Wedlake Bell

QUARTERLY IN ADVANCE

WINTER 2023

NEWS AND VIEWS FROM OUR REAL ESTATE TEAM

IN THIS ISSUE

DEAR GEMMA

An extra bank holiday has been announced for the coronation which means an extra-long weekend but does this affect my property completion date?

On 6 November 2022 the Prime Minister proclaimed an extra bank holiday in honour of the coronation of His Majesty King Charles III. The bank holiday will fall on Monday 8 May 2023, following the Coronation on Saturday 6 May 2023.

Even though it is January 2023, it is still possible that parties could have contracted to complete on 8 May 2023 and the bank holiday could throw a spanner into the works because:

- it won't be possible to transfer completion money as the banks will be closed; and
- the professionals involved will be on leave.

What is the completion date?
It might be that the bank holiday doesn't affect many transactions given that six months' notice has been given. Ideally the parties can think ahead and avoid using 8 May 2023 as the completion date.

But sometimes a completion date is not fixed and instead, it is triggered by the happening of a certain event. This event is often referred to as a condition precedent. For example, a sale and purchase might be conditional upon the grant of planning permission. The completion date for such a deal could be 5 – 10 working days after the satisfaction of the relevant condition.

In this situation, much will depend on the definition of 'working day' in the contract. The Standard Commercial Property conditions ("**SCPCs**") are usually incorporated into most commercial sale and purchase contracts. The SCPCs define a working day as "any day from Monday to Friday (inclusive) which is not Christmas Day, Good Friday or a statutory Bank Holiday". If this definition is used, 8 May 2023 would not be included as a working day and would be excluded from the relevant period and completion would naturally fall to 9 May 2023.

But what happens if there is already an existing contract and completion is fixed for 8 May 2023?
Everyone involved in the deal is going to need to be pragmatic.

The risk of being unable to pay the completion money on the completion date is one for the buyer. Under the SCPCs, the non-payment on the relevant day will attract interest. The seller also has the ability to serve a 'notice to complete'. The effect of the notice to complete is usually to set a specified time frame by which the money has to be paid and completion has to have occurred, otherwise the seller has the ability to terminate the contract and keep any deposit paid by the buyer for itself.

Hopefully, everyone would proceed as planned but complete a day later being the first working day afterwards. The Banking and Financial Dealings Act 1971 provides that:

- no-one can be compelled to make a payment on a bank holiday, and
- the making of a payment on the first working day after a bank holiday is deemed the equivalent of making a payment on the due date.

Everyone would pre-agree that the operation of law means completion will take place on Tuesday 9 May 2022 and ideally, also pre-agree what is going to happen about any interest due in advance.

Recording the agreed changes to the contract
There is a difference between agreeing completion will take place on 9 May 2023 by operation of law and making other changes.

The Banking and Financial Dealings Act 1971 defers the obligation to pay completion money to the following working day. This dovetails with case law that if an act required by a contract is impossible to perform lawfully at a given time, then enforcement of the obligation cannot take place until the act can be performed lawfully (*John Lewis Properties v Viscount Chelsea [1994] 67 P&CR 120*).

If a change of date to 9 May 2023 is the only change, there is a statutory change to the contract pursuant to the Act and the contract is unlikely to need to be formally varied. If completion is going to be any date other than 9 May 2023, or if other changes are made to the contract, it will be necessary to comply with section 2 of the Law of Property (Miscellaneous Provisions) Act 1989 and formally vary the contract.

Any party should take specific advice as to the precise terms of their contract as much can depend on the given circumstances.

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THE BUILDING SAFETY ACT 2022 10 THINGS YOU NEED TO KNOW

On 10 October 2022 our construction team held the first in a series of seminars about the Building Safety Act ("**BSA**") which will have a significant impact on building owners and all those involved in real estate development. The seminar presented practical and understandable guidance with one attendee telling us that it was *"a thoroughly interesting and informative presentation"*. Anyone who would like to attend future seminars, which we will run as more of the BSA comes into force in 2023, please register ***here***.

In the meantime we set out below the top ten things you need to know for now.

- The BSA provides for a new **Building Safety Regulator** who will be responsible for the building control regime for higher-risk buildings in construction which will include buildings of **18 metres in height or 2 storeys which contain two residential units, care homes and hospitals**.
- There are three "Gateway" points for **new higher risk buildings** which must be complied with before the development proceeds:
  - Gateway 1 – Introduced via existing planning legislation on **1 August 2021** in relation to higher risk buildings;
  - Gateway 2 – Hard stop – Approval must be obtained prior to commencement of construction. Anticipated to apply from **1 April 2023**;
  - Gateway 3 – Hard stop – A completion certificate will be required prior to registration and occupation. Anticipated to apply from **1 April 2023**.
- Requirement to register **existing higher risk buildings** with the Building Safety Regulator (anticipated to be required by **October 2023**).
- Provision for a "**golden thread**" of building information to be created, **stored digitally and updated** through the Gateway process and throughout the building's life-cycle.
- An ongoing duty on the **new Accountable Person** (i.e. the building/ estate owner or entity under repairing obligations of common parts) to assess building safety risks, provide safety case reports to the Regulator and apply for building assessment certificates.
- Changes to the Defective Premises Act to **extend the limitation period to 30 years retrospectively before 28 June 2022 and 15 years prospectively after 28 June 2022**.
- New **Dutyholders** (clients, principal contractor, principal designer, designers and contractors) will be required for all building works but with additional duties for higher risk buildings.
- New regulation and liabilities in relation to construction products.
- New orders available to assist with pursuing those responsible for defects which pose a **building safety risk** and their associated persons.
- **New homes ombudsman scheme** and obligation to provide to the **purchaser a new build home with a warranty** and provide to a prescribed person with a **warranty for any common parts**. More regulation of building control/approved inspectors. Registration deadline for building inspectors and building control approver expected to be by **October 2024**.

Any queries should be directed to Sarah Elliott or Natalie Pilagos in the construction team.

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I DON'T KNOW ABOUT YOU, I'M FEARING SECTION 20 TOO

Service charge payments will be a familiar term to most residential and commercial lessees. The amount you have to pay in service charge in any given year is dependent on a number of factors, and the starting point is always to check the terms of your lease. However, in certain periods tenants may see fluctuations in the service charge demands received, which can often be attributed to the landlord having carried out a significant set of works to a property which they want to reclaim (some) of the cost.

