



**Real
Estate**

Winter 2020

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News in brief



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Support for tenants during Covid-19

The government has put in place a range of measures to provide extra support for tenants:

- The Corporate Insolvency and Governance Act 2020 made some temporary changes to insolvency law to provide support to those in financial difficulty. The temporary ban on presenting winding-up petitions based on statutory demands for unpaid rent (served on or after 27 April 2020) has now been extended to 31 March 2021.
- The protection from commercial rent arrear recovery (CRAR) has been extended until 31 March 2021. From 25 December 2020, the minimum net amount that must be outstanding before CRAR may be enforced is 366 days' rent.
- The protections from forfeiture for non-payment of rent for business tenancies have been extended to 31 March 2021.

Stamp Duty Land Tax on residential purchases

To boost the housing market following the pandemic, the SDLT nil rate band for residential property purchases increased from £125,000 to £500,000 for transactions with an effective date between 8 July 2020 and 31 March 2021. This change applies

whether or not a buyer has owned a home before.

Business rates

Businesses in the retail, hospitality and leisure sectors in England will not have to pay business rates for the 2020-2021 tax year, due to Covid-19.

Environment and Sustainability

Energy White Paper

On 14 December 2020 the government published the Energy White Paper, which sets out the government's ambitions for a clean energy system as the UK transitions to net zero carbon. The white paper targets emission-free electricity generation by 2050.

The white paper sets out the government's aims to support a green recovery from Covid-19, including supporting up to 220,000 jobs in the next 10 years.

The white paper also aims to keep consumer bills affordable by making the energy market truly competitive. This includes making it simpler to switch to a cheaper energy tariff and tackling loyalty penalties, by testing whether consumers could automatically be moved to cheaper contracts.

Net Zero Review (interim report)

A few days after the Energy White Paper, the Treasury published its interim Net Zero Review report, which informs the next steps in the UK's green transition. The report did not make any policy recommendations, but found that although the UK has made significant progress in decarbonising its economy it needs to go much further to achieve net zero. The final report will be published in spring 2021.

Environmental Bill 2019-21

This important Bill sets out the framework for all things environmental post Brexit and contains key environmental objectives across a wide range of issues, for example, air and water quality, waste and recycling. The Bill will now be carried over to the next Parliamentary session, with Royal Assent expected in the autumn.

Lease health check – planning for your future



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“With the continued uncertainty, now is the time to review your occupation of your premises and assess your options”

We have made it through a tumultuous 2020. Most of us navigated a temporary return to the office by making our premises Covid-19 secure. Our immediate priorities were to complete enhanced risk assessments and to put in place increased hygiene measures, one-way systems, distanced workstations and provisions for continued remote working.

We are now in the midst of a third lockdown and Brexit has taken place.

Even with the fantastic news of the vaccine, there are uncertain times yet to come, and now is the time to review your occupation and assess the options available. What can you do now to secure the future of the workplace for the longer term?

1. Expiry date

If your lease is coming to an end, you need to check whether or not you have a protected tenancy. This will determine whether you need to serve a notice to bring your lease to an end or negotiate rights for continued occupation.

2. Break rights

If you intend to exercise a break right, you need to make sure you comply with any pre-conditions, serve the relevant notice, and move out in time. Failure to strictly comply

with any pre-conditions could invalidate the break. If you have had any rent concessions, then you will need to do a careful review of what has been paid and what is owed.

Farah's article on page 20 has more on break rights.

3. Alienation

If you want to dispose of your premises you need to check your lease to make sure you can do this. This can either be done at lease expiry, by exercising a break right or by sub-letting, assigning or surrendering your lease.

If you are assigning or sub-letting, you will need to make sure you can find a suitable tenant to take over the space. In both instances you will almost certainly have a continuing liability as you will either remain the head tenant or enter into an authorised agreement guaranteeing the performance of the incoming tenant.

If none of those options are attractive or possible, you could ask your landlord to take a surrender of your lease. Your landlord does not have to agree and is likely to require a lump sum payment if a surrender is agreed.

