

OVERAGE

1. Concept

1.1 Overage is in principle a simple concept. The principal objective can be easily grasped particularly by the landowner. A single sentence towards the end of the Heads of Terms stating that there will be an overage arrangement with an agreed percentage will illicit a warm glow of satisfaction in the vendor but a sense of gloom in the solicitors acting for the vendor and purchaser. The giving of the instruction is far simpler than the implementation. When negotiating a sale of land a disproportionate amount of time can be spent on the intricacies of the portion of the documentation relating to the overage arrangement. The reason for this is that the concept does not slot into such a transaction in the same way as a traditional property right. There may be a need to negotiate over the precise terms of an easement or restrictive covenant but the manner in which they are included will be well known and easily accepted. Overage on the other hand is a hybrid which needs careful thought on both sides as to how it is formulated and protected. It can result in substantial rewards for the vendor, substantial liabilities for the purchaser and painful headaches for the lawyers.

1.2 Under the overage arrangement the landowner is to sell land and in addition to the immediate purchase price is to receive further payments in the event that by whatever means there is an uplift in the value of the land during the overage period. Normally this uplift will result from the grant of planning permission or the carrying out of a development. Mr. Justice Robert Walker (as he then was) stated that

"Overage means simply a deferred payment agreed to be made, in addition to the basic purchase price, the amount of the additional payment (if any) being determined by a formula which depends on unpredictable future events."¹

1.3 Overage plays an important role in land transactions. It is a means by which landowners can be persuaded to sell land when they believe that the future value of the land may soar but do not themselves have the expertise to achieve such an increase in value. The owner of land may often

¹ Titanic Investments v Macfarlanes 27th June 1997

be caught between two conflicting desires. On the one hand he may wish or need to sell the land and realise the current value. On the other he may be reluctant to do so because of a belief that at some stage in the future the land's value will significantly increase due to an event such as the grant of planning permission for a more valuable user or an improved planning permission allowing, for example, more dwellings to be constructed on the land. Provisions for overage help the owner overcome these conflicting pressures and enable land to be sold that might otherwise be retained. Additionally, it may be the route by which the landowner can be persuaded to sell to those who unlike the vendor have the ability to achieve the hoped for increase in the value of the land.

1.4 The structuring and drafting of such a mechanism is far from simple. Often the arrangement is to continue in force for a substantial period and the full implications will not have been thought through by the person giving the instructions. Attempting to anticipate and cover all future eventualities is a headache. There is no simple formulation which will suit all cases and no sure-fire method which will guarantee that the overage obligation will continue in all circumstances to be enforceable as intended.

1.5 The vendor will want to be assured on a number of aspects. In particular the vendor will want assurance that come what may the further amount will be paid on the occurrence of the appropriate circumstances. This means not just that the formula adopted results in the intended full amount of overage being achieved but that the right to overage will not be defeated by any steps taken by the purchaser or any successor-in-title. This requires that the provision be properly protected so that there is someone (whether the original purchaser or a successor) against whom the obligation can be enforced. Careful consideration will also be needed to be given to the fiscal implications for the vendor.

1.6 In contrast the purchaser will want to prevent the overage provision unnecessarily reducing the value of the purchased land, cluttering the title, hindering the raising of finance and preventing sales off following the start of a development. The purchaser if a developer will usually be determined to avoid entering into an open-ended liability. In particular the developer will not want any nasty surprises as occurred in *Chartbrook v Persimmon*². The existence of overage provisions can be a very considerable burden particularly if the arrangement is to last for a substantial period.

2. Legal Quandary

² [2009] UKHL 38

2.1 There is a basic legal problem facing overage arrangements which cannot be avoided. At the heart of any overage arrangement is an obligation to pay the overage which is positive and not negative in character. As a matter of law positive covenants are not enforceable against successors of the covenantor in the same manner as, say, restrictive covenants or easements. They do not run with the land and do not enure against third parties. The House of Lords in Rhone Trusts v Stephens³ firmly shut the door against any such suggestion.

2.2 It means that an obligation to pay overage will not automatically be enforceable against a person deriving title to land through the covenantor. The right to an overage payment has no separate legal identity other than that it is a chose in action - the right to enforce the covenant. Unlike a restrictive covenant it has no recognition in the context of land law as an independent and enduring interest. This presents not just a legal hurdle but also a practical one because it is difficult for a client to appreciate that such a hurdle exists.

2.3 To ensure that the overage obligation is enforceable against successors to the covenantor it will be necessary to put in place a structure which allies the overage right with an interest which is enforceable not just against the covenantor but also against third parties (as to which see the discussion in section 7 below).

3. Alternative types of agreement

3.1 The first issue to be addressed is the format of the overage agreement to be drafted. In most cases the landowner will want to realise an immediate sum whilst retaining the ability to receive a sum or sums in the future but having no involvement or responsibility for the future. In such circumstances there is really no alternative but for there to be a straight sale with a covenant for overage to be paid. The overage covenant will normally need to be protected. If the land owner can wait for payment then a conditional sale or option will be preferable.

3.2 However, in some cases and it is an increasing trend the landowner wishes to retain a degree of control possibly even ownership. Joint ventures involving the landowner and a builder or property developer are one possibility. This will often involve the land being put into a company or the title to the property being held by a company as a bare trustee for the parties

³ [1994] 2 AC 310

in the joint venture. Such arrangements raise their own problems as regards tax and the type of protection that is built into the arrangement. It also means that there is shared ownership and control. Unless there is an express ability to recover the land from the joint venture the original landowner will have given up exclusive ownership.