Section 20 of the Landlord and Tenant Act 1985 ("**1985 Act**") sets out the landlord's requirement to consult a residential tenant in relation to certain service charge contributions due from the tenant.

Who does it affect?

Section 30 of the 1985 Act indicates that consultation will apply to all landlords who have a right to enforce payment of service charge. The consultation requirements extend beyond just freeholders and will apply to any management company or head tenant who has the right to enforce service charge payments. In terms of who and what falls under the service charge costs category will largely depend on the terms and definitions contained in the lease.

What works trigger consultation requirements

Given the associated time implications in following the section 20 procedure the requirement to consult a tenant will only be triggered if they fall into the category of either "qualifying works" or "qualifying long-term agreements".

- **Qualifying works** – defined as a single set of works that will cost any one contributing residential tenant over £250. In a building made up of several residential tenants who contribute differing amounts of service charge the need for consultation will be triggered if just one of those tenants has to pay over £250.
- **Qualifying long-term agreements** – an agreement entered into by the landlord with a third party provider for a period of more than 12 months, where the amount payable by a residential tenant in any one accounting period is over £100.

The consultation process and failure to consult

The consultation process is as set out in **The Service Charges (Consultation Requirements) (England) Regulations 2003**, in brief the consultation involves a four stage process:

- Notice of intention;
- Inspection of proposed works;
- Duty to have regard to observations; and
- Landlord's response to observations.

The consultation period under the regulations is designed to be formulaic. However, there is a risk that where the residential tenants push back on a landlord's intended works the landlord may face significant delays in proceeding with the works.

KEY POINTS

- **Section 20 procedure offers an important level of protection to residential tenants who pay a service charge.**
- **A landlord's failure to consult may result in the costs they are able to recover from the tenant being capped.**
- **Both the landlord and the tenant need to pay close attention to their lease terms and how those terms cater for service charge payments.**

One option for a landlord is to apply to the First-tier Tribunal for a dispensation from the need to consult. The application can be retrospective to carrying out the work, for example where the work needed was urgent. In deciding whether to award dispensation the tribunal will consider a number of factors including whether the residential tenants suffered any prejudice as a result of the landlord's failure to consult.

Otherwise, where the landlord has failed to consult they are at risk of being capped for the amount of service charge they may recover from their tenants. For example, for Qualifying Works that cap will be set at £250 which can be a significant drawback depending on the cost of the work proposed.

Conclusion

The section 20 procedure should not be something that either a landlord or a tenant fears. It provides clear guidelines a landlord should follow when looking to recover service charge for any qualifying works. Landlords will need to consider questions such as commerciality, i.e. is the time taken for consultation proportionate to the level of costs they are seeking to recover. It similarly gives a tenant an important level of protection against what could be otherwise excessive service charge costs.

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WELCOME

Megan Bruce

Megan joined the Wedlake Bell Construction team as a solicitor in October 2022 having trained at Winckworth Sherwood. Megan has gained further experience through her time as a Construction Arbitration Paralegal at White & Case and as a Real Estate Paralegal at Devonshires.

Before joining Wedlake Bell in 2022, Megan undertook two construction secondments to housebuilder clients. She is experienced in drafting, negotiating, and advising on construction documents including building contracts, professional appointments, collateral warranties, reliance letters, performance bonds and deeds of novation. Additionally, Megan has assisted clients in relation to building and fire safety issues in existing buildings.

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HOW COULD SANCTIONS AFFECT PROPERTY TRANSACTIONS?

The UK government brought in various measures to restrict the use of assets as a result of the invasion of Ukraine. The measures are known as the sanctions regime. Andrew Griffith, the economic secretary to the Treasury, said: "As staunch defenders of democracy, the UK is united with its allies in opposition to Russia's barbaric and unprovoked invasion of Ukraine. We have imposed the most severe sanctions ever on Russia and it is crippling their war machine". Sanctions have now been imposed on over 1,271 people – including the former Chelsea FC owner Roman Abramovich – according to a recent review of the Office of Financial Sanctions Implementation ("**OFSI**").

KEY POINTS

- **It is a criminal offence to make a payment to a sanctioned designated person.**
- **Check OFSI's register of designated persons before proceeding, and consider applying for a licence.**
- **Seek legal advice if you are concerned a transaction may breach the sanctions regime.**

What does this mean for those not on the sanctions list?

Those not on the list of sanctioned people might still see the consequences of the sanctions regime. For example, in the context of a property deal, there could be a financial sanction such as an asset freeze, imposed upon someone you were looking to transact with. There are other types of sanctions (for example trade, immigration and arms embargoes). But we focus here on the freezing of assets as a financial sanction.

When a person is subject to an asset freeze, they must not deal with their assets, or make them available to, or for the benefit of, a "designated person". In short, the law restricts anyone from:

- receiving payment from or making funds available to designated persons on the sanctions list;
- dealing with their economic resources;
- making even legitimate payments to those persons.

So in a property context, tenants are susceptible to breaching the sanctions regime because payment of rent to a sanctioned landlord may be unlawful. This can place a tenant in a difficult position because, as a matter of contract law, if a tenant withholds payment due under its lease, the lease contains mechanisms for the landlord to seek redress for non-payment of rent and other amounts payable under the lease. These mechanisms include:

- adding interest to late payments; and/or
- the more draconian right of forfeiture. In certain circumstances and subject to the landlord complying with the statutory procedure, that right enables the landlord to re-enter the premises after the rent due under the lease is unpaid for a specified period of time to regain possession of the premises.

The OFSI, part of the Treasury, helps to ensure that financial sanctions are properly understood, implemented and enforced in the UK. It 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. Its powers are rooted primarily in the Sanctions and Anti-Money Laundering Act 2018. The OFSI helps everyone understand their financial sanctions obligations, monitors compliance and assesses suspected breaches.

What are the consequences of breaching the sanctions regime?

In short:

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

The OFSI can impose monetary penalties on any person who breaches financial sanctions. In this context, this could be the landlord and also the tenant. The maximum penalty is the greater of (a) £1,000,000 and (b) 50% of the estimated value of the funds or resources involved in the transaction. The OFSI takes several factors into account when considering a proportionate penalty value: this will be based on the facts of each case with reductions applied particularly in cases that have been voluntarily disclosed to the OFSI.