Amy's article on page 17 explores this topic in further detail.

4. Rent and service charge

When is the rent review? Is there scope to negotiate a lower rent now in exchange for the landlord having the certainty of your continued occupation?

Is there a service charge cap or can one be negotiated now as part of collaboration between landlord and tenant as to the future management of the building?

With the need to reduce carbon emissions drastically there may be scope to negotiate cleaner ways of running the building and apportioning the service charge between tenants to take account of any changes.

5. Alterations

Do you need to make alterations now to ensure a more stable working environment for long-term social distancing? If you are seeking to sub-let, then you will need to carry out works to divide the premises. Review your lease provisions carefully as you are likely to need a licence to alter.

6. Use

If you are considering repurposing your space, perhaps bringing multiple sites together, remember that any alterations to your premises could require landlord's consent, and any possible changes to your IT may require wayleaves as well as

landlord's consent.

You might be thinking of creating a hub space, to be shared with other organisations. This would require you to review your lease to make sure you can share space and carry out the necessary alterations – and you may need planning consent for change of use.

Conclusion

In the midst of constant change this can be an opportunity for organisations to trial using their premises to create their strategy for the future.

1. Review your lease
2. Review your organisational needs
3. Create your property strategy for the future.

Fixed fee packages

We are currently offering two fixed fee packages for landlords and tenants to help you with your real estate needs:

- (a) a lease review of your options to terminate or vary your lease and
- (b) a rent concession guidance.

[Find out more here.](#)



Heads of terms

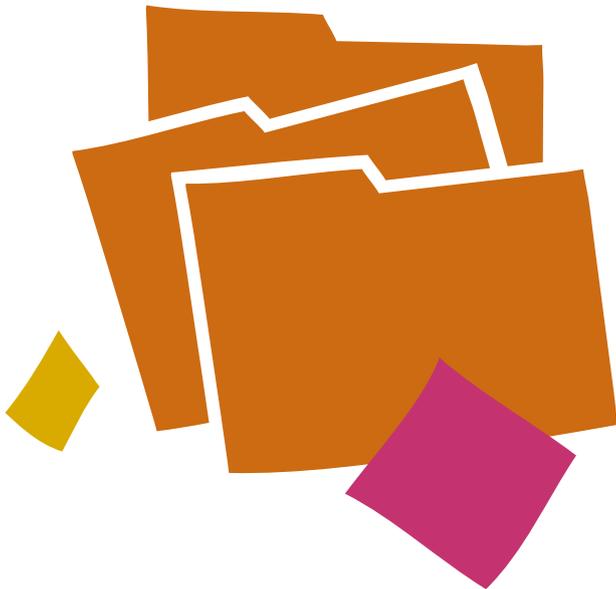


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“A well-drafted heads of terms can avoid commercial discussions and delays down the line”



Heads of terms set out the key commercial terms that have been agreed between the parties.

A well drafted set of heads of terms will help the transaction run smoothly and avoid unnecessary commercial discussions and delays down the line.

What can you expect in heads of terms?

These are key terms you would expect for a lease transaction for a floor of an office block.

- Property – a detailed description and accurate plans are crucial. Both sides should be clear as to exactly what is being demised.
- Parties – the names, company registration numbers and registered addresses of the landlord and tenant. If there is a guarantor involved, its details should also be listed here.
- Term – how long is the lease for? If there are any break rights, are they landlord or tenant or both? These should be set out here, together with any conditions to the break.
- Security of tenure – is the lease to benefit from the security of tenure provisions of the Landlord and Tenant Act 1954? If so, the tenant has a right to

automatic renewal of the lease. If not, the tenant must vacate the property unless it negotiates a new lease with the landlord.

