

Unapproved Assignments and Landlord's Remedies

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Desperate times call for desperate measures. Tenants under ever-increasing financial pressure are looking to off-load their lease liabilities to whoever will take them and quickly. What can a landlord do if it discovers that its tenant has made an unapproved assignment of its lease to an assignee of weaker covenant strength?

What is the legal effect of the unapproved assignment?

An assignment in breach of covenant is nevertheless effective to assign the lease¹.

An assignment must be made by deed and must pass the legal estate of the assignor:

Where a lease is unregistrable (i.e. the term has less than 7 years to run), a deed of assignment alone will be effective to transfer the legal estate; there will be a breach of the covenant not to assign as soon as the transfer deed is completed.

Where a lease is already registered or the assignment triggers first registration (i.e. the term has 7 years or more to run), only a deed of assignment followed by registration will be effective to transfer the legal estate; an assignment of a registrable lease that has not yet been registered will result in an equitable assignment and will not be in breach of a covenant not to assign (although it will be in breach of a covenant not to hold on trust or part with possession).

There is no obligation at common law upon either the assignor or the assignee to give notice of the assignment to the landlord.

Liability: against whom does the landlord have redress?

The Assignor and its predecessors in title

A tenant who assigns its lease without first obtaining from the landlord a licence in accordance with the terms of the lease will, in most cases, remain liable to the landlord for the breach of covenant, notwithstanding the assignment or the acceptance of rent from the assignee.

Leases granted prior to 1996

During the term of the lease, the original tenant will be liable to the landlord for a breach that it commits or any breach by a future assignee under the doctrine of privity of contract.

A tenant who has acquired the lease by way of assignment and has assigned over the lease without the landlord's consent will be liable under the doctrine of privity of estate as the breach of covenant has occurred while the lease was vested in it.

Where there has been a chain of assignments, each assignee will usually have given a direct covenant to the landlord in a licence to assign when it was assigned the lease so will remain liable throughout the term for any breaches of covenant by future assignees under the doctrine of privity of contract.



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¹ *Old Grovebury Manor Farm Ltd. v. W. Seymour Plant Sales & Hire Ltd (No.2)* [1979] 1 W.L.R 1397.

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Leases granted after 1995

The Landlord and Tenant (Covenants) Act 1995 (the “**Act**”) does not apply to an assignment in breach of the covenants of a tenancy; an ‘excluded tenancy’ within the meaning of the Act. The assignor will therefore remain liable for any breach that it commits or any breach by the unapproved assignee. However, a release from liability will occur on the next assignment of the tenancy which is not an excluded assignment.

Similarly, if the landlord has an AGA from a previous assignor, such assignor will not be released by the current assignor's unapproved assignment: the landlord will have recourse against the previous assignor until the next assignment of the tenancy which is not an excluded assignment.

Assignor's guarantor

The liability of the assignor's guarantor is subject to the same principles: if the assignor remains liable, the guarantor remains liable. This is, of course subject to the terms of the guarantee which may release the guarantor.

Assignee

Leases granted prior to 1996

The unapproved assignee is liable only for breaches of covenant committed while the lease is vested in him, for privity of estate exists only while the assignee holds the estate: an assignee is under no liability for breaches committed before the lease was assigned to him, unless they are continuing breaches, which an unapproved assignment is not.

Leases granted after 1995

The Act preserves the rule that the assignee of a lease incurs no liability for breaches of covenant committed by the assignor.

However, an assignee who accepts an unapproved assignment in clear breach of the alienation provisions of a lease induces the assignor to breach the lease and therefore commits a tort against the landlord of wrongful interference with contract.

What are a Landlord's remedies for an unapproved assignment?

Accept the assignment but negotiate improved security

The landlord may decide to consent retrospectively to the assignment. A licence to assign should be put in place, at the cost of the assignor/assignee and if the lease is dated after 1995, the assignor should provide an AGA.

Where an assigning party is in an insolvency situation there may be little point in the landlord obtaining an AGA from them, indeed such party may not be able to give an AGA legally (e.g. if it is already in or about to enter into administration). The landlord should seek improved security from the assignee as an alternative, such as a third party/parental guarantee.

Negotiate a further assignment

The parties may negotiate a further assignment to an assignee with a stronger financial covenant (e.g. an associated company of the illegal assignee). If the lease is dated after 1995, this authorised assignment will release the original assignor under the unapproved assignment so the landlord should ensure that both the original assignor and the new assignor enter into AGAs (this is permitted by the Act). The original assignor and the new assignor will remain liable until the new assignee assigns the lease (with consent).

Forfeit the lease

To a landlord who does not want the unapproved assignee as its tenant, re-entry may be the obvious answer but is not commercially appealing during a recession, particularly given empty rates liability.

The lease is liable to be forfeited in the hands of the assignee no matter when the breach occurred, unless and until the right to forfeit is waived. An unapproved assignment is a once and for all irremediable breach therefore any act which is inconsistent with treating the lease as being at an end will waive the landlord's right to forfeit. The acceptance of rent accrued due after the unapproved assignment, once the landlord has notice of the unapproved assignment, will almost certainly amount to a waiver. Thus, as soon as the landlord becomes aware of the unapproved assignment, a quick and pragmatic decision will be required as to whether it is more important to reserve the right to forfeit the lease by returning any rent received after this date or whether it is more important in all the circumstances to receive the rent.

