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Real Estate Quarterly

Spring 2011

Real Estate

Contents

A budget for growth

George Osborne promised a budget for growth in his address to the House of Commons and the measures he delivered have been received with cautious optimism by the real estate industry. Will Gay, Harry Spurr and Jane Dockeray review some of the highlights.

REITS

There was good news for REITs in the form of a proposed informal consultation aimed at reducing barriers to entry and investment and reducing the regulatory burden. Key to these hurdles will be abolishing the conversion charge and relaxing the requirement for a listing on a recognised stock exchange.

SDLT

There was good news also for investors in the residential market with a change to the SDLT calculation for purchases of multiple residential properties. The rate at which SDLT is charged will now be determined by reference to the mean value of the properties, rather than their aggregate value.

However, what the Treasury gives with one hand is often taken away with the other and three SDLT avoidance schemes were swept away as from 24 March. The three schemes involved:

- Combining reliefs for sub-sales and alternative property finance to remove all SDLT charges on the purchases;
- Setting up as a "financial institution" merely by acquiring a consumer credit licence and then making use of the alternative property finance reliefs;
- Exchanges of land which "manipulated" the market value of the interest acquired.

The breadth of the change in law to combat this last scheme may produce an unexpected result for some transactions. Prior to 24 March, where there was an exchange which included a "major interest" in land (ie a freehold or lease), SDLT was charged on both legs of the transaction primarily by reference to the market value of the interest(s) acquired. From 24 March, the chargeable consideration in each case will be the higher of the market value of what is acquired and the chargeable consideration for the acquisition calculated without reference to the market value rules.

This potentially brings into the calculation VAT chargeable on the supply of property within an exchange. It is established that the market value of a property does not include VAT on its supply, regardless of whether (as a matter of fact) the supplier has opted to charge VAT on the property. Historically, applying the exchange rules meant that no SDLT was chargeable on the VAT charged on supplies of property. As a result of the new rules, where Party A pays £40m + VAT to acquire a freehold from Party B and grants B a lease of another property also in consideration for the acquisition, Party A's SDLT liability is no longer limited to 4% of the market value of the freehold (say £40m), but would actually be 4% of the VAT inclusive amount (£48m) given for the acquisition. In this example, the additional SDLT payable will be £320,000.

PLANNING

The Budget was also notable for its proposals for reform of the planning system, all part of the Government's wider "localist" agenda. Two of these are particularly eye-catching.

First, the concept of land auctions (trailed in the press in recent weeks) is designed to increase housing delivery by encouraging landowners to sell land to councils for development and allowing those councils to grant planning permission before selling the sites on to the development industry at a profit. In practice a land tax by another name. Understandably, industry experts are already raising doubts about the proposal – how, for example, will it work on brownfield sites where land assembly is often a difficult and complex issue? The prospect of councils benefitting directly and financially from the sale of land on which they grant planning permission is likely to raise issues of propriety. Finally, by allowing councils to 'cream-off' much of the development value of land, the Government risks disincentivising the industry further, at a time when the economic climate acts as a significant deterrent already.

Second, the promise to speed up the application determination process is warmly welcomed. Whether it will be possible to achieve the proposed guaranteed 12 month maximum determination period for all applications, including any appeals, is questionable, but that the Government has recognised the importance of reducing delays is a positive move, and should be applauded.

Other measures set out in the Budget, all previously trailed, include a new policy presumption in favour of sustainable development, proposed changes to allow the conversion of commercial premises into residential accommodation without planning permission, removing nationally imposed targets, and the creation of 21 new enterprise zones.

THE VERDICT

Whether Mr Osborne has ultimately delivered the budget for growth that he has promised remains to be seen, but for many commentators, the outlook is promising.

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Consult before you charge: Requirements of the Landlord and Tenant Act 1985

Paul Tonkin examines a recent Court of Appeal decision which highlights the serious financial consequences which may face landlords who fail to comply with the consultation requirements imposed by the Landlord and Tenant Act 1985.

The Landlord and Tenant Act 1985 continues to generate a steady stream of litigation between residential tenants and their landlords including tenants and landlords in mixed use schemes. One particularly contentious aspect of the Act is the requirement for a landlord to consult with tenants before undertaking certain works or entering into certain long-term service contracts where it wishes to recover the costs by way of service charge. Whilst the principle of consultation is difficult to argue with, many landlords feel that the rigorous consultation regime imposed by the 1985 Act often proves unworkable in practice and allows tenants to rely upon *"technicalities"* to avoid significant service charges.

The recent case of *Daejan Investments v Benson*[1] provides a salutary lesson on the importance of complying with the consultation requirements and the serious consequences which can flow from non-compliance.

WHEN DO THE CONSULTATION REQUIREMENTS APPLY?

The consultation requirements apply where a **landlord** of a **dwelling** proposes to carry out **qualifying works** or to enter into a **qualifying long term agreement** and intends to recover the associated costs from its **tenants** by way of service charge. *"Dwelling"* is widely defined and will include flats and houses. *"Tenant"* will cover most residential tenants, including sub-tenants, although, in practice, the requirements will mainly arise where tenants occupy under long-leases as short term leases such as Assured Shorthold Tenancies tend not to include service charge obligations.

"Qualifying Works" are any works to which any individual tenant will have to contribute more than £250. *"Qualifying Long Term Agreements"* are, in broad terms, service agreements entered into by the landlord (including management agreements) which will run for over 12 months and where the contribution payable by the tenant will exceed £100 in any service charge year.

TO WHOM DO THE CONSULTATION REQUIREMENTS APPLY?

The requirements clearly apply to direct landlords of residential tenants (assuming those tenants pay a service charge). However, following the case of *Oakfern Properties Limited v Ruddy*[2] it appears that the requirements also apply to a landlord of residential property even if he is not the **direct** landlord of the residential tenants. The *Oakfern* case involved a not uncommon scenario where the landlord of a mixed use block had let all of the residential element to a single tenant (who then underlet individual flats to subtenants) but leased the commercial space under a separate occupational lease to a commercial tenant. The Court of Appeal held that the single tenant of the residential premises was a tenant of a dwelling for the purposes of the 1985 Act and therefore the freeholder was required to comply with the Act in carrying out works, the cost of which it intended to recover through the service charge of the leases.

HOW DO I COMPLY?

The steps which must be complied with to satisfy the requirements vary depending upon whether the landlord intends to carry out Qualifying Works or enter into a Qualifying Long Term Agreement. In essence, the requirements are intended to ensure that the tenants have a say in the scope and cost of the works and who carries them out. The steps which, broadly speaking, must be required by a landlord intending to carry out Qualifying Works can be summarised as follows:

The landlord must give notice of intention to carry out works to each tenant and any recognised tenants' association (the Stage 1 Notice).

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The notice must:
- describe in general terms the works proposed (and a description must be made available for inspection);
- state why the landlord believes the works are necessary;
- invite written observations on the works within 30 days;
- invite nominations for contractors within 30 days.

↓

The landlord must have regard to observations made within the 30 day period.

↓

The landlord must (subject to certain limitations when more than one nomination is received) try to obtain an estimate from contractors nominated during the 30 day period.

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The landlord must prepare and serve a statement of at least two estimates, which must include any from contractors nominated by the tenants and must summarise any observations made and the landlord's response. All estimates must be made available for inspection and the landlord must invite written observations on the estimates within 30 days (the Stage 2 Notice).

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The landlord must have regard to observations made within the 30 day period.