- Rent – what is the annual rent? Is this an inclusive rent – including service charge and insurance? What is the frequency of payment – quarterly or monthly basis are the norm. Is there a rent-free period?
- Rent review – is there a rent review and, if so, how often and on what basis? The usual basis is open market rent or using the RPI index.
- Rent deposit – does the tenant need to provide a rent deposit? What is the amount and what are the repayment terms?
- Service Charge – if the property is part of a building, service charge is likely. What is the proportion payable and how is this calculated? Is there a service charge cap?
- Insurance – the landlord usually insures the building with the tenant contributing towards the premium. What is the tenant's proportion? Is terrorism covered?
- Use – what is the permitted use of the property?

Real Estate team

We can advise you on the full life cycle of your property assets, including supporting you on development projects and funding, as well as buying, selling and landlord and tenant matters.

We'll solve disputes. We also handle planning and tax issues, as well as insolvency and receivership.

If you're a charity, we'll also make sure you understand your responsibilities and how charity law affects your property plans.

To assist our clients to navigate the coronavirus crisis, we're offering fixed fee packaged services:

[Covid-19 fixed fee packages](#)

- Repair – the tenant is usually responsible for the repair and maintenance of its internal demise and the landlord for the common parts and external and structural elements of a building. Is the tenant’s repairing obligation limited to a schedule of condition or is it full repair?
- Alterations – what is the tenant permitted to do? External and structural alterations are usually prohibited. Internal and non-structural alterations are normally permitted with landlord’s consent, not to be unreasonably withheld or delayed. Does the tenant have to remove all alterations at the end of the lease?
- Alienation, that is, the ability to dispose of the property – is the tenant able to assign, underlet or share its property?
- Other specific rights granted or reserved – these include car, motorcycle or bicycle parking rights; rights to use any communal shower and changing room facilities; rights to use the personnel / service / goods lifts; rights to use communal garden / rooftop space; and rights to use communal toilets in the building. What is available and offered will depend on the type of building and bargaining power of the parties.
- Conditions – do the parties need to obtain board approval? Are there any third-party consents, such as the landlord’s bank / lender or the superior landlord’s consent?
- Advisers’ details – the details of the parties’ agents and solicitors usually appear at the end.

Lease Code 2020

The RICS Lease Code 2020, which came into effect on 1 September 2020, has a template heads of terms and checklist and also sets out lease negotiation best practice and a guide for landlords and tenants.

Conclusion

Agreeing these key commercial points at the outset will help the transaction run smoothly. It is well worth seeking advice from professional advisers when you are negotiating any heads of terms.

Rent reductions – mitigate the impact of Covid-19



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Rent reductions

With the significant economic impact of Covid-19 and the associated closure measures, many organisations are having to modify their strategies to adapt and survive.

Tenants of commercial property should consider whether to seek a renegotiation of their rent payment obligations. Any renegotiation should be done in good faith, and the government has encouraged those businesses that are able to pay full rent to continue doing so.

In order to obtain a concession from your landlord both parties will need to be flexible. You should be transparent and prepared to share to an appropriate extent any relevant financial information in order to support your requests.

Many landlords will try to be accommodating, but will have their own financial commitments to assess, including potentially their own rent obligations if they are not the freeholder.

Without an agreed renegotiation between the landlord and the tenant, the legal position remains that you must continue to comply with the obligation to pay rent. So, if

you are struggling with the rent you should raise this with your landlord at the earliest opportunity.

There are various options to consider when renegotiating rent payment obligations:

1. Rent reduction

You should consider the amount and time period of any reduction. This will largely depend on your individual circumstances.

2. Rent-free period

This could cover any time of enforced closure. However, if you are struggling financially you may wish to request an additional rent-free period.

3. Landlord and tenant to split the cost for the unoccupied period

This could relate to any period of enforced closure, or any other time that you have decided to keep the property closed. If you are in a more secure financial position, then this is a more equitable option than a rent-free period.

4. Change the frequency of the rent payments

It is common in commercial leases that the rent is paid quarterly, but you may

find that paying rent monthly helps with cashflow.