Increasing regulation

Most recently, the Economic Crime (Transparency and Enforcement) Act 2022 ("**2022 Act**") has introduced further changes to the sanctions regime. The 2022 Act has made it easier for the OFSI to impose monetary penalties because the 2022 Act has made breaching sanctions requirements a strict liability offence. In other words, there is no longer a requirement to prove that the individual or entity committing the breach had knowledge, or reasonable cause to suspect, that they were in breach of financial sanctions. This amendment applies only to civil liability and imposing a monetary penalty. It is not relevant to any assessment of whether a criminal offence has been committed under the sanctions regulations.

How could a tenant comply with the rules if a landlord is sanctioned?

On its website, 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 landlord, is a designated person according to that list. If so, in certain circumstances, a tenant can apply for a licence from the OFSI to enable payments to continue to be made to its landlord.

A licence can be obtained where the proposed transaction (here the payment of rents) covers either prior obligations (such as a pre-existing lease) or the payment of fees/service charges for routine holding or maintenance of frozen funds or economic resources (such as the payment of rents or service charges). The OFSI needs as full an explanation as possible, and evidence of the proposed transaction for which you need a licence. It may also ask for:

- the amount of an intended payment;
- the intended purpose of the transaction/funds;
- the intended payment route;
- details of the sender and receiver of funds (including any intermediaries) and beneficiaries;
- how the funds will be accounted for; and/or
- an explanation of the reasonableness of any proposed payment.

There is no guarantee that the OFSI will grant a licence. The OFSI can issue a licence only where there are legal grounds to do so. The OFSI expects that legal and professional advisers will have fully considered the relevant law and formed a view about an application before the OFSI is approached for guidance or an application is submitted.

If the OFSI grants a licence, then it would authorise payments that would otherwise be prohibited by the sanctions regime.

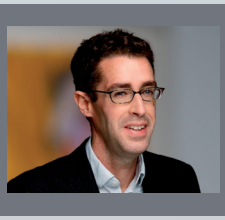
Any other tips?

The OFSI recommends applying for a licence as early as possible before a licence is needed. Licence applications can be legally and commercially complex. A high-profile licensee is Roman Abramovich. It has been reported that the former Chelsea FC owner holds an OFSI licence to enable ground rent payments to continue to be made to the Crown Estate for a property on Kensington Palace Gardens in West London, owned by Roman Abramovich or companies associated with him.

How has the market responded to the sanctions regime?

Jeremy Grey, a managing director at James Andrew International which manages buildings in London, told Bloomberg on 30 November 2022 that "the lesson is it's going to go on for a long time. There's no light at the end of the tunnel — when I spoke to the government about sanctions back in 2011 they said most of the funds they've frozen never get unfrozen."

The sanctions regime is here to stay. Various governments in recent years have made the direction of travel clear, increased surveillance and regulation on many aspects of financial dealings, especially, property related dealings, is something all parties need to be aware of as it is not just the sanctioned party that could be caught.



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WITHOUT PREJUDICE AND SUBJECT TO CONTRACT, AND THEIR APPLICABILITY TO COMMERCIAL PROPERTY TRANSACTIONS

"Without Prejudice" and "Subject to Contract" are labels commonly used in the context of negotiations. This article will give an overview of their meaning and applicability to commercial property transactions.

Without Prejudice

Without prejudice is a rule of privilege applicable to communications the purpose of which is a genuine attempt to settle a dispute. If it applies, the relevant communication or statement made is not admissible in court.

The rationale for the existence of this rule is one of public policy – to assist the settlement of disputes out of court, as parties are more likely to settle when able to communicate openly, without fear of admissions or statements against their interest being used against them in future litigation.

It is worth distinguishing the phrase "without prejudice save as to costs". If the rule applies, communications with this label will render the statement admissible on questions of costs, but not as part of the substantive dispute.

The key criteria for the rule to apply are:

- the existence of a dispute at the time of the communication; and
- that the communication was a genuine attempt to settle such dispute.

As to whether there is a dispute at the relevant time, this will be decided on a case by case basis, however the courts have said in this context that *"The concept of dispute is given a wide scope so that an opening shot of negotiations may fall within the policy even though the other party has not rejected the offer" – see Avonwick Holdings Limited v Webinvest & Anor, [2014] EWCA Civ 1436, paragraph 17.*

Therefore, labelling correspondence as "without prejudice" at an early stage where it becomes apparent that the circumstances could lead to a potential dispute may protect a party's position, where matters later evolve into litigation.

On this note, labelling correspondence as "without prejudice" is not determinative as to its treatment, as the courts will look at substance over form as to whether such correspondence is a genuine attempt at settlement. Such a label, however, assists the court in determining the intentions of the author, so is certainly advisable where litigation is a possibility.

With this in mind, some situations arising in routine commercial property transactions where it may be helpful to label correspondence (whether sent by lawyers, agents or the party itself) as without prejudice include:

- negotiating applications for landlord consent to assign, where perhaps a landlord is attempting to impose unreasonable conditions on its consent;
- negotiations in respect of 1954 Act renewals, including applications for extensions of time in respect of the same;
- negotiating dilapidations settlements following the expiry of a lease; or
- negotiations in respect of arrears settlements.

The recent case of *Octagon Overseas Ltd and others v Circus Apartments Ltd [2022] UKUT 302 (LC)* in the Upper Tribunal (Lands Chamber) gives an example of where the without prejudice rule has been upheld in the context of a property dispute. The dispute relates to a management order made in 2016, in respect of the leasehold flat buildings at the Canary Riverside Estate, a mixed-use residential and commercial development at Canary Wharf, comprising 325 apartments in four towers, together with a hotel, various restaurants, a cafe and a health club.

Circus Apartments Ltd ("**CAL**") is a long-leaseholder of apartments in one of the buildings on the estate and had been identified in the management order as one of the "commercial tenants". In March 2021, CAL applied under the Landlord and Tenant Act 1987 ("1987 Act") to vary the management order to remove reference to itself as a "commercial tenant", as CAL believed that being so described could prejudice its interests for certain parts of the 1987 Act.

In response, the landlord filed a witness statement referencing a text message sent in 2016 by a director of CAL, arguing that this text message suggested CAL's interest in the management order related to its aim to enhance its investment in the estate, rather than any concern with the quality of management of the estate. This meant the text message was relevant to the decision to renew the management order, given the purpose of Part II of the 1987 Act to protect residential leaseholders' interests (as opposed to promoting the interests of property managers). CAL sought to strike out this part of the witness statement, on the grounds that without prejudice privilege applied to the text message.

