Landlord's consent to assign or sublet: Is the pendulum swinging back?

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This article considers the recent case law on consent to assign or sublet with particular reference to the recent Court of Appeal decision in *NCR Ltd v Riverland Portfolio Ltd* [2005] EWCA Civ 312.

Introduction

The position at common law of a tenant who sought consent to assign or sublet was invidious. Assuming that there was no absolute prohibition, when faced with an unreasonable refusal of consent, he could only seek a declaration in advance or proceed with the assignment or subletting and then defend any forfeiture claim. Neither of these courses of action was particularly attractive to most tenants.

The common law position still applies in relation to applications for consent to carry out alterations and for change of use. (For recent judicial discussion of the common law principles, see: *Ashworth Frazer v Gloucester CC* [2001] UKHL 59 and *Sargeant v Macepark* [2004] EWHC 1333 (Ch)). But the common law in relation to consent to assign or underlet has been altered significantly by two important statutory provisions. First, s.19(1) of the Landlord and Tenant Act 1927 makes any term in a lease which prevents a tenant assigning or subletting without his landlord's consent subject to a proviso that the consent is not to be unreasonably withheld. This has now, of course, to be read subject to the parties' rights, under the Landlord and Tenant (Covenants) Act 1995, to stipulate in advance situations in which the landlord can refuse consent. Secondly and more significantly, the Landlord and Tenant Act 1988 has made three fundamental changes:

- It imposes a statutory duty on a landlord who receives a written application for licence to assign or sublet to give consent unless he has reasonable grounds not to do so. He must also notify the tenant of his decision and his reasons within a reasonable time. Further, if the consent is subject to any conditions, not only must these be reasonable but they must also be spelled out in the landlord's reply.
- The Act places on the landlord the burden of showing that any refusal or the imposition of any conditions was reasonable. He need only show that his conclusions were such as might have been reached by a reasonable man in the circumstances, but it is for him and not the tenant to prove this.
- The Act gives a tenant the right to sue for damages suffered as a result of a landlord's unreasonable refusal.

Prior to the Court of Appeal decision in *NCR Ltd v Riverland Portfolio Ltd* [2005] EWCA Civ 312, the case law had illustrated how far the pendulum had swung in favour of tenants.

Cases prior to *NCR Ltd v Riverland Portfolio Ltd*

In *Go West v Spigarolo* [2003] EWCA Civ 17, the tenant had applied for consent on March 13, 2001. The landlord had written refusing consent on May 30, 2001. However, correspondence continued until the date of issue of proceedings on July 10, 2001. The judge found that, whereas the landlord's refusal of consent on May 30 was unreasonable, as a result of the subsequent correspondence, it was not unreasonable in refusing consent on the day proceedings were issued. He thus dismissed the tenant's claim.

The Court of Appeal overturned his decision. The court emphasised that a landlord cannot rely upon reasons for refusing consent which he has not put forward in writing within a reasonable time. The reasonableness of a landlord's refusal must be judged as at the expiry of the reasonable time. When this period expires, in turn, must depend upon all the circumstances of the case, including, if relevant, events after the tenant's application. If, for example, a tenant applies for consent and the landlord, within a reasonable time, asks for further information, the time within which the landlord must respond will not expire until after the tenant has given satisfactory replies. Similarly if, following the expiry of what otherwise might be deemed to be a reasonable time, the tenant writes giving the landlord a further deadline within which to respond, then it seems that the landlord's time for responding will not expire until after this deadline has passed. However, once a landlord has responded, the reasonable time automatically expires. Thus, in this case the reasonable time expired on May 30, 2001 and the subsequent correspondence was irrelevant. Perhaps of most significance, the court said this:

> ". . . I find it hard to imagine that a period anything like as long as that which elapsed from 13 March to 10 July 2001—a period of almost four months—could ever be acceptable, save perhaps in the most unusual and complex situations. I repeat, and for my own part would wish to emphasise, Sir Richard Scott V-C's references in the *Norwich Union* case [1999] 1 W.L.R. 531 to the landlord dealing with his tenant's application 'expeditiously' and 'at the earliest sensible moment'. . . It may be that a reasonable time . . . will sometimes have to be measured in weeks rather than days; but even in complicated cases, it should in my view be measured in weeks rather than months."