5. Rent varied to the current market rate

The current market rent may be lower than your existing rent. This needs careful consideration and you may wish to speak to a surveyor or agent before requesting this. If you have not had your rent reviewed in a long time, the current market rent could be higher than your previous rent.

6. Rent linked to turnover

This will be particularly relevant for retail or hospitality businesses. The amount of rent to be paid could be linked to a percentage of your turnover. If your turnover is lower, you would pay less rent. Retail businesses who already have turnover 'top-up' rent provisions may wish to remove the requirement to pay base rent and instead pay rent based solely on turnover.

7. Waiver of the requirement to pay interest on arrears

It is standard that a tenant will need to pay interest on any unpaid and overdue sums, and the amount of interest will depend on the lease. The landlord could waive the requirement to pay interest and arrange a payment plan with the tenant for any overdue rent.

8. Drawing from rent deposits

It is usually a requirement that if the landlord withdraws from the rent deposit then the tenant must 'top up' the deposit to its full amount. You could agree that the landlord may withdraw from the rent deposit, but on the understanding that the deposit is not topped up until it is reasonable for you to do so.

Tenants should be aware that landlords may request a change beneficial to them in exchange for the above. For example, removal of a tenant's break right or an extension of the lease.

It is important to consider how any changes would affect you both now and in future. We suggest that you carefully consider all potential options before contacting your landlord, so that you are fully prepared and understand your opportunities and limitations.

Any renegotiation that is agreed should be formally documented in a deed of variation or a side letter. We recommend that you obtain legal advice on such documents to ensure that you are adequately protected.

Repurposing your office space



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“It may be that it is not the size of your space, but how it is laid out that is the issue. Any internal alterations may need landlord’s consent”

Many organisations will be considering their longer-term strategy for survival. Office space is often a large expense, so it is a good time to review whether the space you occupy still meets your needs.

Most occupiers of office space have a leasehold interest – you should check the terms of the lease carefully to ascertain what rights you have and what conditions may be attached.

If your office space no longer meets the needs of your organisation but it is not the right time to move, you may wish to consider some of the following options.

Underletting of part

If permitted by the lease, it will usually require landlord’s consent, which should not be unreasonably withheld or delayed. There may be other conditions for the terms of the underlease. It is worth establishing these at the outset to inform discussions with any possible undertenants.

Sharing with a group company

It is common for modern leases to allow companies within the same group as the named tenant to occupy the same space. This will not usually require landlord’s consent, but the landlord should be kept informed about who is in occupation.

Desk licences

This is a more informal arrangement to an underletting of part and permits third parties to use individual desks and to use communal areas and facilities. This has not been favoured by landlords, but the trend towards more agile and flexible working has forced landlords to be more accommodating. It is likely that your lease prohibits sharing of occupation (other than with group companies) – so desk licences would be in breach. However, a landlord may still agree with suitable parameters – such as a limit to the number of desks licenced at any one time and notification requirements.

Alterations to redesign the space

It may be that it is not the size of the space but its configuration that is the issue. If alterations will allow you to make more efficient use of the property, you first need to ascertain the changes that would be required. A tenant is usually able to make non-structural internal alterations, but the lease may require landlord's consent. You should submit detailed drawings and specifications to the landlord for approval at the earliest opportunity.

It may be that your office space no longer meets the needs of your organisation but none of the above options are available

or suitable. If you need to leave your office space, you will need to consider:

Break clauses

If there is an option to bring the lease to an end prior to the contractual end date, you will need to check whether there are any specific break dates and conditions that must be met in order for any break notice to be valid.

Take a look at Farah's article on page 21 for more details on break clauses.

Assignment

This involves disposing of your interest in the remainder of the term of the lease to a third party who will step into your shoes as tenant. Landlord's consent will be required and should not be unreasonably withheld or delayed where the incoming tenant is able to satisfy the landlord that it can comply with the tenant obligations under the lease.