3.3 In some cases the landowner does not want to pass across any direct interest in the land until the stage has been reached at which the full value of the land is capable of being realised following the grant of a planning permission. Until such time is reached the landowner wishes to retain possession and enjoyment of the land. A conditional sale or an option are not acceptable to the landowner. However, the landowner does not have the ability or possibly finance to achieve the uplift in value and needs the involvement of a person with the necessary skills, finance and commitment to successfully obtain a valuable planning permission. One option in such circumstances for the landowner is to enter an agreement under which the land is retained by the landowner whilst the other party applies for planning permission. Once planning permission has been granted then the land is sold and the proceeds divided in a manner agreed by the contract. The other party never acquires the land and bears the risk that the costs of obtaining planning permission are wasted. If no planning permission is granted then the ownership of the land continues as before and the other party has no continuing interest in the land.

4. Traps

4.1 Before becoming occupied with the drafting of such an overage arrangement it is sensible to pause and consider the issues that have come before the Courts in respect of such arrangements. There is an advantage to be gained from knowing the problems areas. There had been very little judicial consideration of overage arrangements before the 1990s. It is striking when advising now on overage arrangements from the 1980s how simple and unsophisticated they are. Often they completely fail to cover the problem areas now elaborately addressed.

4.2 Even now there is not a substantial and coherent body of judgments concerning such arrangements. However, what has become apparent is that there are a growing number of cases involving disputes over the manner in which the particular overage arrangement is claimed to operate. In some the overage arrangement has been shown to be defective and in others there is a clear difference between the parties as to what was intended to happen. Often the dispute has moved on to the next stage and the

issue is whether there has been professional negligence in the preparation of the overage arrangement.

4.3 The increasing use of overage arrangements combined with the dramatic rise in land values and the ever-growing complexity of commercial property transactions mean that it is likely that this trend will accelerate. A consideration of the problems that have been litigated highlights the problem areas and serves to emphasise those areas in which measures need particularly to be taken to avoid such problems.

4.4 The areas that have been the subject of judicial consideration are not surprisingly those which cause the greatest concern when formulating a structure for the overage arrangement and drafting the documentation. For the commercial property lawyer there will be no great surprises on a quick read through the list rather a knowing groan of recognition. This list may assist in providing a reminder of the known problem areas but a consideration of the judgments will not provide a clear overview of the operation of overage. Each case grapples with the particular problem raised in that case. A more general picture only arises in the case concerning the proper means of protecting the overage right against third parties (para. 4.5.10 below)

4.5 These problem areas that have been judicially considered are:

4.5.1 Overage Formula – Chartbrook Limited v Persimmon Homes Limited⁴ which was a battle to the House of Lords over different constructions of formula for Additional Residential Payment which meant parties £3.7 million apart;

4.5.2 Adjustment formula if change in number of flats – George Wimpey UK Limited v VI Components Limited⁵ concerning a battle over a failure to include amount for enhancements in calculation of overage;

4.5.3 Car parking rights - Bride Hall Estates Limited v St. George North London Limited⁶ in which the issue was whether the full purchase price for a flat and car parking space should be apportioned before overage calculated;

⁴ [2009] UKHL 38

⁵ [2005] EWCA Civ 77

⁶ John McDonnell Q.C. at first instance ([2003] EWHC 927) upheld by the Court of Appeal ([2004] EWCA Civ 141).

- 4.5.4 Costs of release of restrictive covenants – Anglo Continental Educational Group (GB) Limited v Capital Homes (Southern) Limited in which protracted litigation it was held by the Court of Appeal that waiver of a planning condition did not mean that there would not be a reduction in the price to allow for the cost of securing the release of restrictive covenants⁷ and then that amount was determined by Roth J.⁸**
- 4.5.5 Informing client of terms - Titanic Investments v Macfarlanes⁹;**
- 4.5.6 Overage period - the Mayor and Burgesses of the London Borough of Barnet v Barnet Football Club Holdings Limited¹⁰;**
- 4.5.7 Planning Permission – Micro Design Group Limited v BD Trading Limited¹¹ which was concerned with whether a planning permission obtained by the vendor was a trigger for overage to be paid.**
- 4.5.8 Area of land covered by the overage arrangement - Virgin Management v De Morgan Group¹² involved a professional negligence claim after the vendor had accepted overage in relation to the first phase of a development and not the second phase as well.**
- 4.5.9 Release of land from overage arrangement –**
- (i) Ministry of Defence v Country and Metropolitan Homes (Rissington) Limited and another¹³- 35 out of 37 houses demolished and remaining two converted to shops raising issue whether any overage payable under provision operating if all demolished; and**

⁷ [2008] EWHC 2201 (Ch)

⁸ [2010] EWHC 2649 (Ch)

⁹ Mr. Justice Robert Walker (as he then was) at first instance (27th June 1997) and the Court of Appeal (3rd December 1998) but on appeal only on the issue whether trustees of part of the land had no claim on the ground that they would not have acted differently if they had been properly informed about the terms of the overage arrangement.

¹⁰ [2004] EWCA Civ 1191

¹¹ [2008] EWCA Civ 448

¹² Court of Appeal (24th January 1996)

¹³ [2002] EWHC 2113 (Ch)

- (ii) **Primaplus Limited v Hall Aggregates Limited¹⁴** - sports use of land excepted from overage and issue whether inclusion of golf shop at public golf driving range and sports hall caused overage provision to operate;

4.5.10 Failure to properly protect overage right/trigger - Akasuc Enterprise Limited v Farmar & Shirreff¹⁵ was a negligence claim concerning an overage payable in the event that the purchaser developed the sale land but the purchaser sold so avoiding the overage. A similar point arose in **Tecof International v Town Castle Limited¹⁶**.

4.5.11 Abatement of overage – Transview Properties Limited v City Site Properties Limited¹⁷ a failed rectification claim.

4.5.12 Negotiations – in Connolly Limited v Bellway Homes Limited¹⁸ Connolly failed with a claim to rectify a formula intended to protect against inflation but succeeded in deceit based on a false statement made as to current market value during negotiations by Bellway’s negotiator.

4.6 Each of these areas will need to be borne in mind when drafting the overage arrangement. Defects in the drafting can result in substantial losses. They are not the only matters which have to be covered and to aid the task of obtaining comprehensive instructions the use of a checklist may be useful. The next section discusses the content of such a checklist and a possible form is contained as an attachment.

