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# ADR FORUM

**Glamorgan Business Centre**
University of Glamorgan, Treforest, Mid Glamorgan
Friday 29th April 2005

# LANDLORD AND TENANT DISPUTES

## Paper

## "Regulatory Reform (Business Tenancies) Order 2003 : Renewable business leases"

By

Gerwyn Griffiths and Professor Michael Stuckey

Law School
University of Glamorgan

# "The First 300 Days – a Look Back at the Regulatory Reform (Business Tenancies) (England and Wales) Order 2003"
# Renewable business leases

by Professor Michael Stuckey* and Gerwyn Ll. H Griffiths*

## INTRODUCTION

In marked contrast to those other major leasehold sectors which have a statutory framework or code to regulate them, (agriculture, residential and public sector) the area of the business tenancy [1] has, until recently, remained free of the rapid changes in the law which have characterised the others. Until as recently as ten months ago, the legal framework was, essentially, that put into place fifty years ago by Part II of the Landlord and Tenant Act 1954.

Indeed, Michael Haley, writing in 1999 commented that

> *"The controls established in 1954 have, remarkably, survived almost intact and, subject to some fine tuning, may continue to do so"*[2]

Equally surprisingly, when changes were finally introduced, a new piece of primary legislation was not felt to be necessary Changes were introduced under the Regulatory Reform Act 2001 by the Regulatory Reform (Business Tenancies) (England and Wales) Order 2003 (SI 2003/3096). The basic structure of Part II of the Landlord and Tenant Act 1954 has of course been retained, but its provisions have been amended. Thus, in dealing with disputes involving business leases the practitioner needs to be acquainted with: Part II of the 1954 Act in its amended form; subordinate provisions contained in the Order and new regulations made under the 1954 Act (including new statutory notices).

The changes came into force on 1 June 2004, but they are not retrospective. Now, some ten months later[3], the time seems opportune to revisit the actual changes made, evaluate their actual and possible effects and consider appropriate strategies. We take the view that the greatest source for potential problems is the ability given under the Order for contracting out, and for this reason we look in detail at this and make some suggestions in matters such as drafting, interpretation and procedure which may help both to prevent future problems and resolve them if they do arise

## THE KEY CHANGES- COMMENT AND EVALUATION

### 1 Agreements to exclude security of tenure

The system of having to obtain the court's approval to contract out of the security of tenure of Part II has been abolished. Instead, there has been substituted a prior "health warning" notice served by the landlord.

### 2 Surrenders

Agreements to surrender now need no special arrangements or court approval, but there are safeguards similar to agreements to exclude security of tenure (above).

* Professor and Head of the School of Law and Reader in Equity and the Law of Property, respectively, of The University of Glamorgan. Gerwyn LL H Griffiths acknowledges the comments of Professor Peter Luxton on an earlier draft of this paper

1 The term' business tenancy' is used because the great majority of Government publications use this term. It is, however, the authors' contention that a better description is that of 'the renewable business lease' since it is only when the period of the original tencnay comes to an end that the distinctive features marking out such a lease from any other come into play

2 Haley, " The Statutory Regulation of Business Tenancies- Privater Property, Public Interest and Politicial Compromise" [1999] *Legal Studies* 207

3 The "Three Hundred Days " of the title

## 3 Termination by the tenant

There is clarification of what the tenant must do to avoid its contractual obligations extending beyond the agreed date for the end of the lease (*i.e*. 3 months' notice, or quit by the end of the lease)

## 4 Notices requiring information

The parties are required to update information for six months (*i.e*. on transfer of interests) and there are more effective enforcement procedures

## 5 The Landlord's Termination Notice

Landlords not opposing renewal are required to set out their proposals for a new tenancy in the landlord's termination notice. Such proposals have to be accompanied by a "health warning"[4] informing the tenant that it is not obliged to accept the terms.

## 6 Procedures for Renewal and Termination

The old- and often criticised- regime of the tenant's counter-notice (in response to a landlord's termination notice) is abolished. The final deadline will be the date in the landlord's s 25 notice or the day before the date specified in the tenant's s 26 request. The parties can agree to extend the deadline for applications to the court (to enable further negotiations to take place) without having to go to court.

