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REAL NEWS

The quarterly Real Estate newsletter from DLA Piper UK LLP

EVERYTHING MATTERS

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CONSENT – YES, NO OR MAYBE?

With the markets again forecasting difficult financial times ahead, parties will be looking for ways to get out of potentially onerous contracts. Termination provisions in agreements will be tested to extremes and parties will seek to exploit any grey areas to their advantage. One such area is the question of whether and, if so, when a landlord or superior landlord has consented to a dealing. Like many potential problem areas, this is matter that should be capable of being managed by careful drafting. However, if there is any uncertainty, it is an area that can be exploited or capitalised upon to great effect, depending on your objectives.

In 2004, our London Real Estate Litigation Team acted in the case of *Old Monk plc v Puzzle Pub Co Ltd* [2004] EWHC 3457 in which Lindsay J commented:

"…it is an area now in the light of rather contentious authorities such as Aubergine, that one can at least arguably have a consent in circumstances where, once upon a time, it would not have been seen."

In July 2011, judgment in the unreported case of *British Telecommunications Limited v Rail and Safety Standards Board Limited* was published. The case concerned an agreement for underlease between BT and RSSB which was conditional upon the superior landlord, Prudential, giving its consent to (1) the underletting and (2) a programme of works to be undertaken by RSSB. The agreement contained express definitions of "Licence to Underlet", "Licence for Alterations" and "Superior Landlord's Consent" and provided that either party could terminate the agreement by written notice if the superior landlord's consent had not been obtained by 5 October 2007. "Superior Landlord's Consent" was defined as:

"…the consent of the Superior Landlord to the grant of the Leases by way of the Licence to Underlet and to the Tenant's Works by way of the Licence for Alterations."

On 20 November 2007, RSSB served notice to terminate the agreement. At that time, the Licence to Underlet had been executed by Prudential, BT and RSSB and the only matter outstanding on the Licence for Alterations was for RSSB to execute it. Neither document had been completed. The question the Court had to decide was whether the agreement required Prudential's consent to be provided by way of completed licences or whether the unilateral act of consent by Prudential in principle was sufficient.

The definition of "Superior Landlord's Consent" seems to require completed licences for the consent to be given. However, the Judge held that "Superior Landlord's Consent" referred to the consent of Prudential and not to the completion of the Licence to Underlet and the Licence for Alterations. His reasons were:

- The agreement centred on the "consent" of the landlord and not the licences.
- The parties were focussed on providing for the agreement of Prudential and not on providing themselves with an opportunity to change their minds about the transaction as a whole. Against that

background, the Judge thought it unlikely that the parties intended for the landlord's consent not to exist until the licences were completed.

- The words "by way of" show the way in which the consent will ultimately exist and be recorded but that does not preclude the consent being "given" on the basis that it will exist and be recorded in licences.
- The agreement required RSSB to (a) provide all reasonable assistance to facilitate the grant of the Superior Landlord's Consent and (b) to join in the Licence to Underlet. Accordingly, the Judge thought (b) added little or nothing to the arrangement if the grant of consent referred to in (a) referred to the completion of the licences.
- The cases of *Mount Eden Land Ltd v Prudential Assurance Company Ltd (1997)* P&CR 377 and *Aubergine Enterprises Ltd v Lakewood International Ltd* [2002] EWCA Civ 177 show that parties can contemplate identifying "consent" at a stage other than the stage of a completed licence without that producing uncertainty or a consent upon which the parties cannot rely.

The decision is a little surprising as it may have suited either party to have the flexibility to terminate the agreement if the licences were not completed. It would appear that if it is your intention that consent can only be provided by way of a completed licence/deed, anything short of a clear and unambiguous provision to that effect may give rise to uncertainty as to when the consent is "given" as opposed to "recorded". This remains an area where there can be great uncertainty even if the agreement looks, at first blush, to be clear.

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LOCALISM ACT 2011 & THE NATIONAL PLANNING POLICY FRAMEWORK

The Localism Act 2011 ("**Act**") received Royal Assent on the 15 November 2011. Eric Pickles has described the Act as *"the beginning of a historic shift of power from Whitehall to every community to take back control of their lives"*. The Act is a significant milestone in the Government's localism agenda and based on the much heralded theme of the *"Big Society"*, where the intention is to largely pass the power to the communities themselves to promote the type of development they actually want to see in their own locality.