5. Checklist

5.1 The heads of agreement for a sale of land may often contain a single sentence providing for overage to be paid. In many cases this will be viewed by both sides as a substantial and valuable right. In a few it may be regarded as a sop by the prospective purchaser thrown into encourage the landowner to sell but with the expectation that nothing will be payable in the future. No chances can be taken. Whatever the expectation at the time of the sale and purchase those drafting the overage arrangement have to exercise care in ensuring that the terms achieve the client’s objective to the extent

¹⁴ [2000] All ER (D)2374 and [2001] New Property Cases 11

¹⁵ [2003] EWHC 1275 (Ch)

¹⁶ [2009] All ER (D) 104

¹⁷ [2009] EWCA Civ 1255

¹⁸ [2007] EWHC 895 Civ

practically possible and that the client properly understands the arrangement.

5.2 To assist in carrying out the task it is sensible to have a checklist of points to be covered when formulating the overage arrangement. This can be used both to obtain specific instructions from the client and to enable a check to be made that the draft covers all the relevant points. It is a means by which shape can be given to the particular overage arrangement and the client assisted to focus on the important points of principle. There is no magic to the form or content of the checklist and if adopted in practice will be subject to continual adaptation and expansion.

5.3 As stated a possible form for the checklist is contained in the attachment. Many of the items contained on it will be self-explanatory and there is no benefit to be gained here from running through each individual item. However, there are certain points of general significance which will need to be decided before drafting can start and these will be considered here.

5.4 Property – it is an obvious point but nevertheless one of overriding importance. What area of land is to be covered by the overage arrangement? It is important to clearly define that area so that it is known by reference to which land the overage right is to be triggered or calculated. It is also important to establish whether any part of the land is to be kept out of the overage arrangement. It may, for example, be the purchaser's intention to retain part of the land for a home and this area is to be excluded.

5.5 Not only is it important to accurately describe the excluded land but in such circumstances it is vital to consider what easements and services will be needed by the remainder of the land over the excluded land if it is to be developed. Unless provision is made for this it will allow a ransom argument to be raised on the ground that before there could be any future development of the overage land it would be necessary to purchase the required rights and services over the excluded land.

5.5 A particular problem which can arise in respect of the definition of the land is if the overage is to be determined by reference to the proceeds realised from the development. Slip ups are possible as to which phase of the development is to be used for the purpose of the overage.

5.7 For example, in the Virgin Management case¹⁹ detailed overage provisions had been included in a sale and leaseback agreement in relation to

¹⁹ see para. 4.5.8 above

development of the particular site in stages. A dispute had arisen regarding the manner in which these provisions operated and in particular whether only the first stage of development was taken into account or the second stage as well. Negligence claims were pursued against the vendor's surveyor and solicitor on the basis that the amount of the overage was to be determined by reference only to Phase 1 and not Phase 2 of the development. The claimant had been advised by leading counsel that there was no doubt that this was the correct construction. The Official Referee held that this was correct but the Court of Appeal then held that it was wrong and that Phase 2 was in fact included in the overage arrangement. The decision is yet another good example as to how very easy it is for different interpretations to arise in respect of overage arrangements. The consequences were striking because overage had been accepted by the vendor on advice for an amount less than the Court of Appeal held the vendor was actually entitled to and in addition the vendor had incurred all the costs of the ultimately unsuccessful negligence claim.

5.8 A general point of importance for commercial property lawyers arising from the case was the acceptance by the Court of Appeal²⁰ that a solicitor was not under a duty to draft in such a manner that no rational argument could be put in favour of a construction against the client's interest. Either the drafting was correct or it was wrong and there was no half-way house. Even if an overage arrangement gives rise to a significant dispute so long as it is won there will be no come-back.

5.9 Duration – this is another simple but extremely important point. How long is the overage arrangement to continue in force? There will be a clear conflict between the interests of the two parties on this aspect. Obviously, the vendor does not want to agree to a period which the purchaser or a successor may be prepared to sit out before taking steps to enhance the value of the purchased land but periods longer than 21 years would usually be unreasonable. The longer the period agreed then the greater the hindrance there will be to the purchaser. However, there has been a tendency for vendors to seek longer periods than previously was the case. In some cases eighty years is insisted on. Acting for a solicitor on a purchase of a family country home with an adjoining paddock his vendors insisted on an overage arrangement in relation to the paddock lasting for a period of 80 years. The vendors regarded the overage provision as a family asset for future generations. It will be interesting to see whether there are any changes in the overage period requested with the removal of the perpetuity rule for property interests.

²⁰ at page 11

5.10 Single or multiple triggers – closely linked to the question of duration will be the all important issue as to whether the overage is only to be payable once during the overage period or on more than one occasion during that period. This will self-evidently affect the value of the overage right but will also have a considerable influence on the drafting. There will be a greater need to ensure that the trigger event achieves the intended overage if the entitlement is to only a single overage payment.

5.11 Care will need to be taken to ensure that the trigger event cannot be manipulated so as to produce no or only a low overage amount. For example, if under an arrangement overage is to be determined by reference to the land value with planning permission and will become payable on the occasion of the grant of the first planning permission during the overage period the overage could easily be defeated. An application for a planning permission which does not increase the value of the land or only to a minimal extent will result in a small or no overage payment. Provisions need to be inserted to prevent such applications defeating the overage entitlement. Multiple triggers are safer for the vendor.

5.12 Nature of trigger event – another influence on the draft will be the type of event which triggers an overage payment. From the purchaser's point of view this will be particularly important as it will affect cash flow. If the trigger is the grant of planning permission then the overage payment will have to be found before any proceeds have started to flow from the development of the land in accordance with the new planning permission. In contrast if the overage payment is triggered by the sale of houses once the development has been carried out then the problem of the purchaser's cash flow is solved. To achieve such a benefit in the negotiations an enhanced overage may have to be agreed. A half-way house is for the commencement of the development to trigger the overage payment. It still leaves the purchaser with a cash flow difficulty but it is less acute.