Underletting of whole

Your lease may allow you to create a further leasehold interest in favour of a third party, so that you will be the landlord of the space. You remain liable for the tenant covenants, but the obligation to comply will be passed on to the undertenant in the underlease.

Break rights and the pandemic



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As a result of the ongoing pandemic a number of organisations are reviewing their operational needs. In a number of cases this means that their current office space is no longer required. As such, organisations are looking to utilise the break right to bring their lease to an end early.

For this to be successful, you must strictly adhere to any pre-conditions set out in the lease for the exercise of the break right. Otherwise the landlord could hold the tenant to the lease after the break date.

Like almost every aspect of life, compliance with these pre-conditions can be affected by the current pandemic.

The most common pre-conditions found in break clauses are:

1. Provision of vacant possession on the break date; and
2. Payment of all rents and other sums due under the lease up until the break date.

A less common – but more onerous – pre-condition that can sometimes be found in a break clause is:

3. Material compliance with all of the tenant’s obligations under the lease.

“You must strictly adhere to any pre-conditions set out in the lease for the exercise of the break right”

Taking these in turn:

1. Vacant possession

Providing vacant possession means you must hand the property back empty of people, furniture and tenants' fixtures and fittings, and having terminated any third-party rights of occupation.

This is not normally a big issue, but during the 2020 lockdowns this became a real problem and is likely to be the case during this third lockdown. Even when restrictions start to ease, it might take longer to move, so you should factor this into your calculations and discuss it with your landlord as early as possible if you may not be able to provide vacant possession by the break date.

2. Payment of sums due under the lease

Tenants who have sought any rent concessions during the pandemic should ideally have ensured the concession was properly documented in a side letter, taking account of the effect this might have on the exercise of any break right.

If the concession was that the rent payment was delayed, then this might have to be paid in full to protect the right to break.

3. Complying with the tenant's obligations under the lease

This is an onerous obligation at the best of times. If a financial settlement cannot be agreed regarding dilapidations, then – again – you will need to consider the timing of the break, as reinstatement and dilapidations works are taking longer to conclude due to the pandemic.

Break options can also be a useful negotiating tool at this time. Landlords are likely to want certainty of income by having a tenant remain in situ.

You may, therefore, want to consider the option of forfeiting an upcoming break right in return for a lower rent or the right to surrender part of your demise where the entire space is no longer required.

If you are looking to exercise a break right, or you want to consider other options to terminate or vary your lease we would be happy to help.

Karli's article on page 6 has details and a link to the two fixed-fee packages we currently have on offer to assist with these.

Reflections on post-Covid-19 lending



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“Office use will evolve, with property strategies based on how buildings add value and support productivity”

The rebound predicted for GDP in 2021 will depend on the coronavirus being relatively contained.

What has this meant for lending and what trends do we see emerging?

Residential – Higher LTVs have been significantly affected and banks are scrutinising even more carefully the ability to repay. Volumes fell sharply in Q2, picking up a little in Q3. At the time of writing – just before the latest lockdown – enquiries have remained resilient.

Buy to Let – London rents have come under greatest pressure, with average rents across the capital falling by 7%. Outside London most areas have seen small rent rises. The mortgage market was pretty much back to normal towards the end of 2020, although some lenders have become cooler on high LTVs and also on student lets and HMOs.

Mainstream commercial lending – Lenders continue to be busy with lending under CBIL – Coronavirus Business Interruption Loan scheme – preferring a government guarantee. This has led private banks and specialist lenders to reoccupy the market as they did in 2008. With the CBIL scheme ending, we expect to see an increased appetite to lend from mainstream lenders, with the cost of borrowing unlikely to rise.

Valuations – Retail and leisure valuations have been hardest hit. Yields for offices have seen only a slight increase while food stores and distribution are pretty much unchanged.

RICS Chief Economist, Simon Rubinsohn, has said:

“As the economic impact of Covid-19 has deepened, so too has the impact on commercial real estate. Sentiment among investors and occupiers has naturally weakened, with broad acceptance that rental and capital values will fall over the next year.

