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Time to Renegotiate?

In these recessionary times increasing numbers of tenants are facing difficulty in meeting rent and service charge payments. Landlords are also finding it more and more difficult to attract and retain tenants and maintain a steady flow of rental income vital for their cash flow.

Both landlords and tenants may wish to consider whether now is an opportune moment to re-examine the provisions of their leases to see whether these should be altered (on either a temporary or permanent basis) to enable tenants to continue to trade.

As recently as 18 months ago property was in high demand by tenants and as a consequence lease terms were quite onerous from a tenant's point of view with landlords all too frequently able to dictate terms to tenants.

• Crunch Time

With the recession continuing to bite, increasing number of tenants now find themselves in the position of having to service high levels of rent in extremely difficult trading conditions.

As a consequence, many tenants have considered taking some form of insolvency action. There have been a flood of pre-pack administrations over recent months as companies look to off load some of their onerous contracts which make it impossible for the company to trade profitably. The key issue for these companies is often the cost of their leases and an administration gives an opportunity for the tenant to relinquish certain of its unprofitable properties and to renegotiate the lease terms on the others.

Other tenants may consider entering into a Company Voluntary Arrangement ('CVA') so that it could consolidate its affairs and re-structure whilst continuing

to trade. These CVA's can also lead to tenants agreeing settlements with landlords in relation to certain properties and renegotiating terms on other properties.

The position for landlords has been exacerbated by the recent alterations to the rules associated with business rates. These changes mean that the landlord could find itself not only at risk of losing rental income if its tenant goes bust, but it could also end up having to pay the business rates for the property if the property remains vacant for a long time.

With these insolvency processes being available and actively used by tenants, and the possible difficulties in re-letting property in this current climate as well as the threat of having to meet a rates liability for the property, it is perhaps not surprising that increasing numbers of landlords are now exploring the possibility of renegotiating some of the terms of their leases in an effort to retain tenants and keep their properties let.

• Time to Renegotiate?

There are a number of different lease concessions open to landlords which might assist their tenants.

This could simply involve agreeing to change the payment cycle so that the tenant pays rent on a monthly basis rather than quarterly as has historically been the norm. Whilst the total rental sums received by the landlord do not change this concession can have significant benefits for the tenants' cash flow in these times where conserving cash is paramount.

Alternatively, the landlord might agree to an actual cash benefit given to the tenant. This can take many forms. Some of the most common methods are as follows:

- The landlord could allow a "rent free" period to give the tenant some extra breathing space if it is experiencing particularly difficult times;
- The parties could agree a reduction in the rental level taking into consideration the environment that the tenant now operates in compared with that from when the lease was granted;
- Another method, particularly for retail tenants, might be to switch the rent to a "turnover rent" whereby the landlord takes a fixed percentage of turnover generated from the property. This means that the landlord shares the pain when the tenant's turnover is reduced and thus reduces the pressure on the tenant.

Landlords may well consider that some rent received, now or in the future, might be better than no rent at all, particularly if the prospect of re-letting the property is not good.

- **Rent Review**

Historically rent review provisions would almost certainly stipulate that rent would be reviewed on an upwards only basis (based on open market rental value at the time of review). In the current climate few rents might be increasing on rent review as there are generally downwards pressures on rental values, but modern leases are not likely to permit any reduction in the level of rent.

In today's more difficult trading conditions, such upwards only reviews seem somewhat out of touch with reality. Rent levels negotiated during a property boom may simply no longer be reflective of the current market conditions (and hence the market value of the lease). Upwards or downwards reviews could be considered as being fairer to the tenant and renewal leases could be negotiated with these provisions, or existing leases varied by agreement between the parties.

- **Conclusion**

Landlords and tenants do of course need to consider each case on its own merits but are well advised to approach these matters in an open minded way and to explore all possibilities as it is in everyone's interest that commercial premises be kept open and trading throughout these difficult times.

Buyer Beware – purchasing commercial property at auction.

The recent collapse in the property market together with the effects of the credit crunch is currently resulting in increased numbers of distress sales of property at auction. Typically auctions are used as a process for sale by lenders who have exercised their power of sale by appointing a receiver or by a seller who wishes to be able to sell their property quickly.

