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Review

Property @ction

Welcome to the Fifth Edition of the Quarterly Review from by Hammonds' Property@ction Team. In this issue we will look at the following:

(i) The New Valuation Tribunal Regime;

(ii) Section 17 Notices: A necessary evil?;

(iii) Bridging the rental gap;

(iv) Open all hours - Remedies for breaching "Keep open" clauses;

(v) Virtual Assignments;

We welcome all contributions to this review and if you would like to discuss this further please contact any of the editorial team.

The New Valuation Tribunal Regime

Non-Domestic Rates (rating) have a long history which is both legislative and set out in case law. Over the last 20 years those of us who deal with rating have become used to seeing changes to the regulations dealing with appeals, however, last year saw the first significant change to the Valuation Tribunals who deal with the appeals.

There has been no significant change to the appeal regulations, but as of 1st October 2009, 52 independent Valuation Tribunals for England have been amalgamated into the Valuation Tribunal England (VTE). To a limited extend, we had already seen some practical amalgamations following the creation of the Valuation Tribunal Service (VTS) but the Tribunals themselves had retained their own members, chairmen, etc.

The Valuation Tribunal for England (Council Tax and Rating) (Procedure) Regulations 2009 came into force on 1st October 2009 and were matched by new appeal regulations (for rating this is The Non-Domestic (Alteration of Lists and Appeals) (England) Regulations 2009).

The VTE has now published a series of Practice Statements which will govern the procedural aspect of hearings - this is the first time that a comprehensive set of rules have been made available. How they will work in practice has yet to be tested. The procedures do bring a degree of clarity to the process which is to be welcomed. The introduction of guidance for the Tribunal members on how to weight evidence and draw conclusions should bring greater consistency in the decisions, which is also a positive and welcome change.

One new procedure allows for witnesses to be summoned, specifically aimed at witnesses who are unlikely to attend without a summons being issued. This is unlikely to be used often, but may prove invaluable to ratepayers in a few extreme cases. However, there are potential downfalls to the new procedures. One strength of the former Valuation Tribunals was that the hearings were informal, which allowed easier access for unrepresented ratepayers and greater latitude within a hearing to explore the pros and cons of each side's case, with evidence rarely having to be proved. The lay members of the Tribunal have been ably assisted in the past by experienced, normally IRRV qualified, Clerks who could advise on points of law and case law where necessary. Although there will still be a Clerk/Tribunal Officer at the hearing, he/she will be excluded from the Tribunal's deliberations unless requested by the members to assist them. The procedures require the Clerk to advise during the hearing, and (after the decision has been made) to write up the decision. It seems anomalous that the Clerk is excluded from the

deliberations as, in my experience of more than 26 years attending Tribunals, this is the time the lay members are most in need of advice.

The new procedures allow for lead cases to be identified (i.e. test cases) and other related appeals to be stayed. This procedure will be used for the arguments on office over-supply in Leeds. However, it does raise issues of which cases should be identified and how the costs of the hearing can be shared (or not) by the other appellants. Although the Valuation Tribunal is itself free from cost, the preparation of evidence, Expert Reports and a hearing are not free to the ratepayer. A related issue that needs to be considered is that Chartered Surveyors attending a hearing are now subject to the Code of Practice for Expert Witnesses. Part of that Code has been modified so that the Expert at a VT can still be remunerated on the basis of the outcome (Rateable Value reduction, or rate savings) of the hearing. However, that fee arrangement must be disclosed and could be prejudicial to the ratepayer if the Tribunal members fail to accept the independence of the Expert's opinion. This is creating pressure for a fixed, or time based, fee irrespective of the outcome.

There are other problems showing a lack of joined up thinking. For example, the Valuation Tribunal need only give two weeks' notice of a hearing in accordance with the regulations (although the procedure recommends more). The Valuation Office only needs to give two weeks' notice of evidence to be used from statutory forms. If a ratepayer intends to make a written submission, the procedural requirement is that this must be made two weeks prior to the hearing date. From a practical viewpoint, the fact that all three run on a two week minimum period means that the ratepayer may have to make a submission as soon as the Notice of Hearing is received and before having the opportunity to consider the Valuation Officer's evidence. Prior to the change to the appeal regulations, the Valuation Officer had to give three weeks' notice, and the Tribunal gave a minimum of four.