The Act includes potentially radical measures such as the power of general competence for local authorities, community rights to challenge to take over the running of public services and to bid for assets of community value and new neighbourhood planning powers.

In principle, the Act aims to give local communities greater (or indeed ultimate) decision-making power on matters ranging from the location of new housing, the type of new community facilities they need, and the distribution of new infrastructure in their areas. This will be delivered through the new 'neighbourhood planning' process in the form of a new tier in an areas statutory Development Plan – the Neighbourhood Plan. Theoretically, therefore, pro-development neighbourhoods could effectively market themselves as 'open for business', with them earmarking sites for new housing or employment in their areas.

The Government's growth agenda has resulted in the draft National Planning Policy Framework ("**NPPF**"), which was published on the 25 July 2011. The NPPF intends to integrate the current suite of national planning policy documentation into a single concise document of only 58 pages with a presumption in favour of sustainable development.

Much of the opposition to the draft NPPF is centred around the presumption in favour of sustainable development which has been interpreted by some as a radical departure from the previous law. However, it is in fact nothing of the sort. There has always been, since 1947, a presumption in favour of sustainable development i.e. development which meets the needs of the present without compromising the needs of future generations. The NPPF therefore communicates the positive role that planning can play in providing such development of the prosperity of the UK.

Such opposition has been reflected in the Communities and Local and Local Government Committee report which was published on the 21 December 2011. The report recommended a number of changes including removing the default answer of 'yes' to development. The Chair of the Committee said:

"The way the framework is drafted currently gives the impression that greater emphasis should be given in planning decisions to economic growth. This undermines the equally important environmental and social elements of the planning system."

The report has been welcomed by such organisations as the National Trust and RTPI and indicates that there are likely to be a number of changes to the final version of the NPPF.

The inherent tensions in the Act between the Government's desire to facilitate economic growth through the NPPF and development while also increasing local power over planning decisions are likely to throw up different hurdles.

However, in viewing the Act against the wider background of Whitehall initiatives on the local economy offers a potentially more consistent reading of the Government's reasoning. The main reasoning being that it is simply **all about the money**:

"Governments with money centralise and claim the credit. Governments without cash decentralise and spread the blame." (Nick Robinson BBC Political Editor)

The ultimate impact the Act and the NPPF will have upon developers and landowners working within the planning system is still uncertain. The provisions of the Act and the NPPF are expected to be in force by April 2012 – so watch this space!

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ARBITRATORS THE LAST WORD?

The recent determination of *Cordoba Holdings Ltd v Ballymore Properties Ltd [2011] EWHC 1636 (Ch) (Ch D)* highlights that the Court is keen to uphold the legislative role of The Arbitration Act 1996, designed to restrict the opportunity for the Court to intervene in disputes which the parties have agreed to deal with by arbitration.

Facts of the Case

By three leases, all containing materially the same terms, Ballymore let various floors of the subject premises to Cordoba Holdings Ltd. The leases were each subject to upwards only rent reviews.

On the second rent review, the parties were unable to agree. An arbitrator was duly appointed to determine the rent at which the premises might reasonably be expected to be let on the open market, "*making the Assumptions but disregarding the Disregarded Matters*". Any increase in rental value attributable to improvements carried out by the tenant was included in the "Disregarded Matters".

The premises were originally used as offices, but had been converted to use as a data centre. The tenant contended that use as a data centre was possible due to works which the tenant had undertaken to establish an enhanced power supply to the premises. The improvement works which were undertaken by the tenant were to an area outside the demise and so were not caught by the disregard. In any event, Cordoba could not provide any evidence of the nature of the improvements, who carried them out, when or at what cost.

The arbitrator determined the rent at £2.8m per annum on the basis that the premises could be used by the hypothetical tenant as a data centre, not just as offices. Cordoba sought permission to challenge the arbitrator's determination, arguing that the arbitrator was wrong to determine that the premises could be used as a data centre, because use as a data centre was only possible as a result of the improvements made by the tenant.