What is clear, however, is that there will be no going back to the old normal, even after a protracted economic recovery and significant government interventions. Underlying trends have been accelerated by lockdowns, whether the global rise of e-commerce or remote working, coming to the fore, changing the nature of demand for many ‘traditional’ commercial assets. We will see investors, landlords and tenants continue to adapt to a new reality – not least, in their approaches to office space.”

But it is premature to call the death of the office. Yes, many organisations are rethinking their footprints and the need for large spaces in city centres, but office use will evolve. Property strategies will be increasingly data-led, based on the performance of buildings, and how they support the productivity of employees.

This will lead to refitting and altering the design of our offices and an increased focus on green loans and sustainability backed loans. While already high on the agenda of many socially responsible businesses, green finance will continue to expand.

I also predict an increased use of CVAs as companies seek to emerge from the ravages of Covid-19 in a viable state.

And finally, what of government intervention? The voluntary Code of Practice for the commercial property sector encourages commercial tenants and landlords to work together to protect viable businesses and I think it is likely we will see further intervention. This will be welcomed by lenders.

Sustainability and ESG reporting



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The concept of sustainability means functioning efficiently now without compromising the needs of future generations. Real estate investors have started to look at **environmental, social and governance** (ESG) business practices to establish a framework for assessing the impact of sustainability on financial performance in commercial real estate.

ESG

Out of the total world energy consumption, **about 35 to 40% of total energy was consumed in buildings in developed countries**. Commercial real estate (CRE) is a high carbon asset and ESG reporting is now being used to assess its sustainability:

Environmental factors

A company is assessed by their use of energy, waste generation, pollution produced and utilisation of resources. An ability to mitigate environmental risks may have a direct positive influence on financial performance and increase competition.

Social factors

Diversity and inclusion in the workplace, human rights, and data privacy. Policies and practices that promote equality attract new customers and maintain and develop commercial partnerships.

Governance factors

Relationships with stakeholders and employees; transparency reduces conflict, promotes happier workplaces and retains talented staff.

Landlords

For landlords in CRE, committing to sustainability and high ESG performance means:

1. Properties are better managed and more efficient, and in turn attract more capital investment, reducing their risks, and receiving higher returns on their investments;
2. Properties maintain their value and overall building costs over time are reduced. Ensuring good environmental performance future proofs high ESG performing CRE as we see a shift towards 'green' legislation;
3. Increasing competition for CRE spaces that are higher performing ESGs;
4. Greater tenant satisfaction and marketability.

Occupiers

For occupiers in CRE, committing to sustainability and high ESG performance means they:

1. Maintain sustainable business practices and corporate social responsibility, and attract talented individuals;
2. Reduce running costs and overheads and increase efficiency; and
3. Encourage sustainable behaviour internally and externally.

With 64% of commercial buildings in London completed prior to 2000, **there is opportunity to enhance value by innovatively 'greenifying' these buildings.** The move to sustainability is reflected in the focus on CRE being 'greener' in order to attract investment, retain talented individuals and grow.

In 2019, the UK became the first major economy to pass a net zero emissions law mandating that greenhouse gas emissions **must reach net zero by 2050.** These regulations are directly impacting the real estate market, including the London office market, through for example, the Minimum Energy Efficiency Standards regulations.

The UK government has also just started a consultation process on the prospect of tightening minimum EPC ratings to 'B' (subject to a payback test) by 2030. This reflects the UK's drive to increase sustainability both now and for the future.

Positive impact

Both landlords and occupiers can demonstrate their commitment to sustainable business practices by creating accountability for themselves. One way of doing this is to become a **B Corporation**, as Bates Wells did in 2015.

As well as encouraging innovative and sustainable business practices, joining a community of other businesses that share similar commitments creates many opportunities for collaboration.

If you would like to find out more about being a B Corporation, please contact your usual Real Estate contact or any member of the team.

You may also be interested in our **[Handy Tips for B Corporations guide](#)**



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