The text message actually related to a previous dispute between CAL and the landlord. CAL had requested consent to vary its underlease to construct additional floors in its building, and also to assign or underlet its lease to a newly incorporated company. The landlord was withholding its consent to the request to assign or underlet, which CAL considered unreasonable. The content of the text was a proposal from CAL to send the landlord the deed of variation requested and to pay £1 million if agreed, or alternatively CAL would issue proceedings for the delay in consent to the underletting or assignment, and also "throw [their] full support behind the neighbours" in their application for the original management order.

A key argument from the landlord for the text message to be admissible in the subsequent proceedings was that it related to different proceedings to those in which it was later put before court. This argument was rejected by the judge (albeit it is worth noting that the judge considered that the disputes could be connected). The court was satisfied that, despite not being explicitly labelled as "without prejudice", as the text message referred to a genuine offer of settlement to a dispute, the without prejudice rule applied and the message was not admissible.

Subject to contract

This label is frequently used by solicitors and agents to indicate that an agreement made over email or wording accepted in a draft document is not binding until such time as formally documented. The Court of Appeal has recently confirmed the use of such phrase in *Joanne Properties Ltd v Moneything Capital Ltd [2020] EWCA Civ 1541*, citing a number of previous cases in which the term had been considered, including the following passage from the judgement in *Generator Developments Ltd v Lidl UK GmbH [2018] EWCA Civ 396*:

"The meaning of that phrase is well-known. What it means is that (a) neither party intends to be bound either in law or in equity unless and until a formal contract is made; and (b) that each party reserves the right to withdraw until such time as a binding contract is made."

KEY POINTS

- **The without prejudice rule renders communications made in a genuine attempt to settle a dispute inadmissible in court proceedings.**
- **Whether or not such communications are labelled as "without prejudice" does not conclusively determine whether the rule will apply but assists the court in determining the intentions of the parties.**
- **The rule has application in a variety of contexts within commercial property transactions, including in the recent case example of *Octagon Overseas Ltd and others v Circus Apartments Ltd [2022] UKUT 302 (LC).***
- **Labelling communications as "subject to contract" clarifies the intention of the parties that any agreements are not binding until such time as they are formally documented, however property solicitors should still take further care in the context of licences for consent to ensure that consent is not inadvertently given by written communications, even where headed subject to licence.**

Particular care is still required, however, in the context of licences for consent. The case of *Aubergine Enterprises v Lakewood International [2002] EWCA Civ 177* makes it clear that a landlord's solicitor or agent must be careful to avoid inadvertently granting consent to alterations, assignments or underlettings, where the landlord's consent was deemed given despite some communications being headed "subject to licence". Before corresponding with another party on a licence, the precise terms of the lease should be checked to ensure that they stipulate that landlord's consent must be given by deed (as opposed to simply being "in writing") and any party should be careful to clarify in all correspondence that consent is not being given by virtue of the issue of a draft licence.

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RE'FLEX'IONS ON OFFICE WORKSPACES POST-PANDEMIC

KEY POINTS

- **Businesses are responding to the need for flexible workspaces to accommodate a more flexi-style workforce.**
- **There is still a need for office spaces. Employees may be eager to embrace a more flexible working style, but not at the expense of office interaction altogether.**
- **The commercial property market has proven itself more resilient and capable of change than might have been thought previously.**

It quickly became clear when the COVID-19 pandemic seized the globe, that the work landscape was going to change irreversibly. The relatively smooth switch for most office based businesses to remote working, afforded by the digital era in which the pandemic struck, meant that flexible working would be here to stay. Flexible working was no longer the apologetic request of the working parent. Instead, it became a convenience for all.

It was not an outlandish assumption, therefore, that business tenancies would see permanent changes including shrinking office spaces, fewer lease extensions or a reduction in office spaces altogether. Indeed, it was thought that many businesses might forego their offices and move to permanently remote working.

Almost three years on from the start of the pandemic, those assumptions for the commercial property market haven't quite panned out to that extreme.

Indeed, statistics show that businesses are increasingly looking to switch from long leases to flexible ones (also known as 'flex space'). An independent survey by flex space operator Orega revealed that, of businesses looking to reduce their office space, more than half are considering a switch from long leases to flex spaces. Flex spaces are commercial multi occupier spaces which focus on offering more flexible space allotment and lease terms.

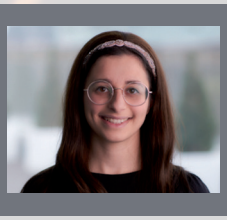
A flex space letting could be shorter term (up to 12 months) or even up to 10 years – and most flex space providers have different size spaces available so that occupiers can more easily accommodate growth changes or varying staff work patterns. This is particularly helpful in the early post-pandemic years, where businesses are still potentially working out the after-effects of COVID-19 on their sustainability and profitability as well as establishing a future direction.

Some organisations are investing in higher quality office spaces to improve the office experience. Others are adapting spaces within their offices for other purposes to keep encouraging office attendance for collaboration reasons or social or morale boosting purposes.

There are fears of hybrid working, such as the creation of a two-tiered workforce (where staff who work primarily or exclusively from home find themselves 'out of sight, out of mind' when it comes to contributing ideas, or being put forward for promotions); a reduction in performance (with less opportunities for ideas to organically flourish); and disadvantages for juniors or trainees who could find themselves with less opportunity to learn from experienced staff (listening to phone calls, being given ad hoc chances to observe client meetings etc).

Such fears might explain why the post pandemic commercial property market has become more flexible, just like the more flexible workforce that use the properties. But, not everything is super flexible. Some organisations are setting minimum office attendance requirements or even compulsory days. These actions might be taken to sustain the viability of the business premises as well as encourage in-person collaboration.

As confirmed by the Landmark Information Group, the commercial market has been more stable than the residential market since the onset of the pandemic. In fact, Landmark are seeing that larger commercial planning applications have surpassed 2019 levels overall in the past seven months. The demand and need is still there. Economic pressures have increased, particularly in recent months with the onset of a recession, but commercial lettings have not reduced as drastically as one might have thought they would back in 2020. What is clear is that commercial property lettings are adapting to accommodate the more flexible landscape of hybrid-working.