In *Blockbuster Entertainment v Barnsdale* [2003] EWHC 2912 (Ch), the lease contained a clause compelling the tenant, in the event of a proposed subletting, to provide the landlord with a "certificate" setting out the rent and service charges under the proposed sublease. The tenant wrote asking for consent to underlet on May 28, 2002. Despite the fact that the letter did not contain a certificate, the judge held that the statutory duty on the landlord arose from that date. He held that the landlord had all the necessary information by June 19, 2002 and should have granted consent on or before June 26. In fact, the landlord did not give its consent until July 15, 2002 and was thus in breach. It was held liable in damages when the proposed underletting went off.

In *Mount Eden v Folia* [2003] EWHC 1815 (Ch), there was some dispute as to whether the tenant's application for consent to sublet had been sent on June 11 or 17, 2002. However, Peter Smith J. accepted that it had been received on June 18, 2002. The judge also found that the landlord had considered the application on June 20, 2002 and decided on that day to refuse it on a number of grounds. Thereafter, the landlord had instructed a solicitor and taken advice. Despite a chasing letter from the tenant dated July 10, 2002, the landlord did not respond until July 15, 2002, when it refused consent for the reasons decided on June 20.

In addition to finding that none of the grounds put forward was reasonable, the judge held that the letter of July 15, 2002 was not served within a reasonable time of either June 11 or 17. Given that the decision had already been made on June 20, he was of the view that the reasonable time had expired "by a few days after 21st June 2002". Given that the landlord had not given any grounds for refusing consent by that date, it was under a duty to consent. In relation to the subsequent letter from the tenant, dated July 10, 2002, which asked for a response "by return", he said:

> ". . . if [the landlord] had responded by return then it would have been difficult for [the tenants] to contend that they had not responded within a reasonable time."

Thus, he granted the tenant a declaration and, for good measure, awarded indemnity costs against the landlord. He also added, albeit obiter, that there was no reason why, in an appropriate case, exemplary or punitive damages should not be awarded to the tenant. This was a theme to which the same judge returned in a later case, namely, *Design Progression Ltd v Thurloe Properties Ltd* [2004] EWHC 324 (Ch). In that case, the tenant applied on January 21, 2002 for licence to assign the two-year residue of the lease. The premises were under-rented and the assignee had offered a premium of £75,000. The judge found that the landlord adopted a deliberate strategy designed to achieve the maximum rental income from the property. It wanted to obtain possession of the premises to re-let at a higher rent. When the tenant refused to surrender for no premium, the landlord set out to frustrate the proposed assignment and "see off" the assignee. The landlord raised a series of

requests for further information and for references which the judge styled as "delaying tactics".

The judge, however, found that the landlord had all the necessary information by March 21, 2002 and that the reasonable time for it to respond expired then. It should have consented on or before that date. Despite this the landlord, for the next month, made further demands for information which the tenant and the assignee attempted to answer. The landlord never expressly refused or granted consent. The assignee, however, went elsewhere. Having considered his previous decision in *Folia* and the House of Lords case of *Kuddus v Chief Constable of Leicestershire* [2001] UKHL 29, the judge held that he could award exemplary damages. Having awarded well over £100,000 in compensatory damages, he awarded an extra £25,000.

NCR Ltd v Riverland Portfolio Ltd

Briefly, the facts were that the tenant formally asked for consent to under-let on June 30, 2003. After considerable correspondence and the provision of a considerable amount of information by the tenant about the proposed under-lessee, the judge found that the application for consent to underlet was fully "submitted" by July 28, 2003. That was the date by which the tenant had provided to the landlord all the information which could reasonably have been required. That was the date from which the reasonable time for the purposes of s.1(3) of the Act would be measured. Having reviewed all the documents and heard oral evidence, the first instance judge found that the reasonable time expired on August 11 that is 2 weeks or 11 working days from the date the application had finally been submitted. Indeed he found that a period of seven days should have been sufficient. The landlord had not replied until August 20 (when it refused consent) and thus had not consented within a reasonable time and was therefore in breach of its statutory duty.

