

property litigation update - winter 2006

Premiums for leasehold extensions and enfranchisement set to rise

It has become commonplace for residential leaseholders to extend their long leases, if the term is becoming too short, or for groups of leaseholders to collectively enfranchise by purchasing the freehold of their building either through informal negotiations or by using the procedures laid down in the Leasehold Reform, Housing and Urban Development Act 1993. The 1993 Act provides a complicated formula for valuers to follow when assessing the premium payable on a lease extension or enfranchisement based, amongst other things, upon the assumption of the amount which at the valuation date the freeholder's interest might be expected to realise if sold upon the open market to a willing buyer. This figure is obtained by ascertaining the open market value of the freehold with vacant possession at the valuation date, and then applying a discount, called the "deferment rate", to reflect the fact that vacant possession will not actually be available until the term of the lease expires. The lower the rate, the greater the premium payable. In recent years, valuers in the South East (outside London) have tended generally to apply a deferment rate of between 7% and 8% in their calculations. In the Lands Tribunal case of *Earl Cadogan and Cadogan Estates Limited v Sportelli*, which involved five appeals heard together on 15 September 2006, the Tribunal recommended that when making these calculations valuers should take into account not only property market evidence but also financial evidence similar to that used for other investments. The Tribunal felt that as yields on all other investments had been dropping over the years, it was unfair on freeholders for the deferment rate to remain unchanged. Consequently, the Lands Tribunal now recommends a deferment rate of 5% is adopted and applied irrespective of the location of the premises, its condition or the length of term left. The consensus amongst practitioners is that the outcome of the *Sportelli* decision will see freeholders demanding significantly higher premiums, and for ongoing cases the risk of some difficult renegotiations over premiums. Freeholders and leaseholders facing lease extensions or enfranchisement are recommended to

obtain professional legal and valuation advice at an early stage.

Forfeiting tenancies of mixed use premises

Premises let only for business purposes may be forfeited for rent arrears by the landlord either re-entering the premises or issuing and serving court proceedings seeking a possession order against the tenant. If forfeiture is effected by physical re-entry, the landlord may not force entry to the premises, if there is someone present on the premises who opposes the entry, as this is a criminal offence; but if at the time no-one is at the premises this is not an obstacle. The position is markedly different to that of residential premises, where a tenant enjoys additional protection from forfeiture under section 2 of the Protection from Eviction Act 1977, which provides that premises let as a dwelling cannot be forfeited otherwise than by court proceedings if the tenant is residing there. However, the position for tenancies with a business and residence use, normally a shop and accommodation above, was not clear until the recent Court of Appeal decision of *Pirabakaran v Patel*. In that case the landlord sought to forfeit the tenancy by re-entering the shop premises, as forfeiture occurs once any part of the premises are re-entered. Later on, after the tenant seriously damaged the premises and was arrested by the police, they took back the residential part as well, on the basis that the earlier forfeiture was effective to end the tenancy. The Court disagreed, and decided that in the case of mixed business and residential use the phrase "let as a dwelling" under the 1977 Act also applied to the shop. Thus, the tenant was allowed to return to both the shop and the residence. Interestingly, the Court considered Human Rights principles to support its decision.

This case sends out a clear warning to landlords wishing to terminate tenancies of mixed use premises that there is now a grave danger that re-entry without a court order will be both ineffective and a criminal offence; increasingly traditional self-help remedies are being curtailed by legislation and the Courts, and for tenants and landlords there is ever greater reason to seek legal help.

Licensing Act 2003 - Licensing authority powers

Following the introduction of the new Licensing Act 2003 on 25 November 2005, most owners and managers of licensed premises have now had a year to get accustomed to the new licensing regime. The new Premises Licences, issued by local authorities, replaced the old Justices' Licences. Unlike Justices' Licences, which had to be renewed every 3 years, Premises Licences last indefinitely. However, Premises Licence holders should be aware of the wide powers that local licensing authorities have been given under the new Licensing Act to vary, suspend or even revoke them in certain circumstances. Under the Act, after a Premises Licence has been granted, a responsible authority, such as the police, or an interested party, like a local resident, can apply to the local authority to review a Premises Licence, if they have any complaints. On completing their review, a local authority may issue the Licence holder with an informal warning with recommendations for improvements. In more extreme cases, the licensing authority may order that the conditions of the Licence be varied or modified, such as reducing opening hours. In the worst cases it may even order the suspension or revocation of a Premises Licence. In addition, the police also have increased powers under the Act. The Police can close licensed premises down for up to 24 hours either because of disorder at the premises, noise nuisance or in order to protect public safety. In certain circumstances, this 24-hour closure period can be extended by a further 24 hours by a senior police officer, if the public disorder or noise nuisance continues at those premises. The breach of a closure order can lead to a fine of up to £20,000 and/or 3 months in prison. Hence, while the days of a refusal by the licensing magistrates to renew are gone, Licence holders and local residents may wish to take legal advice, if the police are called to deal with disturbances at the premises.

Commercial Rent Arrears Recovery

The European Convention introduced by the Human Rights Act 1998 is indirectly giving rise to changes in areas of the law not specifically covered by the Convention, but where the State considers that compliance with it requires improvement of existing laws. The Tribunals, Courts and Enforcement Bill has been introduced with the intention of abolishing the ancient common law right of landlords to distrain on the tenants' goods for arrears of rent. At present distraint is a useful and speedy remedy for landlords of commercial premises and is regularly used as a shot across the

tenant's bow to persuade a defaulting tenant to pay the current arrears and all future rent on time. No advance warning is required to be given, to avoid the risk that the bailiff will otherwise find nothing of value at the demised premises other than the tenant and his or her spouse (whom the tenant might gladly hand over). Further, modern commercial leases reserve as rent not only the amount payable for the tenant's occupation but also service charges, insurance premiums, Vat, interest, etc. The landlord then has the option of distraining for all payments reserved as rent. If the Bill in its present form receives Royal Assent, distraint will be abolished and commercial landlords will have to adopt a procedure called Commercial Rent Arrears Recovery ("CRAR"). This procedure will apply to rent payable for possession and no other payments such as service charges, etc, even though they may be reserved as rent. In relation to these other payments the landlord must use other remedies, such as debt recovery proceedings issued by the Court and/or forfeiture action. The CRAR procedure allows the tenant to make deductions for sums the tenant claims are due from the landlord, e.g. set-off for landlord's breach of repairing obligations. Accordingly, the clause commonly found in leases providing that rent is payable without deduction etc, will no longer be effective. In addition there will be a notice procedure that must be followed, thus eliminating the element of surprise and possibly the number and nature of the goods found at the premises. The Court will have the power to intervene, if asked by the tenant and to decide whether CRAR is applicable and whether its procedures have been complied with. The Court may in the case of a dispute suspend the use of CRAR, pending resolution of that dispute. The Bill may be amended as it passes through Parliament, but in its current form it provides an indication that the seizure and threatened sale of tenant's goods will almost certainly become less of an effective remedy.

Our Property Litigation Team is part of the Dispute Resolution Department. The Head of Department is Peter Radula-Scott e-mail: pradula-scott@ts-p.co.uk

The team members are -

Raymond Beard - Partner; Solicitor e-mail: rbeard@ts-p.co.uk

John Spence - Solicitor e-mail: jspence@ts-p.co.uk

Alison Sparks - Legal Executive Associate e-mail: asparks@ts-p.co.uk

Mark Steggles - Solicitor e-mail: msteggles@ts-p.co.uk