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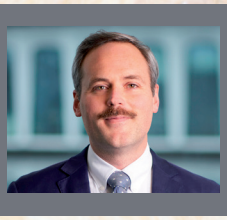
ON THE *HILLSIDE* AGAIN – AN UPDATE ON INCONSISTENT PLANNING PERMISSIONS

Last year we ***reported*** on a Court of Appeal decision which introduced some uncertainty around the validity of overlapping or 'drop in' planning permissions for multi-phased development schemes and also cast doubt over whether development lawfully undertaken in part of a scheme could be subsequently made unlawful if further development was carried out over a remaining part of the scheme not yet built out, under a new planning permission that is not consistent with the original permission. An appeal against that decision has now been rejected, and we now have the benefit of the Supreme Court's judgment with further clarity on the following points:

- consistent with the earlier decision, the Supreme Court reaffirmed (in even stronger terms) the *Pilkington* principle that "a planning permission does not authorise development if and when, as a result of physical alteration of the land to which the permission relates, it becomes physically impossible to carry out the development for which the permission was granted (without a further grant of planning permission)". The Supreme Court did state that the Pilkington principle should not be interpreted to mean that any departure from the permitted scheme, however minor, will be unlawful and that no further development is authorised unless it complies exactly with what has been approved; this would be "unduly rigid and unrealistic". They emphasised that the *Pilkington* principle will apply when the departure from the permitted development is material;
- addressing the doubt arising from the earlier decision, the Supreme Court held that development that has been carried out pursuant to a planning permission is not rendered unlawful by the failure or inability to complete development or further development under a new, inconsistent planning permission being undertaken over the remaining part of the scheme; and
- while the Supreme Court's judgment essentially recognises that 'drop in' applications remain a potentially valid avenue by which to seek to vary parts of a larger multi-phase development, the scope of situations where this option can be used appears to have narrowed. For 'drop ins' to be possible, the original permission must be capable of being "severed" into separate pieces, and in some cases it may be necessary to submit a new application that covers the entire site to which the original planning permission applies.

KEY POINTS

- **A departure from the permitted scheme will render unlawful the development already carried out due to the undertaking of further complete under a new, inconsistent planning permission.**
- **It will be necessary to take greater caution when relying on 'older' planning permissions that have been varied over time.**
- **'Drop in' applications now have a more limited use and will require particular care.**



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GREENER BUILDINGS NEED GREENER LEASES

A recent survey of prices paid for offices in London shows that a premium has developed for buildings that have accreditation for sustainability from organisations like British Research Establishment (**BREEAM**) and US Green Building Council (**LEED**) when compared with buildings which don't have these green credentials. According to the analysis, the gap between the prices has reached 25%.

Investors are increasingly focussing on sustainability. Other landlords (and tenants) need to be aware of the issues as well so they are not caught out by future changes in the minimum energy efficiency standards (**MEES**) required in respect of commercial property. See our ***article*** in this issue for more information about MEES. This article will consider the impact of MEES on lease drafting both in terms of new leases and interpreting existing leases.

Lease issues

It is estimated that one million commercial buildings need to be improved for efficiency purposes by 2030, which is 85% of the stock.

Landlords are liable for compliance with the MEES regulations. They don't impose a positive obligation on landlords to carry out energy efficiency improvement, but they do expose them to enforcement action and financial penalties in the event of breach of the regulations.

Landlords should be auditing their portfolios to understand how the length of lease terms may impact upon their position. Do they have leases expiring so that they will have an opportunity to carry out improvement works whilst the building is vacant? Landlords need to especially consider existing leases which will continue through 2023, 2027 and/or 2030 and whether lease provisions allow them to carry out upgrading works whilst the tenants are in situ.

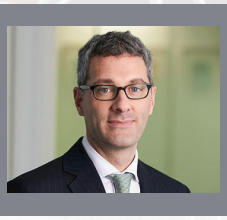
Landlords and tenants negotiating new leases have an opportunity to agree lease provisions to deal with any works that may be required, access to carry them out and who will bear the cost. Furthermore, landlords may well struggle to introduce novel provisions on renewals of existing leases. A recent case in the County Court (*Clipper Logistics Plc v Scottish Equitable Plc*) held that a landlord could not introduce certain green lease provisions in the context of an unopposed lease renewal under the Landlord & Tenant Act 1954. Although non-binding, this decision shows a potential obstacle to greener lease renewals.

Relevant clauses

The main areas to consider are:

- do the rights reserved to the landlord go wide enough? The clause may be too limited to cover the landlord entering the premises and carrying out improvements. Note however, that such a clause will probably mean that the landlord is unable to seek to rely on the consent exemption discussed in the ***article*** in this issue.
- checking service charge provisions for recoverability. If the landlord wishes to recover the costs of the upgrades through the service charge, then, as on the face of it the works will be improvement works, they may well not fall within the heads of recoverable expenditure under standard service charge provisions. Astute tenants will resist attempts to make them pay.
- if the landlord carries out improvement works to the common parts or shared services of the building, will this cause an interruption to the delivery of services by the landlord? This may put a landlord in breach of its obligations.
- do the alteration provisions prevent the tenant from carrying out alterations which would adversely affect the environmental performance or EPC rating of the premises or the building?
- are there provisions which restrict the tenant's ability to commission an EPC? From the landlord's point of view, they should only be able to do it with landlord consent and/or using the landlord's energy assessor.
- do the leases contain green lease provisions? Examples of these such as those published by the Better Buildings Partnership have been around for some time now.

The MEES deadline coming in April 2023 is a timely reminder for landlords to consider how the MEES regulations impact upon their properties, but also how the provisions in their leases may affect their strategy for compliance.



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INFLATING RENTS?

Rents linked to inflation, rather than to open market levels, have been a feature of the logistics sector for a number of years now. If other sectors are considering these, what should they be aware of?

First, pick your index. The long-established retail prices index ("**RPI**") often shows a higher rate of inflation than the modern consumer prices index ("**CPI**"). This is partly because they measure different things: CPI is internationally comparable and so doesn't include mortgage costs. However, there is a version of the CPI which does reflect the quirks of the UK housing market – CPIH – which can be used rather than the CPI main all items index. The differences are also due to the age of the two indices. RPI was based at 100 in 1987 while CPI was based at 100 in 2015. When your index is at 100 and inflation increases by 1%, the index rises to 101. But when your index has risen to 200 and inflation increases by 1%, the index rises to 202. As the index creeps up, it tends to overstate the impact of small increases, highly relevant when RPI as at August 2022 is 343.2 and CPI is 123.1. The other difference is the formula – RPI uses arithmetic mean but CPI uses geometric mean. The Financial Times notes that since January 2015 the average reduction in inflation due to this formula effect is 0.81 percentage points.

