Encouraging transactions with advice – Overage and other approaches

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1. **The approach to be adopted in this paper is deliberately different to normal. It is not an analysis of a specific legal point, subject or recent case. The aim of this paper is to explore whether in a time of recession it is possible for commercial property lawyers to give advice which encourages clients to sensibly enter transactions and to consider whether there are reasons for caution with regard to some natural responses to the recession.**

2. **The origins of this paper stemmed from the question whether it is possible during a recession to modify advice given as a property lawyer in a positive fashion?**

3. **It is very easy for the gloom caused by the recession in the property world to take a firm hold and to exclude any positive thoughts. It is clearly not possible to give advice which will override the economic and financial problems. Notwithstanding these problems is there advice which taking account of the difficulties may assist in bringing about or progressing transactions or cause them to be restructured.**

4. **This in turn raises two separate issues. First and importantly is there such advice. Second if there is such advice then how is it carried out and are there any warnings or caveats that apply.**

Overage

5. **One important rationale for overage is to encourage an owner of land to sell now whilst retaining a share in any future uplift in the value of the land sold. The owner may be torn between wanting or needing to realise capital from the sale of the land now and retaining the land so as to benefit from any expected future uplift in value. The present economic circumstances are likely to have increased the**

number of such conflicts and to have heightened their intensity. Currently owners of land may be suffering an increased requirement for cash whilst at the same time seeing even more clearly than usual that if they are able to hold on to their land it will in time significantly increase in value. The owner's conflict is even more acute than normal. The pressure to realise the land may be great but so also will be the understanding that in a few years time the price achievable for the land may be far in excess of current valuations.

6. **The role of overage in such circumstances is enhanced when times are hard. As a concept it provides a solution to bridge the gap between the owner's needs and aspirations. The bridge is a longer one in recession because the gap is wider. Overage enables capital to be realised now to fend off the financial pressures on the owner whilst retaining for the owner a share of the future uplift in value which is more likely to occur.**

7. **<u>Owners' perspective</u> –**

7.1 If due to financial circumstances the land owner is under some compulsion to sell then any overage is a bonus. Efforts should be made to seek to obtain it but whether it is possible will depend on the relative negotiating strengths of the parties. It is a not uncommon experience to find requests for overage by forced sellers to be refused because of their circumstances.

7.2 If the owner is in two minds as to whether to sell then overage may be the factor which persuades him to sell and but for the overage the owner would grit his teeth and ride out the recession. The degree of persuasion is far more forceful in a recession because the expectation of value in the overage is that much greater.

7.3 If the owner decides to go down this route in such financial circumstances it increases the onus on the owner's solicitor to ensure a viable and secured overage regime. In ordinary times the overage will often just be the icing on the cake. It is more likely now that the sale would probably not take place but for the inclusion of the overage so if the purchaser

circumvents the operation of the overage provisions or manages to reduce the amount of the overage payment the owner will be looking to recoup from his solicitor.

8. <u>Purchaser's perspective</u> –

8.1 in a recession the offer of an overage may be the inducement which causes an owner to sell. With prices low without such a provision an owner may take the view that the land should be retained until such time as values improve. Overage provides an alternative which enables the argument to be put that the land can be freed up for use or development but with the prospect that the owner can benefit from any uplift. It gives prospective purchaser a strong counter-argument to the impact of the recession on current and short term land values.

8.2 It is reasonable to expect that over a period there will be an increase in value as the country comes out of recession. There is no reason in principle why a land owner should not sell now but still share in that improvement through overage.

9. <u>Course of negotiations</u>

9.1 In times of increasing values there was a tendency for owners to require overage without having thought through what exactly was wanted. There was then the danger that the negotiations relating to the overage could become out of proportion to the negotiations as a whole and distort the whole process. This was never desirable but it is even less so now. It is important that sufficient thought should have been given to the structure and nature of the overage that is to be required and that thought should have been at an early enough stage so that the introduction of the overage does not disrupt the negotiations.

9.2 Standard form provisions are often a solution for conveyancing forms but with overage that is much more difficult. There is a greater tendency than with other property rights and interests for the particular set of provisions to have to be drafted especially for the particular sale and purchase. To try and address the issue of certainty regarding the substance of the overage regime as a first step

it may be helpful to have an overage checklist which has been gone through at an early stage so that the client has an understanding as to what needs to be covered in order to create the particular overage regime. A link to a copy of a basic checklist is included on the website.