Outcome

The Court rejected Cordoba's challenge. As a matter of law, it found that the onus was on Cordoba to establish that the improvements were to be disregarded, and Cordoba had failed to do so in the course of the arbitration. The arbitrator was therefore entitled to proceed on the basis that the improvements were not to be disregarded.

Procedure

Despite the fact that in this case the tenant was unable to back up its contention that it had carried out improvement works to the premises, the case illustrates the Court's reluctance to deviate from an arbitrator's determination.

Any party seeking to challenge the decision of an arbitrator faces significant obstacles and will only be able to do so in limited circumstances.

In any rent review dispute, we need to consider and cover off every possible issue when preparing for the arbitration hearing. If a further legal issue does arise during the arbitration, it may be sensible to request an adjournment for that legal issue to be determined separately, before the arbitrator's decision is made. Once the decision is made, it seems it will be difficult to argue with it.

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REAL ESTATE ROUND UP

FARMING TODAY

The phrase "all purposes with or without vehicles" does not extend to driving animals

Alford v Hannaford and another [2011] EWCA Civ 1099

Mrs Alford had the benefit of a right of way granted to her over land owned by the Hannafords. She had purchased agricultural land from the Hannafords' predecessor in title including a right of way along a track "... at all times and for all purposes without or without vehicles to pass and repass over and along the track...". The transfer containing the grant also contained a reservation of a right of way in favour of the seller which expressly referred to driving animals. Disputes arose over whether the right granted to Mrs Alford also included the right to drive animals by implication or was limited to pedestrian and vehicular use. The judge at first instance found that it was limited.

Mrs Alford appealed on the grounds that the nature and location of the properties concerned made it obvious that a right to drive animals must have been intended to be included: but the Court of Appeal found against her. The Court said that background facts could be used to assist in the construction of an agreement where it was obvious that something had gone wrong with the language. If those special circumstances were not present, the court had to give the language used by the parties its natural meaning consistent with the context.

The exact extent of a grant of a right of way might be implied either under the principle of non-derogation from grant or from the general words set out in the conveyance or transfer. It was established law that under the rule in *Wheeldon v Burrows* a buyer would take the benefit of any quasi-easements which were necessary for the reasonable enjoyment of the property sold and which had been and were at the time of the grant used by the common owner for the benefit of the land being sold. Mrs Alford, however, could not rely on that principle since there was no evidence of the degree of use to which the land had been put prior to the transfer. The fact that the effect of section 62 had been expressly excluded elsewhere in the transfer was further evidence that no additional or wider right than that set out expressly was being created by implication.

Precise drafting is essential in relation to the grant or reservation of easements. You need to precisely define the dominant land and the servient land, the exact area over which the easement can be exercised and the nature of the use permitted. Practical difficulties and disputes can sometimes be resolved by applying the rules of implication, but they cannot be relied on.

IT'S OFFICIAL! LAND REGISTRATION RULE TO BE "IGNORED"!

New rules took effect on 1 October removing the requirement that overseas companies with a UK establishment registered at Companies House must also register at Companies House certain charges created over UK Property. This means that rule 111A of the Land Registration Rules 2003, which provides that one of the following must be supplied when registering a charge created by an overseas company at the Land Registry:

- evidence that the charge has been registered at Companies House; or
- a statement that the charge, when created, did not require to be so registered,

is now redundant. The Land Registry says it should be "ignored" until it is formally repealed.

TENANTS' GRUMBLES – SERVICE CHARGES AND GREEN ISSUES

In late 2011 two behemoths of the real estate world, the Property Industry Alliance and CoreNet Global, released their ***fifth annual survey*** measuring the satisfaction of commercial occupiers in the UK. This shows that tenants' satisfaction with service charge arrangements had barely changed over the year (will the coming into effect of the second edition of the RICS Code of Practice, ***Service Charges in Commercial Property***, on 1 October make a difference?).

It also shows that "sustainability remains an important issue for occupiers, who gave this factor the lowest score and feel that landlords still have a lot to improve upon in terms of interaction with them on this issue".