## 7 Applications to the Court by the landlord

Now, under the new provisions, the landlord is able to apply for renewal (so countering any delay by the tenant), or for termination and no renewal. In the latter case:

- if court agrees that the landlord has grounds of opposition to a new tenancy, then it will refuse the order for a new tenancy;
- if landlord fails to establish ground of opposition, court will order grant of new tenancy (and fix the terms) without the need of a separate application by the tenant

## 8. Ownership and control of business

A major feature of the Order was that the ownership and control provisions have been rationalised, so that Part II now applies to business entities separate from the landlord or tenant named in the lease, provided that they are under the same effective control. Tenants are thereby placed in the same position as landlords.

## 9. Interim rent

Tenants are now able to apply for an interim rent. Rules on timing of the interim rent have been changed to remove any incentive for delaying the renewal proceedings. The method of calculating the interim rent has been changed with a view to its being fairer to both parties.

## 10 Compensation

The tenant is now able to claim compensation from the landlord where the tenant was induced not to apply to the court or to withdraw an application for a new tenancy because of misrepresentation. (Previously, of course, the tenant could claim compensation from the landlord for misrepresentation only where the court had refused to grant a new tenancy by reason of the landlord's misrepresentation).

## 11 Other changes

- A tenant wishing to terminate a continuation tenancy does not now have to give more than three months' notice (*i.e*. it is no longer necessary for the continuation tenancy to end on a Quarter Day).

[4] Considered p 5, *infra*.

- The court is able to order the grant of a new lease for up to fifteen years (instead of 14 as previously), as this will fit more conveniently with three- and five-yearly rent reviews
- The procedure can be used where there is a single lease but several different landlords

## A PARTICULAR ISSUE
## PROBLEMS OF CONTRACTING OUT UNDER THE NEW REGIME

The old provision of the 1954 Act, (s 38(4)) which provided for contracting out of Part II with the approval of the court, was, of course, repealed (2003 Order, para 21(2)). Instead, the parties are able to contract out, without court approval, where the landlord serves a prior notice (a health warning[5]) on the tenant. The new contracting-out provisions do, we feel, give rise to a number of potential problems which will become more apparent and for this reason we consider it in some detail

### 1. Impact of the transitional provisions

***(a) conditional agreement entered into before 1 June 2004***

If the parties entered into an agreement before 1 June 2004 to contract out of Part II (*i.e.* an agreement subject to the approval of the court), the old regime for contracting out applies. The court's approval is therefore still required, even after 31 May 2004. This is clear from Article 29 of the 2003 Order, which states (words in square brackets are not part of the Order):

> **(4) If a person has, before the coming into force of this Order,** [*i.e.* before 1 June 2004] **entered into a agreement to take a tenancy, any provision in that agreement which requires an order under section 38(4) of the Act to be obtained in respect of the tenancy shall continue to be effective, notwithstanding the repeal of that provision by Article 21(2) of this Order, and the court shall retain jurisdiction to make such an order.**

*Drafting point: Where the (conditional) agreement was entered into before 1 June 2004, but the lease is itself granted on or after that date, the lease should itself recite the date of the agreement pursuant to which it is made. This is particularly important where the court order approving the contracting out was itself also made on or after 1 June 2004. The recital is to ensure that there can be no argument at any future time about when the agreement was made and so whether the lease was validly contracted out or not*

***(b) court approval obtained before 1 June 2004, but no agreement before that date.***

Under the old regime, the application to the court could be made before the lease had been granted, or before any contract for a lease had been entered into. In these circumstances, the application to the court had to append a draft contract or lease. The agreement between the parties (a contract, or the grant of the lease) would then be entered into only after the court order had been obtained.

What is the position if the parties, not being contractually bound at that time, applied to the court, and the court made an order approving the contracting out before 1 June 2004, but the parties only become contractually bound (whether by entering into an agreement or by entering into the lease without any prior agreement) after 31 May 2004?

