THE AGA SAGA

ASSIGNMENTS AFTER VICTORIA STREET

by

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A: Introduction

1. In the cases of GOOD HARVEST V CENTAUR [2010] Ch 426 and K/S VICTORIA STREET V HOUSE OF FRASER (STORES MANAGEMENT) LTD [2012] Ch 497 first the High Court and then the Court of Appeal had to grapple with what had previously been a much debated question. This was whether a guarantor of an original tenant can lawfully be made to enter into an Authorised Guarantee Agreement (or AGA) under the Landlord and Tenant (Covenants) Act 1995 ("the act") or whether any such arrangement is avoided by section 25 of the act. There have now been a number of reported decisions since these two cases and, now that the dust has settled somewhat, I would like to try to draw some conclusions and analyse exactly where we are. Although some definitive conclusions can now be drawn, there are questions left unanswered.

B: The previous law

2. In my view one cannot really consider the meaning and effect of the act unless and until one considers the previous law. One has, in other words, fully to appreciate the mischief which the act was intended to address.

3. Under the previous law, the doctrine of privity of contract held sway. Thus:

    (i) An original tenant was liable (under the doctrine of privity of contract) on the covenants in a lease for the entirety of the term.

    (ii) The liability of a guarantor of an original tenant was co-extensive with that of the original tenant.

(iii) Whereas an assignee of the term was only liable under the covenants in the lease for the period during which the term was vested in him (under the doctrine of privity of estate) it was common for assignees to enter into an express covenant with the landlord to comply with the covenants for the remainder of the term.

(iv) If an assignee had given such a covenant, then any guarantor of such an assignee would also be liable for the remainder of the term.

(v) Although the effect of the doctrine of privity of contract could be abrogated by express agreement, this was rarely if ever done because landlords were in a "dominant position in the market" and had "greater bargaining power"

See e.g: Woodfall paragraph 16-111. This law continues to apply to "old tenancies" that is those entered into before 1st January 1996. The original tenant's liability remains even if the rent is reviewed upwards after the tenant has assigned (see CENTROVINCIAL ESTATES V BULK STORAGE (1983) 46 P&CR 393). Indeed, the original tenant remained liable for the increased rent. This was so even if the rent had been increased following alterations carried out by an assignee and agreed to by the landlord despite there being an absolute covenant against such alterations (see SELOUS STREET PROPERTIES V ORONEL [1984] 1 EGLR 50).

4. Thus, prior to the coming into force of the act, on an assignment of the term, there was no need for the landlord specifically to require the original tenant or its guarantor to guarantee the obligations of the assignee. Both the original tenant and its guarantor

remained liable after the assignment in any event. The same was true in respect of an assignee and its guarantor if (as was frequently the case) that assignee had given a direct covenant to the landlord to comply with the tenant covenants throughout the remainder of the term.

5. The potentially disastrous consequences of the operation of the previous law on original tenants and their guarantors became very clear during the economic recessions in the early 1980s and early 1990s. For example in AVONRIDGE V MASHRU [2006] 1 EGLR 15, Lord Nicholls said this (at paragraphs 10 and 11):

> *"One of the principal mischiefs the Act was intended to remedy was that, as the law stood, the original tenant of a lease remained liable for performance of the tenant's covenants throughout the entire duration of the lease. A tenant might part with his lease and many years later find himself liable for substantial amounts of unpaid rent, perhaps much increased under rent review provisions, and for the cost of making good extensive dilapidations…This was considered unfair. This potential liability was not widely understood by tenants, and it could lead to hardship…"*

6. This concern lead to a Law Commission Report in 1988 (No. 174). The Law Commission concluded that:

> *"(a) it is intrinsically unfair that anyone should bear burdens under a contract in respect of which they derive no benefit and over which they have no control: contractual obligations undertaken in a lease should only regulate relations between current owners with interests in the property.*
>
> *(b) When a demand is made under the continuing liability of the original tenant it will often not only be unexpected, but beyond the means of the former tenant;*

there is no logical way in which a former tenant who does understand that there is a contingent liability can estimate its amount...

(f) Landlords who are in practice the main beneficiaries of the privity of contract principle are unduly protected. They have the ability to enforce obligations undertaken by tenants by action against both the original tenant and the current tenant, as well as, in many cases, against intermediate assignees who enter into direct covenants with the landlord before taking their assignments. This makes the principle one-sided, and unreasonably multiplies the remedies available to landlords."

Thus, the Commission concluded that reform was required.

7. It was not until 1995 that Parliament got round to acting. By the time of enactment, there had been considerable departures from the proposals of the Law Commission. Not only was the act to apply only to tenancies created after the date of enactment, but the provisions of the act were a compromise following the strong representations from the landlord lobby who extracted three major concessions:

    (i) section 19 (1A) of the Landlord and Tenant Act 1927;

    (ii) their own release on assignment;

    (iii) the ability to compel the tenant to enter into an AGA.

C: The provisions of the act

8. The relevant statutory provisions are as follows:

    (i) By section 5(2):

"If the tenant assigns the whole of the premises demised to him, he—

(a) is released from the tenant covenants of the tenancy…as from the assignment.

(ii) The following definitions are in section 28:

"tenant", in relation to a tenancy, mean[s] …the person…entitled to that term…"

Whilst:

"tenant covenant", in relation to a tenancy, means a covenant falling to be complied with by the tenant of premises demised by the tenancy"

(iii) The provision specifically providing for the release of any guarantor is section 24 (2) which provides:

"(2) Where—
(a) by virtue of this Act a tenant is released from a tenant covenant of a tenancy, and
(b) immediately before the release another person is bound by a covenant of the tenancy imposing any liability or penalty in the event of a failure to comply with that tenant covenant,
then, as from the release of the tenant, that other person is released from the covenant mentioned in paragraph (b) to the same extent as the tenant is released from that tenant covenant."