As I said at the outset, the fact that we now have a unified set of regulations for the whole of England is to be welcomed. However, there is a lack of joined up thinking, and a risk that the informality (and therefore relative cheapness) of hearings will be lost. We already have an appeal court at the Lands Tribunal which is economically beyond the reach of all but a select few. If the Valuation Tribunal becomes too formalised, most ratepayers will only be able to afford to go if they have no advice.

Colin Hunter
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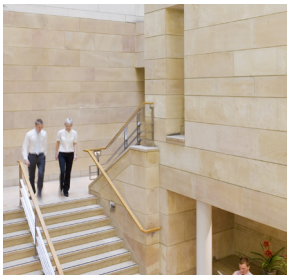
Section 17 Notices: A necessary evil?



As a commercial landlord, the prospect of a tenant becoming insolvent and failing to pay the rent is bleak, and landlords are increasingly looking to former tenants and guarantors to fulfil their obligations under authorised guarantee agreements ("AGAs") as a result. However, any landlord wishing to go down this route must comply with Section 17 of the Landlord and Tenant (Covenants) Act 1995, which provides a specific procedure for notifying former tenants of their obligation to pay.

Procedure

1. Identify previous tenants

For leases dated 1 January 1996 or later (known as "new leases"), the landlord can only request monies outstanding from the current tenant from the previous tenant and guarantor, if they signed an AGA before assignment to the current tenant. For old, pre-1996 leases, however, eligible Section 17 addressees can include all tenants and guarantors.

There is no restriction on how many of the qualifying previous tenants can be served with a Section 17 notice; the landlord is free to serve notices upon all qualifying previous tenants, or to focus its attention on those most likely to pay. However, the landlord cannot make a double recovery.

2. Calculate the amount to claim

Section 17 permits recovery of "fixed charges". This is a fairly wide definition, and includes rent as specified in the lease, service charges, and any other amount payable under a covenant of the lease as payment for the tenant's failure to observe the terms of the lease. Only sums falling due in the six months prior to service of the Section 17 notice can be reclaimed by the landlord, so it is imperative that the landlord acts quickly to recover unpaid rent.

3. Serve the notice

A Section 17 notice must be in the prescribed form, and served on the previous tenants/ guarantors. It is advisable to send two copies of the Section 17 notice, one by recorded delivery and one by first class post to every known address for the intended recipient.

Further complications

- A Section 17 notice only applies to the charges it claims, so a fresh notice must be served every time the landlord wishes to recover further sums as they fall due.
- A previous tenant/guarantor who makes full payment of the sums due under a Section 17 notice can call for an overriding lease of the premises which is then interposed between the landlord's interest and that of the current tenant. This is an issue that must be given careful consideration by the landlord when deciding which of the former tenants to serve with a Section 17 notice.

Despite these complications, however, the process remains relatively cheap and easy to complete, and in the current economic climate, landlords are increasingly finding Section 17 notices a necessary evil/blessing.

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Bridging the rental gap

The payment of interim rent bridges the rental gap during the period of holding over of an existing tenancy before the commencement of a renewal lease or the return of possession to the landlord. The Regulatory Reform (Business Tenancies) (England and Wales) Order 2003 ("2003 Order") introduced major changes to the law in relation to interim rent.

Who can apply?

Both landlords and tenants can now apply to the court for interim rent to be determined. In a rising market there is an incentive for landlords to make the application but in a falling market there is the opposite incentive for tenants to make an application as a reduction in the amount of rent payable may be achieved.

When will interim rent be payable from?

Interim rent is payable from the earliest date that could be specified in the Section 25 Notice or Section 26 Request, which is 6 months from the actual date of service.

When to apply?

Either party to a lease can make an application for interim rent at any time after the service of the Section 25 Notice or Section 26 Request. The 2003 Order also introduced a long stop date for interim rent applications, allowing retrospective applications to be made up to 6 months after the existing lease has come to an end, which will differ depending on whether the lease renewal is progressed with or without court proceedings.