10. Drafting

10.1 Triggers - In normal times there are a variety of events which can act as a trigger for the payment of overage. Usually it is linked to an event which will result in an uplift in value such as the grant of planning permission or the implementation of a development project. However, with the recession the question arises whether other possibilities could be added which would increase the encouragement to the owner to sell. For example, a specified increase in a defined index could be a trigger.

10.2 Overage Formula - Should there be a guaranteed future amount or alternatively triggers which include a valuation by reference to a particular index so that even if there is no "uplifting" event there is still a payment. Should elements in the overage formula be amended to allow for recession? For instance, if the overage is calculated by reference to the increase in value attributable to a planning gain should the Base figure be link to an index of house prices?

10.3 Deferment - Instead of the overage being determined as at the trigger date it may be that the person entitled to the overage should have a right to defer the date by reference to which the overage is calculated. This would mean that if the trigger event occurs during the recession it is possible for the determination of the overage sun to be delayed to a later date but still taking into account the effect on the land value of the trigger event. By then the recession may have lifted. Such a power of deferment could have implications as regards the continuing protection for the overage particularly if there is a desire or need to realise the land in the meantime. In the event of the exercise of such a power alternative protection for the overage may be needed. This could be provided from the proceeds of the realisation. In the event that there is a deferment should some advance be made in favour of the person entitled to the overage.

10.4 Realisation – should the person entitled to the overage have some say in the realisation of the land and should the purchaser undertake more onerous obligations with regard to the obtaining of planning permission or whatever event is to trigger the overage payment. This would not be normal with an overage agreement but may be required when the overage arrangement takes on greater significance. Alternatively, instead of straight purchases with an overage it may be more appropriate to enter arrangements involving planning promotion agreements. Under these the owner retains the land and the other party agrees to promote the land for planning purposes (as to which see section 15 below).

11 Caution – it is not appropriate in this paper to consider in detail the structuring of overage arrangements. The focus of the paper is not on the detail of overage. However, it has to be borne in mind that although overage is a valuable tool particularly in times of recession there are concerns which have to be borne in mind. The need to ensure that the overage regime is effective and secured is greater and as the rights are hybrids will require greater thought than with more straightforward conveyancing transactions relating to recognised rights and interests in land. The concerns are that:-

11.1 Overage arrangements nearly always involve complicated drafting. It is rare that the drafting can merely replicate previous drafts.

11.2 Great care needs to be taken with the formulation of the overage sum. It is an area in which real problems have occurred and been litigated over. The decision in Chartbrook v Persimmon Homes Limited [2009] UKHL 38 is a prime illustration as to how such problems arise and the cost involved. If possible there is advantage in including worked examples to illustrate how the formula is understood to operate.

11.3 Securing the protection of the overage is not simple and straightforward and needs to be addressed. It is easy to create an overage which can be defeated by a simple

transfer as in Akasuc Enterprise Limited v Farmar & Shirreff [2003] EWHC 1275 (Ch).

11.4 The duration of the arrangement raises particular issues allied with the question whether there is to be a single trigger or multiple triggers. The longer the duration of the arrangement the greater the chance there is of an unexpected event. It is impossible to draft an arrangement which covers every eventuality.

12. <u>Reverse overage</u> –

12.1 What if it is the prospective purchaser rather than the owner who is in two minds? Such a person may want the property but be concerned that the property market or the value of this property may go down further. The owner may be very keen to sell for whatever reason. The fear of further reductions in value may be preventing the prospective purchaser from taking the plunge. Instead of the purchaser agreeing to pay additional consideration on the occurrence of specified circumstances it is open to the vendor to agree to return part of the price if there is a fall in values within a specified period. It would remove some of the fear for the purchaser.

12.2 By way of example, a new residential estate has been completed by a developer but sales of the new houses are being held back because there is a concern that prices may go even lower over the next year or so. To meet this fear the developer agrees within any purchaser that in the event that a specified index of house prices is lower on, say, the later of a specified anniversary of the completion and a subsequent completion of a bona fide arm's length sale by the purchaser then an amount will be repaid to the purchaser. Alternatively, it could only be repayable if there is a sale after a specified period. To qualify the sale may have to be no earlier than a specified date. The amount could be determined by reference to the fall in the index. The idea would be to provide a safety net for the purchaser which would in turn benefit any financier of the purchase. The "reverse overage" would be charged along with the property and so the mortgagee would have some protection against any fall in value.