EASEMENTS AND COVENANTS – A GLIMPSE OF THE FUTURE

The Law Commission is fast-tracking proposals on easements and covenants. A quick look at its proposed reforms:

- a simplification of the law relating to the creation of easements (including a repeal of the Prescription Act 1832);
- the introduction of a new method of attaching obligations to land which introduces a new regime relating to restrictive covenants and a means of enabling positive obligations (to be called "land obligations") to be enforceable against successors in title;
- allowing the Lands Chamber of the Upper Tribunal (what we used to call "the Lands Tribunal") to make orders modifying or discharging land obligations and those easements created after the reforms have taken effect;
- the disapplication of the rule requiring unity of seisin in relation to registered land;
- clarifying the position as to abandonment of easements;
- reversing the rule in ***Wall v Collins*** [2007] EWCA Civ 444 so that (unless the parties otherwise agree) any right granted to a tenant ceases to have effect on the termination of the tenant's lease regardless of how that termination is effected; and
- the abolition of the ouster principle which invalidates an easement that prevents the servient owner from making any reasonable use of its land (as long as the dominant owner's use of that land stops short of exclusive possession) with a view to validating easements to park vehicles.

THE FUTURE'S BRIGHT, THE FUTURE'S REIT

The Finance Act 2012 is to contain important relaxations of the REIT rules with a view to making real estate investment trusts ("REITs") more attractive to investors. The Treasury has now responded on a consultation it held earlier this year and the upshot is that all the positive proposals will be taken forward in draft legislation to be published on 6 December. In particular:

- the entry charge for companies joining the REIT regime is to be abolished;
- listing will be allowed on AIM and on PLUS Markets but (as yet) private REITs will not be allowed;
- REITs will have a grace period of three years to meet the non-close company requirement (with no penalties imposed if the failure to become non-close is due to legitimate reasons);
- institutional investors will be able to take advantage of a diverse ownership rule (subject to details to be revealed in the draft legislation);
- cash is to be treated as a "good" asset for the purpose of the balance of business test (the idea is not to force REITs to spend at a time which is commercially inappropriate;
- only interest on excessive borrowing will be included in the interest-cover test; and
- the six months' time limit for meeting the distribution requirement is to be extended.

These relaxations will assist existing REITs, institutional investors and those contemplating converting into the REIT regime and in some cases, makes REITs a real alternative to an off-shore investment company.

VAT DESIGN AND BUILD CONTRACTS TO REMAIN ZERO-RATED

HMRC has agreed, following a number of representations, that design and build contracts will remain VAT zero-rated supplies where the construction itself qualifies for VAT at the zero rate.

As a result of HMRC's interpretation of a VAT decision in the European Court, HMRC had proposed a change in policy which would have meant that the design element, even when included within a lump-sum design and build contract, would no longer be considered as a single supply and would have been subject to VAT at the standard rate. Had this change in policy gone ahead, these additional VAT costs would have been largely irrecoverable by the housing association, charity and not-for-profit sectors.

Following extensive lobbying by affected organisations, HMRC has reconsidered its proposals and has agreed that there is sufficient legal argument to allow the zero-rating of design and build composite supplies to continue.

HMRC will now set out the circumstances where fees of architects, surveyors and other construction professionals included within lump-sum design and build contracts may continue to be treated as a composite supply of zero-rated construction services.

FLY IN THE OINTMENT. AVIATION BUSINESS SUCCESSFULLY CLAIMS A PERIODIC TENANCY OF KEY PARTS OF AN AIRPORT

Mann Aviation Group (Engineering) Ltd (in administration) v Longmint Aviation Ltd and Gama Support Services (Fairoaks) Ltd [2011] EWHC 2238 (Ch)

Fairoaks Airport in Surrey was, in property law terms, run in a fairly casual manner. Mann, an aviation engineering business, occupied three hangars and an office there on an informal basis, paying rent to its landlord, which latterly became a company in the same group. This easy-going system worked well until Mann went into administration. The landlord felt that the arrangement with Mann constituted a mere licence and gave the administrators notice terminating that licence. The administrators successfully claimed that Mann held a periodic tenancy of airport properties that it occupied.

The judge took into account the following factors:

- Mann had physical control of the property.
- Mann could only have held its licence from the aviation authorities if it had that control and could exclude others from the hangars.
- The mutual intention of the landlord and Mann was that Mann would enjoy a periodic tenancy.