5.13 It is important to ensure that the vendor cannot unduly influence the occurrence of trigger. For example, a planning permission obtained by a vendor should not be an overage trigger. Care should be taken to ensure that it is only planning permissions wanted by the purchaser which trigger overage.

5.14 Overage formula – life is much simpler for the drafter if the overage payment is to be a fixed amount. The complexities of the operation of a formula do not have to be grappled with. All that needs to be ascertained is that the vendor has appreciated that regardless of subsequent increases in

value the overage payment will remain fixed. If the overage is not to be a fixed amount then producing the draft will be more demanding for both sides. Each case will have its own peculiarities which will have to be taken into account when formulating the manner in which the overage payment is to be determined. This is particularly so when there is more than one trigger event. There will be a number of factors to take into account dependent on the nature of the trigger event. Should there be a base amount with the overage calculated by reference to the excess? What deductions should be allowed? How is inflation to be taken into account?

5.15 As is obvious from the cases listed above overage formulae throw many problems. The Chartbrook case is a prime example. The formula for the Additional Residential Payment was expressed in words:-

“23.4% of the price achieved for each Residential Unit in excess of the Minimum Guaranteed Residential Unit Value less the Costs and Incentives”

The Minimum Guaranteed Residential Unit Value was the aggregate of the residential units divided by the number of such units

This formula could be construed in a number of ways none of which were satisfactory. In the end the House of Lords held that it was obvious from the wording that there was a mistake and rectified the overage agreement. In doing so it upheld the refusal to admit the negotiations as evidence on the construction issue even though this clearly showed that the formula was not to provide part of the purchase price but to top up if there was an unexpected increase in the price of the flats.

5.16 The decision emphasises that such formula are best set out as a mathematical formula rather using words. Worked examples attached to the provisions are a valuable assistance. A number of different scenarios should be worked through to seek to ensure that it is comprehensive. Carrying out such an exercise before exchange will increase the chances of finding any faults in the formula before the parties become bound.

5.17 Triggers of part – one issue in the context of triggers which merits a separate mention is the issue whether the overage arrangement will operate only in respect of the whole of the land or also in respect of parts. There is a strong attraction for the drafter in having the overage arrangement operate only in relation to the whole of the land. To provide that it can operate in respect of part only will need careful thought to ensure that on subsequent trigger events the overage is calculated fairly. With large areas of land it

would be unfair for the overage arrangement to only operate in relation to the whole particularly if there may be multiple trigger events.

5.18 As discussed above (para. 5.5 above) in the context of land sales in which some of the land has been excluded from the overage arrangement it is important to ensure that for the purposes of any valuation in the future it is not possible to argue that a ransom payment has to be taken into account because easements and services have to be purchased to allow a proposed development to proceed. This could be a particular problem if the trigger under an overage arrangement can operate in respect of part only of the overage land. An absence of the right to the required easements and services in favour of the relevant part over the remainder of the overage land for the purposes of the development of that part will affect the valuation of the part and thus possibly in turn the amount of the overage payment.

5.19 Protection - this topic is considered in more depth in section 7 below. Due to the hybrid nature of overage entitlements some ingenuity is required when seeking to protect the entitlement against third parties. There are two independent issues which have to be borne in mind and it is important to keep them separate.

5.20 Continuing liability - The first issue is that the overage arrangement must not be drafted so that on a disposal of the land the original purchaser ceases to be liable to pay overage in the future but the new purchaser does not become responsible for the overage. This will occur, for example, if the overage arrangement provides that the trigger event is the obtaining of planning permission by the original purchaser or the carrying out of a development by that person. No overage will be payable under such an arrangement if the planning permission is obtained or the development is carried out by a person other than the original purchaser. This is an unmitigated disaster from the vendor's point of view. Such an arrangement cries out for the original purchaser to sell on the land in order to defeat the vendor's overage entitlement.

5.21 It is exactly what happened in *Akasuc Enterprise Limited v Farmar & Shirreff*.²¹ Under the arrangement in that case the purchaser covenanted to make a payment if it developed the purchased land but did not also covenant to develop and sell. No provision was included in the overage arrangement which protected the overage payment as against third parties. It was an open invitation to defeat the overage obligation by selling to another developer. The original purchaser was not liable to make a payment if the

²¹ [2003] EWHC 1275 (Ch)

land was developed by a third party and the right was not enforceable against that developer. The purchaser did sell to a developer and as a result a claim was then made by the vendor against the solicitors who had acted on the sale.

5.22 The decision serves to emphasise the importance of the drafter not taking his or her eye off the ball. In the heat of high speed negotiations this is always a risk. To receive the overage there must be a trigger event and the vendor's solicitor must ensure that the trigger event cannot be avoided by a disposal of the land by the purchaser.

5.23 Binding against third parties – Separate from ensuring that the purchaser cannot defeat the overage entitlement by selling on there is also the issue that needs to be addressed as to whether it is to be protected against third parties. In some cases the circumstances may be such that it is clear that the purchaser is going to develop the site and the purchaser's covenant will be enough provided that for the reasons discussed above the trigger event is not linked to the identity of the purchaser. Clear instructions should be obtained from the vendor if such a course is to be adopted and such instructions should be either received or recorded in writing.

5.24 Save for such circumstances a method of protection has to be settled on with a view to protecting the overage entitlement against disposals of the overage land. The normal method is for a restriction to be imposed on the registered title to the land preventing any disposal (other, possibly, than exempted disposals) without the consent of the vendor and providing in the overage arrangement that such consent will be forthcoming if the prospective disponee enters into a direct covenant with the vendor to perform the overage obligations. Mr. Justice Peter Smith in *Akasuc Enterprises Limited* supra²² appeared to harbour reservations regarding such restrictions but they are in common use now not just to protect overage entitlements but as a means of attempting to make covenants which will not otherwise run with the land enforceable against third parties.