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If the landlord contracts with a contractor who was not nominated by the tenants or did not give the lowest estimate he must within 21 days of contracting serve written notice of his reasons along with a summary and his response to any observations received in response to the Stage 2 Notice.

This diagram is not comprehensive and reference must be made to the statutory provisions themselves. There are slightly different requirements which apply in relation to Qualifying Long Term Agreements or where the works are governed by Public Works or Public Supply Regulations.

Continued...

WHAT HAPPENS IF I DON'T COMPLY?
The penalties for non-compliance are severe. A landlord who fails to comply with the consultation requirements before carrying out Qualifying Works is limited to recovering just £250 from each tenant in respect of the cost of the works. A landlord who enters into a Qualifying Long Term Agreement without complying can only recover £100 per tenant per year toward the costs of the agreement. It is not possible to contract out of the consultation requirements.

The Leasehold Valuation Tribunal (LVT) does however have a discretion to dispense with the consultation requirements and that discretion can be exercised retrospectively in circumstances where the landlord has already carried out the works. It is however clear from the case of *Daejan Investments v Benson* that this discretion will be exercised sparingly.

DAEJAN INVESTMENTS LIMITED V BENSON
The facts of the *Daejan* case were straightforward. Daejan was the landlord of a block in Muswell Hill, North London, which contained commercial units on the ground floor and seven flats above. In 2005 it became clear that major repair works were required. The landlord accordingly served the notice of intention to carry out works on the residential tenants as required. The works were put out to tender and four tenders were received. However, only two of those were made available for inspection by the tenants. Nonetheless, the landlord purported to serve Stage 2 notices on 29 July 2005 and informed the tenants on 11 August 2006 that the contract had been awarded (before the 30 day period for observations had expired).

Following completion of the works the landlord sought to recover over £270,000 from the residential tenants by way of service charge in respect of their share of the cost. The tenants refused to pay on the basis that the consultation requirements had not been met.

The landlord argued that the requirements had, in all material respects, been complied with and, in the event that they had not, sought a retrospective dispensation from the LVT. In particular it argued that any failure to complete the consultation process had not caused any prejudice to the tenants (on the basis that it would have still awarded the contract to the same contractor). It also argued that a dispensation should be granted given the financial implications of it being refused; namely, that the landlord would only recover £250 per tenant and be left with irrecoverable costs of almost £270,000.

The LVT had no hesitation in deciding that the consultation requirements had not been complied with. In particular, the landlord had not made all of the tender responses available for inspection and had cut short the second stage of the consultation process. Moreover, the LVT refused to grant a dispensation. It refused to speculate as to what might have happened if the consultation requirements had been met and held that the fact that the residents had been deprived of the opportunity to comment upon the tenders was in itself significant prejudice. It also considered that the financial detriment to the landlord of not granting dispensation was not a matter which it could take into account: the consequences of non-compliance were clearly stated in the 1985 Act and it could not be right that a landlord could rely upon these to justify dispensation. Otherwise, the more expensive the works were, the stronger the case for dispensation. The LVT felt that this could not be right given that it was in cases where great expense was concerned that tenants needed the protection of the consultation requirements the most.

The landlord appealed to the Lands Tribunal (now the Upper Tribunal) who upheld the LVT's decision. The landlord then appealed again to the Court of Appeal.

The Court of Appeal made clear that, in considering whether or not to grant dispensation, the key issue was whether or not the failure to comply had caused significant prejudice to the tenants. It agreed with the LVT that the loss of the opportunity to engage in the consultation process could, in itself, be significant prejudice, regardless of what the outcome of that consultation may have been. The Court also agreed that it was not appropriate to take into account the financial effects upon the landlord of a refusal to grant compensation. The Court suggested (by way of a non-exhaustive list) that the following scenarios might merit dispensation:

- The need to undertake emergency works;
- The availability, realistically, of only a single specialist contractor;
- A minor breach of procedure, causing no prejudice to the tenants.

These scenarios were not however relevant to the case before it and, for the reasons given by the LVT, the Court of Appeal refused to grant dispensation.

WHERE DOES THIS LEAVE US?
Landlords should be under no illusions; a failure to comply with the consultation requirements can be extremely costly – in Daejan's case, to the tune of £270,000. Although the Court of Appeal judgment makes clear that it is compliance with the substance, rather than the form, of the consultation requirements that is paramount, landlords and their managing agents should think about the consultation process at an early stage and seek advice if there is any doubt as to how and whether the requirements apply. In particular, do not assume that dispensation will be available in the event of non-compliance. It is clear from *Daejan* that dispensation is very much the exception rather than the rule.

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1 [2011] EWCA Civ 38
2 [2006] EWCA Civ 1389

The long arm of the bribery law

Jeremy Cole and Michael Roberts outline the essential elements of the new Bribery Act 2010 which overhauls the UK's corruption legislation in favour of a tough, new regime.

New bribery and corruption legislation is being rolled out across Europe and beyond. At the same time, prosecutors in a number of different jurisdictions are starting to flex their muscles. As a result, corporations face the challenge of new and overlapping regulatory regimes and, at the same time, increasingly active, and competitive, prosecutors. It is hardly surprising that almost 50% of General Counsel reportedly view corruption as the issue of most concern for their business.

In April 2010, the UK's new Bribery Act was finally passed into law. The Bribery Act radically overhauls the UK's outdated corruption legislation and introduces a tough new regime, which in many respects is more stringent, and broader in its jurisdictional reach, than even the US Foreign Corrupt Practices Act.

- **Strict Liability** – Most significantly, the Bribery Act provides that corporations may be strictly liable for bribes paid on their behalf, including by agents, employees, subsidiaries and other third parties, unless they can prove that they had in place *"adequate procedures"* to prevent such action.

- **Long-Arm Jurisdiction** – This new offence will apply to any entity carrying on business in the UK, and not just to UK corporations or those with a UK listing. As a result, many multi-national corporations will in future be subject to UK jurisdiction in relation to bribes paid anywhere in the world, including by third parties acting on their behalf (and even without any link between the payment and the UK).

- **Personal Exposure** – Equally importantly, the Bribery Act targets individuals as well as corporations. It allows prosecutors to hold individual directors liable for bribes paid by the corporation even where the directors were not themselves involved in the criminal conduct.

- **No *"Safe Harbours"*** – Finally, the Bribery Act applies to payments made to both public and private sector recipients. It contains no *"safe harbours"* in relation to either promotional expenditures or facilitation payments, and potentially captures a wide range of current commercial practices. In particular, whilst the UK authorities have sought to offer comfort in relation to how the Bribery Act will be enforced, the language of the Act may technically prohibit any corporate hospitality for foreign public officials.

The implications of this are potentially far-reaching, particularly when coupled with the increasingly aggressive approach to enforcement taken by the UK authorities and the increased sentences possible under the Bribery Act (up to 10 years' imprisonment and/or an unlimited fine).

The Bribery Act is not yet in force, and implementation has been delayed to allow businesses some additional time to ensure that their compliance procedures, and their systems and controls, are *"adequate"* to meet the new bar being set. On 30 March 2011, the Ministry of Justice published its long-awaited guidance on the Bribery Act and confirmed that it will come into force on 1 July 2011. All businesses should take steps now to ensure that they are compliant.