How much interim rent is payable?

The amount of interim rent will be determined by the court, unless agreed between the parties.

In the vast majority of unopposed lease renewals of the whole premises (subject to satisfying certain conditions), the interim rent will be the same as the rent payable under the new lease. However, if there have been "substantial changes" in the rental market or the holding over period has been unduly protracted, either party can apply to have these factors taken into account by the court in setting the interim rent.

In all other cases the amount of interim rent will be calculated on a modified version of the old rules as an amount that is "reasonable for the tenant to pay". This will apply in a number of common cases including renewals of part, sub-let properties and where no new lease is granted. This approach involves a considerable degree of judicial discretion and is generally considered to result in the tenant paying an interim rent lower than market rent in most cases.

Tactics

The earliest date that interim rent can become payable is the day after the contractual termination date of the current lease. In order to maximise the interim rent period, the landlord's Section 25 Notice or the tenant's Section 26 Request should be served not less than 6 months before the contractual termination date of the tenancy.

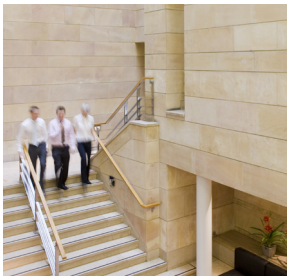
In the majority of unopposed renewal lease cases, the interim rent will be assessed at the same level as the rent payable under the new lease. For this reason, parties usually settle the interim rent as part of the lease renewal negotiations. Depending on market conditions this approach can have significant advantages. For example, a landlord faced with a falling market may seek to minimise its loss by agreeing the amount and period that the interim rent will be payable and incorporating those terms into the renewal lease.

If the negotiations for an unopposed lease renewal of the whole premises are becoming protracted or the terms of the new lease proposed by one party will substantially change the new lease, the landlord or the tenant could threaten to apply for those factors to be taken into account when setting the interim rent.

Conclusion

Interim rent is often viewed as a matter to be dealt with at the end of the lease renewal process. However, landlords, tenants and their advisers should consider the implications of interim rent at the outset of the renewal process.

Open all hours



Keep open clauses are a feature of many commercial leases, especially leases of retail development units, and are often a bone of contention for tenants who wish to close down their business. This article explores the remedies available for breach of a keep open clause.

What is a keep open clause?

Put simply, a keep open clause is a positive obligation on the tenant to use the premises for a specific purpose during set times. A successful keep open clause should set out clearly what the landlord expects of the tenant during its opening hours, whilst allowing the tenant sufficient flexibility to develop its business.

Is it enforceable?

Breach by the tenant of a keep open covenant may entitle the landlord to forfeit the lease and remove the tenant, however, in most cases this is precisely what the landlord wishes to avoid by enforcing the keep open provision.

The landlord may wish to attempt to enforce the keep open provision through a specific performance action in the courts. However, in *Co-operative Insurance Society Ltd v. Argyll Stores (Holdings) Limited*[1] it was decided that, other than in exceptional circumstances, injunctions will not be granted to enforce keep open clauses. The court's reasoning was that an injunction would require constant supervision by the court, would lead to further disputes surrounding the meaning of the clause, and could subject the tenant to far greater losses than the landlord would suffer by the closure of the shop.

Conversely, the position under Scots law as stated in the case of *Highland and Universal Properties Limited v. Safeway Properties Limited*[2] is that an injunction generally will be granted against a tenant who ceases to trade in breach of their keep open covenant.

In England the position remains that the only remedy generally available to the landlord is an award of damages.

What damages can be recovered?

The quantification of damages caused by a tenant's breach of its keep open covenant is not an exact science. The courts take a wide view of the heads of loss that can be recovered by landlords, and have awarded damages in relation to:

- The decrease in value of the landlord's interest as a result of the tenant's breach;
- Any other adverse effect on resale of the landlord's interest caused by the breach (for example, if the closure of the tenant's premises puts off a certain type of buyer that would be expected to pay a higher price for the landlord's interest);
- The effect of the tenant's breach on rent reviews of other units owned by the landlord;
- The knock-on effect of the tenant's breach on the viability of other units where, for example, the tenant is an anchor tenant whose presence would be expected to pull in passing trade to the development.