5.25 There are other methods of protection as discussed in more detail below. The traditional approach was to rely on restrictive covenants but that requires the vendor not just to retain land but for that land to benefit from the existence of the restrictive covenant. It is likely that there will be an increase in the number of challenges on the ground that the restrictive covenant does not provide a continuing benefit for the land. In any event restrictive covenants are vulnerable to attack by applications in the Lands Tribunal under section 84 LPA 1925 or from local authorities. A right of re-

²² At para 86 and 87

entry would be a powerful means of protecting the overage entitlement but the objection of financiers has meant that it is rarely used. Charges, even second charges, face the same objection. They have been employed but usually in cases in which the vendor is in a strong bargaining position such as on sales of government land.

5.26 The hurdle presented by the inability of the burden of the overage entitlement to run with the freehold land is not present if the overage is agreed in the context of a landlord and tenant relationship. It is possible to have the burden run with the term of years but the purchase of long leases is less likely to be acceptable.

5.27 Serious consideration needs to be given to this issue of protection in every case of an overage arrangement. It is likely that the imposition of a restriction will be the course adopted.

5.28 Other matters – the above tend to be the matters which feature strongly in most cases and on which clear instructions are required before the serious drafting can start. There are a number of other points which the draft will need to address and are not unimportant. These are covered in the checklist and cover, for example, issues such as sureties. They will be considered in more detail in section 6 with regard to the particular provisions. Consideration will need to be given as to the procedure by which disputes will be resolved and in particular whether the agreement will provide for an expert to determine any disputes (see *Aviva Life and Pensions Limited v Kestrel Properties Limited* [2011] EWHC 3934 (Ch) as to whether the relationship between such a procedure and the Court's jurisdiction).

6. Drafting overage entitlement

6.1 In this section consideration will be given to the drafting of the overage entitlement and the important issue of protecting that overage entitlement will be considered separately in the next section.

6.2 Covenant – as discussed above the overage entitlement is exclusively a chose in action and does not itself create any proprietary interest in the land. It is important that the entitlement should be clearly set out. Dependent upon the complexity of the provisions relating to the payment it will probably be best to set out the provisions relating to the entitlement in a separate schedule.

6.3 It will also be prudent to express the obligation to pay by way of covenant. This can be either in the agreement itself or in a separate deed of

covenant executed and delivered at completion. If the agreement is under seal then the advantage will be gained that the applicable limitation period shall be extended from six years to twelve.

6.4 This means that in addition to the purchase price to be paid at completion taking into account the deposit there will be an additional provision. This will provide both for the overage payments and the interest due thereon. It is a matter of personal drafting style whether the provisions are set out in a schedule or included in the body of the agreement or deed. There is an advantage in having the provisions separate when their duration is going to be longer than with the other terms of the arrangement.

6.5 Overage entitlement – in most cases the amount of the overage and, if it is not a fixed sum, the formula to be used to calculate it will be a matter of negotiation in each case. Usually there will be particular circumstances which cause the overage entitlement to be different from other cases. There are a variety of possibilities.

6.6 Fixed sum or sums – obviously the simplest form for the drafter is a further fixed payment on the occurrence of a particular event such as the grant of planning permission. Then the only issue with regard to the entitlement is whether the sum should be index linked. A slightly more complicated variant is if more than one fixed sum is due. Instead of a single lump sum the entitlement may provide for a series of payments. For example, a developer purchases land with a view to obtaining planning permission for a residential development and agrees that on the completion of the sale of each residential unit a fixed sum is payable. Normally this will be subject to a maximum total amount payable. From the developer's point of view such an arrangement has the very real advantage that the payment of the overage is synchronised with the receipts of the proceeds of the development rather than having to be funded ahead of receipt.

6.7 Formula based on fixed sum with multiplier - a step away from the simplicity of the fixed sum is if the overage is calculated by a formula involving the multiplication of a fixed sum by a multiplier. In the example given above of a developer purchasing to seek planning permission for a residential development the landowner may not be prepared to wait until the dwellings have been constructed and sold. Instead a payment may be required once the planning permission has been obtained and the amount is determined by the number of residential units which are permitted. Such negotiations could result in overage being a fixed sum multiplied by the number of residential units permitted by the subsequent planning permission or constructed by the developer. It is not uncommon for such a formula to be

limited in operation to those residential units which are not affordable housing.

6.8 Such a formulation may also be used when there is already an existing planning permission but the landowner considers that the purchaser may achieve in the future an improved planning permission which will increase the number of residential units permitted on the land. The landowner may want to sell on in order to take advantage of a good market but also retain the ability to share in any improvement in the planning position. This will be achieved by an overage comprising a fixed sum multiplied by the increase in the number of residential units permitted (disregarding for the purposes of such calculation any affordable housing).

6.9 An important point with such an overage arrangement is the period it is to run. It is unlikely in such circumstances that the period will be two or three years unless there is a particular outstanding planning permission which has been the reason for the landowner requesting the overage arrangement. The overage period is more likely to be twenty years when the overage is to last for such a period it is imperative that the arrangement is protected (as to which see section 7 below).

6.10 Instead of the formula being related to the number of permitted residential units the formula may be related to another factor such as the aggregate of the area of internal space for each of the permitted residential units. This is particularly appropriate for a residential development relating to flats. Overage could be related to the number of flats permitted or alternatively could be banded by reference to the aggregate internal area of the flats.

6.11 Valuations – one difficulty with fixed sums or a formula based on fixed sums is that each side has to make a guess as to future valuations. Notwithstanding that such guesses may be based on lengthy experience the longer the overage arrangement can run the less likely that such a guess will be satisfactory. There is a risk that as a result one or other of the parties may be treated unfairly. This can then have serious consequences if it is considered that the other side has contributed to this unfairness (see *Connolly Limited v Bellway Homes Limited supra*). To remove this risk instead of a fixed sum a valuation at the appropriate time may be substituted.

