Falcon Chambers

"Navigating the Quays to Consent: Lessons learnt from No. 1 West India Quay (Residential) Limited – v – East Tower Apartments Ltd"

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1. Qualified covenants against assignment and section 1 of the Landlord and Tenant Act 1988 are like a pair of old comfortable slippers that we can find in our sleep and amble about in without really having to turn on the brain. We do so safe in the knowledge that nothing really changes in this area of the law and that our tried and tested procedures would comfortably withstand judicial scrutiny if it ever came to that. The decision in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* [2016] EWHC 2438 (Ch) is a salutary warning against that kind of complacency. In today's talk, we will consider the decision to see where and how we might all need to think again.

The Facts

2. *No. 1 West India Quay* held a headlease of a block of 158 flats. East Tower Apartments held long underleases of 42 of those flats. The underleases were in standard form. They contained a covenant against assignment, with an express proviso that consent should not be unreasonably withheld, and a tenant's covenant to pay any costs incurred

by the landlord in consequence of an application for consent to assign (irrespective of its outcome).

3. The parties fell out over service charges and the tenant decided to sell its underleases. The first few assignments passed without incident, the landlord having imposed no conditions other than payment of its legal costs (of £1,250 plus VAT). However, when it came to two of the later applications for consent, the landlord sought to impose the following conditions on the grant of consent:

   (i) Provision of a UK bank reference for any prospective assignee;

   (ii) An inspection of the flats to take place prior to the grant of consent and an undertaking to pay the landlord's surveyor's fees for that inspection in the amount of £350 plus VAT;

   (iii) An undertaking to pay the landlord's legal costs associated with the assignment in the amount of £1,250 plus VAT.

4. When the tenant declined to pay the costs of the inspection, the landlord refused consent. In the proceedings that followed, the tenant contended that all three conditions had been unreasonable. HHJ Walden Smith agreed on all three counts.

5. Whilst the proceedings primarily concerned the reasonableness or otherwise of the landlord's *refusal* to consent to two of the proposed assignments, the tenant also sought a declaration that the landlord had unreasonably *delayed* the grant of consent, in breach of the duty in section 1 of the Landlord and Tenant Act 1988 ("the 1988 Act"), in respect of a third application for consent to assign.

6. The tenant's claim for breach of the statutory duty in section 1 of the 1988 Act turned on the question of when time started to run for the purposes of the legislation. The lease provided that any application for consent must be served on the landlord at its *registered* office. However, the landlord had sent out a "sales pack" to the tenant, at the time of its acquisition of the underleases, in which the landlord stated that any application for consent to assign should be sent to the landlord at an *alternative* address. The tenant's first letter requesting consent was sent to the address given in the sales pack (some 47 days before the application was determined); a second letter was send to the registered office (14 days before the relevant determination).

(1) Bank References

7. The first instance Judge found that the requirement for provision of bank references was an unreasonable requirement because:

   (i) The assignees were paying hefty premiums for the underleases which, in and of itself, showed that the assignees were of financial substance.

   (ii) If, following the assignment, arrears of service charge accrued, the landlord could forfeit the lease which, in turn, would either lead to the windfall of vacant possession or payment of the arrears as a term of relief.

   (iii) If the assignee acquired the underlease with the aid of a mortgage, the mortgagee would almost certainly step in and pay the arrears in order to protect its security by avoiding the forfeiture.

8. On appeal, Henderson J was not impressed by any of those arguments. He noted that, in one of the textbooks on the subject, it was said that the provision of bank references was "invariable" practice. It was difficult to see how the landlord could be stigmatised as having acted unreasonably if its actions were standard industry practice.

9. The fact that the assignee had paid a large sum of money to acquire the underlease did not, of itself, eliminate the possibility that the assignee would thereafter fail to comply with the covenants in the underlease. The funds for the purchase might have been provided by way of gift from a family member or alternatively with the aid of a mortgage that would then need to be serviced. In either case, the risk of default by the assignee remained a real one and the landlord was entitled to seek reassurance about that.

10. Moreover, the mere fact that the landlord had certain remedies, in the event of *default* by the assignee, which might ultimately result in the breach being remedied, either by the assignee or its mortgagee, did not disable the landlord from taking steps to ensure that the proposed assignee would comply with the covenants in the first place.

11. The tenant offered an additional reason for upholding the Judge's conclusion on this issue, namely that the requirement for bank references had been tactically (rather than genuinely) imposed, bearing in mind that bank references had *not* been sought in respect of the previous assignments. That argument foundered on procedural, rather than substantive, grounds. The proceedings had been Part 8 proceedings with no

cross-examination of the witnesses who provided the witness statements. Accordingly, the landlord's explanation for the change in policy[1] had not been challenged in evidence and the first instance Judge had not been at liberty to go behind it.

(2) The Inspection and associated costs

12. The first instance Judge had concluded that the landlord had been unreasonable in requiring the tenant to permit and pay for an inspection for these reasons:

    (i) There was a general right to inspect, in the *Jervis v Harris* clause, which enabled the costs of that exercise to be recovered if and only if the tenant was found to be in breach; the alienation covenant did not itself confer a right to inspect when an application for consent was made.