Inevitably, the risks in this area vary from sector to sector, and from jurisdiction to jurisdiction. However, the construction industry is generally considered to be particularly vulnerable, and therefore often comes in for particular scrutiny from the authorities. This reflects the fact that:

- Construction projects are often large-scale and involve significant sums of money;

- Third parties are often appointed on behalf of developers by project managers and architects;

- There is inevitable interaction with government officials in relation to various aspects of construction projects; and

- Overseas projects may necessitate the use of local agents in jurisdictions where *"facilitation payments"* to local officials (which are illegal under English law) may be prevalent.

It should be noted that, pursuant to the EU Public Procurement Directive, if a company, its directors or *"any other person who has powers of representation, decision or control"* over the company is convicted of a bribery offence, they will be de-barred from tendering for public projects across the EU.

Real estate investors should also ensure that *"adequate procedures"* are in place to prevent bribery offences being committed by third parties appointed to manage their portfolios or individual assets on their behalf. More generally, any business which has third parties acting on its behalf, and particularly if they are negotiating contracts or interacting with public officials, needs to ensure that it has proper procedures in place for controlling and monitoring the conduct of those third parties.

As noted above, businesses cannot afford to wait until the Bribery Act comes into force before acting. It also should not be assumed that an established anti-corruption compliance program will necessarily be *"adequate"* in every respect.

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"Vacant possession": what does it mean?

The phrase *"vacant possession"* is widely used in the property world. It can be found in a sale and purchase contract, a leasehold rent review clause or a covenant to yield up, a settlement agreement or even in a court order for possession. But what constitutes *"vacant possession"*? Nicholas Cheffings and Vivien King explain.

Ask a layman to define "vacant possession" and he would probably say that the property was unoccupied and that no personal items (or chattels, as the lawyers refer to them) had been left there. In other words, it was "empty". This ignores the possibility that someone has an entitlement to occupy or exercise rights over the property and begs the question as to what comprises personal items or "chattels" (as opposed to fixtures). Despite these shortfalls, however, a description of the property as "empty" might suffice.

But is that how a lawyer might describe the concept? Lewison J gave judicial guidance in *Legal & General Assurance Society Limited v Expeditors International (UK) Limited*[1]. (The case concerned a settlement agreement between landlord and tenant relating to conditions attached to a break clause, including the giving of vacant possession. Whilst the decision that the lease had effectively been terminated was appealed to the Court of Appeal, Mr Justice Lewison's analysis of 'vacant possession' remained unchallenged.

THE JUDICIAL PERSPECTIVE

Lewison J confirmed the hypothetical layman's view that chattels which constitute a "substantial impediment" to the use of the property cannot be left on it. He also helped with the issue of when a chattel becomes a fixture by considering what amounts to the subject property.

"If something has become part of the premises by annexation then it is part of a thing of which vacant possession has to be given. Its presence does not amount to an impediment to vacant possession itself."

Annexation is discussed below but it is necessary to eliminate one red herring: in law, there is no such thing as a "fitting". Items are either fixtures or chattels. Fixtures can be landlord's fixtures (such as air-conditioning plant) or tenant's fixtures (such as a shop fit-out required for trading). Only the latter may be removed by a tenant at the end of the lease - unless the lease prevents it.

Lewison J also considered the presence of rubbish, namely chattels abandoned by a vendor. He cited *Cumberland Consolidated Holdings Limited v Ireland*[2] (in which two thirds of the cellars included in warehouse premises were filled with rubbish). This held that *"leaving the premises in that condition was a breach of the obligation to give vacant possession."*

In *Cumberland*, the Court of Appeal also looked at the right of a purchaser to unimpeded physical enjoyment of vacant possession. To quote Lord Greene MR, *"what he [the vendor] bargains for is not merely the right in law, but the power in fact to exercise the right"*.

Putting these two factors in context, Lewison J said:

"The first test looks at the activities of the person who is required to give vacant possession. If he is actually using the property for purposes of his own otherwise than de minimis, he will be held not to have given vacant possession."

"The second test looks at the physical condition of the property from the perspective of the person to whom vacant possession must be given. If that physical condition is such that there is a substantial impediment to his use of the property or a substantial part of it then vacant possession will not have been given."

CHATTELS BECOMING FIXTURES

The tests and the judges assume that the removal of items belonging to the vacating party have not become annexed to the premises. But it might not be as simple as that. The degree of annexation must also be considered. The items may have become part of the premises themselves.

In *Lyon v London City & Midland Bank*[3] Joyce J said:

"No doubt a chattel on being attached to the soil or to a building prima facie becomes a fixture, but the presumption may be rebutted by showing that the annexation is incomplete, so that the chattel can be easily removed without injury to itself or to the premises to which it is attached, and that the annexation is merely for a temporary purpose and for the more complete enjoyment and use of the chattel as a chattel."

A picture hanging on a wall by virtue of a single nail is attached to the wall but it can usually be removed without injury to itself or the wall. It must therefore be and remain a chattel. But what about the nail? It may not be damaged upon removal, but the wall will suffer injury, albeit the hole that has been made will be small and can safely be regarded as *de minimis* so, the nail too, is a chattel.

An underfloor central heating system covered by the floor screed cannot be removed without injury to both the contingent parts of the system and the floor and must therefore be considered a fixture. (In fact, a heating system such as this will normally be installed by the landlord but it offers a good example of a fixture.)

What about partitioning installed by a tenant? Part of it might be affixed to the floor by a couple of bolts through plates and may be easily removed without harming the partitioning and causing only minimal damage to the floor. That would tend to make it a chattel, which has to be removed when giving vacant possession. However, some partitioning will be affixed to or through both the floor and ceiling and considerable damage might be caused by its later removal. That makes it a tenant's fixture; it will have become part of the property and will not have to be removed as part of giving vacant possession.

However, does the phrase "vacant possession" take on a different meaning according to the context in which it is used?

DIFFERING CONTEXTS

In *Topfell v Galley Properties*[4] Templeman J (as he then was) dismissed the hypothetical layman's view that vacant possession means empty (as argued for by the vendor in this case).

Although he preferred the purchaser's view that the words equated to *"the right to occupy and enjoy the property"* he stated that the meaning of the words can *"vary from context to context"*.

Applying Lewison J's analysis in *Legal & General*, HH Judge Bullimore recently considered the issue of vacant possession on the exercise of a tenant's break in *Ibrend Estates BV v NYK Logistics (UK) Ltd*[5]. He said that the general rule that a tenant seeking to exercise a break clause has to comply strictly with any conditions attaching to the exercise of the break applies to formal compliance with formal conditions, rather than with issues such as vacant possession.

In a ruling that illustrates the importance of understanding precisely what is required by the covenant, he held that, in this case, there was no obligation on the tenant to complete any works before vacating the premises; the obligations were to pay rent up to date and give vacant possession.

If the tenant failed to do so, the lease would not come to an end but there was no obligation to carry out any repairs in order to bring the lease to an end.

There was nothing to stop the tenant from vacating the premises on the break date, leaving any dispute about unrepaired items to be resolved at a later date. Had it done so, it would have complied with the conditions of the break clause. By carrying out works after that date, the tenant had remained in possession for its own purposes and its use of the premises was more than *de minimis*. As a result, it had not given vacant possession and so had not complied with the break clause[6].

The test for vacant possession may be altered by the words of the contract:

- in a contract for the sale and purchase of premises, there may be a requirement to leave some chattels on the premises; they cannot therefore be "an impediment" to the use of the property as they are intended to be enjoyed with it;
- in a rent review clause, the hypothetical lease may require an assumption that the premises are to be in a physical state that requires the removal of fixtures that would not fall to be removed by the assumption of vacant possession;
- in a dilapidations claim, the covenant to re-instate and yield up in a required physical state may go beyond the removal of chattels to include the removal of tenant's fixtures;
- in a rent review clause, an assumption of vacant possession may not be sufficiently wide to disregard subtenancies granted before the lease came into effect.