[5] For an informative discussion of this concept, see Hewitson: "Reform of Business Tenancies Legislation" [2002] *Conveyancer and Property Lawyer* 261

The answer turns upon the interpretation of the relevant part of Article 29(2) of the 2003 Order:

> **(2) Nothing in this Order has effect in relation –**
> **(a) to an agreement –**
> **(ii) which was authorised by the court under section 38(4) of the Act before this Order came into force** [*i.e.* before 1 June 2004]

There are two possible interpretations, which turn on whether the words "before this Order came into force", apply to the agreement or to the authorisation of the court:

(i) The words may refer to the agreement. If this is correct, then even if the parties have obtained a court order before 1 June 2004, the order is effective only if the parties contract (or enter into the lease without prior contract) before 1 June 2004. If they fail to meet this deadline, then the new regime will apply, so if contracting out is to be valid, the landlord will have to service the health warning notice.

(ii) The words may refer only to the authorisation of the court. If this is correct, then provided the court order was made before 1 June 2004, then any lease made pursuant to it is contracted out under the old regime, even if the parties only became contractually bound after 31 May 2004.

It is clear on either interpretation that the court would not be approving "an agreement" at the time, since this would then still be only a draft agreement or draft lease; but the Article evidently means that the court is approving what later becomes "an agreement", *i.e.* it is a figure of speech.

We would suggest that the first interpretation is the correct one, applying the principle that legislative changes are not presumed to have retrospective effect. If the second interpretation were correct, then the effect would be to nullify a court order obtained before 1 June 2004 where the parties had not proceeded to agreement by that date. However, we cannot be sure which is the correct interpretation until this is clarified by the court.

## 2. Only a tenancy for a term of years certain can be contracted out

The new contracting-out regime is contained in a new section, s 38A, to the LTA 1954, Part II (2003 Order, para 22(1)), the relevant parts of which are as follows:

> **Agreements to exclude provisions of Part 2**
>
> **38A. –(1) The persons who will be the landlord and the tenant in relation to a tenancy to be granted for a term of years certain which will be a tenancy to which this Part of this Act applies may agree that the provisions of sections 24 to 28 of this Act shall be excluded in relation to that tenancy.**

- As under the old law, it is possible to contract out of the security of tenure provisions under Part II only in respect of a tenancy for a term of years certain. A periodic tenancy is not for this purpose a tenancy for a term of years certain: *Nicholls v Kinsey* [1994] 1 EGLR 131 (CA).
- An attempt to use the 'new' procedure to contract out in relation to a periodic tenancy will result in the tenant's obtaining the protection of Part II.
- A tenancy is for a term of years certain even though it contains break clauses; so the parties can achieve a similar result to the forbidden contracted-out periodic tenancy by the grant of a fixed-term lease with break clauses on either side exercisable regularly, *e.g.* every year of the term.

## 3. The health-warning notice

Section 38A(3) provides:

> **(3) An agreement under subsection (1) above shall be void unless –**
>
> **(a) the landlord has served on the tenant a notice in the form, or substantially in the form, set out in Schedule 1 to the Regulatory Reform (Business Tenancies) (England and Wales) Order 2003 ("the 2003 Order"); and**
>
> **(b) the requirements specified in Schedule 2 to that Order are met.**

***(a) the form of notice***

The form of notice set in Schedule 1 to the 2003 Order is as follows:

**"FORM OF NOTICE THAT SECTIONS 24 TO 28 0F THE LANDLORD AND TENANT ACT 1954 ARE NOT TO APPLY TO A BUSINESS TENANCY**

To: …….

[Name and address of tenant]

From: ……

[Name and address of landlord]"

So, we can see that the form is very simple:

– the names and addresses of the tenant and the landlord are the only pieces of information that need to be inserted;

(although these need to be correct – suppose a minor error in one of the names, *e.g.*

- the name of the tenant company?;
- change in identity of contracting parties after serving notice?
- cf ***Brighton and Hove City Council v Collinson*** [2004] 21 EG 150 (CS)

***Brighton and Hove City Council v Collinson*** [2004] 21 EG 150 (CS)
Here the court had approved a contracted-out lease to a company under the old procedure. After the court's approval, the solicitor for the company's directors, on the advice of the company's accountant, suggested that they would prefer if the lease were granted, not to the company, but to directors (who were brothers). The prospective landlord agreed, and a lease reciting the fact that it was contracted out, was later granted to the brothers. When the lease expired, the tenants, the brothers, argued that the lease had not been contracted out, since the court had approved a contracted-out lease to the company, not to the brothers. This argument succeeded in the lower court, but failed in the Court of Appeal. The brothers had been parties to the application for contracting out as they had been intended to be guarantors, they were aware of the effect of contracting out of Part II, and the court would have had jurisdiction to approve a contracted out lease to them. (The court approved its earlier decision in ***Palacegate***, considered below).