Second, check whether your chosen index will survive as long as your lease. CPI has been the official government measure of inflation since 2011; two years after that the Office for National Statistics declared that RPI was no longer an official statistic. What will happen to your index linked rent review if the ONS stops publishing the RPI? Most standard clauses allow for a new index to be substituted if the original one is no longer published. But is it really the case that the CPI would be the right substitute for the RPI for a lease dated after the CPI became the official measure of inflation or dated after 2013 – when RPI stopped being an official statistic?

Third, think about how much the rent will vary with inflation. It's not unusual to see a cap on the amount of any inflation-linked increase, which is the maximum the rent will rise. These are accompanied by a collar, or a guaranteed minimum increase. Collars also protect landlords from falls in rent if inflation becomes negative (also known as deflation). The combined effect is to smooth rent changes over the duration of a lease.

Inflation-linked rent reviews could happen every year. It's not unusual to see them compounded – the rent nominally changes each year but the increase only takes effect every five years. The compounding is market standard but be sure to get the formula correct. If the numerator and denominator are mismatched, tenants might find themselves paying far more than they'd intended. Run a worked example to make sure compounding works as you intend, going to the end of the term.

In *Arnold v Britten [2015] UKSC 36*, the service charge increase was 10% a year. The compounded effect of this meant that the annual cost rose to become more than the mobile homes paying the service charge were worth. Index linked rents can avoid long and contested rent reviews, but traps for the unwary remain.

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TOWN AND VILLAGE GREENS – BACK TO BASICS

The rights associated with Town and Village Greens ("**TVGs**") trace back to English customary law. Legal protections for the use of land for highly localised purposes and pastimes arose from the mere fact that such use fell into *custom immemorial* (i.e. the origin of the use extended beyond living memory). Despite the distinction between "Town" and "Village" in the title, there is no legal differentiation between the two; indeed a TVG is just as likely to be representative of a bucolic English or Welsh idyll as it is an urban ghetto.

The Commons Registration Act 1965 ("**1965 Act**") and the subsequent Commons Act 2006 ("**2006 Act**") which repeals it, formalised how land may be recognised as a TVG. The 1965 Act created the first register of TVGs and offered the possibility to register new TVGs after 20 years of continuous eligible use was established.

Registration

In the absence of any 'trigger events', explained further below, an application can be made to register land as a TVG under section 15 of the 2006 Act when 'a significant number of the inhabitants of any locality […] have indulged as of right in lawful sports and pastimes on the land for a period of at least 20 years and continue to do so at the time of the application.' It is not necessary to be the owner of the land in order to apply to register it as a TVG.

Registration of land as a TVG has huge consequences for developers and landowners. Any activity on TVG land that causes damage or interrupts its use as a TVG could be a criminal offence. The TVG land will also have become essentially sterile for development purposes. Since 1990 it became increasingly common to apply to register TVGs as an attempt to thwart future development proposals, seemingly opening up a loophole capable of undermining legitimate development proposals.

'Trigger events'

The government sought to address this loophole. Among other changes aimed at facilitating local development, the Growth and Infrastructure Act 2013 ("**2013 Act**") introduced a series of 'trigger events' which function to exclude the right of making a TVG application. These include a planning application and the publication of any draft plans *identifying land for potential development*, as well as the publication of similar documents during public consultations.

Each trigger event is coupled by a 'terminating event', such as the withdrawal of a planning application. Terminating events open up the possibility of later TVG applications, but start the clock again for the accrual of the required 20 years of continuous use. Trigger events occurring before the 2013 Act came into force in 2013 may still bite to prevent TVG applications from being successful.

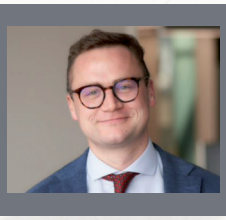
A TVG application can have significant consequences on the capacity for a site to be developed, meaning that it is critical for developers to be able to clearly understand whether a trigger event exists that could negate the prospects of any potential TVG applications. The High Court recently provided additional clarity on how to identify a true trigger event in *R (On the Application of Bellway Homes Ltd) v Kent County Council* [2022] EWHC 2593 (Admin). In Bellway, the Court held that 'identifying' land for 'potential development' meant *specifically* identifying the land in a plan, for instance by verbal description or by a line on a map and the general mention of an area was insufficient to act as a valid trigger event. The Court also looked at whether it was the meaning and purpose of the local plan in question to specifically identify land for potential development. Fundamentally requiring an understanding of the Council's policy at the time, the Court held that determining what constituted 'potential development' was a question of law for the Court to answer, and also that doing so involved taking a *realistic* rather than *theoretical* approach to the policies underpinning the local plan. Ultimately the Court dismissed Bellway Homes' claim that the identification of their land in the local plan in question was a trigger event, because their land was not sufficiently identified, and the local plan did not expressly propose potential development of it. The outcome was that the Council could still determine applications to register TVGs at the site, and the local action group retained the ability to make their application. While the Bellway case was fact specific and turned on the specific ambiguities and nuances of the relevant local plan, it adds to the limited body of judicial guidance available on TVG trigger events, and indicates the approach the Court might take when interpreting development plan policies.

Deregistration

Owners of a TVG can apply for land to be released from registration. The procedure for doing this is complex, and legal advice should be sought. If a TVG proposed to be deregistered is greater than 200 square metres in area, then the application must include a proposal to register a suitable alternative site as a TVG in exchange for the release of the original land. If the TVG is less than 200 square metres, then the swapping requirement is not mandatory.

KEY POINTS

- **The law surrounding TVGs is complex with many risks, including potential criminal offences.**
- **Once land is registered as a TVG, it is essentially sterile for development purposes.**
- **If an application has been made to register a TVG, careful attention should be given to whether a trigger event may arise that could scupper the application.**
- **TVGs can be deregistered, however this is not a given nor straightforward. It may be costly and require the acquisition of additional land.**
- **When purchasing land it is essential to establish if any part is vulnerable to being registered as a TVG.**



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COMMON 'MEE'STAKES – WHAT YOU NEED TO KNOW

With less than three months to go until the government's next deadline in its energy efficiency agenda, landlords need to take action now to either comply or register a valid exemption.