CONTEXT IS ALL

There are no easy answers. "Empty" is a good starting point in assessing whether vacant possession has been given. It is also wise to ask whether anything prevents a party from using the entirety of the property but, as with so much in the property world and in law, it is always necessary to understand the context in which the question is being asked, as the Ibrend case so clearly illustrates.

An earlier version of this article was originally published in Estates Gazette on 29 January 2011.

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1 [2006] EWHC 1008 (Ch)
2 [1946] 1 KB 264
3 [1903] 2 KB 135
4 [1979] 1 WLR 446
5 [2010] PLSCS 186
6 Note that this case was the subject of an appeal, which was heard by the Court of Appeal on 8 March 2011. Judgement was awaited at the time of going to print.

Partnerships and SDLT: a new layer of confusion

New HMRC guidance has muddied the waters when it comes to how LLPs are treated for SDLT purposes. Kevin Ashman and Suzanne Hill explain.

The Stamp Duty Land Tax (SDLT) rules on partnerships have been frequently altered. The cornerstone, however, has always been that partnerships, of whatever type, are 'looked through' for SDLT purposes. This cornerstone has recently been undermined by new guidance from HM Revenue & Customs (HMRC) which has given rise to anomalies.

On 11 October 2010, HMRC issued guidance outlining a change in its views on how Limited Liability Partnerships are treated for the purposes of SDLT group relief. In doing so, HMRC introduced arbitrary distinctions between different types of partnership. The availability of group relief where there is a partnership in the structure now depends upon whether that partnership is an LLP, an English partnership or a Scottish partnership.

In addition, the rules for SDLT and stamp duty continue to treat LLPs differently. This leads to the illogical result that the availability of group relief on a transfer of shares may be different to that on a transfer of land between the same entities.

THE PARTNERSHIP RULES

The basic SDLT rule for partnerships is that they must be disregarded so that a purchase or sale of land by the partnership is a purchase or sale by the partners.

The basic rule is altered for transactions between the partnership and the partners (or connected persons). These 'special transactions' are charged on a proportion of the property's market value, which will be broadly equal to the economic interest changing hands.

The basic rule and the rules relating to 'special transactions' apply equally to LLPs and to general and limited partnerships (whether English or Scottish). However, since HMRC's statement, the way each of these entities is treated for group relief purposes differs.

GROUP RELIEF

SDLT group relief is available where the vendor and purchaser are both bodies corporate and are grouped. Bodies corporate are grouped where one is the 75% subsidiary of the other or both are 75% subsidiaries of another company. The 75% test depends partly upon ownership of ordinary share capital, which can be direct or indirect through other bodies corporate.

PARTNERSHIPS AND GROUP RELIEF: HMRC'S VIEWS

Before 11 October 2010, HMRC took the view that an LLP was not a body corporate. Its revised approach considers that an LLP is a body corporate and can be the parent of a group but that it does not have ordinary share capital and therefore cannot be a subsidiary. It breaks the group between companies above and below it. Despite this revised approach, where SDLT group relief has previously been incorrectly claimed because an LLP has been disregarded in establishing a group, HMRC will not revisit the claim.

The statement also sets out HMRC's views on English and Scottish partnerships. An English limited or general partnership is not a body corporate and does not have separate legal personality so must be disregarded ('looked through') when assessing whether companies are grouped. A Scottish limited or general partnership, although not a body corporate, has a separate legal personality and therefore cannot be disregarded in this way.

What does this mean in practice for different forms of partnership?

TRANSFERS BETWEEN PARTNERSHIP SUBSIDIARIES

Group relief will potentially be available on a transfer between subsidiaries of an LLP, since an LLP is a body corporate and can be a parent company.

Where the partnership is an English limited or general partnership, the existence of the partnership must be ignored in establishing whether or not the subsidiaries are grouped. This will instead depend upon the partnership interests of the partners. If a partner has a 75% interest, it may form the SDLT parent of the partnership subsidiaries and group relief may be available.

For Scottish partnerships, group relief will not be available since the partnership will not be a body corporate and cannot be 'looked through' to the partners.

TRANSFERS BETWEEN A PARTNERSHIP AND ITS SUBSIDIARY

Group relief will not be available on a transfer between an LLP or a Scottish partnership and its subsidiary. In these cases, the partnership is disregarded as a party to the transaction, so that the partners will be deemed to be buying or selling; it will not be disregarded in establishing whether a group relationship exists between the partners and the subsidiary. As such, the LLP or Scottish partnership breaks the group.

Group relief may be available on a transfer between an English partnership and its subsidiary if a partner has a sufficient interest to be grouped with the subsidiary.

TRANSFERS THROUGH A PARTNERSHIP

Group relief will not be available on a transfer between a company above an LLP or a Scottish partnership and a company held by the LLP/Scottish partnership. The latter is treated as breaking the group. With an English partnership, relief may be available if the 75% test is met.

TRANSFERS BETWEEN A PARTNERSHIP AND A PARTNER

The availability of group relief on a transfer between a partnership and a partner is unaffected by the type of partnership because the 'special transactions' rules apply. The partnership is ignored and the availability of group relief depends upon whether or not the partners are grouped.

LLPS AND STAMP DUTY

The complexities described above are compounded by the fact that the rules for stamp duty group relief for LLPs (which applies to shares) differ from the SDLT rules. HMRC states that transfers of shares between an LLP and its subsidiary can qualify for stamp duty group relief (despite the fact that land transfers between such entities do not qualify for SDLT group relief). However stamp duty group relief cannot be claimed on a transfer of shares between a parent of an LLP and the LLP (although SDLT group relief might arise on a land transfer between such parties if the LLP partners are grouped, as described above).

CONCLUSION

HMRC's statement is welcome insofar as it allows SDLT group relief on transfers between LLP subsidiaries.

However, the arbitrary distinctions that have been created between different types of partnership are unsatisfactory and the differing treatment of LLPs for SDLT and stamp duty purposes seems illogical.

When establishing partnerships (whether within a group, for joint ventures or for real estate funds) it will be necessary to consider which land transactions may be undertaken and the potential SDLT consequences.

HMRC is reviewing the group relief legislation for both SDLT and stamp duty purposes, including the change of interpretation in its statement, to see how well it reflects the underlying policy aims in relation to LLPs. Further change seems likely.

One way of avoiding distinctions between different types of partnership might be to amend the legislation so that all partnerships are 'looked-through' for all SDLT purposes. This would have the advantage of simplicity, although it would potentially deny relief on transfers between subsidiaries beneath a partnership unless the partners were grouped with those subsidiaries.

An earlier version of this article appeared in Estates Gazette on 11 December 2010.

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Penalty clauses in agreements: how to avoid a red card

In this article Nathan Searle and Kate Wilford explain why the real estate industry should be alert to potentially unenforceable penalty clauses and suggest ways to tackle these issues in leases and other contracts.

WHAT IS A PENALTY CLAUSE?

A penalty is a clause designed to deter a breach of contract that provides for a breaching party to pay (or forfeit) a stipulated sum to the innocent party upon breach of contract. A clause will not be a penalty if it was a genuine pre-estimate of the loss likely to be suffered by the innocent party following breach (often referred to as a liquidated damages clause). Whether a clause is a penalty or a liquidated damages clause is a question of construction to be judged at the date that the contract or lease was entered into, not at the date that the breach actually occurs.

