

## **SALES & SUBLEASES**

### **Overview**

A tenant's rights in relation to transfer, sub-letting, alterations, works and change of use are of key importance under a lease. The areas raise common issues. The Landlord and Tenant Acts create certain rights for tenants in relation to these areas which may override what the Lease says. In some cases, it is not possible to agree to the contrary.

Issues in relation to transfers and sub-leases, alterations and works and change of use will frequently come up during the course of a lease. Typically the Landlord's surveyor will negotiate with the Tenant's surveyor in relation to the terms of any consent.

For the very reason that it might be tempting, the Landlord is not entitled to charge a sum of money for any of these consents. He is, however, entitled to his reasonable costs including surveyors costs and legal fees in considering and preparing the terms of a consent licence.

### **Transfers and Sub-Leases by the Tenant**

An assignment is the sale or transfer of the tenant's interest under the lease. A Landlord may have granted the lease or may have purchased an investment property on the assumption on a financially strong and low risk tenant would continue to pay the rent. If the Tenant was to be permitted to transfer the Lease to a person or company of no financial substance then clearly the Landlord's investment may have been devalued.

On the other hand the law seeks to allow the Tenant freedom to transfer and sell its interest. The Lease can, depending on its original terms and the economic climate will be either an asset or a liability. The law seeks to find a balance between the interest of the two parties. Before 1996, the original tenant remained liable under the lease for the entire term. The position in England since 1996 has changed in that even an original tenant may cases to be liable on the lease if he transfers the lease.

A sub-lease is a Lease by the tenant to a further sub-tenant. In this case the Landlord will have no direct relationship with the sub-tenant. It is essential where a landlord grants consent to a sub-lease, that the he reviews its terms carefully as he will be bound by them. It is essential from the Landlord's perspective that the sub-lease contains protections equivalent to those under the lease so that the party in occupation of the premises has obligations equivalent to those of the Tenant.

A landlord should secure that there are tight restrictions on assignment and sub-letting in the lease so that the value of the tenant's covenant is protected and control of the premises is not lost. Most leases provide that a tenant may assign the lease with the Landlord's consent and that the Landlord's consent may not be unreasonably withheld or delayed.

The onus on the Landlord to prove "reasonableness" is, broadly speaking, higher in England and Wales than in Ireland. In Ireland a Tenant who is refused consent, must, in effect go to Court to show that the Landlord is acting unreasonably, if the Landlord does not accept that this is the case. In Ireland, the Landlord does not have to give reasons for refusal of consent and does not have to respond within any time limit. In England, this original legislation was reformed to prevent perceived abuses.

In England, the Landlord is obliged by law to act promptly and give reasons for his decision. If the Landlord fails to so act he can be legally liable to the Tenant for loss incurred by the Tenant. This significantly alters the balance relative to the position in Ireland.

### **Lease Transfers by the Tenant**

"Assignment" is the process whereby a tenant transfers his interest in the property to another tenant and is usually thereby released from the lease obligations. If the Lease says nothing, the tenant is free to assign. Most Leases therefore contain restrictions on assignment.

Unlike in Ireland, it is possible to have an absolute restrictions against Assignment of a Lease. Where this is the case, the Tenant will be at the mercy of the Landlord who

may refuse consent quite unreasonably, subject only to the restrictions imposed by the law on the grounds of sex, race or disability. This kind of provision is usually found in short term Leases.

Nearly all Leases of more than 5 years, allow for the tenant's right to assign subject to the landlord's consent, which is not to be unreasonably withheld. There will usually be an absolute prohibition on dealing with part of the property (e.g. selling part). The Landlord and Tenant Act provides that notwithstanding anything to the contrary where there is a restriction in a Lease in relation to assignment, sub-letting, charging or parting of possession without Landlord's consent, then such consent must not be unreasonably withheld.

Where the Tenant has made an application for consent, the Landlord owes a duty to give its decision on the application within a reasonable time and owes a duty to the Tenant not to unreasonably refuse consent. Giving consent with an unreasonable condition is a breach of this duty. The Landlord must also within reasonable time, serve written notice of its decision specifying any relevant conditions or if consent is withheld, specifying the reason for withholding consent. The burden of proving unreasonableness is imposed on the Landlord.

This is significantly different to the position in Ireland. In Ireland a Landlord can give no reasons and can delay in giving any reason. This, in practice, means that the tenant in Ireland may have lost his prospective assignee by the time he has gone to court to prove the Landlord's refusal is unreasonable. In contrast, in England, the Landlord must give written objective reasons within a reasonable time. The Landlord runs the risk that if he fails to do so or if his reasons are later found unreasonable by a court, he will be liable in damages to the tenant.

In the case of Leases granted after 1996, the Landlord may specify certain terms and conditions which need to be satisfied before he will be give consent to assignment. If the Landlord withholds consent on these specified grounds, he will not be unreasonably withholding consent. If he relies on other grounds, they must be reasonable.