Seek a mandatory injunction to reverse the unapproved assignment

During the recessionary years of the mid-nineties another remedy was added to a landlord's arsenal of weapons. Where an underlease was entered into in wilful breach of a covenant restricting underletting in the headlease², the court held that the tenant and subtenant had intentionally induced a breach of the headlease and that the subtenant had committed the tort of inducing or aiding a breach of contract: to prevent the tenant and

2 *Hemingway Securities Ltd v Dunraven* [1995] 1 EGLR 61.

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subtenant taking advantage of their wrong, an injunction requiring the immediate surrender of the underlease was granted. This decision was upheld in 2005 in *Crestfort v Tesco Stores*³ and was also applied to an unapproved assignment in *Test Valley BC v Minilec Engineering*⁴. The assignee's knowledge that the assignment will be in breach of the lease is paramount.

The assignor and the assignee are likely to counterclaim that the Landlord would have consented to the assignment or that it is unreasonably withholding consent to the assignment. If a tenant concludes that consent is being unreasonably withheld (and that conclusion is correct), it is free to assign the lease because the landlord's unreasonableness effectively removes the tenant's obligation to seek consent⁵. A landlord who seeks an injunction will therefore have to be confident that either:

- The tenant has not made a valid application for consent or the alienation covenant imposes mandatory pre-conditions that have not been satisfied, in which case the landlord is not obliged to consider the application for consent (and no duty under s.1 of the Landlord and Tenant Act 1988 arose)⁶; or
- It is obliged to consider the application for consent but is acting reasonably in withholding consent; this is always a question of fact in each particular case, and any clauses in the lease stipulating when the landlord will be acting reasonably⁷ will be taken into account.

There is a plethora of guidance on the reasonableness test, which is beyond the scope of this article. However, it is worth mentioning that recent case law has shown that where a landlord has genuine concerns regarding an assignee's ability to perform the covenants in the lease, then these are reasonable grounds for refusing consent and further, once the landlord has raised such concerns, the onus will be on the tenant to demonstrate that an assignee is of satisfactory covenant strength and if it fails to do so, a refusal of consent is likely to be reasonable⁸.

A mandatory injunction is an equitable remedy so the court will always retain its discretion to consider what is proportionate and fair in the circumstances. For this reason it is likely that an injunction will only be awarded to a landlord who has 'clean hands' i.e. who has acted reasonably. Further, the court will consider the hardship likely to be caused to the assignee if the injunction is granted. However, an injunction can be granted even if a landlord has suffered no serious damage or inconvenience. If a landlord has acted properly and reasonably and the assignee has accepted the assignment in wilful breach of the alienation provisions, it will be very difficult for an assignee to argue that an injunction is not a fair and proportionate remedy.

A landlord who seeks an injunction should take prompt action, as under equitable principles delay in seeking relief will, after the lapse of what is in the circumstances a sufficient time, amount to a waiver.

Claim damages

The fundamental principle governing the award of damages for breach of covenant is that the injured party must be placed, so far as money can compensate, in the position in which he would have been if the covenant had been observed. Damages should therefore reflect the effect that the breach has on the value of the landlord's reversion. However, it may be very difficult for the landlord to prove damage to his reversion by breach of the alienation covenant so the amount of damages may be nominal.

In *Crestfort*, damages were awarded in addition to the injunction, assessed in the light of what sum the landlord might reasonably have demanded as a premium (at the date of the breach of covenant/commission of the tort) for relaxing the alienation covenant so as to permit the underletting for the period that no injunction was in force.

3 [2005] 37 EG 148.

4 [2005] 2 EGLR 113.

5 *Treolar v Bigge* (1874) L.R. 9 Ex.151.

6 *Allied Dunbar Assurance plc v Homebase Ltd* [2002] EWCA Civ 666. Note that in *Crestfort* (ibid) Lightman J considered that a tenant might raise an argument in estoppel against a landlord who has actually been considering the application.

7 S.22 The Landlord and Tenant (Covenants) Act 1995

8 *The Royal Bank of Scotland v Victoria Street (No. 3) Limited* [2008] EWHC 3052 (Ch).

A note on virtual assignments

A tenant may not have completed a legal assignment but may have virtually assigned its lease, whereby the economic benefits and burdens of the lease (including any management responsibilities) are transferred to a third party without a legal assignment of the leasehold interest or a change in the occupancy of the premises in question.

Virtual assignments have been used widely to avoid the requirement for landlord's consent on the basis that where there is no legal assignment there is no breach of a covenant not to assign without consent. This view was recently upheld by the court⁹. However, the court also held that the effect of the virtual assignment amounted to a parting with or sharing of possession and as such any covenant in a lease preventing the same without consent was breached.

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⁹ *Clarence House Limited v National Westminster Bank PLC* [2009] EWHC 77 (Ch).

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