So the court there was unwilling to allow the technicalities of the application to defeat the contracting out. But will this same relaxation apply under the new regime? No, since the landlord's notice must be served on the person who is to be the tenant. Had the circumstances in the ***Collinson*** case occurred under the new regime, a landlord's notice served on the company would not have been a valid notice in respect of a lease later granted to the brothers.

- There is no requirement that a draft lease or draft agreement for a lease are attached - indeed, the form itself does not even seem to require that the parties have agreed (subject to contract) all the terms of the lease;
- But it is important for the landlord that there is evidence at the time of service of a draft lease or draft contract that the parties have already agreed (subject to contract in each case) at the time the notice is served. Why?: because s 38A(1) requires the notice to be served in relation to a tenancy "to be granted", and that seems to require that the parties have already agreed the terms of the tenancy (subject to contract) at the time the notice is served.

  Is agreement (subject to contract) of "heads of terms" (*i.e.* material terms) sufficient?
- It *might* be argued that it is sufficient if the parties have agreed the main terms to be included in the lease at this time, without having agreed all the exact wording of the lease. It depends whether the principle under the old law established in ***Receiver for the Metropolitan Police District v Palacegate Properties Ltd*** [2001] Ch 131 still applies.
- In the ***Palacegate*** case, the district judge had approved the contracting out of a draft lease for a term of five years at a specified rent; but the draft lease left gaps to be filled in: the date of the lease, the date for commencement of the term, the date of the proposed exclusion order, and also the time for the payment of the rent. This last omission meant that, by implication of law, the rent was payable in arrears. After the court's approval, the lease granted took the form of the draft with the gaps filled in, and provided for the payment of the rent quarterly in advance. Towards the end of the term, the landlord received a section 26 request for a new lease from the tenant, which argued that the lease had not been contracted out, since (the tenant argued) it did not conform to the draft lease approved by the district judge. This argument succeeded at first instance, but failed in the Court of Appeal. The Court of Appeal took the view that section 38(4) was intended to enable the court to satisfy itself that the prospective tenant understood that it would be forgoing the protection of ss 24-28 of the 1954 Act. It pointed out that s 38(4) used the words "in relation to that tenancy", and this did require that that terms of the actual lease should bear a substantial similarity to that previously approved by the court. It drew a distinction between material and non-material changes – only the former would nullify the approval obtained. On the facts of the case itself, the solicitors for both parties agreed that there had in fact been an agreement for rent to be payable in advance, so that the draft lease, by omitting this, did not represent the agreement of the parties; the Court of Appeal was clearly unwilling to allow the tenant to acquire security of tenure through a mistake, and treated the term for payment or rent as immaterial.
- Note that the new s 38A(1) also uses the expression "in relation to a tenancy". This suggests that the ***Palacegate*** principle might well survive, so that agreement (subject to contract) of the material terms is sufficient. What would be the material terms? From ***Palacegate***, these appear to be terms that might well affect a tenant's decision to enter into a contracted-out lease – so the length of the term is material, since a tenant is less likely to wish to incur large capital expenditure on premises under a short lease where there is no prospect of renewal under the Act. For the same reason, the presence of a break clause would be material, as would be the identity of the premises to be leased, and the rent to be paid. The precise date of commencement of the term, however, would not be material; and a change in the tenant's address between the draft agreement and the grant of the lease would also be immaterial (as was admitted by the tenant in ***Palacegate*** itself).

- Reliance on the ***Palacegate*** principle under the new contracting-out regime is rather dangerous from the landlord's point of view, as we cannot be sure that the courts will apply it to the new regime. The risk for the landlord is that that the tenant (or a successor in title) may later argue that, unless it had notice of the precise wording of the draft lease at the time the notice was served, it could not be said that it had the requisite notice. The landlord therefore needs evidence that the notice relates to the lease that is actually granted later. So to preserve such evidence, it might be best to attach the (subject to contract) draft lease or agreement to the notice sent to the tenant. Furthermore, the lease itself should contain a declaration that the notice served related to the lease itself.