By negotiating terms and conditions where assignment will always be refused, the Landlord will strengthen this position to the Lease. The Landlord can thereby give

prior warning of these circumstances to the Tenant. In contrast, in Ireland, even where specific criteria for consent are inserted in the lease, they will be subject to the overall “reasonableness” test. The fact they are in the Lease will be relevant, but will not prevent a court deciding a refusal of consent is unreasonable.

The legislation contemplates that there two categories of criteria for refusal namely factual or discretionary criteria. Factual criteria might include a requirement that the company is a quoted company or has pre-tax or its net profit equals three times the rent or a requirement that the assignor enters into an Authorised Guarantee Agreement or the assignee procures guarantors.

Discretionary criteria are those which require judgement. This will only be valid if they either provides for an independent third party reference in the event of a dispute or if the Landlord commits itself to making a reasonable determination. An example might be that the Landlord must be of the opinion that a proposed assignee is the equivalent financial standing to the present tenant and that the matter can be referred to an independent third party. Another example of a discretionary condition would be a provision that the assignee must, in the reasonable opinion of the Landlord, be in competition with other tenants.

The above provisions only apply to restrictions on assignments and does not apply to those subletting, mortgaging or sharing conditions. What is reasonable will depend on the entire circumstances. Where the above provisions so apply it will be a matter for the court to decide what is or is not reasonable. The courts have said that the Landlord is only entitled to refuse consent on ground that are based on the relationship of Landlord and Tenant. The Landlord need not prove the conclusions where justified if they were conclusions which might be reached by a reasonable Landlord. The Landlord is usually obliged to consider the application on the basis of its own interests, although there may be cases where there is such disproportion between the benefit of the Landlord and the detriment to the tenant that the refusal could be deemed unreasonable.

The most critical issue will usually be the financial strength of the incoming tenants. Unless specifically stated in the lease, a Landlord would not generally be entitled to refuse consent to an incoming tenant on the basis that he is not of the same financial strength as the outgoing tenant provided that he is of the sufficient strength to pay

the rent and perform the lease obligations. Other considerations which may be relevant, include existing breaches of the leases, the possibility that the assignee might compete with the Landlord and possible devaluation of the Landlord's interest.

Examples of where courts have decided that the refusal consent is unreasonable, include cases where the Landlord has some a personal advantage, and where there are minor breaches of the lease.

Since 1996, an original tenant can cease to be liable on a lease or assignment. To balance this change in the law, a lease may require an "Authorised Guarantee Agreement". In effect this means that upon an assignment, the outgoing tenant will have to guarantee the incoming tenant's responsibility.

### **Sub-Leases by the Tenant**

A sub-lease is a lease by a tenant to a further tenant, usually referred to as a sub-tenant. In the case of a sub-lease the landlord will be required to the terms of the letting. It is vital from the investor's point of view that the sub-lease does not undermine the lease and for this reason leases will often set out in detail mandatory provisions which must be contained in a sub-lease. A sub-tenant can itself obtain statutory rights of renewal and compensation so it is vital that appropriate provision is made in the consent licence document.

A sub-lease can be of all or part of a premises. With a sub-lease there will not usually be a direct relationship between the head landlord (i.e. the landlord under the original lease) and the sub-tenant. However the terms of the consent for the grant of the sub-lease would typically change this position, so that the sub-tenant undertakes directly with the head landlord to comply with the terms of the sub-lease and/or the head lease insofar as they affect the property concerned.

In the case of a sub-lease, the original tenant is fully "on the hook" for the rent and all other obligations. The tenant has rights and obligations under the sub-lease as against the sub-tenant and the tenant remains fully liable on his lease covenants (unlike in the case of an assignment). A landlord would usually require that the sub-

lease rent is at least the current market value rent. It will usually be a requirement that reviews are undertaken in tandem with the Head Licence.

Many of the considerations set out above in relation to assignments will also arise in relation to sub-lettings. A subletting is different to an assignment in that the original tenant remains liable to the Landlord. Although the original tenant will still be “on the hook”, there is no automatic direct relationship between the sub-tenant and the Landlord. It will usually be provided in the terms of the consent licence that the sub-tenant will undertake directly to the Landlord to comply with the obligations in the sub-lease.

A well drafted Lease will specify in detail the types of conditions that must be imposed by a tenant in a sub-lease, (provided the Landlord’s consent is forthcoming). It is essential for the Landlord to ensure that consent is not given for any sub-lease which would alter the balance of the rights between landlord and tenant. Therefore, the sub-lease must be at market value and with no premium. It is essential that the sub-lease covenants comply with the main lease covenants and it would be desirable that there are provisions for rent review in tandem with the head lease rent. Consents for the application of sub-leases would always be considered very careful.

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This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

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