(iv) The anti-avoidance provisions are in section 25. In particular section 25(1) which provides:

"(1) Any agreement relating to a tenancy, is void to the extent that—
(a) it would apart from this section have effect to exclude, modify or otherwise frustrate the operation of any provision of this Act, or
(b) it provides for—
(i) the termination or surrender of the tenancy, or
(ii) the imposition on the tenant of any penalty, disability or liability,
in the event of the operation of any provision of this Act, or
(c) it provides for any of the matters referred to in paragraph (b)(i) or (ii) and does so (whether expressly or otherwise) in connection

with, or in consequence of, the operation of any provision of this Act.

(v) Finally the provisions for Authorised Guarantee Agreements (or AGAs) are in section 16 which provides that:

"(1) Where on an assignment a ***tenant*** *is to any extent released from a tenant covenant of a tenancy by virtue of this Act ("the relevant covenant"), nothing in this Act (and in particular section 25) shall preclude* ***him*** *from entering into an authorised guarantee agreement with respect to the performance of that covenant by the assignee.*
(2) For the purposes of this section an agreement is an authorised guarantee agreement if—
(a) under it ***the tenant*** *guarantees the performance of the relevant covenant to any extent by the assignee; and*
(b) it is entered into in the circumstances set out in subsection (3); and
(c) its provisions conform with subsections (4) and (5).
(3) Those circumstances are as follows—
(a) by virtue of a covenant against assignment (whether absolute or qualified) the assignment cannot be effected without the consent of the landlord under the tenancy or some other person;
(b) any such consent is given subject to a condition (lawfully imposed) that ***the tenant*** *is to enter into an agreement guaranteeing the performance of the covenant by the assignee; and*
(c) the agreement is entered into by ***the tenant*** *in pursuance of that condition.*
(4) An agreement is not an authorised guarantee agreement to the extent that it purports—
(a) to impose on ***the tenant*** *any requirement to guarantee in any way the performance of the relevant covenant by any person other than the assignee; or*
(b) to impose on ***the tenant*** *any liability, restriction or other requirement (of whatever nature) in relation to any time after the assignee is released from that covenant by virtue of this Act."*(emphasis added)

D: Judicial comment prior to Good Harvest

9. In the 15 or so years between its enactment and the Good Harvest case, there had been surprisingly little judicial comment on the provisions of the act. The most

significant case was, of course, the House of Lords decision in AVONRIDGE V MASHRU. Their Lordships emphasised that the whole thrust of the act is to limit the liability imposed at common law on original tenants for the whole of the term of a lease. The act was intended as a radical departure from the previous law-see paragraphs 10-12, 16 and 26. Lord Nicholls described the effect of section 5 as "far-reaching". There was also the decision of Neuberger J (as he then was) in WALLIS FASHION GROUP V CGU (2001) 81 P&CR 28 (at paragraph 21) where he said that the act represents a "sea change in the law".

10. In particular, in AVONRIDGE their Lordships described section 25 as a "comprehensive anti-avoidance provision" in "wide terms" which is to be "interpreted generously" (see paragraphs 14, 18 and 33).

11. Following the coming into force of the act, it rapidly became clear that there was uncertainty over whether a guarantor of an original tenant (as opposed to the tenant himself) could be made to guarantee the obligations of an assignee. What tended to happen was that landlords would seek, and tenants and their guarantors would generally concede, a provision compelling the guarantor to enter into a guarantee on assignment. Such a guarantee would either be a direct guarantee, jointly and severally with the tenant, of the assignees obligations or an indirect guarantee (or sub-guarantee) of the tenant's obligations under an AGA.

12. Two other things tended to happen. Firstly, on assignment, guarantors would meekly enter into a guarantee along with their tenants. Until the Good Harvest case, no one appears to have taken a challenge to the validity of such an arrangement all the way to trial. Secondly both the leases and the guarantor's guarantees generally contained a severance clause which sought to preserve the validity of the remainder of the agreement if the guarantor's guarantee was avoided by section 25.

E: A changing landscape

13. It is perhaps also worth pointing out that, just as the act came into force, so market forces were effecting a significant change to lease terms. It seems clear that the paradigm which Parliament was considering in 1995 was the long term lease to an individual tenant or small company. Certainly prior to the mid 1990s, it was much more common for commercial leases to have terms of 15, 20 or even 25 years with no break.

14. However, as the learned editors of Lewison's Drafting Business Leases (8th edition) (at paragraphs 5.01 and 5.02) point out, shorter lease terms have become much more prevalent since the late 1990s. This market trend has been exacerbated by the introduction of SDLT and the change to the land regsitration provisions introduced by the 2002 LRA. My impression is that the standard commercial lease is now likely to be for a term of five years or of ten years with a break clause after five.

15. The upshot is, of course, that the mischief with which Parliament sought to deal is perhaps much less prevalent now than it once was.

F: Good Harvest:

The facts

16. On 5th October 2001 a lease of warehouse premises was granted to Chiron for a term of 10 years from 16th July 2001 with Centaur, the Defendant, acting as guarantor for Chiron. The rent was initially £206,387 annually, but subsequently rose to £245,000 per year.

17. The lease contained the following terms:

    (i) By clause 5.9.3 the tenant covenanted:

    "Not to assign underlet or charge the whole of the premises…without the prior consent of the Landlord such consent not to be unreasonably withheld or delayed";

    (ii) By clause 5.9.6 it was provided that:

    "The Landlord may impose any or all of the following conditions (which are specified for the purposes of the Landlord and Tenant Act 1927 Section 19(1A) on giving any licence for an assignment by the Tenant of the whole of the Premises…
    5.9.6.1 upon or before any assignment and before giving occupation to the assignee the Tenant making the application for the licence to assign and its guarantor (if any but not someone who has already given an authorised guarantee agreement) shall enter into an authorised guarantee agreement in a form permitted by Law and agreed between the parties…".