12.3 Clearly the vendor would wish to protect itself against having to pay reverse overage. This could perhaps be achieved by insurance although this could run the risk of creating a new "sub-prime" type problem. In some circumstances it may be appropriate to provide for a call option exercisable by the vendor at the original purchase price less an amount as credit for the benefit of the occupation of the land by the original purchaser.

12.4 It would have to be borne in mind that unlike ordinary overage the obligation to pay the reverse overage could not be secured on the subject matter of the sale. In some cases a put option exercisable by the purchaser against the vendor could provide additional protection

12.5 The fiscal consequences could be unusual and require very careful consideration.

13. <u>Market in overage rights</u> - When I first started in practice in the mid 1970s there was a strong and recognised market in trust interests. Sales and mortgages of these interests were conducted through Foster and Cranfield. Specialist advice was needed and titles were deduced in much the same way as for unregistered land. Since then I imagine the number of such transactions has reduced greatly although the market still operates. A new market has grown up dealing with life policies. There are funds which have developed just to hold such policies. Now that overage has been a recognised concept for some time it seems to me that such a market could also be established in relation to overage rights. There must be a significant volume of such rights in existence now. With the recession now could be a good time to acquire such rights subject to consideration of their terms and the ability to assign the rights.

14. <u>Overage Audit</u> - apart from the possibilities of sales to third parties now would be a good time for an audit of such rights by companies that have purchased land and agreed to overage arrangements. If the finance is available then securing the release of those rights by purchase would be a worthwhile long term course of action by the original purchaser if still liable to pay it or any successor who has

taken over the liability. The fall in the value of land would affect such overage rights if the overage is linked to the value of land. Even if it is linked to other matters there is the possibility that the value of the rights will have fallen and so it will be attractive to buy the rights in. However, care will have to be taken in the negotiations to avoid breach of any duty of good faith that may be implied (Ross River v Cambridge FC [2007] EWHC 2115 (Ch) and see article on intervention of equity in property transactions to which there is a link on the website).

15. **<u>Planning Promotion agreements</u> – an alternative to a straight overage arrangement is a planning promotion agreement. The possible returns for the promotion of the land are varied and the possibilities are limited only by the boundaries of the advisers' ingenuity. In a recession it has some of the advantages of an overage agreement in that it ensures that the landowner will receive a benefit from any increase in value. The main difference is that the landowner does not transfer the land but retains it whilst the promoter seeks to obtain planning permission. In consequence the landowner retains far greater control over the realisation of the land as and when planning permission is obtained. The attraction to the landowner of this in a recession is very strong. It means that progress can be made with improving the value of the land during the recession with the expectation that land values will have improved by the time that the land is sold and the gain realised. On the other hand it means that the landowner does not as with an overage arrangement receive the current value of the land on entry into the contract.**

16. **There is no single template for such an agreement and the degree of involvement of the promoter with the land can vary considerably. At one end of the spectrum would be an agreement under which the promoter receives a simple fee whilst at the other would be a conditional sale. In some cases instead of a fixed fee being payable the fee is related to a proportion of the increase in value resulting from the grant of planning permission. In others the promoter's position can be closer to that of a tenant in common in that the landowner is obliged to sell the land with planning permission and to share a proportion of the proceeds of sale with the promoter. The promoter may even have an option in certain**

circumstances to purchase the land or to develop the land jointly with the landowner. In the present climate the obtaining of a planning permission may not be enough and thought would have to be given as to how to realise the value of the land with planning permission once the grant has been obtained.

