Response to the Law Commission's Consultation Paper 1: models of security of tenure

This is a response to the Law Commission's Consultation Paper 1: models of security of tenure, provided on behalf of the City of London Law Society Land's Law Committee.

About the City of London Law Society

The City of London Law Society represents approximately 21,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The City of London Law Society responds to a variety of consultations on issues of importance to its members through its 22 specialist committees, one of whom is the Land Law Committee.

If there are any questions for the City of London Law Society in relation to this response, please contact Kevin Hart of the City of London Law Society at 4 College Hill, London, EC4R 2RB, email address kevin.hart@clls.org and telephone number 020 7329 2173.

Response

The City of London Law Society's Land Law Committee is pleased to respond to this important Law Commission consultation on models of security of tenure. The use of "we" in the response to the Consultation Questions refers to the City of London Law Society's Land Law Committee.

We respond to the Consultation questions in Chapter 5 of the Consultation Paper, as follows.

Consultation Question 1.

We invite consultees to tell us about any particular considerations or experiences in Wales, which consultees think are relevant to potential reform to the model or scope of security of tenure in Wales.

Response:

We have no response to this question.

Consultation Question 2.

We invite consultees' views as to which model of statutory security of tenure they consider should operate, along with the reasons for their choice of model:

(1) mandatory security of tenure;

(2) no statutory security of tenure (abolition);

(3) contracting-in (so that a tenancy only has statutory security of tenure if the parties opt into a statutory scheme); or

(4) contracting-out (so that a tenancy has statutory security of tenure unless the parties opt out of a statutory scheme) (the current model).

Response:

Our comments on the respective models are included below and some of our comments are separated under particular headings. We have a few further general observations.

As an important point, whichever model is adopted, the changes should only apply prospectively and any transitional arrangements should be carefully considered.

Whichever model is determined by the Law Commission, the legislation should also allow the landlord and the tenant to move from a lease benefitting from security of tenure to a lease without security of tenure, or vice versa without requiring any surrender and/or re-grant arrangement.

Also the current requirement in section 38A(1) of the Landlord and Tenant Act 1954 that the contracting out agreement can only apply to a tenancy to be granted for a term of years certain, should be removed. The decision in "Van Staden" London Borough of Newham v Thomas-Van Staden [2008] EWCA Civ 1414 (29 July 2008) highlights the problems caused by the requirement for a term of years certain. We recommend that this issue is addressed regardless of which model is chosen.

Contracting-in is the preferred model

We consider that the **contracting-in** model of statutory security of tenure should operate.

Business efficacy and problems with the current contracting-out process

The primary reason for this is business efficacy.

The majority of leases that we encounter are contracted out of sections 24-28 of the Landlord and Tenant Act 1954.

The current process for contracting out involving the service of a warning notice and the making of a simple declaration/swearing of a statutory declaration is unnecessarily administrative and problematic.

If there are any defects in the carrying out of the process, the tenant may benefit from statutory security of tenure, even though the landlord and the tenant agreed in the heads of terms (or equivalent) that the tenant would not have statutory security of tenure. There is even a statement in the lease by which the landlord and the tenant agree that sections 24-28 do not apply.

A large amount of time is expended on the contracting out process by prospective landlords and tenants and their respective legal advisors. If a statutory declaration is used, tenants will need to attend an independent commissioner of oaths/solicitor, which takes time and ultimately costs money.

Uncertainties about whether to re-do the contracting-out process

There are uncertainties about whether, and the circumstances in which, the current contracting-out process needs to be re-done if the form of lease changes after the process is carried out, or if there is an

exchanged agreement for lease and a change is required post-exchange to the agreement or the form of lease to be granted, such change occurring before lease completion.

There are also similar issues with contracting-out in an option to renew situation.

In those situations, the landlord's legal advisor will usually consider whether the process should be re-done. Due to the serious consequences for the landlord if the process is carried out incorrectly, a cautious approach may be taken and the contracting out process is re-done, which again takes time, costs money and potentially delays the transaction.

There are uncertainties with the current contracting-out model where the landlord or the tenant changes after the warning notice is served and/or the simple/statutory declaration made, but before the lease is completed.

There are also uncertainties about whether a warning notice needs to be served on, and a simple/statutory declaration needs to be made by, a guarantor (which includes a current guarantor or a guarantor under an authorised guarantee agreement (AGA) or a guarantor of an AGA). The current law is unclear on this point.

Since most leases, from our experience, are contracted out, to adopt the contracting-in model would mean that the contracting-out process, with all its issues, is avoided. It also prevents a tenant unwittingly benefiting from statutory security of tenure, in a situation where that was not the intention of the landlord and the tenant. Also adopting the contracting-in model so that the default position is that there is no statutory security of tenure, overcomes difficulties associated with contractual break rights in the light of the Landlord and Tenant Act 1954. The Act can end up frustrating the parties' intentions that the landlord is contractually entitled to break the lease, by affording the tenant statutory security of tenure, notwithstanding what the lease states on the face of it regarding the landlord's right to terminate.