18. On 1st September 2004 the lease was assigned to THED and at the time of that assignment, pursuant to the obligation set out above, both Chiron and Centaur entered into a document called an "Authorised Guarantee Agreement" in the form which had been annexed to the lease.

19. The relevant terms of the AGA were as follows:

(i) The gist of the obligation is in clause 3.1 as follows:

> *"In consideration of the Landlord's consent to the Assignment,* ***the Tenant and the Guarantor each covenant with the Landlord and without the need for any express assignment with all its successors in title as follows…3.1.1 the Assignee will at all times from the date of the Assignment until the next lawful assignment of the Underlease pay when due without set-off or counterclaim or any other deduction whatsoever the rents reserved by the Underlease and all other sums and payments agreed to be paid by the lessee in the Underlease at the times and in the manner provided for in the Underlease and will also duly perform and observe all the covenants conditions and stipulations on the part of the lessee contained in the Underlease*** *and will through and in the event of the default of the Assignee forthwith on demand pay and make good to the Landlord all the aforementioned payments due under the Underlease and will perform and observe the covenants and conditions on the part of the lessee contained in the Underlease and indemnify the Landlord against all losses damages costs and expenses resulting from such non-payment, non-performance or non-observance.."* (emphasis added)

(ii) By clause 7.5 it was provided that:

> *"All covenants by any party to this Agreement shall be deemed to be joint and several covenants where that party is more than one person."*

20. Following the assignment, the assignee became part of the Woolworths group which went into administration in 2008. The rent was unpaid from the December 2008 quarter. Following this, and service on Centaur of notices pursuant to section 17 of the act in respect of two quarters rent, Good Harvest, by then the landlord, sued Centaur for the rent on the basis of its guarantee liability. The latter defended on the basis, inter alia, that it had no such liability because its guarantee agreement was void by reason of section 25 of the act.

21. There are a number of important features about the facts of the case which are worth noting:

    (i) Centaur's obligations in clause 8 of the lease were purely as guarantor (and not for example as principal).

    (ii) There was an express condition which the landlord could impose obliging both the tenant and the guarantor to enter into an AGA as a condition of the grant of consent for any assignment.

    (iii) The AGA was a direct covenant by the guarantor, jointly and severally with the former tenant, to guarantee the fulfilment by the assignee of the tenant covenants in the lease. It was not a sub-guarantee of the former tenant's guarantee obligations.

    (iv) The case concerned an AGA which had actually been entered into and not a situation where a guarantor was refusing to enter into such an agreement.

    (v) The AGA contained a severance clause.

The outcome

22. The judge found that the AGA was avoided by section 25 insofar as it purported to impose any liability on the guarantor. His reasoning was as follows.

23. Parliament intended by section 24 (2) to relieve the guarantor of any liability he might otherwise have had in respect of the guarantee he had given. If the guarantor was required to enter into a further guarantee when the lease is assigned, that further guarantee would, as a matter of language, fairly be said to "frustrate the operation of any provision of [the] Act" (to quote from section 25(1)(a)), in that it would, if valid, impose on the guarantor obligations equivalent to those from which section 24 was designed to secure his release. Section 25 was after all to be interpreted generously.

24. The landlord had argued that the guarantor would be undertaking new obligations which were not subject to section 25. The judge held that the same could be said of the tenant entering into the AGA. Yet Parliament had, in section 16, expressly provided for the tenant to enter into an AGA. Thus the premise underlying section 16 is that a tenant could not otherwise give any guarantee. In other words, section 16 represents an exception to a general prohibition. If (subject to section 16) the Act precludes tenants from giving guarantees for assignees, it is difficult to see why guarantors should not likewise be barred from giving such guarantees.

25. Further, had Parliament intended guarantors to be able lawfully to enter into AGAs then it could easily have said so. It did not. Section 16 refers only to tenants giving AGAs. It cannot be construed as permitting a guarantor to enter into one.

26. If a tenant's guarantor could be required to give a guarantee for an assignee of the tenant, there was nothing to limit that guarantor's exposure to the period before that first assignee himself assigned. Liability under an AGA given by a tenant has to come to an end when the tenant's assignee himself assigns (see section 16(4)). Since, however, section 16 makes no reference to guarantors, there would be no similar restriction on how long such a guarantor's liability could continue. Yet for a landlord to be able to call on a tenant's guarantor to give a guarantee for assignees other than the first could drive a "coach and horses" through the legislation.

27. The reference in section 17(3) to the guarantor guaranteeing the tenants performance "of such a covenant as is mentioned in subsection (1)" referred to the phrase "*a tenant covenant of the tenancy under which any fixed charge is payable"* in subsection (1) and not to "an authorised guarantee agreement". Thus the application of section 17 (3) to guarantors is restricted to "other" or old tenancies.

28. Similarly, the words "where a person ("the guarantor") has agreed to guarantee the performance by the former tenant of a tenant covenant of the tenancy" in section 18(3) were not apt to describe either a direct guarantee or a sub-guarantee.

29. Although the case concerned a direct guarantee and not a sub-guarantee, the judge expressed doubts as to the validity of the latter. He said:

> *"I do not think it is by any means clear that the Covenants Act permits a guarantor to sub-guarantee a tenant's obligations under an AGA"*

Arguments not raised

30. The landlord did not raise (and the judge did not specifically deal with) two arguments which had been discussed by some academic commentators.

31. The first of these was that section 25 applied only to avoid executory and not executed agreements. Thus, it might have been argued that, whereas Centaur could lawfully have refused to enter into the AGA, once it had done so it was bound by its terms.

32. Some had also argued that, by reason of section 25(4), section 25 only applied to agreements made in or before the lease. Again, the words of section 25 are wide enough to include an agreement made after the date of the lease and section 25(4) does not purport to so limit the ambit of the section.