  *Procedural tips:*

  – *unless and until the Palacegate principle is held to apply to the new contracting-out regime, the landlord should ensure that the exact terms of the lease have been agreed (subject to contract) at the time the notice is served;*

  – *such agreement must be "subject to contract", as the notice must precede the tenant's becoming contractually bound;*

  – *in order to preserve evidence of such (subject to contract) draft lease or agreement, it might be best to attach such document to the notice sent to the tenant; and*

  – *if the parties agree any changes to the (subject to contract) draft lease or after the notice has been served, the landlord should serve a fresh notice on the tenant (even though such notice will be identical to the first).*

  – *if the parties agree any change to the identity of the prospective tenant after the notice has been served, a fresh notice should be served on the new prospective tenant.*

  *Drafting point: the lease when granted should contain a declaration that the notice served related to the lease itself.*

  This drafting point is belt-and-braces if the draft lease or agreement (subject to contract) was annexed to the notice, but even then it is useful in case the notice and accompanying draft has been lost.

***(b) the period of the notice***

According to Schedule 2,

- if the notice is served on the tenant no less than 14 days before the tenant enters into the tenancy to which it applies, or (if earlier) becomes contractually bound to do so, then the tenant must make a declaration in the form (or substantially in the form) set out in paragraph 7.
- if the notice is served on the tenant less than 14 days before that time, then, the tenant or a person duly authorised by him to do so, must before that time make a statutory declaration in the form, or substantially in the form, set out in paragraph 8.

So the basic difference is that an *ordinary* declaration suffices for the longer period, whereas a *statutory* declaration is required for the shorter period.

The Order clearly envisages that normally the parties will use the longer period, but it is understood that in practice most contracting out since 1 June 2004 has occurred less than 14 days before the agreement or lease is entered into, so that the statutory declaration route is becoming the norm. From the landlord's point of view, unless it can rely on the *Palacegate* principle, it is vital that the draft lease has been drawn up (subject to contract) by the time the notice is served, and the tenant will usually be anxious to move in and start trading, and may not wish to have to wait a further 14 days.

**What is the 14-day period?**

The notice for the 14-day period must be served no less than 14 days before the tenant becomes contractually bound. So it is necessary to count forward 14 days from the date of service to ascertain the earliest date the contract or lease can be made.

So if the notice is served on Monday, 6 September 2004, the earliest date that the parties can become contractually bound (or enter into the lease) will be Monday, 20 September.

***(c) method of service***

Recorded delivery is evidentially desirable; and since s 23 LTA 1927 applies to notices served under the 1954 Act, the notice will be deemed to be served at the date the letter is handed to the Post Office (discussed further under Service of Notices in Business Tenancies below).

**4. The tenant's declaration**

***(a) The forms of declaration***

The form of declaration where the 14-period of notice is given is as follows (para 7):

I ……...…….

(*name of declarant*) of

……...……

(*address*) declare that –

**1**. I/

……...……

(*name of tenant*) propose(s) to enter into a tenancy of premises at

……...……

(*address of premises*) for a term commencing on

……

**2.** I/The tenant propose(s) to enter into an agreement with

…….

(*name of landlord*) that the provisions of sections 24 to 28 of the Landlord and Tenant Act 1954 (security of tenure) shall be excluded in relation to the tenancy.

**3.** The landlord has, not less than 14 days before I/the tenant enter(s) into the tenancy, or (if earlier) become(s) contractually bound to do so served on me/the tenant a notice in the form, or substantially in the form, set out in Schedule 1 to the Regulatory Reform (Business Tenancies) (England and Wales) Order 2003. The form of notice set out in that Schedule is reproduced below.

**4.** I have/The tenant has read the notice referred to in paragraph 3 above and accept(s) the consequences of entering into the agreement referred to in paragraph 2 above.