WHAT IS THE EFFECT OF A CLAUSE BEING HELD TO BE A PENALTY?

Under English law, courts will not enforce a provision of a lease or contract that is a penalty. This means that an innocent party would not be entitled to obtain an order for payment under a clause that constitutes a penalty. However, the innocent party would still be able to claim damages for breach of contract provided that it could show it had suffered loss as a result of the other party's breach of contract and such claims were not excluded under the terms of the lease or contract.

PAYABLE UPON BREACH

A clause will only be a penalty if it provides for a sum to be payable upon breach of the agreement. Accordingly, one way to avoid a clause being a penalty is to structure the agreement so that the payment is not triggered by breach. The distinction was considered by the Court of Appeal in the recent case of *UK Housing Alliance (North West) Ltd v Francis*[1].

Mr Francis entered into a sale and leaseback transaction with UK Housing. The agreement provided for 70% of the purchase price to be paid upon completion of the sale of the property to UK Housing. The final 30% was to be paid to Mr. Francis upon the expiry of 10 years and Mr Francis giving up possession of the property.

The sale contract provided that Mr Francis would lose the right to receive the final payment if UK Housing validly terminated the lease in accordance with its provisions.

Notably, the lease provided that UK Housing could terminate the lease and obtain a court order to evict Mr Francis if he failed to:

- pay rent within 14 days of demand after it had fallen due; or
- comply with any of his obligations under the lease.

Mr Francis failed to pay rent. Consequently, UK Housing terminated the lease and refused to make the final payment of the purchase price to Mr Francis. Mr Francis claimed the final payment on the basis that the clause, which deprived him of the final payment, was a penalty.

It was accepted that the clause could not be a penalty because it was not a sum payable on breach by Mr Francis, but a sum payable if UK Housing exercised its right to terminate the lease. Had the sale agreement provided that Mr Francis would lose his entitlement to the final payment automatically upon failing to pay rent or comply with any of his other obligations under the lease, then the result may well have been different.

Mr Francis argued that the principles applicable to the irrecoverability of penalties were applicable to cases of relief against forfeiture. However, the Court did not need to decide this issue because it had no jurisdiction to grant relief against forfeiture to Mr Francis since he had no proprietary right in the final payment. It was merely a contingent right to payment of a debt.

DEFAULT INTEREST

A very high default interest rate can also constitute a penalty. The recent decision of the High Court of Justice in Northern Ireland in *Fernhill Properties (Northern Ireland) Ltd v Mulgrew*[2] held that a contractual interest rate of 15% was a penalty and therefore unenforceable. Consequently, the seller was only able to recover interest at a rate of 5%.

The case concerned a contract for the sale of land where the buyer had defaulted and the seller claimed damages together with interest at a contractual rate of 15%. When assessing whether the interest rate was penal, the Court looked at rates at the time that the contract was entered into and not at the time the purchaser had defaulted. This was important as rates had fallen sharply between the time of contract and time of default.

The Court found that *"For the rate of 15% here to be a genuine pre-estimate of loss it seems to me that the [seller], with a then base rate of 5.25% would have had to say that it was going to pay or was at a foreseeable risk of paying 9.75% above base for continuing borrowings in the event of non completion by the [buyer]."* The seller had not proved that it would have had borrowing costs approaching this level and had declined an opportunity to lead evidence of its actual borrowing costs. The Court found that *"It may well be that a rate of 10% or even 12% might have been justified"* but *"the high and round figure of 15% was clearly, on the balance of probabilities, a penalty designed to deter a purchaser from defaulting on completion."*

However, a great deal will depend on the circumstances of the case. The Court in *Fernhill* distinguished the English Court of Appeal decision in *Taiwan Scott Company Limited v The Master Golf Company Limited*[3] which held that a 15% contractual interest rate was enforceable. The Court distinguished *Taiwan Scott* on the basis that it related to an agreement between two commercial concerns in respect of a contract for the importation of goods into China. However, the Court also questioned whether the English Court of Appeal had applied the right test, as it had said that the contractual rate was *"not in any way exorbitant"* and therefore not a penalty. The judge in *Fernhill* considered that whether an interest rate was *"not in any way exorbitant"* and whether it was a *"genuine pre-estimate of loss"* were not the same test and that the English Court of Appeal had therefore not applied the appropriate test.

NEGOTIATING TIPS

There is a presumption that a clause is a penalty where it provides that a single lump sum is payable by way of compensation on the occurrence of one or more or all of several breaches, some of which may occasion serious and others trifling damage. Accordingly, if parties agree a liquidated damages clause to cover more than one type of breach, and which are likely to result in different levels of losses, they should consider agreeing a sliding scale so that the sum payable varies depending on the number, type or severity of the breaches. Such an approach is more likely to be regarded by the court as reflecting a genuine pre-estimate of loss.

As the court will be judging the issue of whether a clause is a penalty at the time that the lease or contract was entered into, parties should consider including statements to the effect that they have attempted to make a genuine pre-estimate of the loss and consider the sum payable to be reasonable and/or have obtained legal advice on the clause. Such statements are helpful as they indicate that the parties considered these issues at the time of entering into the contract, but will not preclude a court from finding that the clause is a penalty.

Key points

- Parties should consider whether provisions for the payment of sums triggered by events relating to the performance of leases or other contracts might be a penalty. If there is a risk that they may be a penalty, then the parties should seek legal advice as to whether there is some way to structure the provisions so that it is not payable upon breach but upon some other event (such as the exercise of a right of termination).
- When they enter into an agreement, parties should attempt to ascertain what losses are likely to result from a breach and use this as a benchmark to set the sum payable.
- Parties should consider recording in the agreement or elsewhere a statement as to the estimations of loss to increase the likelihood that a Court will regard the sum as a genuine pre-estimate of the loss.
- Failure to mitigate the risk of a clause being a penalty could result in it being unenforceable.

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1 [2010] EWCA Civ 117
2 [2010] NICh 20
3 [2009] EWCA Civ 685

The Building Regulations 2010

Those involved with construction projects in England and Wales know they must comply with the Building Regulations but, for many, the procedures for compliance remain a mystery. Against the background of a recent consolidation exercise by the UK government, Mark Crossley provides an overview of the regime and highlights questions that purchasers of a property should ask.

WHAT ARE THE BUILDING REGULATIONS 2010?
Building regulations apply to most types of domestic, commercial or industrial building. On 1 October 2010, the Building Regulations 2010 (the "Regulations") and the Building (Approved Inspectors etc) Regulations 2010 (the "Approved Inspectors Regulations") came into force in England and Wales. These regulations consolidate the Building Regulations 2000, the Building (Approved Inspectors etc) Regulations 2000 and all subsequent amendments. This consolidation was required following criticism that the 2000 regulations had been amended piecemeal, making it difficult for parties to understand which rules applied to any particular project.

The building regulations regime was originally introduced to ensure the health and safety of people in and around buildings and now also aims to reduce carbon emissions from new buildings. Building work must be carried out with adequate materials, in a workmanlike manner and in compliance with certain requirements and minimum standards. These requirements are addressed in different sections of the Regulations, usually referred to as Parts A to P, in relation to which technical guidance is also published. This guidance is gradually being updated by the government.