The MEES Regulations require a minimum energy efficiency standard ("**MEES**") to be met before properties in England and Wales can be let and, from 1 April 2023, continue to be let.

KEY POINTS

- **From 1 April 2023, the MEES Regulations will make it unlawful for landlords to continue to let a property with an EPC rating of F or G without a valid exemption.**
- **Exemptions must be registered on the Private Rented Sector Exemptions Register.**
- **There are no blanket exemptions. Most will require action on the part of the landlord together with evidence of such actions.**
- **No exemption lasts more than five years.**

F&G-Day Deadline – 1 April 2023

At present, landlords cannot grant new leases to either new or existing tenants of properties that have an Energy Performance Certificate ("**EPC**") with a rating of F or G, unless they have registered a valid exemption.

From 1 April 2023, the MEES Regulations will apply to all existing leases, meaning that it will be unlawful for landlords to continue to let a property with an EPC rating of F or G without a valid exemption.

MEEStakes and emptions

The key exemptions available to commercial landlords are:

- No EPC required: when a property is not required by law to have an EPC, the MEES Regulations do not apply.

  Listed buildings – there is a common misconception that listed buildings are automatically exempt from the requirement to obtain an EPC. Rather, they are exempt 'insofar as compliance with certain minimum energy performance requirements would unacceptably alter their character or appearance'. This will need to be looked at on a case by case basis and should not be considered a blanket exemption.

  Renewal leases – there is a conflict in the government guidance for the EPC and MEES regimes. Under the EPC guidance, EPCs are only required on a 'sale or let' and it specifically excludes lease renewals from the definition of 'sale or let.' This conflicts with the MEES guidance which suggests an EPC is required on a renewal. Despite requests for clarification, the government has not amended either but the market seems to have moved towards the more conservative approach with EPCs being requested and provided on any renewal.

- **Consent**: where the landlord has been unable to obtain any necessary third party consent (for instance from a tenant, a superior landlord or a lender) to carry out the proposed works, or where a third party has granted consent subject to a condition which the landlord cannot reasonably comply with.

  The landlord may require access to the tenant's demised premises in order to carry out any relevant energy efficiency improvement works and, unless the lease reserves a right of access for the landlord to carry out such works, the tenant will need to grant the landlord access. This may prove difficult as some tenants may refuse on the basis that it would disrupt their business, or may be willing to grant access but in exchange for a concession, such as a rent-free period or alternative premises for the duration of the works.

  Therefore, it might be better not to reserve the necessary rights for the landlord so that the landlord is more reliant on the tenant providing its consent. However, the landlord will need to show that it has made 'reasonable efforts' to obtain consent, and provide evidence of this when registering the exemption. There is no definition of 'reasonable efforts' but more than just a token effort will be required.

  A landlord will not meet the reasonable efforts threshold if it indirectly seeks to undermine its application for consent by:

  – emphasising that the tenant will bear the costs of any works as they are to be recouped via the service charge regime;

- not challenging a refusal of consent, particularly where, under the lease provisions, the tenant must act reasonably when considering applications for consent;
- exaggerating the nature and duration of the works; and/or
- offering some inducement for refusal of consent.

- **Devaluation**: where the landlord has received a report from an independent surveyor stating that the relevant improvements would result in a reduction of more than 5% of the market value of the property. For example if the works would reduce the lettable space within the property, the market value could be affected.

- **Temporary** exemptions:
  - **New landlord**: on purchasing a sub-standard property which is currently let to tenants, the new landlord has a six month 'grace period' from the date of purchase to improve the property's energy efficiency; and
  - **Seven year payback**: where the landlord can show that the expected value of savings on energy bills over seven years is less than the cost of the necessary energy improvement works.

- **All relevant energy efficiency improvements made**: where all the relevant energy efficiency improvements for the property have been made, or there are no relevant energy efficiency improvements that can be made, and the EPC rating of the property remains below an E.

One point regularly overlooked is to claim an exemption, the landlord must register itself on the Private Rented Sector Exemptions (PRS) Register to avoid the possibility of enforcement action. Any exemption doesn't come cheap. Exemptions involve administrative and other costs to demonstrate that the exemption applies.

No exemption lasts more than five years, so landlords will need to either register a new exemption before the original one expires, or carry out the relevant energy efficiency improvements in the meantime. The availability of a substitute exemption is also not guaranteed.

Consequences of non-compliance

Importantly, where a property is let (or continues to be let) in breach of MEES, the lease remains valid and in force but the landlord will be exposed to penalties. The enforcement authority can impose both financial penalties (up to £150,000) and publish transgressions which may have PR implications. As penalties can be levied in respect of each unlawful tenancy, financial penalties could add up quickly, for instance in a multi-let building.

Next steps – action to take before 1 April 2023

- **Review portfolios** to identify properties with an EPC rating of F or G, and/or properties without an EPC. Consider whether a new assessment is required.

- Seek advice on whether a property falls within any of the **exemptions** and if so, register any exemption to avoid enforcement action.

- **Obtain fee proposals** for the cost of improving a property to bring it to the required target EPC rating - this will help to make an informed decision and potentially help claim (and prove) an exemption. Consider taking expert advice on what cost-effective improvements could be made to improve the rating to meet the requirements for 1 April 2023, as against more substantial works to meet the requirements that are forecast to follow in 2027 and 2030, which may deliver a longer-term benefit.

- Check the terms of the lease to see if the landlord is allowed to carry out works to improve the EPC rating, and whether any **tenant or third party consent** is needed. Where consent is required, apply for consent; consider opening a dialogue now with tenants or third parties, and keep a full record of any communication with them.

- Check the terms of the lease to establish whether any **costs can properly be classed as service charge items**.

- If no exemptions can be registered or renewed, **plan and implement the relevant improvements before 1 April 2023**, liaising with tenants as appropriate.

- **Consider how the property can be future-proofed**. The direction of travel is clear – MEES obligations are anticipated to step up again, with government proposals for requirements of a minimum EPC rating of C in 2027 and B in 2030. Landlords may therefore wish to implement any energy improvement works with this in mind, looking to ways to improve the energy efficiency of their properties in the longer-term.