The situations mentioned above are all examples of why there should not be a prior process (potentially involving a third party) to establish a position on statutory security of tenure. Whichever model is chosen by the Law Commission, there should not be a need for a prior process. We mention below a suggested alternative approach of simply dealing with this in the lease itself.

Why is there a warning notice for contracting out, but not for other lease provisions?

It is also illogical why there is a specific process for advising the tenant on the rights that it is losing by contracting out the lease, but there are no warning notices for other aspects of the lease that may have a more immediate impact such as alienation, repair or rent review – the current process seems to attach undue importance to one particular aspect of the lease.

Considerations where there is an unrepresented party

In a situation where both the landlord and the tenant are legally represented, their respective advisors will advise on whether statutory security of tenure will apply and the implications of this. For an unrepresented landlord or tenant, we consider that the terms of the lease bargain will be better understood with the contracting-in model. The unrepresented party will have a more complete picture, because the lease terms (plus any supplemental documents) will encapsulate the whole deal between the landlord and the tenant and there will be no misunderstanding as to any statutory rights, because none will apply.

By contrast, if the contracting-out model is used, the unrepresented landlord or tenant may not appreciate that the terms of the lease are not the full picture and that statutory security of tenure may apply, either because any required contracting-out process was not carried out or was carried out incorrectly. An unrepresented tenant may not appreciate that staying in the premises a day beyond the end of the contractual term brings section 27 into operation and the tenant is bound for at least another three months.

An alternative to the contracting-out process – a confirmation/health warning on the face of the lease

It is important to learn the lessons of the problems with the current contracting-out model in relation to the proposals for contracting-in. We do not believe that there should be a process (potentially involving a third party such as a commissioner of oaths for a statutory declaration) and, instead, there should be a new contracting-in provision on the face of the lease (whether as an endorsement on the front of the lease, or in its prescribed clauses (where the lease has prescribed clauses) or elsewhere in the lease).

The provision would confirm that the tenant has statutory security of tenure and include a health warning summarising which statutory rights the tenant has, as a result of benefiting from statutory security of tenure. It would be helpful for specific wording for the provision including the health warning to be prescribed in legislation, which can be included in the lease. The legislation should allow for reasonable departures from the wording, such as "or substantially in the form".

We need to ensure that the contracting-in model is not overly prescriptive or administrative and avoids tenants unwittingly not obtaining statutory security of tenure when it was the parties' intention that the lease is protected. If a prior process is avoided and there is a contracting-in provision on the face of the lease, this should address the Law Commission's concerns about disincentivising landlords from offering protected tenancies under a contracting-in model.

Comments on the other models

Contracting-out model

Our next preferred model is the contracting-out model but with significant change.

We understand that this model more clearly highlights to the tenant the statutory rights that it is not receiving. However, as mentioned above, for the model to be retained, it needs significant change.

The current contracting-out process is too administrative and susceptible to error, which can lead to the tenant unwittingly benefiting from statutory security of tenure, and consequential disputes drive potential litigation and additional costs and aggravation.

We, therefore, consider that the warning notice and simple/statutory declaration should be scrapped and replaced by a new contracting-out provision on the face of the lease (whether as an endorsement on the front of the lease, or in its prescribed clauses (where the lease has prescribed clauses) or elsewhere in the lease). The provision would confirm that the tenant does not have statutory security of tenure and include a health warning summarising which statutory rights the tenant does not have. It would be helpful for specific wording for the provision including the health warning to be prescribed in legislation, which can be included in the lease. The legislation should allow for reasonable departures from the wording, such as "or substantially in the form".

We need to ensure that the revised contracted-out model is not overly prescriptive or administrative and avoids tenants unwittingly obtaining statutory of tenure when it was the parties' intention that the lease is not protected.

We should add that while contracting-in is our preferred model, we would have no objection in principle to the contracting-out model, provided that there is no prior process and the contracting-out provision including any health warning are included in the lease.

Mandatory security of tenure

We reject this model. It would be unacceptable to the majority of landlords since it would cause the landlords to lose control of their let premises. Landlords would be unable to ensure that their tenants leave at the end of the contractual term and would have to go through a statutory process to end the tenant's occupation, which may fail or lead to the payment of compensation. This uncertainty as to recovery of the let premises at the end of the contractual term is problematic for where the property is required for re-development, but also for any other purpose that the landlord may have for its property. While we are not valuers, we believe that the impact of this uncertainty would have a significant valuation impact. A landlord may choose to grant its tenants statutory security of tenure, but that should be the landlord's choice for the appropriate transaction.

No statutory security of tenure

We reject this model. We see a place for tenants to have statutory security of tenure for the appropriate transaction, but this should be agreed by the landlord and the tenant.

An argument in favour of this model might be that the parties can agree a contractual lease renewal right which might be more flexible than the statutory model. However, this will mean reinventing the wheel for each transaction with an increased chance of inconsistency and error. While acknowledging that the statutory process can be improved, it does provide greater certainty and predictability, including suitable protections for the landlord and the tenant.