The reasons advanced by the landlord for refusing consent were (a) the unusual terms of the proposed underlease and (b) the inadequate covenant strength of the proposed under-tenant. In addition, the judge found that these were not reasonable. Two factors weighed heavily on the judge's mind. The first was the fact that the tenant was applying, not for consent to assign, but for consent to under-let. The tenant would thus still be liable to the landlord under the terms of the lease. In those circumstances, the financial status of the proposed under-lessee was of no great or vital significance to the landlord.

Secondly, much of the relevant information had been in the hands of the landlord well before July 28 and from as early as June 30. Perhaps of more interest, the judge summarised the principles to be applied. He put forward 10 propositions:

> "(1) A landlord owes a duty to a tenant to give a decision on an application for consent within a reasonable time: section 1(3) of the Act.
> (2) What will amount to a reasonable time will depend upon all of the circumstances of a particular case.
> (3) The assessment of whether a reasonable time has elapsed in which the landlord has to give a decision will be made at the time at which it is claimed that a reasonable time has elapsed, and in the light of the facts at that time. Amongst the factors that will be borne in mind in assessing whether a reasonable time has elapsed is that the purpose of the Act is to 'enable there to be fair and sensible dealing between landlords and tenants [and] a state of certainly to be achieved at the earliest sensible moment'.
> (4) If, within a reasonable time, a landlord gives notice refusing consent, reasons must be given for the refusal: see section 1(3) (b) (ii) of the Act.
> (5) The burden is on the landlord to show that it was reasonable, by reference to the reasons given in the notice, to refuse consent. '. . . [I]t is not now open to a landlord to put forward reasons justifying the withholding of consent if' those are reasons which were not put forward in accordance with section 1(3)(b), that is they were not reasons which were put forward in writing within a reasonable time.
> (6) Once a notice has been given by a landlord, that landlord cannot subsequently justify a refusal of consent by referring to reasons which are not set out and relied upon in that notice.
> (7) An unreasonable refusal of consent renders a landlord liable to pay damages to a tenant for breach of statutory duty. The measure of damages will be the tortious measure: see section 4 of the Act.
> (8) A failure to give a decision within a reasonable time will be treated as equivalent to a refusal of consent without reasons. This conclusion necessarily follows from the fact that it is the landlord's obligation to make a decision within a reasonable time.
> (9) It also follows that a failure to communicate a decision on a tenant's application within a reasonable time, will also make a landlord liable to pay damages to a tenant. That liability will not be avoided or mitigated even if a landlord is able subsequently to show that there were reasonable grounds for withholding consent.
> (10) A landlord will discharge the burden of proving that a refusal of consent is reasonable if it can show that some landlords, acting reasonably, might have refused consent for the reasons given, even though some other reasonable landlords might have given consent."

This recitation of the relevant principles was (at least impliedly) approved by the Court of Appeal (see para.[11] of the judgment), which allowed the landlord's appeal. There are a number of interesting points in the judgment of Carnwath L.J. (which was the only reasoned judgment given).

The court drew a distinction between "informal exchanges" between the parties, on the one hand, and "the formal process of application and decision" on the other. This was because:

> "The serious legal consequences resulting from the statutory scheme require that the process of application and decision should be subject to a reasonable degree of formality".

That said, the court held that the judge was correct to hold that the letter of July 28 was the formal "application" for consent. In relation to the time within which the landlord had to make his decision, although the court recognised that the assessment of the proposed under-lessee's financial strength was a relatively simple task, it felt that that was not the end of the matter. Due to the potentially serious consequences of an unreasonable refusal, the landlord was entitled to further time to consider whether its misgivings about the financial strength of the under-lessee justified a refusal of consent. The court felt that the judge had been too harsh on the landlord. It found that the letter of 20th August refusing consent *was* sent within a reasonable time of July 28:

> "In the absence of exceptional circumstances, a period of less than three weeks (particularly in the holiday period) cannot in my view be categorised as inherently unreasonable."