    (ii) On the facts, there was no particular reason for the landlord to suppose that the tenant had been in breach of the repairing and alterations covenants in the underleases;

    (iii) Even if an inspection were justified, there was no need for it to be undertaken by a surveyor (at a cost of £350 per inspection); a managing agent would be just as capable of spotting breaches of the repairing and alterations covenants.

13. Henderson J said that those arguments had apparent force to them, but that, in the final analysis, they did not justify the conclusion that the landlord had been acting unreasonably for these reasons:

    (i) The terms of the *Jervis v Harris* clause were of little assistance; the covenant to pay the landlord's costs associated with an application for consent was more in point. Significant breaches of the tenant's repairing and alterations covenants may found the basis for a reasonable refusal of consent to assign and accordingly it was reasonable for the landlord to find out whether there were any such breaches by inspecting. That was so irrespective of whether the landlord already had grounds to suspect the existence of a breach.

[1] The landlord had said, in its written evidence, that it had taken on a new in-house assistant solicitor, who had reviewed the landlord's procedures and recommended that bank references be requested from now on.

(ii) Not every significant breach of the repairing and alterations covenants would be apparent to the untutored eye and, accordingly, it was not unreasonable for the landlord to want his surveyor to conduct the inspection.

(iii) £350 was not an unreasonable amount for the landlord to charge for that exercise.

14. Accordingly, the landlord's ground of appeal against this aspect of the first instance Judge's decision was also upheld.

(3) Legal Costs

15. The landlord sought to justify the £1,250 plus VAT charge on the basis that:

(i) The charge covered the costs of (a) liaising with managing agents to ascertain whether there were any breaches, (b) contacting the assignor's solicitors, (c) preparing a draft licence to assign (it used a standard form document) and considering any suggested amendments, (d) arranging an inspection and considering the results of that inspection and (e) arranging the engrossment of the licence.

(ii) The majority of the work was to be carried out by an experienced, in-house solicitor whose charge out rate was £400 p/h.

(iii) Quotations obtained from two (external) firms of solicitors showed a range of £1,350 and £1,500 plus VAT for the equivalent services.

16. Henderson J concluded, by reference to two Upper Tribunal decisions,[2] that the guiding principles were that (i) an application for consent was not an opportunity for the landlord to obtain any element of profit and (ii) the reasonableness or otherwise of the landlord's figure fell to be judged by reference to the work necessitated by the typical or the actual case – not the full gamut of tasks that might conceivably be undertaken in response to an application for consent. Henderson J held that the first instance Judge's decision, that the reasonable costs associated with the two applications for consent was no more than £350 plus VAT per application, was a decision that she had been entitled to reach on the evidence before her.

[2] *Holding & Management (Solitaire) Ltd v Norton* [2012] UKUT 1 (LC) and *Proxima Ltd v Dr Thomas D McGhee* [2014] 0059 (LC).

The overall result

17. The outcome of the appeal was therefore that two of the landlord's reasons for refusing consent were found to be reasonable (bank references and inspection costs), whilst one of them (legal costs) was unreasonable. It was common ground that where a landlord has both good and bad reasons for refusing consent, the refusal will be legitimate unless the bad reasons vitiate the good ones.[3]

18. Here, however, the landlord had indicated, in correspondence with the tenant, that it was "not prepared to proceed with [the application]" unless and until an undertaking for payment of both the (reasonable) £350 plus VAT costs of inspection and the (unreasonable) legal costs of £1,250 plus VAT was provided. Henderson J held that it was therefore clear that, even if the tenant had agreed to provide the bank references and to pay for the inspection, the landlord would not have been prepared to grant consent in the absence of an undertaking for payment the full legal costs. It followed that the good reasons for refusal were indeed vitiated by the bad reason such that the landlord was held to have unreasonably refused consent to assign.

Section 1 of the 1988 Act – unreasonable delay

19. The tenant contended, both below and above, that the landlord had made an unequivocal representation that applications for consent should be sent to the sales pack address and that the landlord was therefore estopped from contending that the application had not been made when the tenant's initial letter had been sent to that address. The landlord maintained that there had been no such representation and that, even if there had, effect should not be given to the putative estoppel because the effect would be to undermine the purpose of the 1988 Act (which provides, in s.5(2), that time only starts to run once a contractually valid application for consent is made).

20. Henderson J held that the contents of the sales pack should not be read as an unequivocal representation that the tenant need no longer send applications for consent to the contractually agreed address. Instead, the sales pack merely invited tenants to send applications for consent, informally, to another address in the hopes that they might be resolved by agreement, without the need for a formal (time-pressured) application to be made. But the Judge concluded that if a clearer representation about service had been made, the estoppel would not have fallen foul of the principle that

[3] See para 11.139 of Woodfall, cited with approval by Henderson J.

equity should not frustrate statutory purpose. The 1988 Act sought to prevent landlords from unreasonably refusing or delaying consent. That purpose would be furthered, not thwarted, if a landlord were held to a clear representation about where the application for consent should be sent.