G: K/S Victoria Street: the sequel

33. This case concerned the Beatties Department Store in Wolverhampton and, more particularly, an agreement dated 26th January 2006 for the sale and lease back of those premises. The claimant was the purchaser and lessor. The three defendants are

companies in the same group. The third defendant was the former ultimate group holding company of the retailers House of Fraser, and the first and second defendants were two of its subsidiaries.

34. By the agreement the claimant acquired the freehold title from, and granted a 35 year lease back to, the first defendant. Under the agreement the sale price was £46m; the lease term was 35 years; and the rental was £2.25m per annum subject to five yearly rent reviews. The third defendant acted as surety for the first defendant's performance of its obligations.

35. The material clauses of the agreement were clauses 3.5 and 3.6. These read:

> *"3.5 The Seller [i.e. the first defendant] agrees to assign the Lease to an assignee (being a Group Company of the Surety [i.e. the third defendant] being of equal or greater covenant strength to James Beattie Limited and if a company is not chosen by 20 April 2006 then the assignee shall be Stores [i.e. the second defendant] and Stores agrees to take that assignment by no later than 26 April 2006 and the Surety agrees to enter into a deed of guarantee of that assignee's liabilities as surety in the form set out in Schedule 3 of the Lease.*
> *3.6 The Parties agree to settle the documentation for the assignment and guarantee referred to in Clause 3.5 as soon as practicable".*

36. However the defendants did not arrange for the assignment of the lease to any other company by 26th April 2006 or at all. The lease remained vested in the first defendant. There was then a change of ownership of the House of Fraser group when it was bought by Icelandic purchasers, followed by the global financial crisis. The group removed the PLC status of the third defendant and changed some of the internal group arrangements. The result of that and the economic crisis was to bring about a situation in which: the second defendant was still a valuable company with a

good balance sheet; the third defendant was not (it having a negative balance sheet); whilst the first defendant's covenant was never worth anything.

37. In due course the claimant demanded that the defendants bring about the assignment of the lease to the second defendant required by clause 3.5 of the sale agreement. The defendants failed to do that. Eventually it brought a claim for specific performance of clause 3.5 which the defendant sought to resist on a large number of grounds one of which was that that the clauses were void and unenforceable by reason of their contravention of section 25 of the 1995 Act as interpreted by Mr. Justice Newey in the Good Harvest case.

38. At first instance the Deputy Judge rejected the claimant's arguments and (albeit with some reluctance) followed the Good Harvest case holding that that part of clause 3.5 which provided for the existing surety to guarantee the obligations of the named assignee (but not the remainder of the clause) was void by reason of section 25.

39. The landlord appealed to the Court of Appeal.

40. However it is also important to note that there was a second instalment in the action ([2010] EWHC 3344) in which Mann J found against the defendants on another part of the case which involved a matter of contractual interpretation. The relevant clause, 3.15(F) was contained at the end of the alienation provisions. It provided as follows:

> *"(F) Notwithstanding the provisions of this clause where the Tenant is [the first defendant] or any other Group Company of [the third defendant] consent shall*

not be required to an assignment of the whole to another Group Company of [the third defendant] provided [the third defendant] acts as surety to the assignee Group Company."

The argument raised was that the effect of section 25 on this clause was to allow an inter-group assignment without consent and without the requirement of the existing guarantor having to guarantee the assignee. Thus, it was argued, it was pointless ordering specific performance of the obligation in clause 3.5 (above) because the term in the lease could be assigned straight back to the first defendant without the requirement of consent. The success of this argument depended on it being shown that this clause was in effect a "stand alone" provision which was not cumulative with any other alienation provision. This argument was rejected as a matter of contractual interpretation. It is important to note however that it was not sought to be argued either at first instance or in the Court of Appeal that the effect of section 25 was to avoid this clause completely.

41. The judgment of Mann J was separately appealed by the defendants and both appeals came before the Court of Appeal constituted by The Master of the Rolls, Lord Neuberger, and Lord Justices Etherton and Thomas.

The Court of Appeal

42. The Court of Appeal dismissed both appeals. On the section 25 point they essentially held that most of the reasoning of Newey J in Good Harvest was correct with, however, one important exception.

43. The Court held that any contractual arrangement contained in the tenancy (or in a prior agreement), which imposes an obligation on an existing or prospective guarantor of the tenant's liabilities, to guarantee the liabilities of a future assignee should be void. This also applied to an arrangement which post dated the tenancy and, as such, the imposition of such an obligation on the guarantor of an assignee was also void (paragraphs 20-24).

44. They upheld the essential reasoning of Newey J as follows.

(i) On the assignment of the Lease by the first defendant to the third defendant in accordance with cl.3.5(ii), the latter will be released from all further liability under the Lease, by virtue of s.5(1) of the act;

(ii) So s.24(2)(a) is satisfied and, as the second defendant existing guarantor is "another person" who is "bound by [the] covenant[s] of the [Lease]", s.24(2)(b) also applies.

(iii) Accordingly, it is the effect and intention of s.24(2) that, as from the release of the first defendant i.e. on the assignment to the second defendant, the third defendant should be released from its liabilities as guarantor under the Lease.

(iv) Any provision such as cl.3.5(iii), which stipulates in advance that the third defendant must re-assume precisely that liability as a term of the assignment, would therefore "frustrate" the operation of s.24(2)(b) , and it is therefore rendered void by s.25(1)(a).

45. The court also held that it was the objective effect of the provisions rather the subjective intention of the parties which was relevant so far as section 25 is concerned. Therefore the fact that none of the parties had in fact intended to evade the provisions of the 1995 Act was irrelevant (paragraphs 28-9).

46. Section 25 was to be interpreted widely and thus it invalidated any agreement which involves a guarantor of the assignor guaranteeing that assignor's assignee and not simply one entered into at the insistence of the landlord. Thus it does not matter that the guarantor is perfectly willing to guarantee the assignee or that the proposed arrangement will be for the benefit of both exiting tenant and guarantor (paragraphs 34-44).

