed inadvertently. By way of example, a property may have been disposed of before 28 February 2022 but registration at the Land Registry remains pending. This means that there is a risk that an overseas entity will still have been the registered proprietor of property on 1 February 2023 (after the end of the transitional period) and will neither be, nor will have applied to be, on the Register. This is an offence. Similarly, an overseas entity which is not on the Register and has not applied to be on the Register, will also technically have committed an offence if it has sold a property but is still the registered proprietor on 1 February 2023 even if it has complied with its disclosure obligations under the Act. Paradoxically, once the Land Registry completes the registration of the disposal, that registration is backdated to the date the application was sent to the Land Registry with the result that the offence disappears. It is to be hoped that the prosecuting authorities take a sensible and pragmatic approach to such issues.

Mission critical

Going forward, it is important to remember:

- If an overseas entity acquires registered land or a lease for a term of seven years or more, it must be on the Register **at the date of the application** for registration at the Land Registry. The Land Registry will reject any application which is not in compliance.
- If an overseas entity owning registered land enters into a transfer/lease/charge, it must have a valid registration on the Register **at the date of the disposition**, failing which the disposition cannot be registered at the Land Registry.

The difference between these two situations is that the first can be cured by getting the overseas entity on the Register and then applying for registration at the Land Registry (although there are other risks). The second situation cannot be cured other than by effectively repeating the failed disposition after the overseas entity is on the Register.

And it is not over yet

The Government has introduced a further Economic Crime and Corporate Transparency Bill which, among other things, will introduce verification procedures for all new and existing directors and persons with significant control. We will keep our readers informed as things progress.

PHILIP MATTHEWS
Partner
T: +44 (0)20 7395 3105
E: pmatthews@wedlakebell.com

BUILDING SAFETY ACT UPDATE

2023 is the year when most of the provisions of the Act will be implemented. This will have a significant impact on all parts of the construction and real estate industry including developers, property owners, building managers and those who manufacture or sell construction products.

Join us on 18 April 2023 for a breakfast seminar update on the Building Safety Act 2022 with construction lawyers from Wedlake Bell and fire engineering experts from DCCH Experts LLP.

DCCH will share their perspectives on the Building Safety Act 2022 based on their extensive knowledge in fire safety, gained from investigating major incidents.

Date: Tuesday 18 April 2023

Time: Registration from 8.30am, 9:00am start

Venue: Wedlake Bell, 71 Queen Victoria St, London EC4V 4AY

For information and to register please click ***here***.

Click ***here*** to manage your email preferences.

Wedlake Bell LLP
71 Queen Victoria Street, London EC4V 4AY, DX 307441 Cheapside
T: +44 (0)20 7395 3000 | F: +44 (0)20 7395 3100 | E: legal@wedlakebell.com

www.wedlakebell.com