It is the developer's responsibility to obtain approval for its "building work" in order to comply with the Regulations. "Building work" is broadly defined and in some circumstances includes demolition works. Depending on the nature of the building work, there are three options a developer can use to obtain approval: applying for approval from the relevant local authority building control service (the "LABCS") under Regulations 13 and 14 of the Regulations; engaging a competent person to carry out the work under an authorised self-certification scheme under Regulation 20 of the Regulations; or applying for approval from a private sector approved inspector under s47 of the Building Act 1984.

PROCEDURES FOR OBTAINING APPROVAL FROM THE LABCS
There are two different procedures for obtaining building regulation approval through the LABCS: giving a building notice and depositing a full plans application. For both procedures, a charge must be paid, the developer must give notice to the LABCS prior to and following completion of the works and the LABCS issues a certificate of completion if the works are properly carried out.

If the full plans applications procedure has been used and there is a dispute between a developer and the LABCS about whether the building works have been carried out properly, a developer may ask for the issue to be determined by the Secretary of State for the Department of Communities and Local Government ("DCLG"). There is no such right under the building notice procedure.

BUILDING NOTICE
The building notice procedure is intended for situations where the work is not particularly complex, but is not available for certain types of building work, such as that involving fire safety or drainage.

To comply with this procedure, the Regulations require a developer to submit information about the works, but not detailed plans, to the relevant local authority. The exception to this is an application for erecting or extending a building, for which a plan and slightly more detailed information is required.

LABCS will inspect the work periodically and advise if the building works do not comply with the Regulations. Once the building notice has been submitted, it is valid for three years and automatically lapses after three years if the building work is not started.

FULL PLANS APPLICATION
A full plans application requires a developer to deposit detailed plans and other information with the LABCS indicating all the construction details.

The LABCS will check the plans, consult with appropriate authorities and issue a decision within five weeks from the date of the application.

If the plans do not comply with the Regulations, the LABCS either may ask the applicant to amend the plans or provide more details or may issue a conditional approval, which will either specify modifications to the plans or require further plans to be deposited with the local authority.

If the plans comply with the Regulations, the applicant will receive an approval notice. A full plans approval notice is valid for three years form the date of deposit of the plans. The building works must be started within three years otherwise the local authority can contact the applicant notifying him that the approval notice has no effect. Once the works are in progress, the local authority will carry out regular inspections to ensure that the Regulations are being complied with.

SELF-CERTIFICATION SCHEME
Self-certification allows certain types of building work to be approved by a person competent to assess the works. This usually involves the works being carried out by persons with qualifications, registrations and trade association memberships set out in the Regulations. For example, because the Cavity Wall Insulation Self Certification Scheme administered by Cavity Insulation Guarantee Agency Limited is listed in the Regulations, the insertion of insulating material into the cavity walls of an existing building by a contractor registered with the Cavity Wall Insulation Self Certification Scheme would automatically be approved under the Regulations. In order to obtain approval under the self-certification scheme, the person carrying out the work must give the developer a certificate.

The main changes introduced by the Regulations were the expansion of the types of work a registered installer may carry out and of the list of bodies authorised to register as installers, and the inclusion of works relating to improving energy efficiency.

This expansion may lead to a decrease in tender costs as the number of works subject to the two LABCS schemes, which incur the expense of local authority fees and the cost of putting together plans, has been reduced.

APPROVED INSPECTOR

The third method a developer can use to obtain Regulations approval is to engage a private sector approved inspector and make a joint initial notice to the local authority, giving the local authority notice of the intended building works. Building work can start as soon as the initial notice has been accepted by the local authority. A notice is treated as accepted unless it has been validly rejected within five days of being given. Building work cannot begin if the local authority rejects the initial notice.

The Approved Inspector Regulations set out the procedures for the supervision of works by an approved inspector. The duties of the approved inspector include checking plans, inspecting the work as it progresses and issuing a final certificate to the local authority when the building works have been completed in compliance with the Regulations. If the approved inspector expresses that he is not satisfied with the work as it progresses, the approved inspector will have to cancel the initial notice unless the works are removed or altered. This will terminate the approved inspector's responsibility for the building works and the LABCS will then step in.

If there is a dispute between the developer and the approved inspector about whether the building works have been carried out properly, the developer may ask for the issue to be determined by the Secretary of State for the DCLG or apply to the LABCS for a relaxation of the Regulations. If the LABCS refuses to grant this, the applicant can ask for the issue to be determined by the Secretary of State for the DCLG.

UNAUTHORISED BUILDING WORK

If work should have been approved under the Regulations but was not, a property owner can apply to the LABCS for the works to be regularised. The owner must submit various pieces of information, including, so far as is reasonably practicable, a plan showing any additional work required to ensure that the unauthorised work complies with the requirements in force when the work was undertaken. The LABCS may request unauthorised work to be opened up and will then decide whether remedial work is required to make it comply with the building regulations as they were at the time the unauthorised building works were carried out. If the LABCS is satisfied that the requirements of the Regulations have been complied with or no work is required to secure the unauthorised work, it will issue a regularisation certificate as evidence of compliance.

ENFORCEMENT OR "BUILDING CONTROL"

If a person carrying out building work contravenes the Regulations, the LABCS may take various enforcement measures. Prosecution in the magistrates' court will generally only take place in cases of flagrant breach. Even if a local authority does not take enforcement action, it will not issue a completion certificate to confirm compliance with the Regulations, which could cause the property owner problems when it wishes to sell the property.

WHAT ISSUES SHOULD PURCHASERS CONSIDER?

Purchasers should ask whether building work was submitted for approval under the Regulations and, if so, how approval was obtained so that the correct certificate can be requested.

If the work was not approved, the purchaser should request that the owner applies for a regularisation certificate.

It is important to remember that any completion and regularisation certificates are not conclusive evidence that the Regulations have been complied with. A party acquiring property where it is concerned that the Regulations have not been complied with may wish to take out indemnity insurance.

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Case update

Paul Tonkin reviews the latest cases.

FREEHOLD AND LEASEHOLD INTERESTS WILL NOT MERGE IF RIGHTS GRANTED UNDER A LEASE WILL BE EXTINGUISHED

BOH Limited v Eastern Power Networks Plc [2011] EWCA Civ 19; [2011] 5 E.G. 104 (C.S.)

Eastern Power was the tenant of plots 1, 2 and 3 under a lease granted in 1953 for 42 years. The lease granted a right of way over plot 4 and a right to lay cables across plot 4, also then owned by the landlord. Eastern Power built an electricity substation on plot 2 and laid cables through plots 3 and 4.

The freehold titles to the plots were sold to separate purchasers. Eastern Power itself purchased the freehold to plot 2. Plots 1 and 4 were purchased by BOH and plot 2 was purchased by Layhawk. BOH and Layhawk argued that the 1953 lease had expired and the rights over plots 3 and 4 were no longer exercisable. Alternatively, it argued that the effect of Eastern Power acquiring the freehold of plot 2 was that its lease merged with the freehold such that the rights granted by the lease over plots 3 and 4 were extinguished and could no longer be exercised in favour of plot 2. Eastern Power argued that even though the 1953 lease had expired, it remained entitled to holdover and seek a new lease under the Landlord and Tenant Act 1954 and, moreover, that the lease had not merged with its freehold title.