6.12 The simplest example is an open market valuation of the land once an Acceptable Planning Permission has been obtained. The overage will be equal to an agreed proportion of the excess of that open market value over either an agreed base value or the open market value of the land at the same

time without the benefit of planning permission. The uplift in the valuation of the land resulting from the grant of the planning permission will be shared between the two parties.

6.13 Proceeds – an alternative base to valuation for calculating overage is to use the proceeds realised by the developer from the land. In the case of a residential development instead of a formula based on a fixed sum it may be based on the proceeds realised from the disposal or development of the land. This will raise two principal issues. First, will the proceeds to be used as the base be gross or net? Second will it be a single lump sum payment or a series of payments?

6.14 If the payment relates to the sale of each residential unit then the overage may well be related to the gross proceeds. It may be an agreed percentage of the sale price for the unit. Developers may be prepared to agree such an overage provided that the true price of the residential unit is used. In particular the developer will want to ensure that any incentives offered to sell the unit are taken into account.

6.15 On the other hand if the overage payment is to be a proportion of the development profits accruing from the development then more complex provisions are required which ensure a proper account is produced containing not just the appropriate receipts but also the full extent of the expenditure incurred in carrying out the development. When the arrangement is the type discussed in section 3 above then such provisions are appropriate. The drawback for an owner selling land to a developer is that the finances of the development are exclusively within the knowledge and control of the developer. It is difficult for the owner to monitor such expenditure. There is greater scope for disputes to arise in the determination of the overage. There are significant attractions for a landowner to opt for an overage entitlement which is simpler and less likely to throw up disputes. However, if the determination procedure works then the benefits may well be more substantial than with, say, a fixed sum.

6.16 From the landowner's point of view it has to be borne in mind that the developer's negotiators will not be prepared to enter into an open ended liability. The overage agreed will be part of the costs of the proposed development and the developer will need to be able to place a cap on the upper amount payable. Consequently, even if the overage is to be determined by reference to the development profits the likelihood is that a maximum limit will be imposed.

7. Protection

7.1 As stated above the overage obligation is a positive covenant and as such is not a burden which runs with the land. A right to overage cannot by itself be enforced against the owner of the overage land from time to time. In some cases reliance only on such contractual rights may be acceptable to the vendor. This can only be if the time span between making the contract and the crystallisation of the overage entitlement is limited. However, the risk of a sale on or insolvency would normally be sufficient to deter such reliance. Normally, and particularly with those cases in which the arrangement is expected to run for a longer period, greater protection is required. There is no one method of protection which ensures complete protection. In cases in which the vendor has a strong negotiating position a number of methods may be adopted. For instance, government departments may insist on charges and restrictions to enforce overage arrangements which in some cases such as the sale off of land for agricultural user may seek a 100% overage payment. Most vendors will not have such a powerful negotiating position.

7.2 Restrictive covenants – one of the methods that often arise for consideration but which may do so less often in the future is the restrictive covenant. A restrictive covenant is imposed on the land limiting the user to the current user or prohibiting certain types of specified user or activities. In the event that a planning permission is granted in the future the release of the land from the restrictive covenant may be negotiated or obtained in accordance with a procedure contained in the original arrangement. The existence of the restrictive covenant will obviously affect the value of the land but will not prevent dealings with it (including importantly the making of charges).

7.3 An example of such restrictive covenants imposed in the context of an overage arrangement is provided in *Primaplus Limited v Hall Aggregates Limited*.²³ In that case the conveyance imposed a restriction for fifty years against any residential, industrial, warehousing retail or other commercial development. There was a provision that if certain planning permissions were obtained then an overage payment equal to 50% of the increase in value attributable to the planning permission had to be made to the vendor and in return there would be a release from the restrictive covenant. Under the arrangement certain uses were permitted and did not trigger an overage payment. These permitted uses included use as a sports and recreation centre. Planning permission was obtained for a sports complex for both the able bodied and the disabled. Oddly it was the person liable to pay overage who was arguing that a payment had been triggered whilst the person entitled to overage was arguing that there had been no trigger event.

²³ [2001] NPC 11

The purchaser's successor argued that the use was not within the class of permitted use and thus an overage payment was due which would lead automatically to a release of the restrictive covenants. The vendor argued that it was within the permitted class so no trigger event had occurred thereby avoiding the loss of a valuable asset for a small payment. The vendor succeeded. It serves to emphasise the great care that needs to be taken when there is a once and for all trigger.

7.4 Unless the benefit is held by a local authority a restrictive covenant can only be used by a vendor who retains ownership of land which is capable of benefiting from the restrictive covenant. If this is not possible then the vendor will not be able to enforce the restrictive covenant. The absence of the ability to retain any land was probably the reason that it was not considered in *Akasu Enterprises*. Retention of the ownership of a road serving the land sold may be sufficient for these purposes but this would need to be considered carefully and the possibility of the road being subsequently adopted taken into account.²⁴ Obviously if the vendor is selling all the land owned then this method is a non-starter. However, even if land is being retained there is still the issue as to whether it will benefit from the existence of the restrictive covenant.

7.5 In particular it may be a trap for a vendor to retain a small area reserved out of the land being sold solely with a view to enabling the restrictive covenant to be enforceable against third parties as a means of protecting. It may encourage the belief that the restrictive covenant is protected when the benefit is annexed to a parcel which cannot actually benefit from the existence of the covenant. This gives rise to separate means of challenge to the restrictive covenant. It may be argued that it is unenforceable as the land does not benefit from its existence. Alternatively, an application may be made to the Lands Tribunal to discharge or modify it on the ground that it does not secure a practical benefit.

7.6 On the first point there is very little authority. Wilberforce J. in *Marten v Flight Refuelling Limited*²⁵ stated that if “an owner of land, on selling part of it, thinks fit to impose a restriction on user, and the restriction was imposed for the purpose of benefiting the land retained, the court would normally assume that it is capable of doing so. There might, of course, be exceptional cases where the covenant was on the face of it taken capriciously or not bona fide.”. There are two possible points which may be raised in respect of the issue of enforceability of the covenant. First, was it taken in

²⁴ *Re Gadd's Land Transfer* [1966] Ch. 56 but not if the road has been adopted and only the sub-soil has been retained - *Kelly v Barrett* [1924] 2Ch. 379.