17. **With any such agreement that involves anything more than just a straight fee to the promoter the manner in which the land and the planning gain are realised will be important. The agreement may leave ultimate control over realisation with the landowner or require agreement by both and in the event of failure to agree provide for a decision by an independent expert or even pass control to the promoter. Whichever approach is adopted it may be necessary now to draft the terms covering realisation to take account of the recession. The landowner may want to provide for the possibility that planning permission is obtained but the recession has still not run its course. An absolute right to defer any sale for a specified period with a cap on the maximum period of deferment would be the best solution from the landowner's point of view. In contrast the promoter may not want a deferment and so will be looking to restrict the landowner's ability to defer. One method would be to have an automatic cut off of any deferment once a specified property index went above a stated level. Alternatively, it may be the promoter who wants to defer the operation of the agreement if, for example, there is other land involved and it needs to reach a certain stage in the planning process or the promoter wants to have another go at an improved planning permission.**

18. **<u>Enforceability</u> - Care has to be taken on behalf of the promoter with the drafting of such agreements if they do not provide for the payment of a simple fee to the promoter. There must be a focus on ensuring that enforceable obligations are created in favour of the promoter. The risk is that the provisions relating to the realisation of the land triggering a sharing of the proceeds with the promoter will be agreements to agree and thus not enforceable. The provisions relating to realisation, valuation and deferment may become so intricate that at the core of the arrangement there is no ability to enforce a sale or payment. The importance of this**

point is emphasised by the recent House of Lords decision in Yeoman's Row Management Limited v Crabbe [2008] UKHL 55 holding that "gentleman's agreements" are not enforceable by the application of the doctrine of proprietary estoppel. It is why the inclusion of the fall back of an option to purchase at the open market value in favour of the promoter or such person as is nominated by the promoter is always a comfort.

19. **<u>Good faith</u> - the participants in such an agreement must be fully aware that the relationship imposes an obligation of good faith on all involved. This can give rise to difficult issues regarding matters such as disclosure. These are considered in an article to which there is a link on the website. It is crucially important that they are borne in mind. This is true if the agreement only involves the land which is the subject to the agreement. If it is part of a larger jigsaw involving the assembly of a site the scope for conflict between the promoter's personal interest and duty of good faith is significantly increased.**

<u>Increased Deposits</u>

20. **One initial response to the recession has been for vendors to increase the size of deposits above the norm of either 10% or a smaller sum combined with the right to require a top up to 10%. I have seen contracts requiring deposits of 20% or more and suspect that will have been other amounts stipulated in excess of 10%. This trend relates particularly to the time when the market was turning and serious worries of default were beginning to arise. It is a natural response on the part of the vendor particularly if a special purchase vehicle is being used for the purchase. However, there is a serious risk attached to such a course.**

21. **<u>Penalty</u> – the concern is that it will be argued that any deposit exceeding 10% is a penalty and so can not be forfeited by the vendor but must be repaid. This is an argument which has not been used as often as it might be. In Omar v El-Wakil [2001] EWCA Civ 1090 which concerned the Court's jurisdiction under s.49 LPA 1925 to order the return of a deposit the Court of Appeal had to consider a deposit which was about 31% of the purchase price but all**

that was said in the judgments was that no argument had been put forward that the deposit was a penalty but no reason was given for this.

22. **Workers Trust & Merchant Bank Limited v Dojap Investments Limited [1993] AC 573 – in this Privy Council decision it was held that a deposit of 25% was a penalty in a sale by a mortgagee bank at auction. Lord Browne-Wilkinson stated that to be a true deposit the sum had to be genuine earnest money and that by long custom in this country and Jamaica a deposit was not more than 10%. This was not an absolute upper limit and if there are special circumstances that could justify an increased amount then that would not be a penalty. In that case the vendor's argument placed reliance in part on a general increase in the amount of deposits upon the introduction of a transfer tax ultimately payable by the vendor but initially paid by the purchaser and in part on a general practice by banks selling at auction. Neither argument was successful. It was said that no class of purchaser could avoid the consequences of the law and the justification of special circumstances had to be determined on an objective test. The treatment of the deposit as a penalty has been disputed. In Amble Assets Limited v Longbenton Foods Limited (in administration) [2011] EWHC 1943 (Ch) Mr. Andrew Sutcliffe QC considered a deposit to be subject to the forfeiture rules and so the court has to determine how much of the deposit it is unconscionable for the vendor to retain. It may be that in practice this will not result in a very much different final outcome. This different approach has not found favour (see, for example, Lewison J. in Ng v Ashley King (Developments) Limited [2010] EWHC 456 para. 22)**

23. **In the Jamaican Court of Appeal it had been held that the excess over 10% should be repaid but that the vendor could retain an amount equal to 10% of the purchase price. In the Privy Council this was set aside and it was held that the whole amount was a penalty and was repayable with interest. In consequence the vendor was deprived of the benefit of any part of the sum stated to be paid by way of deposit.**