The Court of Appeal agreed with the Judge at first instance and held that there had been no merger. Eastern Power was holding over under the 1954 Act and continued to have the benefit of the rights over plot 3 and plot 4. Whilst the rule at common law was that a merger would occur when the lease and its reversion were owned by the same person, there was a presumption in equity that, in the absence of clear contrary intention, a merger would not occur where that would not be in the interests of the person by whom the lease and reversion were held. In this case, merger was clearly not in Eastern Power's interests and it did not matter that it might have been in the interests of BOH and Layhawk as co-reversioners.

ACTUAL USE RELEVANT FOR RIGHT OF WAY UNDER SECTION 62 OF LAW OF PROPERTY ACT

Campbell v Banks [2011] EWCA Civ 61

The Campells and the Banks owned properties that had once formed part of the same estate. The Campells built a stable block on part of their property, from which they ran an equestrian business. The Campells claimed a right of way to ride horses over a lane on the Banks' adjoining land. In particular, the Campells argued that the right of way was created in 1953 as a result of section 62 of the Law of Property Act 1925 when the then common owner of the estate sold the Campells' land and retained the Banks' land.

The Court disagreed. Whilst a right of way could be created under section 62 where an owner sold part of his land, this would only be the case where, as a matter of fact, the land which was sold-off enjoyed the benefit which was claimed over the retained land as at the date of sale. In this case, there was no evidence that the Campells' land had enjoyed the use of the Banks' land for riding horses when it was sold off and therefore no easement could arise under section 62.

BREAK NOTICE SERVED ON INCORRECT LANDLORD VALID WHERE MANAGING AGENT PURPORTED TO ACCEPTED IT

MW Trustees Limited v Telular Corp [2011] EWHC 104 (Ch)

Telular was MW's tenant of commercial premises. Telular had an option to break its lease on 1 March 2010 by giving not less than 6 months' notice in writing. Telular intended to exercise the break option, but wrongly served the notice on the previous landlord who had since sold its interest to MW.

The previous landlord informed Telular of its mistake and Telular then sent an email, attaching the notice, to MW's managing agent. Email was not a permitted method of service under the lease. The agent replied stating that it *"accepted"* the notice and was happy for Telular to exercise the break. However, it asked that the notice be readdressed to MW. Telular failed to serve a readdressed notice and MW argued that the break was not effective.

The Court held that the notice was valid. It found that the use of the word *"accept"* in the managing agent's reply was not merely an acknowledgement of receipt. Rather, it indicated an intention to accept the notice as valid and waive the defective method of service and the fact that it was addressed to the wrong person. The Court was not prepared to find that the request to readdress the notice altered the position. MW (through its managing agent) had represented that it accepted the notice and Telular was entitled to rely upon that representation.

REGISTRATION ON BASIS OF ADVERSE POSSESSION INVALID WHERE ADVERSE POSSESSION NOT ESTABLISHED IN LAW OR FACT

Baxter v Mannion [2011] EWCA Civ 120

Mr Mannion bought a field in 1996 and was registered as proprietor at the Land Registry. Mr Baxter had made use of the field for a number of years and, in 2005, made an application to the Land Registry to be registered as owner of the field on the basis that he had acquired title by adverse possession. The Land Registry wrote to Mr Mannion stating that, if he wished to object, he must do so within the required time limit. Mr Mannion failed to object in time and Mr Baxter was accordingly registered as owner.

Mr Mannion applied to rectify the Register by reason of mistake, arguing that the registration of Mr Baxter was a mistake on the part of the Land Registry because Mr Baxter had not, as a matter of law or fact, established that he was in adverse possession of the field. Therefore his application to be registered as owner should have been rejected. Mr Baxter argued that Mr Mannion was only entitled to object to the application within the time limit provided for by the relevant rules. Once that time limit had expired, it was no longer open to Mr Mannion to challenge the registration.

The Court of Appeal (upholding the decision of the trial Judge) agreed with Mr Mannion. It was implicit in the Land Registration

Act 2002 that only a person who was, as a matter of fact and law, in adverse possession of land could apply to be registered as owner on the basis of adverse possession. Mr Baxter was not in adverse possession and, therefore, the Land Registry's acceptance of his application and decision to register him as owner was a mistake which could be corrected under the rectification provisions in the Act. To conclude otherwise would be an invitation to fraud. It would effectively amount to a decision that a landowner could lose his land without compensation by reason of nothing more than failing to respond to a notice in time and this would be contrary to the Convention on Human Rights.

NIGHTCLUB OWNER NOT LIABLE FOR KNIFE ATTACK ON GUEST

Everett v Comojo (UK) Limited [2011] EWCA Civ 13

Mr Everett was a guest at a night club owned by Comojo. He was seriously injured as a result of a knife attack by another guest of the club. Mr Everett sued Comojo arguing that it had a duty to take reasonable care of its guests and had failed to discharge that duty.

The Court of Appeal accepted that a night club owner owes a duty to take reasonable care of guests whilst on the premises and that this extended to the actions of third parties, including other guests. However, the standard of care to be taken must be fair and reasonable in all the circumstances. The Court considered that the duty was akin to that owed by an occupier under the Occupiers Liability Act 1957 and, in the circumstances, it found that Comojo had discharged its duty and was therefore not liable for Mr Everett's injuries.

PERSONAL RIGHT OF APPROVAL RELEASED ON DEATH OF BENEFICIARIES

Churchill v Temple [2010] EWHC 3369 (Ch)

The Churchills owned 1A Loom Lane. The property was subject to a restrictive covenant which provided that no house was to be erected on the plot of 1A without the approval of *"the Vendors or their surveyor"*. The conveyance by which the covenant was imposed defined *"the Vendors"* as being Mr and Mrs S, previous owners of the land with the benefit of the covenant. Mr and Mrs S had since died and the land that benefitted was now owned by the Temples.

A dispute arose as to whether the right of consent had passed to the Temples as successors in title to Mr and Mrs S and, if it had not, what the effect was of the death of Mr and Mrs S.

The Court found that there was no evidence that the reference to the Vendors should impliedly be taken to refer also to their successors in title. There were very good reasons why Mr and Mrs S might have wanted to retain a personal right of approval over the development of number 1A.

Read literally, the covenant would amount to an absolute prohibition on building following the death of Mr and Mrs S as it would be impossible to secure their consent. However, the Court felt that this could not have been the intention of the parties. The covenant must be made to *"yield to commonsense"*.

A reasonable third party, with the available background information, would have read the covenant as one which applied only during the lifetime of Mr and Mrs S. The effect of their deaths was therefore to release the covenant altogether.

ORDER TO PROHIBIT USE OF RIGHT OF WAY BY TRAVELLERS

Ashdale Land & Property Co Limited v Maioriello [2010] EWHC 3296

Ashdale sold a field at the end of its land and granted the purchaser a right of way over the lane via which the land was accessed, for agricultural purposes only. The land was sold off in plots, some of which were sold to travellers. In 2009 the travellers started to develop the land, including using the lane for access by construction vehicles, in breach of the terms of the right of way. The development of the land also amounted to a breach of planning control. An injunction was obtained to prevent access for non-agricultural purposes, but the works continued in breach of the injunction. Ashdale accordingly placed concrete blocks at the end of the lane, preventing access to the caravan site. However, the travellers then used the lane for car parking, also in breach of the right of way.

The Court granted Ashdale an order prohibiting any use of the right of way by the travellers. The Judge considered that this was proportionate in circumstances where the earlier injunction, which simply prohibited unlawful use of the right of way, had been shown to have been ineffective and was not practicable to enforce.