A periodic tenancy of business premises is necessarily protected under part II of the Landlord and Tenant Act 1954 and so the landlord now faces the tasks both of terminating the protected tenancy and of dealing with the statutory tenancy that will arise on such termination.

THE LAST GREAT NATIONALISATION? THE WATER INDUSTRY (SCHEMES FOR ADOPTION OF PRIVATE SEWERS) REGULATIONS 2011

Sewers are the pipes that take foul sewage and surface water away from more than one property. Lateral drains are those pipes that take foul sewage and surface water away from an individual property to the extent that that pipe lies outside the curtilage of the relevant property.

Up to 50 per cent of properties in England and Wales are connected to a private sewer in one form or another and most of the rest are responsible for a lateral drain.

The Water Industry (Schemes for Adoption of Private Sewers) Regulations 2011 came into force on 1 July 2011. These require statutory sewerage undertakers to take ownership of all private sewers and lateral drains that are connected to the mains on 1 July 2011. The regulations provide for an overnight transfer of ownership on 1 October 2011. The transfer will apply to residential and commercial properties.

Private drains and sewers which are not connected to a public sewer (for example those which drain only to a septic tank) are not affected by the transfer.

Following adoption, the undertakers will be responsible for the maintenance of the sewers and lateral drains. The cost of any works will be passed on to customers through increased water and sewerage bills. Note that the curtilage of a property is not necessarily the same as the parcel of land on which it stands.

A single curtilage may contain a number of individual properties under common ownership (such as a shopping mall) or with separate lease or other arrangements (such as some commercial estates) but which have common drainage arrangements. Such sites should be regarded as having their own internally managed drainage systems which are not private sewers for transfer since the site itself comprises a single curtilage. For sites in common ownership the lateral drains will be adopted up to the curtilage of that site, but drains within the curtilage will continue to be the responsibility of the site owner.

The transfer regulations provide for private pumping stations to be transferred over five years up to 1 October 2016.

Sewerage undertakers do not need to register their interest in the sewers and lateral drains where they run through unregistered land, and cannot register the transfer to them of the sewers and lateral drains where they are in registered land. However, where land providing access to a pumping station is acquired, then registration should be considered.

Sewerage undertakers may enter an agreed notice in respect of their interest in sewers and lateral drains running through registered land. However, such noted rights cease to be overriding interests, and may be at risk if the notice comes off the register of title and the land is then sold.

COURT OF APPEAL LAYS DOWN THE LAW ON AGAS

K/S Victoria Street v House of Fraser (Stores Management) and others [2011] EWCA Civ 904

The Landlord and Tenant (Covenants) Act 1995 effected some fundamental changes in the law relating to liability under leases. But those changes gave rise to a question which had a significant effect on property values and which the Court of Appeal has now answered. The question was whether an assigning tenant's guarantor could validly back up its tenant's liability to the landlord under an authorised guarantee agreement ("AGA"). The answer, in short, is yes – but the means by which this is achieved is important.

Lord Neuberger, formerly a pre-eminent property lawyer, gave the judgment but he acknowledged the contributions that his fellow members of the court had made. Whilst the decision dealt with the fall-out of a problematic sale and leaseback deal involving a House of Fraser store in Wolverhampton, it is of wide-ranging importance to the property industry because it brings what looks likely to be a clear conclusion to what some commentators have called the "AGA Saga". The key points of the judgment are:

- A provision requiring a tenant's guarantor to guarantee the liability under the lease of an assignee from that tenant is void because it infringes the wide-ranging anti-avoidance provisions in section 25 of the Act. Such a provision frustrates the operation of sections 5 and 24(b) of the Act: on a lawful assignment of the lease, a tenant is released; and at that time the tenant's guarantor is released to the same extent.
- There are limited circumstances in which such a guarantor can re-assume liability to the landlord: (1) first, where a landlord can properly require a tenant's guarantor to guarantee the tenant's performance under an (sometimes referred to as a "sub-guarantee"); and (2) secondly, where a landlord can properly require a tenant's guarantor to guarantee the performance of a second or subsequent assignee (see paragraph 51 of the judgment).