Lessons for the future

21. What lessons do we learn from the decision in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* and how should we modify our approach to future applications for consent? I would tentatively suggest the following:

(1) *Bank references*: It will now be a brave tenant who declines to provide bank references for their assignee when requested by a landlord. It is not a particularly onerous requirement to comply with and the risk of derailing an otherwise unobjectionable application for consent is clear from the decision in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited*. That is not to say that a landlord now has an absolute right to require provision of bank references. If, for example, that the proposed assignee is obviously of financial standing (eg. David Beckham or Vodafone), that might be different. If the proposed assignee was known to be a cash purchaser who intended to sub-let, rather than occupy, the flat, a tenant might be able to persuade the Court the rental income would self-evidently exceed the outgoings on the flat and that the provision of bank references in such circumstances is beyond that which might reasonably be required. But even that is perhaps unduly simplistic because, if the assignee has other financial liabilities (ie beyond those associated with the flat), there is no guarantee that the rental income would not be diverted elsewhere. So unless we are in the David Beckham/Vodafone scenario, the counsel of perfection for the tenant is to comply with a landlord's demand for references.

(2) *Inspection*: In principle, at least, *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* provides powerful support for the proposition that it is *not* unreasonable for a landlord to inspect in response to an application for consent in order to check that there are no significant breaches of covenant. But, as ever, this a fact-sensitive issue. If, for example, the landlord inspected the flat a fortnight before the application was made, in the exercise of its general right to

do so under the lease, it might conceivably be unreasonable to do so again in response to an application for consent.

(3) *Costs of inspecting*: If, as was the case in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited*, the lease expressly entitles the landlord to be paid any 'out of pocket' expenses associated with an application for consent, it is all but certain that payment of the reasonable costs of an inspection, by the landlord's surveyor, may be required as a condition of consent.[4] If there is no equivalent indemnity provision in the lease, the same result would probably still follow, but there would be a bit more scope for the tenant to argue the contrary (if it is feeling brave). As far as quantum is concerned, £350 plus VAT is, at least in the residential context, a reasonably safe figure for the landlord to adopt. In the 'plain vanilla' residential case, anything above that figure would invite challenge.

(4) *Legal Costs*: Landlords will now need to think much more carefully and conservatively about the quantum of legal costs undertakings. Until now, landlords have regularly been demanding undertakings of anything between £500 - £2,000. Tenants will now say that £350 plus VAT represents the ceiling for (legitimate) undertakings. Whilst landlords will need to be able to justify any advance on £350, it is probably going too far to suggest that £350 is now a standard tariff. It should be recalled that the appeal, in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited*, was by way of review rather than rehearing. £350 was a figure that Henderson J found the trial Judge was entitled to reach, on the evidence before her – it did not necessarily represent the appellate Court's view about the appropriate figure. Moreover, the figure of £350 was adopted by the trial Judge in a case where the landlord had an in-house solicitor preparing a succession of licences to assign. A more generous amount might well be tolerated in a case where the landlord was dealing with a 'one off' application and needed to instruct solicitors for the first time. Clearly, if the licence to assign will require more than standard form provisions and/or is likely to necessitate specific negotiation between the parties' solicitors as to its terms, that, too, may entitle the landlord to require a more significant undertaking.

[4] Although *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* was a residential case, it would seem still more likely that a landlord under a *commercial* lease would be entitled to require payment of those costs.

(5) *Costs undertaking as a threshold requirement to further consideration of the application:* The reason why the landlord's perfectly good reasons for refusing consent did not carry the day in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* is that the landlord had indicated that unless an undertaking for the full amount of the legal fees was given, the application for consent would not receive further consideration. This is an eminently avoidable trap. If there is even the slightest suspicion that the legal costs undertaking might be open to challenge, the costs undertaking should *not* be expressed as a threshold requirement to further consideration of the application; it should simply be included amongst the list of other conditions that the landlord is minded to impose.

(6) *Part 7 or Part 8?* If a tenant believes that the landlord has imposed conditions which, whilst apparently reasonable, were imposed for purely tactical purposes associated with defeating the application (as distinct from *bona fide* protection of the landlord's property interests), the tenant will need to be astute to ensure that the proceedings are started and in any event concluded in Part 7 proceedings. If, as is common, the proceedings are progressed to trial under Part 8, there is unlikely to be any cross examination of the landlord's representative(s) and any challenge to the landlord's *fides* will founder for that reason alone.

(7) *Mixed Messages*: Whilst the tenant's estoppel argument in *No. 1 West India Quay (Residential) Limited v East Tower Apartments Limited* failed on the facts, it is clear that a clearer representation about the address or method of service might disable the landlord from taking a technical point at a later stage. Landlords and tenants should take heed of the contractual requirements for service of consent applications when assessing the question of when time starts to run. As ever, the counsel of perfection in cases of doubt is: do *both*.