RIGHT ACQUIRED BY LONG USER FOR AGRICULTURAL USE DID NOT EXTEND TO ANCILLARY USES

Dewan v Lewis [2010] EWCA Civ 1382

The Dewans owned a house which abutted a private road, jointly owned by the Dewans and their neighbours. The road was the means of access to an area of agricultural land owned by Mr Lewis. The Dewans and their neighbours sought an injunction preventing Mr Lewis for using the road to drive animals. Mr Lewis counter-claimed arguing that he had acquired a right of way over the road by long user between 1986 and 2006. The Judge accepted Mr Lewis' evidence and declared that a right of way had been acquired for the benefit of Mr Lewis' land at all times and for agricultural purposes with or without animals or vehicles.

The Dewans appealed arguing that, even if a right of way had been acquired, it should not extend to a right to drive livestock along the road as there was no evidence that the road had been used for this purpose throughout the relevant period. Mr Lewis argued that, having established a right of way of general agricultural purposes, this should extend to the driving of the livestock, which was a normal incident to the use of agricultural land.

The Court of Appeal allowed the appeal. Where a right was acquired by long user the extent of the right was determined by the extent of the user. Rights acquired by long user arose as a result of acquiescence by the owners of the land

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subject to the rights and they could not be taken to have acquiesced to use which had not in fact occurred during the relevant period. There was no evidence that the road had been used for the driving of livestock and therefore the right of way acquired should not extend to this use.

NO DISCOUNT TO DAMAGES ASSESSMENT FOR POSSIBILITY THAT BUSINESS MIGHT BE UNSUCCESSFUL
Vasiliou v Hajigeorgiou [2010] EWCA Civ 1475
Mr V was Mr H's tenant of restaurant premises in North London. During the course of refurbishment works to adjoining residential premises, and before the restaurant was able to open for business, Mr H obstructed the fire exit to Mr V's restaurant. The works to the adjoining premises also caused foul water to enter into the restaurant, making the toilets unusable. These were both serious breaches of healthy and safety regulations and rendered the restaurant unusable for over two years. Mr V sued for breach of quiet enjoyment, claiming the lost profits he had suffered as a result of being unable to trade.

The court found that there had indeed been a breach of quiet enjoyment. When it came to the assessment of damages, Mr H put forward evidence to the effect that, even though Mr V had previously been a successful restaurateur, there were signs that he had since lost that ability and therefore the restaurant would not have been a success if it had been able to trade. The Judge rejected this evidence and found that the restaurant would have been a success. He awarded damages on this basis and did not make any discount for the possibility that V's restaurant might have failed.

The Court of Appeal upheld the Judge's finding. Where the Judge had found, as a matter of fact and on the balance of probability, that the restaurant would have been a success, it was not necessary or appropriate to then apply a discount to take account of the possibility that it might not be.

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Q&A

In this edition, Pete Buckley explains how failure to register a charge at Companies House can affect the priority of charges whilst Jane Dockeray and Charlotte Wright consider the implications of companies converting into industrial and provident societies.

Q. I have taken a charge over a property and, although the debenture has been registered at the Land Registry, I have just discovered that it has not been registered at Companies House. What are the consequences of this? In particular, am I vulnerable to subsequent charges over the property or is my priority assured by the Land Registry registration?

A: In order to perfect security over land, a charge must be registered at the Land Registry and also at Companies House[1]. Failure to register at Companies House renders the charge void as against a liquidator and/or administrator and other creditors[2].

However, the unregistered charge is still valid as between lender and borrower and is enforceable until the commencement of the winding up or administration of the borrower, at which point it becomes void against the liquidator or administrator.

You will only therefore have an issue if the owner of the land (i.e. the borrower) gets into financial difficulties at a time before you have enforced your charge or the loan has been repaid. If the borrower were to go into liquidation or administration then a liquidator or administrator (as the case may be) would be able to sell the property free of your charge. Furthermore, if there are subsequent charges over the property that have been properly registered and a liquidator and/or administrator is appointed, these charges would take priority to yours. Such chargeholders would be paid out of the proceeds of sale first, and could exercise their power of sale in priority to you.

When a charge is registered at the Land Registry without a Companies House certificate of registration, the Land Registry is obliged to note on the title register that registration is subject to the consequence of failure to register at Companies House[3]. This note should alert property owners to the potentially serious consequences for the unprotected lender.

In conclusion, when you take a charge over property you must ensure that it is always registered at Companies House and the Land Registry – if you do not then the Land Registry registration will not rectify the omission. Looking ahead, the Government has been considering combining the two applications into one, although its consultation has resulted in identifying many practical problems with this combination[4].

Q. One of my tenants has recently notified me that it has converted from a company into an Industrial and Provident Society. Should I be concerned at this change of status and what does it mean?

A. Under the Industrial and Provident Societies Act 1965[5], a company registered under the Companies Act 2006 may convert to a registered society. An "I&P" Society is a type of mutual, carrying on business either for the benefit of the community or for the mutual benefit of its members. Profits are mostly reinvested in the society. I&P Societies are registered with the Financial Services Authority.

Conversion from a company to an I&P Society requires a special resolution[6]. In order to ensure that conversion has validly occurred, you should ask to see a copy of the special resolution. From conversion, the entity ceases to exist as a company[7]. Its status at Companies House under its old registered number will read "Converted/Closed" and the date of conversion will be given. A new entry will be made at Companies House in the same name, but with a different number containing the prefix "IP". That entry will simply refer you to the FSA. The entity will from then on be listed on the FSA Mutuals Public Register, which is where you can find its FSA registered number, registered address and the date of registration.

As the process of changing from a company to a registered society is one of conversion, no formal assignment of any lease is required. The lease remains vested in the same legal entity, which has simply taken a different form. The obligations and liabilities of the tenant under the lease continue despite the conversion, and the I&P Society remains liable for any past breaches which occurred during its existence as a company.

A registered I&P Society must comply with the regulatory regime relating to registered societies which includes, among other things, having to keep proper accounts, submit an annual return and give notice of any change of its registered office. An I&P Society comprises members rather than shareholders but, if registered, has limited liability and corporate body status with perpetual succession. This means that it continues to exist even if its membership changes and it can act, sue and be sued and own property and other assets in its own name. For a converted company which applies to the FSA to be registered, the nominal value of shares held by any member other than a registered society must be confirmed as not exceeding £20,000.

Information on Industrial and Provident Societies can be found on **http://mutuals.fsa.gov.uk** which also contains the register of I&P Societies.

1 Registration must be within 21 days of the date of the charge (Companies Act 2006, section 860).

2 Companies Act 2006, section 874. You can apply to court to register the charge at Companies House out of time, although there are fairly stringent requirements you would need to satisfy – see Companies Act 2006, section 873. It is more likely that a new charge will be needed.

3 Land Registration Rules 2003, rule 111.

4 See **http://www.bis.gov.uk/Consultations/registration-of-charges?cat=closedwithresponse** for the latest.

5 The Industrial and Provident Societies Act 1965 is due to be renamed the "Cooperative and Community Benefit Societies and Credit Unions Act 1965".

6 Industrial and Provident Societies Act 1965, section 53(1).

7 Industrial and Provident Societies Act 1965, section 53(6).

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This newsletter is written in general terms and its application in specific circumstances will depend on the particular facts.

If you would like to receive this newsletter by e-mail please pass on your e-mail address to one of the editors listed below.

If you would like to follow up any of the issues, please speak to one of the contacts listed below, or to any property partner at our London office on +44 20 7296 2000, or to any property partner in our worldwide office network as listed at the back of this newsletter:

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