²⁵ [1962] 1 Ch. 115 at pages 136/137

order to protect the retained land?²⁶ Second, will the retained land benefit from a restriction affecting a much larger area? The Court will not substitute its own judgment on this issue but will decide whether the view that the retained land is or is not benefited is a reasonable one.²⁷

7.7 The alternative means of challenging a restrictive covenant is of greater practical significance. It is the risk that the restrictive covenant may be modified or discharged by the Lands Tribunal upon an application pursuant to section 84 LPA 1925.²⁸ If the arrangement is not intended to run for a significant period then the risk should not be great. However, the longer the period that it runs the greater the risk. The Lands Tribunal has jurisdiction to act if the covenant restricts “some reasonable user of the land for public or private purposes”²⁹ and the covenant does not secure to the person entitled to the benefit “any practical benefits of substantial value or advantage to them”³⁰. For these purposes a covenant intended to secure a monetary benefit is not regarded as securing a practical benefit and thus if it impedes a reasonable user of the land the covenant will not be protected on the ground that it secures a practical benefit.³¹ An original covenantor is not precluded from making an application.³² There may also be a risk of the Lands Tribunal acting on the ground that the character of the neighbourhood has changed.³³

7.8 The inclusion in the original arrangement of a procedure whereby the release of the purchased land from the restrictive covenant will be obtained in return for a payment to be determined may reduce the risk that the Land Tribunals will act but is likely to be challenged on the ground that it is not a restrictive covenant but is in substance a positive covenant to make a payment in the event of a change of use.

7.9 The Lands Tribunal has pursuant to section 84(1)(aa) LPA 1925 modified a restrictive covenant to allow a development on the basis that it secured no practical benefit of a substantial value. The restrictive covenant had been taken with a view to securing the ability to extract a financial

²⁶ see Brightman J. in *Wrotham Park Estate Co v Parkside Homes* [1974] 1 WLR 798 at page 808 E/F

²⁷ Brightman J. in *Wrotham Park Estates* supra at page 808 D/E

²⁸ as amended by LPA 1969.

²⁹ section 84(1)(aa) LPA 1925

³⁰ section 84(1A) LPA 1925

³¹ Court of Appeal in *Stockport Metropolitan B.C. v Alwiyah Developments* (1983) 52 P & CR 278 followed in *Re Bennett and Tamarlin Limited* (1987) 54 P & CR 378 applied by the Lands Tribunal in *re Withinlee* supra.

³² *Shepherd Homes Limited v Sandham* (No. 2) [1971] 2 AER 1267

³³ section 84(1)(a) LPA 1925.

benefit in the event that the land subject to the restrictive covenant was to be developed.³⁴ One factor in that case was that the land was incapable of any reasonable user by itself.³⁵ Another factor was the possibility that the land could increase in value as a result of the proposed development as the house purchasers could be special purchasers with a view to extending their gardens. No compensation was payable. An attempt was also made in re Withinlee to discharge the covenant as obsolete (para. (a)) but it was held that it could still fulfil its original purpose to extract a financial benefit and so was not obsolete. Even if the retained land is not effectively a ransom strip the same result can occur as illustrated by the Court of Appeal decision in *Graham v Easington District Council*³⁶.

7.10 To rely exclusively on the retention of a small area of land for the enforceability of the restrictive covenant carries with it very serious risks that this may be challenged on the ground that it does not genuinely benefit the retained land. If the overage arrangement relies exclusively on the restrictive covenant this could cause the whole of the overage to be lost.

7.11 In order to ensure that the restrictive covenant affects third parties the restrictive covenant will need to be protected in the appropriate manner either at the Land Registry or the Land Charges Register. If there is no restrictive covenant but only the positive covenant to make the payment then there is no point in expressly attaching the benefit of that positive covenant to a parcel of land. It will not achieve anything but may mislead.

7.12 There is the further risk that the covenant could cease to be enforceable due to the acquisition or appropriation of the land by a local authority for planning purposes. In such circumstances development carried out in accordance with a planning permission will allow any restrictive covenant to be overridden.³⁷ Compensation will be payable but on the basis of compulsory purchase principles.³⁸

7.13 Right of re-entry - In a case in which the vendor does not retain any land to benefit from the existence of the restrictive covenant a right of re-entry may be reserved for the vendor with a view to securing the performance of the restrictive covenant. Such a right of re-entry is enforceable even if the restrictive covenant it is to protect is not enforceable

³⁴ re Withinlee LP/7/2001 13th March 2003 before Mr. Rose

³⁵ para. 32 judgment

³⁶ [2008] EWCA Civ 1503

³⁷ section 237 Town and Country Planning Act 1990

³⁸ section 237(4) TCPA 1990

against the then owner of the land.³⁹ It is a very effective method of protection but not oft used. Such a right will almost inevitably pose problems for the purchaser and be strenuously objected to.

7.14 Chain of Positive Covenants - this alternative method has already been considered with regard to the decision in Akasu. The aim is to set up a chain of covenants whereby every time the land is disposed of the new disponee covenants directly with the vendor. It is to be expected that under the arrangement the obtaining of each new covenant will release the previous covenantee from liability. For the purchaser or any successor to continue to be liable after the disposal of the land would be far too heavy a burden to accept. However, some vendors insist on there being no release and liability continuing. Such a structure will be backed up by a restriction at the Land Registry requiring that no dealing with the registered land is to be registered without consent which will only be given if a new deed of covenant has been entered into by the transferee. This is an essential element in the structure.

7.15 This approach is not wholly satisfactory from the purchaser's point of view. The requirement that any successor enters into a direct covenant will act as a deterrent to sales. It will inevitably raise issues as to what provision is to be made to cater for gifts, leases and mortgages of the land. It is not realistic to expect a mortgagee to enter into a direct covenant. Some form of exception will probably have to be allowed in respect of lettings which are not for a long term. The structure is inevitably a shaky one the longer the arrangement continues. An insolvency in the chain could cause problems.