47. In particular they held that the effect of adopting this wide meaning was to prevent an assignment by the tenant to the guarantor:

> *"It would also appear to mean that the lease could not be assigned to the guarantor, even where both tenant and guarantor wanted it."* (Paragraph 37)

Although this passage was described as "obiter" and "somewhat tentative" by Morgan J in the UK LEASING case (see below), it has now been approved and applied in EMI GROUP V O&H Q1 (see below).

48. However, the Court identified one important exception. Where the assigning tenant could validly be compelled to enter into an AGA pursuant to section 16, then there

was nothing to prevent the assignor's guarantor guaranteeing the assignor's AGA (i.e. entering into a sub-guarantee):

> *"if, where s.16(2) applies, the landlord is entitled to require the assignor to re-assume liability under an AGA, it does not appear to us to be inconsistent with s.24(2) , and hence it would not be void under s.25(1) , for the landlord in such a case to require the guarantor to guarantee the liability of the tenant under the AGA…There appears to be nothing inconsistent with s.24(2) if the assignor's guarantor is required to guarantee the assignor's liability under the AGA: the guarantor is released to precisely the same extent as the assigning tenant."* (paragraph 46)

Thus the doubts expressed obiter by Newey J in Good Harvest about sub-guarantees were wrong.

49. However the court then added (in somewhat Delphic fashion) the following (at paragraph 47):

> *"It may well be that the guarantor could simply act as a co-guarantor under the AGA with the assignor, as might have been the position in Good Harvest Partnership LLP v Centaur Services Ltd [2010] Ch. 426; [2010] 2 W.L.R. 1312; [2010] 2 P. & C.R. 18 —see [5]—rather than being a guarantor of the assignor's liability, under the AGA"*

Thus, having approved the essential reasoning of the judge in Good Harvest, the Court of Appeal might be asserting that the result in that case was wrong! However, they expressly declined to give a definitive judgment on this particular aspect.

50. The Court of Appeal also gave short shrift to the argument that section 25 only invalidates executory rather than executed agreements (see paragraph 43). Thus, on

the facts of the Good Harvest case, it makes no difference that the AGA had actually been entered into.

51. Finally, they court held that there was nothing to prevent an existing guarantor, having been released from liability by one assignment from acting as guarantor again on a second assignment (see paragraph 51):

> *"If a tenancy, granted to a tenant whose obligations are guaranteed by a guarantor, is assigned, and thereafter the assignee assigns it back to the tenant, whose obligations are again guaranteed by the guarantor, it seems unlikely that s.25(1) could possibly have been intended to invalidate the guarantor's renewed guarantee or the tenant's renewed assumption of liability under the tenancy."*

However the court did not deal with a situation in which there are a series of assignments, one immediately following another, the effect of which is to leave the guarantor of the existing tenant as guarantor of a subsequent assignee and in respect of which it might be said that the clear intention of which was to avoid the effect of section 25.

H: The law following Victoria Street: a pause for breath.

52. If you want a summary of the law following the Good Harvest and Victoria Street cases then you could do worse than that set out by Morgan J in the UK LEASING case (see below). He said:

> *(1) a term of the lease, or of an agreement relating to the lease, which stipulates in advance that a tenant's guarantor must reassume the liability of a guarantor in relation to the assignee, as a term of an assignment by the tenant, would "frustrate" the operation of the statutory provision (section 24(2)) which would*

otherwise serve to release the guarantor and is therefore void under section 25(1)(a): [20] — [24] and [34];
(2) the first instance decision in Good Harvest was correct;
(3) the correct interpretation of the Good Harvest decision was (subject to a later qualification) that section 25(1) invalidated any agreement which involved a guarantor of the assignor guaranteeing the assignor's assignee: [34] and [44];
(4) this interpretation gave the 1995 Act an unattractively limiting and commercially unrealistic effect but was nonetheless the law: [36];
(5) there was no distinction between a guarantee freely offered by the guarantor and a guarantee insisted upon by the landlord: [40]-[43];
(6) there was no distinction as to the effect of the 1995 Act on an agreement to give a guarantee and a guarantee actually given: [43];
(7) the qualification referred to in (3) above was that if the assignor gave an AGA in relation to the assignee, the guarantor of the assignor (whilst it was the tenant) could also give a guarantee in relation to the assignor's liability under that AGA: [46]-[48];
(8) if a tenant assigns and the tenant and the tenant's guarantor are thereupon released, there is nothing to stop that guarantor becoming a guarantor again on a subsequent assignment: [51];
(9) the proposition in (8) above applies not only where the subsequent assignee is a new party but also where the subsequent assignee is an earlier tenant whose liabilities were guaranteed by that guarantor: [51].”

I: Subsequent authority

53. There have now been four cases since Victoria Street involving the application of section 25 of the act to the position of guarantors. The first three (certainly) are illustrations of the courts striving to apply section 25 in a way that produces a commercially sensible outcome.

54. The first is the decision of Morgan J in PAVILION PROPERTY V PERMIRA ADVISERS [2014] 1 P&CR 21.

55. This is a somewhat odd case in that it involved an application by a landlord for declaratory relief which relief was not opposed by the tenant or its guarantor. Much

of the judgment is taken up with a discussion as to whether the court should grant declaratory relief by consent. Despite being highly critical of the landlord and its advisers, the judge nevertheless decided that he ought to grant the relief sought.

56. The relevant facts were as follows.

57. A lease was granted on 10th July 2008 by the claimant's predecessor to the first defendant for a term of 16 years. This lease contained a clause which permitted assignment of the term subject to conditions which included the assigning tenant entering into an AGA.