**5**. (*as appropriate*) I am duly authorised by the tenant to make this declaration.

DECLARED this

……

day of

……

**To:**

……

[*Name and address of tenant*]

From:

……

[*name and address of landlord*]

The form of statutory declaration (where the declaration is made less than 14 days after the service of the notice) is as follows (para 8):

I ……

(*name of declarant*) of

……

(*address*) do solemnly and sincerely declare that –

**1**. I/ ……

(*name of tenant*) propose(s) to enter into a tenancy of premises at

……

(*address of premises*) for a term commencing on

……

**2**. I/The tenant propose(s) to enter into an agreement with (name of landlord) that the provisions of sections 24 to 28 of the Landlord and Tenant Act 1954 (security of tenure) shall be excluded in relation to the tenancy.

**3**. The landlord has served on me/the tenant a notice in the form, or substantially in the form, set out in Schedule 1 to the Regulatory Reform (Business Tenancies) (England and Wales) Order 2003. The form of notice set out in that Schedule is reproduced below.

**4**. I have/The tenant has read the notice referred to in paragraph 3 above and accept(s) the consequences of entering into the agreement referred to in paragraph 2 above.

**5**. (*as appropriate*) I am duly authorised by the tenant to make this declaration.

**To:**

……

[*Name and address of tenant*]

**From**:

……

[*name and address of landlord*]

AND I make this solemn declaration conscientiously believing the same to be true and by virtue of the Statutory Declaration Act 1835.

DECLARED at

……

this

……

day of

……

Before me

(*signature of person before whom declaration is made*)

A commissioner for oaths or A solicitor empowered to administer oaths or (*as appropriate*)

### *(b) Timing of the declaration*

There is no express requirement for the tenant to wait the 14 days before making an ordinary declaration (in the form in para 7); so it might be possible for the tenant to make the declaration the day it receives the notice, and the lease will still be validly contracted out provided the parties do not enter into the lease until the end of the 14-day period. Nevertheless, it seems to be *implicit* in clause 3 of the declaration that at least 14 days have past since the notice was served (since how else could the tenant declare that the notice was served not less than 14 days before the tenant becomes contractually bound?).

### *(c) Who can make the declaration?*

Whether an ordinary or a statutory declaration is made, who else can make the declaration? Somebody authorised by the tenant to do so (Schedule 2, paras 3 and 4). If the declaration is made by somebody other than the tenant, the landlord should ensure that there such person is duly authorised to make the declaration, and that evidence is preserved of such authorisation.

Procedural tips: where somebody other than the tenant makes the declaration, the landlord should:

- ask for a copy of the tenant's authorization, and
- ensure that such copy is kept with the relevant documents

Drafting point: where somebody other than the tenant makes the declaration, the landlord should ensure that the lease should include a statement that the person who made the declaration was duly authorized by the tenant to make it.

### *(d) Note or endorsement in the lease*

A reference to the notice, and the declaration (whether ordinary or statutory) must be contained in or endorsed "on the instrument creating the tenancy" (Schedule 2, para 5).

(The declaration cannot itself be in the lease, or the agreement for a lease, since the declaration is that the tenant *proposes* to enter into a contracted-out lease: the declaration must therefore precede the agreement or lease).

Nice point here whether this means the agreement for the lease, if the parties enter into a contract for a lease after the declaration is made, or whether it means the lease itself. Probably not practically significant, since in most instances the parties will proceed directly to the lease without a prior contract; but, an agreement for a lease is also protected under Part II of the 1954 Act (s 69(1)) ("tenancy" includes an agreement for a lease), and the contracting-procedure must apply to an agreement for a lease, whether or not a legal lease is executed later. Therefore, if there is a prior contract, then it is prudent to make the reference in both the contract and the later lease.

## 5. Later variations of the lease

If the lease has been effectively contracted out of the protection of Part II, what is the effect of any subsequent variation of the lease between the parties?

- If the purported variation involves a change in the estate (the identity of the demised premises, or the length of the term), then it is new lease (on the principle in the Court of Appeal in ***Friends' Provident Life Office* v *British Railways Board*** [1996] 1 All ER 336).

  If therefore the landlord wishes the new lease also to be contracted out, the landlord needs to serve a fresh notice and obtain the tenant's appropriate declaration before the variation is binding on the parties.

- If the variation does not involve a change in the estate, *e.g.* a change in the manner of calculating the rent at review, the contracted-out lease simply continues as varied, so no fresh notice procedure is required.