In an e-alert sent to the group's clients and contacts our UK group head, ***Catherine Usher***, commented: "The decision gives a clear and workable answer to a long-standing question over AGAs. Investors and occupiers alike will welcome Lord Neuberger's guidance on how far the 1995 Act limits the principle of freedom of contract. However, property lawyers will need to keep the detail of the judgment in mind both when reviewing and drafting guarantees."

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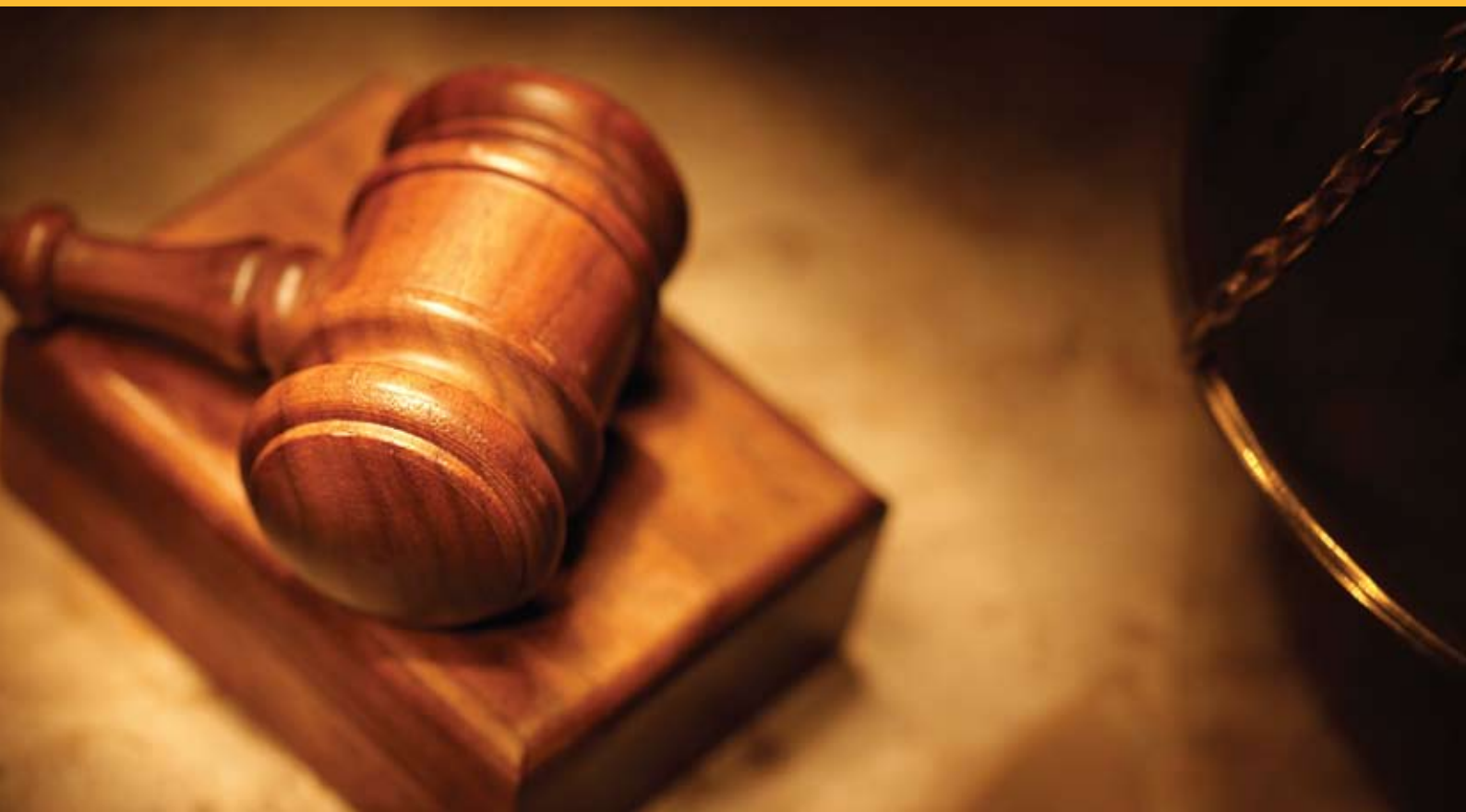

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