

TAKING IT PERSONALLY - DEVELOPMENT AGREEMENTS AND THE NEED FOR CLARITY

The Court of Appeal recently issued judgment in the case of First Penthouse Limited v Channel Hotels and Properties (UK) Ltd, Channel Hotels and Properties (UK) Ltd v Tamimi, [2004] 05EG148.

The case is an interesting one as it highlights the need for extreme clarity in development agreements. This decision provides useful commentary on the correct interpretation of the Landlord and Tenant Covenants Act 1995 and the test to determine whether a covenant will be treated as personal. It also considers the problem of once and for all or continuing breaches in the context of forfeiture proceedings, and clarifies the law on refusal of consent to assign. .

THE FACTS

The facts in the First Penthouse case were complex, but can be summarised as follows:

Britel owned the freehold of a block of flats and entered into a Preliminary Agreement with ACP for the development of the roof space and construction of penthouses.

The Preliminary Agreement

Under the terms of the Preliminary Agreement:

- ACP could require Britel to grant a development lease of the roof space.
- ACP had to construct a number of penthouses by an agreed date. A percentage of the proceeds of sale of the penthouses was due to Britel.
- If ACP had not completed the works by the due date, Britel had an option to call for a sublease of any part of the roof space that had not

been developed. The exercise of the option also triggered a payment to Britel of a percentage of the deemed disposal price of unsold penthouses.

- ACP's obligations under the Agreement were guaranteed by First Penthouse ("FP").

The Introduction Agreement

On the same date ACP entered into an Introduction Agreement with Meretz Investments NV ("Meretz"). This provided that ACP should pay Meretz by way of commission a percentage of the net proceeds of sale of the penthouses as consideration for the introduction to Britel..

Subsequent Events

- Britel granted a lease of the roof space to ACP. The lease obliged ACP to carry out and complete the development works as expeditiously as possible and prohibited an assignment without consent.
- ACP charged the lease to FP.
- ACP subsequently also charged the Lease to Meretz to secure sums due to Meretz under the Introduction Agreement.
- Britel transferred its freehold interest in the whole building to Albert Court.
- Albert Court granted an overriding lease to Channel Hotels & Properties (UK) Ltd (CHAPS), so that CHAPS became the immediate landlord to ACP. Under a Deed of Acknowledgement, CHAPS held the overriding lease on trust for CHAPS, Britel and Meretz.
- Various parties, including Britel, FP and Meretz entered into a Deed of Priorities which provided that a new charge was to rank ahead of all

other charges on the lease. The Deed provided that upon discharge, the FP charge should be reinstated as first charge and come into full force. (This was inconsistent with the provisions of the Introduction and Preliminary Agreements in favour of Meretz and Britel which prevented a sale before practical completion and restricted the full and unfettered exercise by FP as mortgagee of the power of sale.) The new charge was subsequently discharged, leaving FP with full powers of sale.

- ACP ran into financial difficulties and FP decided to assign the lease to Mr Tamimi, who had the finances to complete the development. Application for licence to assign was made by FP to CHAPS but was refused, unless Mr Tamimi agreed to accept and be bound by the obligations of ACP in the Preliminary Agreement. The grounds given for the refusal were that ACP was in serious breach of its tenant obligations to carry out the development. Also, the proposed assignment would deprive Britel of the right to exercise its option to call for a sublease of undeveloped units, and Meretz of its commission on the sale of future penthouses.
- The lease was nonetheless assigned to Mr Tamimi without consent.
- CHAPS served a section 146 notice alleging a breach of the lease covenant to carry out the development works expeditiously, and a breach of the covenant not to assign the lease without consent.

THE HIGH COURT

FP applied for a declaration that CHAPS had unreasonably refused consent to the assignment. CHAPS also issued proceedings to forfeit the lease.

The court had to consider whether there was unreasonable refusal of consent to assign the lease. Also, had there a breach of the lease covenant to carry out and complete the development expeditiously? If so, was it a continuing

breach or a once and for all breach? If the latter, had the right to forfeit been waived?

It was common ground that the consequences of the assignment of the lease would be that ACP was no longer liable under the terms of the Preliminary Agreement to complete the development or to grant the development sublease. Also, Mr. Tamimi was not bound to make payments on further sales of penthouses nor to grant the development sublease.