7.16 However, notwithstanding the rather ungainly nature of such chains such provisions are now a standard approach used by conveyancers to protect rights which do not create interests in land. This was recognised by Mr. Justice Peter Smith in Akasu supra. It is a means by which a covenant which does not qualify as a restrictive covenant can be protected as well as being used in cases in which the original covenantor does not retain any neighbouring land.

7.17 Any restriction if possible should be in a form prescribed by the Land Registry. Use of tailor made restrictions can lead to problems. The Land Registry may refuse to register the restriction if the operation of the restriction requires the Land Registry to form a judgment. For example, if the Land Registry has to decide the character of the land being dealt with.

³⁹ Shiloh Spinners v Harding [1973] AC 691

7.18 Consideration will need to be given to how the restriction is to operate with a view to avoiding delays in the production of any required certificate and avoiding covenants being given by purchasers of individual units. One possibility is for the certificate of compliance with the overage provisions to be capable of being provided by a conveyancer acting for either side and not just the party entitled to the overage.

7.19 Charges – this is the most straightforward course of action. The difficulty is that it will deter future mortgagees so that the purchaser and any successor will not be able to use the purchased land as security. It may be that it can be agreed as part of the arrangement that the vendor’s charge is deferred so that priority could be given to the purchaser’s mortgagee. From the vendor’s point of view such priority would need to be subject to a financial limit. There has been a suggestion that charges to secure future unascertained and contingent sums may not be valid. It is for this reason that some charges to secure an overage arrangement contain both legal and equitable charges.⁴⁰ Disclaimer of the overage arrangement in an insolvency will restrict the scope of the charge to accrued overage as in *Hughes v Grovehold Limited*⁴¹. In practice it can only be insisted on by purchasers in an extremely powerful negotiating position such as government departments.

7.20 Vendor's lien – in *Akasuc* surprisingly the judge considered that a vendor’s lien was a possible means of protection if the contract had been amended so that the overage payments were part of the outstanding purchase price including payments on developments by successors in title rather than payments in addition to the purchase price. The judge commented that this method circumvented the difficulties posed by the restriction method. What was not discussed with regard to this method was why a purchaser would accept an unpaid vendor's lien when a second charge is not acceptable. The lien and charge would appear to pose identical problems. Often the vendor's lien is expressly excluded in the overage agreement. Even if not there can be complications as shown by the Court of Appeal decision in *George Wimpey Manchester Limited v Valey and Vale Properties Limited* [2012] EWCA Civ 233 albeit that the judgments concerned a rather unusual set of facts and use of the argument for an unpaid lien.

7.21 Lease – an alternative to selling the freehold and attempting

⁴⁰ It is worth noting that in the capital gains tax case *Marson v Marriage* (1979) 54 TC 59 the further sum charged to capital gains tax represented a payment to obtain a release of the charge securing the overage payment.

⁴¹ [2005] EWCA Civ 897

to establish covenants which run with the land is for a long lease to be granted and the restrictive covenants included amongst the lessee's covenants with enforcement backed up by the lessor's right to forfeit. This removes the need for there to be separate retained land. The lessor's reversion will inevitably benefit from such covenants. The jurisdiction to modify or remove the covenants conferred by section 84 LPA 1925 applies to leases for terms exceeding 40 years after the expiry of the first 25 years.⁴² The covenants can also be overridden by section 237 TCPA 1990. If the restriction is against the tenant carrying out improvements rather than user then it will be necessary to consider the application of any statutory provisions affecting such restriction.

7.22 In the case of new tenancies an obligation to make an overage payment entered into by the tenant under a lease arrangement may constitute a "tenant's covenant" for the purposes of the Landlord and Tenant (Covenants) Act 1995 and as such the benefit and burden will be transmissible under the terms of that Act. Such a covenant does not need to refer to the subject matter of the lease⁴³ and may be contained not in the lease itself but in a collateral agreement⁴⁴ (as was the case in *George Wimpey Manchester Limited v Valey and Vale Properties Limited* [2012] EWCA Civ 233 discussed at para. 5). The transmission provisions will not apply to personal covenants.⁴⁵ There may be an issue as to whether or not the overage obligation is personal particularly as regards the ability to enforce it and if the obligation is contained in a collateral agreement. It is obviously an issue of great importance. Further, if the trigger event for the falling due of the overage payment is a disposal then consideration will need to be given to the statutory restrictions.⁴⁶

7.23 Even if acceptable to the prospective purchaser and its financiers there is the complication for the owner posed by the anti-avoidance income tax provisions relating to leases. These would need to be considered carefully. They pose a trap for commercial conveyancing solicitors.⁴⁷

7.24 Ransom strips – the retention of a strip of land which will prevent any proposed development is a last possibility but from the purchaser's point of view should be unacceptable. If it is combined with a buy

⁴² section 84(12) LPA 1925

⁴³ section 2(1)(a) 1995 Act

⁴⁴ see definition of "covenant" in section 28 1995 Act

⁴⁵ section 3(6)(a) 1995 and *Chesterfield Properties Limited v BHP Great Britain Petroleum Limited* [2001] EWCA CIV 1797

⁴⁶ section 144 LPA 1925 the operation of which can be expressly excluded

⁴⁷ *Hurlingham Estates Limited v Wilde & Partners* [1997] STC 627

option which is exercisable when planning permission is obtained then the concept is less objectionable. Such an option previously had to be subject to a 21 year perpetuity period.⁴⁸ The vendor runs the risk that the strip may due to changing circumstances cease to be a ransom strip.

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⁴⁸ section 9 Perpetuities and Accumulations Act 1964. The perpetuity rule no longer applies to options entered into on or after 6th April 2010 unless contained in a will executed before that date (Perpetuities and Accumulations Act 2009).