There will be transactions where the investment of the tenant in the let premises justifies more secure occupation rights, or where the state of the letting market gives tenants the negotiating leverage to insist on statutory security of tenure and the legislation should allow for this to be agreed between the parties.

Consultation Question 3.

5.4 We invite consultees' views, together with evidence wherever possible, as to what impact a change to the model of security of tenure will have:

(1) on the parties to tenancies and their advisors; and

(2) on the commercial leasehold market.

Response:

We cover this in our response to Question 2.

In summary, using the contracting-in model ensures that there is less risk of statutory security of tenure being unwittingly granted. This will help to ensure that there is less litigation on esoteric points of the type encountered with the current contracting-out process.

The courts are under huge resourcing pressure and we should strive for a model that reduces the chances of litigation.

The current contracting-out process is a source of professional negligence claims against the legal profession and any model that reduces the number of claims is to be welcomed.

We consider that moving from a contracting-out to a contracting-in model will not have a significant impact on the commercial leasehold market. When heads of terms are agreed by agents for the parties, they are deciding, as a commercial matter, whether or not the tenant is to benefit from statutory security of tenure, not the specifics of the process. That is why we reject the models for Mandatory security of tenure and No statutory security of tenure, because we consider that such models may have a material impact on the market including valuation implications and would take away the parties' rights to agree the position.

In terms of effect on the high street, because the contracting-in model reduces the chances of statutory security of tenure being unwittingly granted, this gives greater assurance to landlords that at the end of the contractual term (or earlier, as permitted by the lease) they have the flexibility to move tenants around, and develop and otherwise use their properties as they wish.

Consultation Question 4.

We invite consultees' views as to whether the existing scope of the 1954 Act is appropriate. In particular, we invite consultees' views as to whether:

(1) the extent of the Use Excluded Tenancies is appropriate;

(2) the extent of the Duration Excluded Tenancies is appropriate; and

(3) there are other types of business tenancy (or business tenancies with certain characteristics) that should be excluded from the scope of the 1954 Act.

We invite consultees' views as to whether their answer would differ depending upon which underlying model for the 1954 Act is recommended.

Response:

Using the numbering above:

(1) We consider that the extent of the Use Excluded Tenancies is appropriate. We do not consider that this should be extended to cover infrastructure leases such as for windfarms (mentioned in the Consultation paper). It will be difficult to define with precision (probably because the arrangements are too technical), which infrastructure should be excluded. In any event, for projects of this magnitude the landlord and tenant will usually have specific negotiations over contractual protections. Our experience is that statutory security of tenure is not a significant commercial point for such transactions.

(2) We can see the benefit of widening the extent of the Duration Excluded Tenancies. We consider that a lease for a term of up to 5 years should be excluded from statutory security of tenure. Prior periods of occupation should be ignored, to simplify the position (currently, prior periods

of occupation encourage landlords to contract out very short term tenancies where there is any doubt as to whether statutory security of tenure applies). The term of leases in the commercial market has over the years become shorter and many leases are for 5 years or less. We consider that by excluding leases for 5 years or less, this will increase certainty as to the landlord's control of its premises at the end of the contractual term and support the overall objective of reducing administration, cost and delay. This exclusion is less significant if the contracting-in model is adopted (since the default position is that the lease is contracted out). It would, however, mean that for leases of 5 years or less, tenants would be unable to contract into statutory security of tenure. In practice, however, our experience is that very few leases of 5 years or less have statutory security of tenure.

(3) We consider that periodic tenancies should be excluded. Such tenancies may slip under the radar on due diligence for the purchase of a property. The fact that they may attract statutory security of tenure is very problematic and they should not be allowed to interfere with the landlord's redevelopment or other plans for its property. When a crucial economic driver is the promotion of growth, landlords should not be constrained in redeveloping properties by statutory rights pursuant to a tenancy that they may know nothing about.

Consultation Question 5.

We invite consultees' views as to whether our assessment of the potential benefits and disadvantages of reforming the scope of the 1954 Act is correct.

Response:

Subject to the points made in our responses to the Consultation Questions, we generally agree with your analysis and congratulate the Law Commission on an excellent consultation document.

Consultation Question 6.

We invite consultees' views, together with evidence wherever possible, as to what impact a change to the scope of the 1954 Act would have:

(1) on the parties to tenancies and their advisors; and

(2) on the commercial leasehold market.

Response:

Please see our response to Question 4.

Consultation Question 7.

We invite consultees to tell us if they believe, or have evidence or data to suggest, that changes to the model of security of tenure, or the scope of the 1954 Act, could result in advantages or disadvantages to certain groups or to individuals based on certain characteristics (with particular attention to age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex, and sexual orientation).

Response:

We do not believe, nor do we have any evidence or data to suggest, that changes to the model of security of tenure, or the scope of the 1954 Act, could result in advantages or disadvantages to certain groups or to individuals based on certain characteristics mentioned in the Question.

Jackie Newstead

Chair, Land Law Committee

City of London Law Society

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