The High Court decided that CHAPS did not seek completion of the development. Instead, it wished to take advantage of the failure to complete on time. CHAPS had waived the right to forfeit the lease for failure to complete the works on time. They had also unreasonably refused consent to the assignment of the lease.

THE COURT OF APPEAL- BREACH OF COVENANT AND THE RIGHT TO FORFEIT

Upholding the decision of the High Court, the Court of Appeal decided that the obligation to complete the works as expeditiously as possible was a once and for all obligation, since it was possible, by referring to the timetable detailed in the Agreement for Lease, to point to a time by which the works should have been completed. However, no steps were taken to forfeit the lease for breach of this covenant. Instead, the lease was affirmed on two separate occasions, including acceptance of ground rent. The right to forfeit had therefore been waived.

THE COURT OF APPEAL-REFUSAL OF CONSENT TO ASSIGN AND EFFECT OF PERSONAL COVENANTS

The Court of Appeal also held that CHAPS had unreasonably refused consent to assign. The Deed of Priorities had conferred on FP the right to override the rights of CHAPS, Britel and Meretz. Consequently, it was unreasonable for CHAPS to refuse consent to assignment on the ground that the assignment

would have the same overriding effect. It was unreasonable in those circumstances to insist that Mr Tamimi also be bound by the terms of the Preliminary Agreement.

Following the recent decision in *Ashworth Frazer Ltd .v. Gloucester City Council* [2001] UKHL 59. The Court of Appeal decided that a landlord is not entitled to refuse consent to an assignment on grounds which have nothing whatsoever to do with the relationship of landlord and tenant in regard to the subject matter of the lease.

The Court considered the effect of S3 and 15 of the Landlord and Tenant (Covenants) Act 1995. This provides that tenant covenants which are not “personal” are enforceable against a tenant’s successors in title by an original landlord (Britel) or by the holder of an overriding lease (CHAPS.) The court held that obligations contained in agreements other than the lease itself could constitute tenant covenants under the 1995 Act. However the covenant to pay commission to Meretz was between parties who were at no stage in a landlord and tenant relationship. The Britel option formed part of the machinery for payment of a premium for the grant of the lease, which is usually regarded as personal.

The court accepted that circumstances can exist where a landlord trustee may be entitled to take into account the consequences of an assignment on beneficiaries under a trust if the consequences have something to with the relationship of landlord and tenant relating to the subject matter of the Lease.

However, in this case the court decided that the considerations relied on by CHAPS had nothing whatever to do with the relationship of landlord and tenant or the subject matter of the Lease. They related to the Preliminary and Introduction Agreements and were personal covenants, totally collateral to that relationship. In the circumstances, CHAPS had unreasonably refused consent to assign.

Conclusion

This decision provides useful commentary on the Landlord and Tenant(Covenants)Act 1995 and the correct test for ascertaining whether a covenant is personal, or one that passes on assignment.

The Court of Appeal confirmed the test for unreasonable refusal of consent to sublet. The reason for the refusal must be directly related to the relationship of landlord and tenant. Personal covenants in collateral commercial agreements will not constitute a valid reason for refusal.

The court will consider the intentions of the parties in deciding whether a covenant is personal. Careful consideration is therefore needed as to whether obligations in development agreements are personal, and what will happen if the landlord cannot lawfully object to an assignment of the development lease.

The complex network of agreements, leases, funding arrangements and options in this case is typical of many development projects. The case demonstrates that each document must be very clear what should happen if the development cannot be completed as anticipated, particularly where an overriding lease is involved.

KEY POINTS

- **Where a specific date is given in a lease for the completion of works, failure to complete on time will constitute a once and for all breach. Any action taken by the landlord affirming the existence of the lease with knowledge of that breach will waive the right to forfeit.**
- **The Court of Appeal confirmed that the reason for refusal of consent to sublet must be directly related to the relationship of landlord and tenant. Personal obligations contained in collateral**

commercial agreements will not constitute a valid reason for refusal.

- **Great care must be taken in the context of Development Agreements to ensure that all agreements are clear as to what will happen if the development is not completed on time.**

1671 words.