24. **Set off - The risk, however, is not the inevitable loss of the full amount of the payment. Lord Browne-Wilkinson held that the vendor can set off against the repayment of the penalty such amount as is the actual loss suffered by the vendor as a result of**

the failure of the purchaser to complete (applying Commissioner of Public Works v Hills [1906] AC 368). In that case the amount was likely to be small so that an enquiry as to the loss was ordered but the full amount of the 25% sum was ordered to be repaid together with interest without awaiting the outcome of the enquiry. This ability to set off the loss means that the argument that the deposit is a penalty may in some circumstances lose its potency particularly when losses are great as in a turning market. The vendor will recoup the losses from the amount deposited even if held to be a penalty. If the losses exceed the penalty then there will be no amount to be repaid by the vendor and in practice the penalty will have operated as a deposit. But this argument will be a real concern when the market has turned and prices are no longer falling as then the losses may not exceed the deposit and the vendor will have to face the prospect of making a repayment together with interest.

25. <u>Counter-arguments</u> - If faced with a dispute as to whether a payment by way of a deposit is a penalty or is capable of being forfeited the following arguments should be borne in mind:

25.1 Whether or not the onset of the recession constitutes special circumstances is an issue which is likely to arise in many legal disputes in the next few years. It will be interesting to see how the Courts respond to such an argument in the context of deposits exceeding 10%.

25.2 The Privy Council's decision in Workers Trust & Merchant Bank expressly left open whether instalments of the purchase price as opposed to a deposit could be validly forfeited. In Stockloser v Johnson [1954] 1 QB 476 the Court of Appeal held that a vendor of quarry equipment was entitled to forfeit the instalments that had been paid prior to default by the purchaser and that this was not a penalty. Although obiter by a majority of 2 to 1 it was considered that relief against forfeiture could be awarded by the Court in such circumstances.

25.3 The contract for the sale and purchase of the property may be linked with another contract such as a contract for the sale of a business carried on upon the premises. In such circumstances the contracts may be regarded as a single arrangement and as such the terms of the whole arrangement can be taken into

account to determine whether the deposit is a penalty. This approach was adopted by the Court of Appeal in Omar v El-Wahil supra albeit not in the context of a penalty argument.

26. <u>Negotiating increased protection</u> - To reduce the risk of the whole deposit being a penalty when an increased deposit is required the spreading of the payment may mean that the initial payment of 10% will be a genuine deposit and not subject to challenge. The further payment or payments could be instalments of the purchase price which would raise the argument discussed in para. 25.2 above. This is a risky approach to adopt.

27. In such cases where there is obviously particular concern regarding default consideration should be given to requiring guarantees to support the purchaser's obligations. Care will need to be taken to ensure that the guarantee provides the protection needed. As with the sale contract any guarantee must be in writing. If there is to be an obligation to bolster the guarantee with security then care needs to be taken to ensure that it provides effective security. Such an obligation really needs to be linked to a specific property rather than a general obligation to provide security.

28. <u>Deposit schemes</u> – the Australian government operates a scheme which it is said is successful. First time buyers save for a deposit under the scheme and the government also makes a contribution so as to boost the size of the deposit. Such a scheme could alternatively be set up by a housebuilder or more generally by a housebuilders association or group of housebuilders. I am not aware of such schemes already being operated. Most incentives from housebuilders are available to purchasers. Deposits are, for example, lent by the builder. Whereas with this scheme it starts at an earlier stage when the first time buyer is saving for a house which has not yet been selected.

29. In the case of a scheme operated for a single housebuilder it would be linked to sales of houses built by that company. With a more general scheme it would presumably be linked to those involved but the contribution to top up the savings would come from the builder of the house to be purchased. It would require the involvement of a financial institution in order to satisfy the

requirements of the FSA and the Financial Services Act. A building society would be the most appropriate.

Second charges

30. I have experienced an increase in questions with regard to second mortgages and suspect that this means that there has been an attempted increase in such borrowing. The change in attitude by lenders caused by the onset of the recession has resulted in an increase in fees and costs so that additional borrowing from the first chargee has become prohibitively expensive in some cases. It has resulted in owners seeking to raise funds from other sources which inn turn as led to an increase in second charges.