Whilst an auction sale can have many advantages for a purchaser, including a competitive reserve price and the certainty of knowing that the seller cannot withdraw from the sale after the auction, there are also a number of pitfalls to be aware of.

The most important thing to remember when considering bidding for a property at auction is that, if you are the successful bidder, you will be contractually obliged to complete the sale of the property as soon as the gavel falls. This means that, if you have not undertaken sufficient due diligence in relation to the property and a defect in title or other problem becomes apparent between exchange and completion, you will either have to proceed with the purchase or risk losing your 10% deposit. In addition, the standard auction contract will preclude you or your solicitor from raising additional enquiries to try to obtain further information about the property from the seller's solicitor after exchange.

The key is, therefore, to carry out full due diligence as soon as you identify a property you may be interested in.

The seller's solicitor will have prepared a legal pack in respect of the property, which will be available to any interested party prior to the auction. This legal pack should include all of the documents needed to carry out a full investigation of title, including searches, title information and replies to standard pre-contract enquiries. The pack will also contain the general conditions of sale and any special conditions which are specific to that particular sale. There may be an opportunity to raise enquiries with the seller's solicitor, who may or may not be able to assist in providing additional information. In certain circumstances, particularly where the sale is being effected by a lender or a receiver, there will be limited information available and the seller will not be in a position to provide any form of title guarantee.

Given that, where you are the successful bidder, you will be contractually bound to purchase the property, usually 4 weeks after the auction, it is imperative that you have your funding for the purchase in place before the auction takes place.

If you are interested in purchasing a property at auction, we would urge you to contact us as soon as possible. We will be able to advise you of any issues which arise, either from our inspection of the documentation, or as a result of a failure by the seller to provide certain information. You will then be in a position to consider whether you still wish to attend the auction and, if you do, to consider whether the price you are prepared to pay needs to be adjusted as a result of the information (or lack thereof) which has been obtained.

It is, therefore, possible to minimise the risks involved in purchasing a property at auction and to ensure that you, as a potential buyer, make a well-informed and reasoned decision before you step into the auction room.

Partially Completed Developments

With the dramatic changes to the property landscape over the past 12 months it is perhaps no surprise that partially completed development sites are increasingly common as both developers and their financial backers are wary of developing sites that might no longer be financially viable. This article looks at what a developer can do to try and keep a planning permission alive in times of difficulty, the problems created by partially completed developments and the powers available to the Local Planning Authority (LPA) when faced with such problems.

Problems caused by partially completed development

There are a number of issues with partially completed developments, which may lead to an LPA taking action. The site may be visually unattractive, which may adversely affect the value of property in the locality and/or lead to reduced investment in an area. Partially completed developments also prevent land from being used to its full development potential, which is generally contrary to Government policy.

Completion of a proposed development may be prevented for a number of reasons, all of which are exacerbated by the current financial climate. Difficulties with the continuing availability of finance for the project, a reduced demand for the particular type of development and reduced valuations may all lead to the developer reconsidering development plans. A developer may also choose to complete the most profitable parts of a site and leave the remainder undeveloped.

Keeping a planning permission alive

There is usually a time limit placed on the commencement of the development from the date of the grant of full planning permission. If the development is not started within this period, the permission will expire

and a new permission will be required. It may prove difficult to obtain a new permission once one has expired, for example, because planning policies or local development plans may have changed in the interim period not to mention the additional costs associated with a new planning application.

If there are any conditions imposed on the planning permission, which need to be complied with prior to the commencement of development, the developer must ensure that these have been complied with and should obtain written confirmation from the LPA of this fact before starting any development works.

To implement a planning permission, the developer must then carry out a "material operation", which includes, for example, digging a trench to contain the foundations of a building. The extent of works required to be a material operation is unclear, but the courts have held that the works need to be more than de minimis – for example the removal of a hedge for a permitted access road was held not to be a material operation.

If a developer decides to carry out work to keep a planning permission alive, it is advisable to keep detailed records of the work, including photographs and to obtain statutory declarations setting out the timetable and extent of the works from the builder.