The main issue was whether the judge was correct to find that the reasons advanced by the landlord did not justify refusal under the Act. The court emphasised that the landlord's reasons did not have to be justified by reference to some objective standard of correctness. It is enough if the landlord has genuine and not unfounded concerns on matters relevant to the value of his interest. Equally importantly, in assessing the tenant's application the landlord was entitled to have regard to his own interests alone, without considering the potential effect of a refusal on the tenant. Those cases, such as *International Drilling Fluids v Louisville Investments* [1986] Ch. 513, in which it might be unreasonable for the landlord not to consider the effect of a refusal on the tenant, were described as "exceptional".

The court held that the judge was correct to find that the landlord's attempt to justify refusal of consent because of the unusual terms of the lease was not reasonable within the Act. However, it found that the judge was wrong to hold unreasonable the landlord's refusal on the ground of the proposed subtenant's lack of covenant strength. Both parties accepted that the covenant strength of both the proposed underlessee and its proposed guarantor was very weak. The judge, however, had found that this was irrelevant given the continuing liability of the tenant. To meet this, the landlord had relied upon the evidence of an expert valuer. He gave evidence to the effect that the present value of the landlord's reversion with the proposed underlease was £500,000 less than its value without it (about 6.5 per cent of the total value). This was on the basis that, if the underletting went ahead, at the end of the term of the lease the underlessee could apply for a new lease of the whole premises under the 1954 Act. The rent which the landlord would receive in that situation would probably be less than it would receive if it acquired vacant possession of the premises at the end of the term (on the assumption that the tenant would *not* want to renew) in which case it could let the premises in parts.

The tenant did not call any evidence in rebuttal, but challenged the landlord's valuer's evidence in cross-examination. The judge made no adverse finding about the expertise or credibility of the landlord's valuer but discounted his evidence on the basis that the damage to the reversion of which he spoke was "speculative and remote". The Court of Appeal held that he was wrong to do so. They held that it was wrong to dismiss this, effectively unchallenged, evidence as no more than remote speculation about the future. Although the valuation evidence involved a degree of speculation about the future, it reflected the discount which a current investor might be expected to apply to the value of the landlord's reversion. More importantly, the court again emphasised that:

> "The question for the judge was, not whether he himself regarded the evidence as "speculative and remote", but whether it helped to show the [the landlord's] concerns about the weakness of

> [the proposed underlessee's] covenant had been reasonable (even if not 'correct or justifiable')."

Nor was this one of those exceptional cases where the landlord had to have regard not only to his own interest but also to the interests of the tenant.

Conclusions

Can any lessons be learned from the *NCR* case? Of course each of the cases described above can (correctly) be categorised as decided on its own facts. There is still no doubt that the 1988 Act is a very "tenant-friendly" piece of legislation. However, there is also no doubt that, with the Court of Appeal decision in *NCR*, the "mood music" has changed. The whole tenor of the judgment is much more sympathetic to the position of landlords than had been the case in the cases immediately prior to it. The following points are particularly noteworthy:

- The court's willingness to "extend" the time which the landlord had to respond to the tenant's request
- Its emphasis on the need for a degree of formality in the communications
- Its emphasis on the fact that the landlord's decision need only be one at which a reasonable landlord might arrive and need not be objectively correct or justifiable.

At the end of the day, the key to the outcome may lie in the following passage in Carnwath L.J.'s judgment (at [20]) in which he castigated the judge for categorising the proposed transaction as "uncomplicated". He stated:

> "[the judge's] view of the relative simplicity of the issue sits oddly with the overall effect of his judgment, which was that [the landlord], even with the assistance of experienced legal advisers, arrived at the wrong answer and thereby incurred a lawsuit involving a claim of some £3m."

Only time will tell whether this judgment will have any effect on the outcome of future claims at first instance. However, it would seem that landlords (or at least those whom the court feels have acted in good faith) are in a relatively stronger position following the Court of Appeal decision that they were before it.