

Heads of Terms

All too often Heads of Terms are agreed without consideration being given to a range of wider issues. Below we will consider a number of factors relevant to both landlords and tenants:

Stamp Duty Land Tax implications

We often see Heads of Terms containing a break clause in favour of a tenant which, if structured in a different way, could result in a potential SDLT saving for the tenant.

Consider the following scenario

- L and T agree a 10 year lease at an initial rent of £100,000 pa with a break clause in favour of T at the end of year 5. T's initial SDLT payment will be £6,816. The present SDLT rules do not permit a refund of the tax paid in the event of T exercising its break.
- If T had negotiated a 5 year lease with an option to renew its SDLT liability would be £3,015. T would still have a right to a 10 year term provided it exercised its option though it would have a further SDLT liability on the exercise of the option.

At worst T would not pay any more SDLT but at best would save £3,801

There are, of course, other factors to consider. Landlords (and their agents)



naturally look for as long a commitment from a tenant as possible not least because their banks prefer to see as long a commitment from a tenant as possible notwithstanding the fact that in each of the scenarios the net result for the landlord is the same.

Tenant's banks may also prefer to see longer leases but in the present economic climate perhaps a tenant's financial prudence will be respected and appreciated by its bank! Of course, a longer lease may be more easily assignable and it is essential that the option to renew (or indeed the option to break) is exercisable by an assignee.

The problem with either scenario is that it places a burden on the tenant to serve

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notice in accordance with the terms of the lease and time is almost certainly of the essence. With an effective diary system the potential saving ought to make the risk one well worth taking.

The message is that landlords need not necessarily be frightened by a request for a shorter lease with an option to renew and that tenants should actively consider it and instruct agents accordingly.

Contents of Heads of Terms

It is vital that the Heads of Terms should reflect as accurately as possible the agreement between the parties. In the circumstances it is important that all professional advisers are consulted prior to the final Heads of Terms being agreed. An agreement on any aspect of the transaction is only as good as the advice received. If no advice is sought or received it may compromise the agreement and create delay, additional cost or may possibly jeopardise the agreement altogether.

In addition to the SDLT issues discussed above, parties should consider: the length of the lease; break clauses; whether the security of tenure provisions of the Landlord and Tenant Act 1954 are to be included or excluded; service charges and numerous other miscellaneous matters that may arise.

We strongly recommend the use of the specimen Heads of Terms contained in the Code of Practice for Business Leases. These act as a useful checklist for parties. It's surprising how few agents use these and opt



instead for heads that contain nowhere near enough information. Far too often these defective heads result in delays whilst matters that were never addressed are considered.

Land Registry – Unrepresented Parties

On 10th November the Land Registry introduced new rules relating to the identification of transferors, landlords, transferees, tenants, borrowers or lenders who do not have a conveyancer acting for them.

Land Registry Practice Guide 67 defines 'conveyancer' as a solicitor, licensed conveyance, fellow of the Institute of Legal Executives, barrister, a duly certified notary public or registered European lawyer. It includes in-house conveyancers.

Confirmation of identity when a party does not use a conveyance is required for all transactions where the true value of the land exceeds £5,000 and the transaction involves a

transfer (whether or not for value), transfers relating to the appointment or retirement of trustees, leases, charges, discharges of registered charges, releases, surrenders of leases and applications for compulsory first registration.

A conveyancer acting for a party who is dealing with an unrepresented party will need to confirm that he or she is satisfied that sufficient steps have been taken to verify the identity of the unrepresented party or enclose evidence of their identity. Confirmation is required for any attorneys acting on behalf of a party as well as the donor of the power.

The Land Registry has issued forms of certificates of identity for individuals (ID1) and bodies corporate (ID2). These require information such as name, address, telephone number etc as well as a copy of a passport or photo driving licence and two of a cheque guarantee card or credit card, utility bill (less than 3 months old), council tax bill, mortgage statement or a current firearm or shotgun certificate. They must be postal and not electronic versions.

From a practical point of view it will be necessary to obtain this information at the earliest possible opportunity in order to avoid situations where contracts are exchanged or transactions completed and a party simply walks away which may render an application incapable of registration.

Transactions involving unrepresented parties are relatively rare but a robust approach will, necessarily, need to be taken with such parties in the future given that criminal sanctions apply to the provision of false statement under the Fraud Act 2006.



Advice for Landlords and Tenants of Commercial Property During Difficult Times

The present economic climate has created difficulties for both Landlords and Tenants of commercial property and below we set out some of the dos and don'ts during difficult trading conditions.

DO:

Talk!