A developer must consider all the circumstances carefully before deciding what course of action to take. There is the possibility that a token implementation may trigger payments or other measures under a planning obligation or highways agreement. There is now an added complication as the Planning Act 2008 contains some potentially significant proposals to introduce the community infrastructure levy. There is potential for the levy to become payable even though the permission has not been lawfully implemented and is liable to expire.

Addressing the problems caused by partially completed developments

LPAs have a number of options available to them. The main powers are as follows:-

Development completion notices

The purpose of a development completion notice is to encourage completion of a development where work has started but appears to have stopped. The completion notice does not require completion of the development. The notices are often used to improve the visual amenity of the partly developed site. There are two stages:-

Stage 1: the LPA serves the development completion notice;

Stage 2: the Secretary of State (SoS) confirms the development completion notice.

The development completion notice will state that, subject to the SoS confirming the notice, the planning

permission will cease to have effect on a specified date, which cannot be less than 12 months after the development completion notice takes effect. This means that any work carried out **after** the specified date will not have the benefit of a planning permission and will be liable to enforcement action if no new planning permission is obtained. Any work carried out **before** the specified date is not affected, provided it complies with the planning permission.

A development completion notice cannot be served until the period specified in the planning permission for the commencement of development has expired (i.e. usually 3 years).

The SoS must be satisfied that the development will not be completed within a reasonable period and has power to change the time period stipulated in the notice. The time period does not start to run until the notice has been confirmed.

Before confirming the notice, the SoS must give any person on whom the notice was served the opportunity of a hearing. The validity of the SoS's decision to confirm a notice can only be challenged on a point of law in the High Court and any challenge must be made within 6 weeks from the date the notice is confirmed.

Although it is the main power available to LPAs, development completion notices are rarely used because they do not guarantee completion of the development. There are no penalties for non-compliance with a development completion notice. If the developer is unable to complete the development within the specified time period, the LPA is left with a partially built, potentially unattractive building that is immune from enforcement action and has no planning permission for the outstanding work. The process also takes a long time to complete.

Planning conditions

Although there are statutory time limits for development to be commenced, there are no statutory time limits for a development to be completed once it has been begun.

Planning conditions can be imposed to ensure that a particular element of a development is completed by a certain stage or before the development is brought into use, for example, a condition may require a new access road to be created before any other development is carried out, or prevent occupation of offices until a car park is complete.

Conditions can also be imposed to ensure that development proceeds in a certain sequence.

Maintenance notices

An LPA may use a maintenance notice where the condition of land or buildings adversely affects the amenity of an area. The notice requires the owner or

occupier of the land to clean it up or deal with the poor state of a building and can require a wide range of works to be carried out. A maintenance notice cannot take effect until at least 28 days after service. If the owner or occupier does not comply with the notice, the LPA can carry out the works themselves and recover the cost from the owner or prosecute the owner or occupier.

There is a right of appeal against the service of the notice. One of the defences is that the state of the land is a result of work being carried out pursuant to a planning permission. Even if work has ceased on site, the owner and occupier will have a legitimate defence against the service of a notice if the condition of the land is a consequence of builders' materials or soil associated with building work that was carried out pursuant to a planning permission.

Discontinuance orders

An LPA may issue a discontinuance order to require a landowner to remove or alter any building or works if it appears to the LPA that this would be beneficial to the "proper planning of their area (including the interests of amenity)". A discontinuance order must be confirmed by the SoS and any person on whom the notice was served may request a hearing before the SoS. If a discontinuance order is confirmed, the LPA is liable to pay compensation to the owner, which can be substantial as it includes the depreciation in value of land and the expenses incurred in complying with the order. This obligation means that discontinuance notices are rarely used in practice.

Conclusion

It remains to be seen what attitude the Government and LPAs will take with regards to partially completed developments as the recession continues. The Government may feel that, as a matter of public policy, it is not appropriate and is actually potentially counter-productive for LPAs to take aggressive action in circumstances where most developers are either unable to continue to finance the project or there is no demand for the finished development. There are also likely to be budgetary constraints on the LPAs themselves. Nevertheless, it is wise for developers to be aware of the remedies available to the LPA and to take all actions which are practicable and prudent in their particular circumstances to protect their position going forward.

Key Contacts



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