58. On 30th April 2009, the claimant landlord granted to the first defendant licence to assign the term to the second defendant. The second defendant covenanted to pay the rent and perform the tenant's obligations until it assigned the term.

59. On the same date the first defendant entered into a separate document with the claimant described as a Guarantee. The first defendant was described as "the Guarantor". Clauses 3 to 13 inclusive of this document contained standard terms whereby the "Guarantor" guaranteed to the claimant landlord the obligations of "the Assignee" who was defined as the second defendant. Thus far there was nothing unusual or problematic about this document.

60. However, the recitals in clause 2 contained the following:

> *"It was a condition of the Landlord's consent that the Guarantor guarantee the Assignee's obligation and that this extended to the obligations of the Next Assignee."*

The "Next Assignee" was defined as:

> *"the assignee to whom the Assignee lawfully assigns the Lease in accordance with the provisions of [the alienation clause] of the Lease"*

Clause 14 of the guarantee then provided:

> *The guarantee in this Guarantee shall remain in full force and effect until the earlier of —*
>
> *(a) the determination of the Term; or*
>
> *(b) assignment of the Lease by the **Next Assignee** in accordance with the provisions of clause 5.17 (Dealings with this Lease) of the lease;*
>
> *(c) the date upon which the **Next Assignee** is released from liability under the Lease by virtue of s11(2) Landlord and Tenant (Covenants) Act 1995 ,*
>
> *but without prejudice to any accrued right of action or remedy of the Landlord."*
>
> (emphasis added)

61. Thus absent the provisions of clause 14, the Guarantee was unobjectionable as it only purported to render the Guarantor liable for the immediate assignee. However, if and to the extent that clause 14 was operative, then it would fall foul of section 25 of the act in that it purported to make the Guarantor liable for the assignee's assignee.

62. The claimant landlord (and the assignee and Guarantor) argued that, for this reason, the guarantee should be read as if the word "Next" was deleted from clause 14(b) and (c). The Judge rejected this line of argument. He held that the Guarantee was valid for two separate reasons.

63. He accepted that, if the Guarantee was held to extend to the obligations of both the "Assignee" and the "Next Assignee", it was either entirely or partially void by reason of section 25. He applied the principle of contractual interpretation expressed in the Latin maxim maxim *"verba ita sunt intelligenda ut res magis valeat quam pereat"* ("validate if possible") and construed the document in a way which would produce a valid rather than void instrument. He thus construed it by holding that, on its correct interpretation, clauses 3 to 13 applied and it thus only extended to the obligations of the Assignee.

64. In the alternative, he held that, by reason of section 25, the entirety of clause 14 was rendered void and was to be severed from the rest of the document. Thus the references to "the Assignee" in clause 3 to 13 were to be read literally and not as references to both the "assignee" and the "Next Assignee".

65. The second case is the recent Court of Appeal decision in TINDALL COBHAM V ADDA HOTELS [2014] EWCA Civ 1215. This dealt with a problem which had been identified following the Victoria Street case. Clauses are frequently encountered which allow inter-group assignments either with or without landlord's consent but so long as the existing guarantor (usually the PLC) guarantees the assignee. It has been argued that the effect of section 25 may be that these will effectively allow assignment without consent and without the need for the PLC guarantee.

66. The Tindall Cobham case involved ten leases (in identical term) of hotels. All had originally been granted to associated companies in the Hilton Group. In all of the

leases the holding company acted as guarantor. In each case the tenant company sought to assign the term to another associated company of £1 value formed for the purpose of taking the assignment. The whole point was to take advantage of a combination of certain terms of the lease and section 25 of the Act to achieve an assignment to a worthless company without the holding company being compelled to act as guarantor. The attempt failed. The assignments were, in any event, made in breach of covenant.

67. The relevant provisions are clause 3.14 in the leases. They read as follows:

> *"3.14.3 Not to assign the whole of the Hotel without the prior written consent of the Landlord (such consent not to be unreasonably withheld or delayed and which shall take the form of a formal licence) provided that for the purposes of Section 19(1A) of the Landlord and Tenant (Covenants) Act 1995 the Landlord shall be entitled:*
> *3.14.3.1 To withhold its consent in any of the circumstances set out in clause 3.14.4*
> *3.14.3.2 To impose all or any of the conditions set out in clause 3.14.5 as a condition of its consent.*
>
> *3.14.4 The circumstances referred to in clause 3.14.3.1 are as follows:—*
> *3.14.4.1 In the reasonable opinion of the Landlord it has not been satisfactorily demonstrated that the proposed assignee has an investment grade rating (being in the case of Standard & Poors at the date of this Lease at least BBB+) with the Appropriate Credit Rating Agency at the time of such assignment ("the Relevant Investment Grade") unless the proposed assignee procures that a guarantor which satisfies the Relevant Investment Grade enters into a deed with the Landlord substantially in the terms set out in the Sixth Schedule*
> *3.14.4.2 The assignee at the time of the assignment operates less than 2,000 hotel rooms in the United Kingdom and Eire*
> *3.14.4.3 In the reasonable opinion of the Landlord the assignee has not demonstrated it has operating standards which are consistent with paragraph (b) of the definition of Operating Standards and is generally recognised by the hotel industry to have operated in accordance with such operating standards consistently for a period of three years prior to the date of the assignment*
> *3.14.4.4 That in the case of the first assignment of this Lease to an assignee that is not an Associated Company of the Tenant or the Guarantor (and for the purposes*

of this Clause 3.14.4 only, "Associated Company" shall exclude the Guarantor) the assignee is anyone other than the Guarantor

3.14.5 The conditions which the Landlord may attach to giving consent to an assignment, referred to in clause 3.14.3.2 are:
3.14.5.1 The Tenant shall covenant by deed with the Landlord that after the date of assignment it will give to the Landlord such information as the Tenant would have had to supply to the Landlord under the Second Schedule in order for the Turnover Rent due up to the date of the assignment to be calculated and to pay any outstanding balance of Turnover Rent within the time limits prescribed in the Second Schedule as if all references to the end of the Financial Year in that schedule were references to the date of the assignment; and
3.14.5.2 The assignee shall provide the Landlord with such further information as the Landlord may reasonably require concerning the operating standards of the proposed assignee
3.14.5.3 The payment to the Landlord of all Rents (including for the avoidance of doubt on account payments in respect of Turnover Rent but not any Turnover Rent which has not been quantified at the date of the assignment) which fall due under this Lease prior to the date of the assignment
3.14.5.4 The Tenant shall enter into an authorised guarantee agreement as defined in section 16 of the Landlord and Tenant (Covenants) Act 1995 with the Landlord in the form set out in Schedule 4.