## 6. Contracted-out sub leases.

### Guarantors

The new provisions appear to raise potentially insoluble problems for landlords in respect of guarantors.

> A common form of guarantee requires the guarantor to enter into a new lease in his own name when requested to do so by the landlord in the event of a disclaimer or surrender of the lease by the tenant's liquidator or trustee in bankruptcy. The new lease is typically on the same terms for the unexpired reside of the existing lease. Such obligation of a guarantor has been variously described as:
>
> - a *conditional obligation*, the contingency being a timeous demand made by the lessor (***Coronation Street Industrial Properties Ltd* v *Ingall Industries Ltd*** [1989] 1 WLR 304 (HL) (Lord Jauncey); and
> - a *conditional contract*, which becomes unconditional, binding and specifically enforceable upon the landlord's request (***Re a Company (No 00792 of 1992) ex p Tredegar Enterprises Ltd*** [1992] 2 EGLR 39, 40 (Mummery J))

A lease entered into since 1 January 1996 is a new lease for the purposes of the Landlord and Tenant (Covenants) Act 1995 (LT(C)A 1995). Under a post-1995 lease, a tenant's liability under the lease ends on a lawful assignment, but the landlord may be able to require the tenant, on assignment, to enter into an AGA, under which the tenant guarantees the liability of its immediate assignee only. An AGA may require the tenant to enter into a new tenancy in the event of the tenancy's being disclaimed after assignment, but only if the term of such tenancy expires no later than the term of the tenancy assigned, and if the tenant covenants which it contains are no more onerous than those of that tenancy: LT(C)A 1995, s 16(5)(c).

When a post-1995 lease is granted, there are therefore likely to be two sorts of guarantors:

- guarantors of the original tenant (*e.g.* where the company is the tenant, its directors); and
- the original tenant as potential future guarantor of its immediate assignee under an authorised guarantee agreement (AGA)

Unfortunately, the new contracting-out provisions do not indicate how they apply to a guarantor who can be required to enter into a lease in its own name. Since a health-warning notice must be served before the tenant becomes contractually bound, it is crucial to determine the moment at which the guarantor's obligation to enter into the lease arises.

Can the obligation of a guarantor to take up a lease at some time in the future in the event of the disclaimer of the lease by the existing tenant's trustee in bankruptcy or liquidator be characterised as an agreement to take such a lease?

There is as yet no answer, but we would suggest that:

(i) an original tenant who enters into a post-1995 lease under which it can be required to provide an AGA on assignment should not be treated as being bound to take a lease under such possible future AGA *from the moment it enters into the original lease*. The obligation to enter into an AGA does not depend solely on a request by the landlord, but on the tenant's proposing to assign. The obligation does not arise until that future time, and it is within the tenant's power to ensure that any obligation to provide an AGA never arises.

(ii) a stronger argument can be put that the obligation of a guarantor to take a new lease arises only *from the moment it enters into the guarantee*; but even this is debatable, since it is subject to the default of the tenant under the lease as well as to the demand of the landlord.

The words of s LTA 1954, 38A(1), "to be granted" seem simply to point to the future, so this sub-section does not seem to give any guidance; but the tenant's declaration forms refer to the tenant's "proposing" to enter into an agreement to exclude security of tenure in relation to the tenancy –the word "proposing" might seem inappropriate when the tenant's obligation is not immediate

(iii) the third possibility is that the obligation of the guarantor to take a new lease arises only *from the moment that the landlord actually demands that it do so*.

From the landlord's point of view, (iii) is the best view, since it considerably reduces the number of notices that need to be served, and declarations that need to be obtained. But remember that, if (ii) turns out to be correct, then, even if the landlord serves a notice before it enforces the guarantee, and the guarantor makes the declaration, the guarantor could later argue that the lease it has taken is not contracted out, since it was already bound to enter into the lease before it was served with the notice and made the declaration.

*Drafting point: If (ii) is correct, then the clause restricting assignment need to be amended appropriately. It should provide either:*

- *that it is reasonable for the landlord to refuse consent to assign unless and until the guarantor has been served with a contracting-out notice and has made the appropriate declaration; or*
- *that the making of the appropriate declaration by the guarantor (following service of the notice upon it) is made a condition precedent to the tenant's acquiring a fully qualified right to assign.*