31. If the first chargee consents then there should be no problem. The second charge can be registered and issues such as enforcement by the second charge and confirming the priority of the first charge can be dealt with by agreement between the two chargees. An objection by the first chargee to the second chargee having the ability to sell the charged property could seriously reduce the protection of the second charge.

32. However, the borrower may not want to approach the first chargee for consent. The restriction on title in favour of the first chargee will then be a barrier to registration of the second charge. Without such registration the second charge will remain enforceable as an equitable charge but the chargee will not be able to deal with the legal title. It will need to be protected by a unilateral notice but this will not protect against a prior equitable charge or interest. It will provide some security but it will not be anywhere near as complete as with a registered second charge.

33. Clog on the equity of redemption – one response to the problem of a first chargee's restriction may be to try and reformulate the borrowing as a different transaction. Then great care has to be taken to ensure that the transaction is not tainted with a clog.

Leases

34. In the context of this paper the consideration of the impact of the recession on landlords and tenants arises in at least two

respects. One is encouraging the grant of new leases and the other is the renegotiation of the terms of existing leases so as to retain for the landlord existing lessees and continued payment of the rent. Similar factors will be in play with both areas. With renegotiations there will be in addition be the need to take care in ensuring that the changes are properly structured, marry in with the continuing terms and do not give rise to unexpected or unacceptable tax liabilities.

35. Audits - the impact of the recession will mean that it is even more important that both landlords and tenants carry out an audit of their leases so that there is a clear understanding of their respective obligations and the extent to which they have been complied with. For example, if there is a break clause then it will be important to both sides to understand what is the position as regards compliance (particularly regarding dilapidations) and whether the tenant is able to exercise such right.

36. Negotiating factors – this section seeks to consider some of the factors will be influential in the recession.

36.1 Rent/Rent reviews – both landlords and tenants may be requiring greater certainty with rents which may mean that more involved rent review clauses are needed. Greater use may be made of reviews by reference to indexes. Instead of just using the Retail Price Index alternative forms of index may be used. The reviewed rent instead of being determined by reference to one method of determination may be prescribed in the alternative with, say, open market rent or if greater an indexed rent. The tenant may seek the imposition of a cap on the extent to which the reviewed rent may increase. On the other hand the landlord may want an assured minimum increase in rent.

36.2 Upwards only rent reviews will be a target for change. Such provisions were criticised by the Governor of the Bank of England as "being designed for a world which has the certainty of upwards-only property values. This pattern is not in the interest of the economy as a whole, and the thrust of our anti-inflationary policy is intended to make it obsolete". The Governor was Robin Leigh-Pemberton and the statement was made in 1993.

36.3 If any such changes are made to an existing lease then the knock on effect as regards the restrictions relating to underleases will need to be considered and in a particular any requirements as to the rent to be obtained by the underlease.

36.4 Duration – break clauses will be far more attractive to lessees who are uncertain as to the future. Such caution on the part of the tenant may be difficult to argue against but if conceded it will be important to guard against the break clause being used not to terminate early the tenant's liabilities upon vacation of the premises but to allow the tenant to exercise the break clause without vacating as a means of applying pressure for renegotiated terms beneficial to the tenant. The impact of the inclusion of such a break clause on any rent reviews during the life of the lease will need to be considered. Initially it could increase the rent determined.

36.5 There is likely to be an increase in the number of exercises of such break clauses. As mentioned above it will be important to understand the precise terms of the clause and what conditions have to be satisfied by the tenant and whether it can comply with such conditions. Often the issue will be whether there has been material compliance with the lessee's obligations and it is important from the tenant's point of view to ensure that compliance does not have to be absolute (Fitzroy House Epworth Street (No. 1) Limited and another v The Financial Times Limited [2006] 1 EGLR 19).

36.6 Green leases – these developed first in Australia and involve a commitment on the part of both landlord and tenant to the proper energy management of the demised premises and to achieve efficiency targets in respect of the premises. There are standard schedules available in Australia and an example of one is to be found at the end of this paper. A quick glance through this schedule will show the scope of the objectives and the detail gone into. The introduction in this country of Energy Performance Certificates ("EPCs") for commercial premises will add impetus to the use of green leases. I notice from the property magazines that it is said that some "light green" leases have been entered into in this country.

36.7 Such leases fit well with the new environmental obligations being imposed. For example, company directors are required by

section 172 Companies Act 2006 to have regard "to the impact of the company's operations on the community and the environment".