3.14.6 ***The Tenant shall not assign this Lease to any Associated Company of the Tenant without the prior consent of the Landlord // Provided Always that for the purposes of Section 19(1A) of the Landlord and Tenant (Covenants) Act 1995 , the Landlord shall be entitled to impose any or all of the following conditions set out in sub clauses (a) and (b) below****:*
(a) that the Tenant shall provide the Landlord with notice of any such assignment within 10 Working Days of completion of the same;
(b) ***that on any such assignment, the Tenant shall procure that the Guarantor and any other guarantor of the Tenant shall covenant by deed with the Landlord in the terms set out in the Sixth Schedule at the Tenant's sole cost***
and subject to the Tenant's compliance with such conditions the Landlords consent shall be given*."*
(emphasis and "//" added)

68. It was accepted by both parties that the condition set out in clause 3.14.6(b) could not be complied with as it fell foul of sections 5, 24 and 25 of the 1995 Act.

69. The tenants argued that the effect of section 25 was to prevent the landlords from exercising their contractual rights to impose the condition set out in clause 3.14.6 (b) as a condition of their consent to the assignment. No part of the clause fell to be excised as a result of section 25 which only invalidated an attempt by the landlord to rely on condition (b). Alternatively they argued that the effect of section 25 was to strike down clause 3.14.6(b) leaving the rest of the clause intact. Either way, the effect was that the landlord had to grant consent to an assignment to an associated company without the Guarantor having to enter into a further guarantee.

70. The Court of Appeal rejected both these arguments. They purported to apply the same "validate if possible" principle applied by Morgan J in the Permira case. On the application and effect of section 25 they said as follows:

> *"[Counsel for the tenants] made the point that legislation which operates to avoid the whole or a part of a contract may produce consequences in terms of the legal position which the parties are left with that may be both capricious and uncommercial. I accept that. Any alteration of the contract will necessarily change the parties' legal relationship from what they intended it to be and the actual impact upon them in terms of the remaining balance of liabilities and obligations may be fortuitous. But that should not be regarded as an invitation to assume that such will necessarily be the case, still less to attribute to Parliament an intention that the legislation should be interpreted and applied in that way when other alternatives are available.*
> *Although the words "void to the extent that" indicate that Parliament did not intend to invalidate more of the relevant agreement than was necessary to safeguard the objectives of the Act in the context of the particular assignment under consideration, those words do not in my view preclude the Court from taking a balanced approach to invalidation which, whilst neutralising the offending parts of the contract, does not leave it emasculated and unworkable… The rules of severance are not therefore of much assistance even by analogy to a determination of how much of the contract the Court is required to treat as invalid or unenforceable for the purpose of s.25 . But in carrying out that exercise I can see nothing in s.25(1) which prevents the Court from looking at the structure of the agreement in an objective and common sense way."*

71. Having held that the arguments of the tenant would:

> *"create an inbalance in the contractual provisions which…the legislation was not intended to create unless unavoidable"*

they held that the correct course was to strike out the entirety of the proviso to clause 3.14.6 (that is all the words after the "//" in the passage quoted above).

72. They held that, in any event, even if the entirety of clause 3.14.6 was struck down, clause 3.14.3 would still have applied.

73. The third case is the judgment of Morgan J in UK LEASING V TOPLAND [2015] EWHC 53 (Ch). Despite its name this was the sequel to the TINDAL COBHAM case. The assignments had been held to be in breach of covenant. The parties now wished to unravel the transaction without falling foul of the 1995 and sought the court's guidance on how this should be done.

74. The circumstances are summarised as follows. A lease was granted to T1. T1's obligations under the lease were guaranteed by G. The lease was a new tenancy within the 1995 Act. T1 assigned the term of the lease to T2. The assignment was in breach of a covenant in the lease. The assignment was effective to vest the term of the lease in T2 and T2 became liable under the tenant covenants in the lease. However, because the assignment was in breach of covenant, by section 11 of the 1995 Act T1, as the original lessee and G as the guarantor were not released under the 1995 Act from their liabilities in relation to the tenant covenants in the lease.

75. By section 11 an assignment in breach of covenant is known as an "excluded assignment. Section 11 (2) reads as follows:

"(2) In the case of an excluded assignment subsection (2) or (3) of section 5—

(a) shall not have the effect mentioned in that subsection in relation to the tenant as from that assignment, but

(b) shall have that effect as from the next assignment (if any) of the premises assigned by him which is not an excluded assignment."

76. Because the assignment by T1 to T2 was a breach of a covenant in the lease, none of the parties was willing to leave that position as it was. All the parties wished to bring about a result whereby the term of the lease was again vested in T1 and whereby the tenant's obligations under the lease were again guaranteed by G. However, they wished to do so in a way which did not fall foul of section 25.

77. The landlords suggested a simple and direct course of T2 re-assigning the term of the lease to T1 and G giving a fresh guarantee of the tenant's obligations under the lease. They submitted that those steps would not be invalidated by the 1995 Act.