Although Landlords and Tenants have,

to a great degree, different needs and desires they do have one common goal – a sensible arrangement that will stand up to the problems created by the present economic climate. If you are a Tenant and are facing problems – speak to your Landlord or the Managing Agent. You never know – they might be prepared to listen and help you. If you're a Landlord – don't ignore your Tenant's cries for help – they could be genuine and you could be left counting the cost of any intransigence if the Tenant's business fails.

Think!

Try to think of sensible solutions to problems. Try to understand the other party's position and plan your strategy accordingly. A little lateral thinking could go a long way. Tenants thinking of assigning could consider sub-letting instead as it may be easier to sub-let to businesses with a weaker covenant strength than it would be to assign the lease and satisfy your Landlord's requirements for a Licence to Assign.

Be reasonable!

Landlords – if you insist that the Tenant adheres to the terms of the lease you could end up driving the Tenant out of business. What is the demand for your type of property? Would you want to pay the business rates on an empty property? A letting at a reduced rent may be unpalatable but far better than no letting at all.

Tenants – do adopt a sensible approach. A clear, well thought out, proposal to vary the terms of your lease may be acceptable to your Landlord whereas an unrealistic one may lead to a speedy end to negotiations.

DON'T:

Tenants – don't bury your head in the sand and fail to pay the rent to the Landlord without having considered the consequences. The Landlord can, and probably will, forfeit your lease. If you are in trouble speak to the Landlord and explore every option available to you.

Tenants – don't over commit yourselves. The longer the term the less likely you are to be the tenant at the end of it. You could end up as a Landlord yourself if you are obliged to sub-let in the event that you no longer need the property and can't assign the lease.

Landlords – don't ignore breaches of covenant by Tenants. Assert your position even whilst negotiating. If you have a defaulting Tenant think of alternative means of recovering any money owed such as a Statutory Demand rather than forfeiture or actions in the County Court. Remember - some Tenants would actually appreciate forfeiture but might be reluctant to risk bankruptcy or liquidation!

Landlords – don't impose unreasonable requirements on a Tenant looking to assign or sub-let and don't delay dealing with a request as you could face a substantial damages award if you do.

And finally, don't forget that there is a lot of property available at the moment. Be careful, take your time and make the right decisions. If you need help contact us to consider your options before committing yourself.

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Stamp Duty Land Tax

Stamp Duty Land Tax (SDLT) celebrated (?) its fifth birthday on 1 December 2008. For Tenants with leases that exceed five years it is a timely reminder that a further SDLT return is required if there is any abnormal increase in the rent paid as a result of a review.

An 'abnormal increase' is generally considered to be an increase in the rent payable excess of twenty percent calculated year on year. In those circumstances there is deemed to be a grant of a new lease from the date when the revised rent became payable. SDLT is payable on the excess rent.

Turnover rents, geared rent and stepped rents will also fall within the abnormal increase rules.

We would advise any Tenants with leases approaching the fifth anniversary to check whether a further return will be required and to speak to us if help or advice is needed.

Pre Budget Report

On 24th November 2008 the Chancellor of the Exchequer delivered his Pre-Budget Report. Of significance for the commercial property world was the re-instatement of empty property relief for commercial properties with a rateable value of less than £15,000 for the year 2009-2010.

Mr Darling also indicated that from early 2009 he would be making it easier for VAT to be applied to supplies of land and property that would otherwise be exempt from VAT. At this stage he has not indicated what the changes might be though it may involve the simplification of the rules relating to options to tax.

Recent Developments

Following the decision of the VAT and Duties Tribunal in *Merlewood Estates Ltd v HMRC* the development of empty roof spaces in blocks of flats will be zero rated for VAT purposes. To qualify, the space must not have been used for residential purposes and it is important that existing tenants do not have access to the space.

The House of Lords decision in the case of *Boss Holdings v Grosvenor* appears to have extended the rights of enfranchisement not only to residential leaseholders but also commercial leaseholders of properties that were originally designed as houses. This is clearly a far reaching decision and of obvious benefit to businesses occupying converted houses who meet the statutory requirements for enfranchisement.

In the case of *Midill (97PL) Limited v Park Lane Estate Limited* and Another the Court of Appeal held that a seller would have the right to retain the deposit paid on exchange when a buyer defaults and the burden of proof is on the buyer to demonstrate that the presumption should be rebutted bearing in mind that even where a higher price was subsequently obtained the seller had borne the risk in the intervening period. The court stated that the buyer would have to prove something special or exceptional to override the presumption. This is unlikely to be a problem that arises often in the foreseeable future!

For further information contact Neil Wright, Head of the Property Department on 020 7317 6769 or email neil.wright@magrath.co.uk