36.8 With properties which lend themselves to efficient energy management such leases may be an attraction to a tenant as it may result in both costs savings for the tenant and a very obvious discharge of environmental obligations which can be publicised. On the other hand with premises which are not so suitable such leases may give rise to problems as they impose obligations on the lessee which could be unexpectedly expensive and as regards the landlord could have the adverse consequence of reducing rents on a rent review because of the increased burden on the tenant. The ability to alter the premises will need o take account of the sustainability principles.

36.9 The introduction of EPC's may be an added reason in the recession for renegotiating an existing lease so as to avoid the grant of a new lease and thus the need to incur the cost of obtaining a EPC in respect of the premises before the grant. Further the EPC will impose an additional burden which could affect the rent achieved as compared to the rent under the existing lease.

36.10 <u>Service charges</u> – requests for caps on the amount payable by the tenant may be more frequent.

37 <u>Renegotiation</u> – there may be strong practical reasons for a renegotiation of the terms of a lease so as to ensure that the lessee continues in occupation paying a rent. This will be preferable to the premises becoming vacant and the landlord becoming liable to pay business rates. It may also be preferable to the landlord having to incur fresh expenditure such as on obtaining EPCs. The manner in which effect is given to the variations renegotiated needs to be thought through.

38. <u>Deeds of Variation</u> - I have noted a tendency for proposals for changes in lease structures to involve the use of ordinary deeds of variations rather than surrenders. This is particularly in case involving a reshuffling of premises with, say, a reduction in areas demised or the amalgamation of demised premises. The use of such deeds is not appropriate if there is to be an addition to the

premises subject to the lease or an increase in the term of the lease. A deed effecting such changes will as a matter of law be a surrender and regrant.

39. This is a point that in my experience the Stamp Office is very quick to highlight in responses to requests for COP 10 rulings. A surrender and regrant will have consequences for stamp duty land tax. It is an exchange for the purposes of that tax. This will be mitigated by para. 16 Sch 17A FA 2003 if the same parties are involved with both the surrender and the regrant even if the premises are different. But it will not be a complete exemption and so when the changes are more complex there will be the risk of additional consideration which will be chargeable to sdlt. If the original grant of the surrendered lease was subject to stamp duty then the overlap relief in para. 9 Sch. 17A FA 2003 may also be available on the surrender and regrant.

40. <u>Partial Surrender</u> - A variation which involves the reduction of the area of premises subject to a lease is one step that has been occurring more often as tenants seek to reduce the extent of their liabilities. The partial surrender of premises will not be a surrender and regrant of the remainder which is important for the purposes of sdlt. It is preferable that this is effected by a surrender of part rather than a deed of variation.

41. If dealing with an "old tenancy" granted before 1st January 1996 for the purposes of the Landlord and Tenant (Covenants) Act 1995 a surrender and regrant will result in a "new tenancy" and the ability to enforce the tenant's covenant against the original tenant unless still the tenant will have been lost.

42. <u>Reversionary</u> leases - With a proposed increase in the length of a term there are two ways in which this can be achieved. There can be a surrender of the current lease and the regrant of the longer term. Alternatively the existing lease can be left in place and the landlord can grant a new reversionary lease to take effect immediately upon the expiry of the current lease provided that the reversionary lease will take effect within 21 years of the grant. Such a course may reduce the tax bill. Considerable care needs to be exercised so as to ensure that

42.1 the two leases cannot pass into different ownerships;

42.2 both will terminate on the forfeiture of the current lease;

42.3 any guarantees extend to the reversionary lease;

42.4 the rent review clauses and other provisions (such as reinstatement on termination) are appropriate.

42.5 the consequence of any alterations as regards reinstatement and rent reviews have been thought through.

43. <u>Shared ownership</u> – there has been some take up for shared ownership arrangements with local authorities as the landlord. In times of recession there is an attraction for tenants who do not want or are unable to make a complete commitment to a 100% purchase. The sample leases provided by the Housing Corporation are an aid. However, the terms of such leases are extremely complicated particularly with the staircasing provisions and there is plenty of scope for future disputes. There is also the problem posed by mortgages and the special provisions that have to be included for them.

44. This type of lease is an example of how in a recession transactions may need to be restructured so as to apportion beneficial ownership and risk in a different manner. This may involve a greater use of joint ventures, put and call options and charges.