The landlord's loss is quantified as at the date of the hearing, so if the premises are re-let to a comparable tenant, that will be taken into account when quantifying the landlord's loss.

Are keep open clauses worth it?

Save in exceptional circumstances, keep open clauses in England and Wales will not be upheld by an order for specific performance. They are highly undesirable to tenants and the inclusion of such a clause will have a negative effect on the value of the lease. However, they may act as a deterrent to tenants who wish to close down their business, and can provide a way for landlords to recover losses suffered by the unexpected departure of a key tenant.

1 [1998] A.C. 1

2 2000 SC 297

Virtual Assignments – Clarence House Ltd v National Westminster Bank plc[1]

What is a virtual assignment?

A virtual assignment is an arrangement whereby a tenant transfers the economic obligations and benefits under a lease to a third party, but there is no actual assignment of a lease. Under such arrangement there is no change in occupancy but the rent is paid to the new appointee under the arrangement and the new appointee manages the property.

Such arrangements are often used when the lease contains covenants against assignment or parting with possession, which often require the consent of the Landlord. The benefits for a tenant of entering into a virtual assignment include: avoiding any delays in obtaining consent from the Landlord to assign and that the property will no longer appear on the company's balance sheet. On the other hand, Landlords tend not to like such arrangements, as they cannot control or monitor the covenant strength of any additional party.

Clarence House Ltd v National Westminster Bank plc

National Westminster Bank PLC (the "**Bank**") occupied a building under a lease with Clarence House Limited (the "**Landlord**"). The lease contained standard alienation provisions by which the Bank covenanted not do the following:

(a) underlet without consent;

(b) assign without consent;

(c) create a declaration of trust; and/or

(d) share or part with possession.

The Bank entered into a virtual assignment with New Liberty Property Holding Ltd ("**New Liberty**"). All the economic burdens of the Bank's leasehold interest were transferred to New Liberty and New Liberty were granted a power of attorney to act on the Bank's behalf. The Bank did not obtain the Landlord's consent to the arrangement. The Landlord sought a declaration from the court that by entering into the virtual assignment, the Bank had acted in breach of the terms of the alienation provision.

The High Court held that entry into a virtual assignment was a breach of the covenant to share or part with possession. The judge based his decision on the general definitions section of the Law and Property Act 1925 which defines possession widely as including "*receipt of rents and profits or the right to receive the same*".

The Bank appealed the High Court decision and the Court of Appeal held that the virtual assignment was not a breach of any covenants under the lease; in particular, that the covenant preventing sharing or parting with possession had not been breached.

In coming to its decision the Court of Appeal took a more restricted view of the meaning of possession. It held that New Liberty was never in legal possession of the premises, as it did not have the required factual possession and intention to possess. Additionally, the Bank had not wholly excluded itself from legal possession of the property. Physical possession was a requirement and the right to receive rents was in fact a contractual arrangement.

Conclusion

The Court of Appeal has given virtual assignments the green light by confirming that they do not affect the underlying legal relationship of Landlord and Tenant. Virtual assignments do not transfer any proprietary right or interest in the property whatsoever. Instead a virtual assignment only transfers the economic benefits and burdens of the lease. The decision by the Court of Appeal will be welcomed by many tenants who have used such arrangements. However, it may be the case that in the future, landlords seek to prevent such arrangements by adopting even stricter wording in alienation provisions in leases.

1 [2009] EVCA Civ 1311

Latin Quarter

Ad coelum et ad infernos

The complete phrase is "**cuius est solum, eius est usque ad coelum et ad infernos**", which means whoever owns the land owns it all the way up to the heavens and down to hell.

In other words, the owner of real property usually owns all the minerals beneath the land and the airspace above. He can sell the minerals separately or grant rights for their extraction and can build up into the airspace.

In fact, the ownership of the airspace extends only to such height as is necessary for the ordinary use and enjoyment of the land and the structures upon it. It is for this reason that an adjoining landowner swinging a crane in the airspace above a building will usually constitute trespass, whilst an aeroplane flying over will not.

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