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GIVE ME A BREAK!

We are all aware of the Bank of England's stark warning that the UK now faces its longest recession since records began, with rising interest rates and inflation running at a 40-year high.

Against this backdrop, and with the cost of occupying commercial premises likely to be a significant overhead for most businesses, tenants may be evaluating their property portfolios and needs to identify if any savings can be made.

A tenant's break option in a lease offers a tenant one such opportunity – whether to exit the lease early and relocate to cheaper premises or to renegotiate more favourable lease terms. Particularly in recessionary times, and where a lease has upward-only rent reviews, this can be a very valuable tool for a tenant to avoid potential cash flow problems that could jeopardise their business.

However, break options are rarely as straightforward as they may seem. The requirements for the form and service of the notice must be strictly adhered to. Additionally, tenant break options usually contain pre-conditions, some of which can be very difficult to satisfy. If there is a failure to comply with any of these, the break will be ineffective and the lease will continue. Consequently, break options need to be approached with great care.

On the other hand, landlords may be scrutinising the exercise of break options if they are facing high occupancy rates.

Plan ahead

Break options typically require the tenant to give formal notice to the landlord if it wishes to bring an end to the lease. Often the notice period is six months but sometimes longer. Therefore, a tenant who wants to break – or simply to use the option as leverage to attempt to negotiate better lease terms with their landlord – should consider the break option well in advance.

It is important to seek legal advice on the exact length of notice required to be given and the break date as the lease wording can be misinterpreted. If a 'fixed date' break option is missed, the opportunity to terminate the lease early is lost.

Another reason to look at the option early on is that it could take several months to satisfy the break conditions (more on this below).

KEY POINTS

- **Break options give tenants the opportunity to end lease arrangements early or to potentially renegotiate terms.**
- **The conditions of break clauses require strict compliance.**
- **Tenants should consider their options well in advance.**

Serving the notice

If the lease prescribes a particular form of notice, it must be used. The notice also needs to be served on the correct party at the right address and the lease may also prescribe how that notice is served. What appears a basic issue has in fact led to an abundance of litigation in this area. Accordingly, a party exercising a break option should tread very carefully.

Compliance with break conditions

Quite often a break option can be drafted on a conditional basis. This means certain things have to happen by a certain date for the lease to terminate on the break date. To comply with even a relatively simple condition may take a good deal of care. For example, a break option requiring the tenant to pay the 'rents' by the break date requires the tenant to establish precisely which rents and how much of each rent is due (remembering that there will be no apportionment of rent unless the lease expressly provides for it).

Depending on the definition of "rents" in the lease, such a condition may also require the tenant to pay any default interest on late payments (even if the landlord has not demanded such interest). In one case the tenant's non-payment of default interest invalidated the exercise of the break, even though the amount involved was only about £130.

In such circumstances – short of agreeing with the landlord what, if any, amounts are owing under the lease (which may include a break premium) – a tenant would be well advised to include a sum to cover any potential interest. It is therefore sensible for a tenant to carry out an audit of the lease payments in sufficient time before the break date to

arrange any payment. More generally, any sums due should be paid, even if in dispute. Payment can be made on a 'without prejudice' basis and the matter contended later.

Where a break clause includes a condition for the tenant to return the premises with "vacant possession" by the break date, the law has historically been far from clear what this means in practical terms, often leading to disputes when items were left behind. Whilst a recent Court of Appeal decision has offered some clarity (determining that vacant possession requires a property to be returned free from people, chattels and legal interests) this remains a challenging condition to satisfy and a substantial amount of work may be needed in the removal of all chattels. A tenant will also need to terminate any existing third party interests, such as sub-leases, and this requires forward planning to ensure that the break options in any underlease(s) dovetail with the main lease or the tenant could fall foul of this condition.

Some break clauses go further and require compliance with 'all tenant covenants'. In such instances, very careful management of the process will be needed as (depending on the specific lease wording) even trivial breaches can invalidate the exercise of the break. In one case the tenant lost its right to break the lease because it had painted the premises 13 months before the break date instead of within 12 months (despite this making no practical difference)! Thus, if the tenant is to successfully break the lease, a considerable amount of work may be required not only by the tenant itself, but also advice and input from the lawyers, agents and dilapidation surveyors if works need to be undertaken to meet the condition.

Avoid distraction from the landlord

It is almost always sensible for the tenant to speak to the landlord about the break option to see if a deal can be done – for example, in exchange for not exercising or removing future break options, the tenant may be able to negotiate other advantages (depending on the parties' bargaining positions and prevailing market conditions):

- a rent reduction or an extra rent-free period;
- removal of future rent reviews provisions;
- a reduction in space; or
- less restrictive alienation rights (e.g. enabling the tenant to more freely assign or sub-let).

However, the landlord has no obligation to enter into such negotiations and, unless and until a legally binding agreement is reached, the landlord can end discussions with the tenant at any time. Therefore, the tenant must not allow such discussions to create a (false) sense of security.

So if, for example, a three month works programme is required to comply with a break option, the tenant would be well advised to commence the works at least three months before the break date to ensure compliance, however close the parties are to doing a deal. If the works do not start, and the tenant is left with insufficient time to comply with the condition, the tenant will face the possibility of non-compliance and, in the absence of agreement waiving the required condition, the lease will continue.

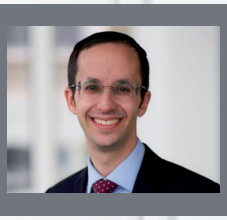
No going back

If a tenant serves a break notice to create leverage for re-gear discussions (if they consider their landlord may prefer to keep them on less advantageous terms rather than suffer a vacant premises), a tenant should start those negotiations without delay as their time for negotiating and documenting the new terms will be lost come the break date if the tenant has no true intention of leaving.

Once a break clause has been exercised by the service of a notice it cannot be withdrawn unilaterally by the tenant. While a tenant could not satisfy a break condition to frustrate the break, the risk remains that the landlord waives that condition and the tenant finds itself without a lease, when that may not have been its intention on serving notice.

Conclusion

The exercise of tenant break options tends to increase during an economic downturn as tenants seek to re-gear their leases or terminate existing arrangements. There are many pitfalls (for both landlords and tenants) when attempting to exercise a break option. Given the stakes, it is important to seek early legal advice.



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