78. The tenants submitted otherwise and, in particular, that the fresh guarantee by G would be void. Their preferred solution was more convoluted. The tenants favoured the adoption of the following steps. First, T2 would assign the term of the lease to a particular associated company which has been identified ("Newco"). Then (a day or so later), Newco would assign the term of the lease to T1 and G would enter into a fresh guarantee of the obligations of the tenant under the lease. The parties agreed

that this sequence of steps would not necessarily be invalidated by the 1995 Act. However, the landlords were concerned that the tenants' side would not carry through all the steps.

79. The Judge preferred the landlord's suggestion. He considered that the way the 1995 act would operate would be as follows:

    (i) On the re-assignment to T1, T2 will be released from the tenant covenants: section 5(2)(a);

    (ii) T1 will be released from the tenant covenants entered into at the time the lease was granted to it: section 11 (2)(b);

    (iii) G would be released from the earlier guarantee which it gave: section 24(2);

    (iv) On the re-assignment to T1, T1 would again become bound by the tenant covenants: section 3(2)(a).

    The problem then was: if G is released under section 24(2) from the earlier guarantee which it gave, could it effectively be bound by a fresh guarantee entered into on the re-assignment to T1? The concern was that the decision in Victoria Street would produce the result that the re-imposition of such a liability on G would frustrate the operation of a provision of the 1995 Act (i.e. section 24(2)) and would therefore be invalid.

80. He held that section 25 did not invalidate the imposition of the new guarantee on G in these circumstances. He purported to apply by analogy the qualification to the general

principle, identified in paragraphs 46-48 of the VICTORIA STREET case, whereby a guarantor of an assigning tenant can be made to give a sub-guarantee of an AGA.

81. He held (albeit with some hesitation):

> *"On my analysis of the position of T1, when the lease is assigned by T2 to T1, T1 is released from its original obligations by reason of section 11(2)(b) but becomes bound by the tenant covenants under section 3(2)(a). If G is released from its original obligations under its original guarantee but enters into a fresh guarantee in relation to the tenant covenants, then G is released to the same extent as T1 is released. Section 24(2) takes effect in accordance with its terms and is not frustrated for the purposes of section 25."*

82. He expressly disapproved the tenant's suggested method. He held that any agreement between the parties in advance of the assignment to Newco, whereby G is required to agree that it will again become guarantor on the subsequent assignment by Newco to T1, would in view of the meaning given in Victoria Street to the phrase "otherwise frustrate the operation of any provision of this Act", frustrate the operation of section 24(2) of the 1995 Act.

83. This was no doubt a sensible commercial outcome, but it seems to me that the reasoning adopted by the Learned Judge is somewhat tenuous.

84. The final decision is perhaps the most interesting. It is EMI GROUP V O&H Q1 LTD [2016] EWHC 529 (Ch).

85. The facts were as follows. By a lease dated 26th September 1996 the landlord let shop premises in Worcester to the tenant. The Claimant was the tenant's guarantor. There

was, it was noted, nothing particularly remarkable about the terms of the lease. At some time the reversion became vested in the Defendant. On 15th January 2013 the tenant went into administration. On 28th November 2014, at the Claimant guarantor's suggestion, the Defendant landlord granted to the tenant licence to assign the term in the lease to the Claimant guarantor and this was done by assignment on the same day. Following the assignment, the Claimant, now the assignee, granted a sub-lease to another group company. It appears that business in the shop still did not prosper and the Claimant was keen to extract itself from its obligations. It therefore brought these proceedings.

86. The Claimant made two arguments:

(i) The assignment by the original tenant to its own guarantor, the Claimant, was void by reason of section 24(2) and 25 of the act.

(ii) The effect of section 25 was that the lease term vested in the Claimant but that the tenant covenants were void as against it.

87. You will recall that, in the K/S Victoria Street case, Lord Neuberger had posited that:

"It would also appear to mean that the lease could not be assigned to the guarantor, even where both tenant and guarantor wanted it." (Paragraph 37)

Here, the Claimant former guarantor was arguing that Lord Neuberger was correct.

88. However, this passage had been described as "obiter" and "somewhat tentative" by Morgan J in the UK LEASING case. He went further in a paper he gave to the Property Bar Association on 4th November 2015. He argued that Lord Neuberger was

wrong because the guarantor/assignee, having been relieved of liability under section 24(2), in fact assumed new liabilities under section 3(2)(a) of the act and this did not itself frustrate the release under section 24(2) and was not avoided by section 25.

89. The Defendant landlord (who was obviously very keen to maintain the Claimant as the liable party under the terms of the lease) argued that:

(i) Morgan J was correct and the assignment to the guarantor was not avoided by section 25.

(ii) Alternatively, even if section 25 did apply, its effect was to avoid the assignment as a whole, thus leaving the term in the lease in the original tenant.

90. The Deputy Judge, after a thorough review of the law, held that:

(i) The assignment was rendered void by section 24(2) and 25.

(ii) The effect of section 25 was to render the entire assignment to the Claimant guarantor void. Thus the lease remained vested in the original tenant and the Claimant remained liable as guarantor.

91. She said this (at paragraphs 78 and ff):

> *The "whole thrust of the Act" is that there should be no re-assumption or renewal of liabilities, whether on the tenant or the guarantor. That is the effect of 5(2)(a) in the case of tenants and section 24(2)(a) in the case of a guarantor (or "other person" bound by the tenant covenants). This means that, if a tenant and the tenant's guarantor are each liable for the same or essentially the same liabilities as a result of the tenant's covenants of the tenancy, the guarantor cannot as a result of assignment by the tenant to it of the tenancy re-assume those very same,*

or essentially the same, liabilities as the tenant. Or, using the terminology used in some of the cases, G1 cannot on an assignment by T1, become T2."

She described an assignment to the guarantor as follows:

The assignment therefore releases G1 from the tenant covenants of the tenancy but, at the very same moment in time, binds G1 (but now as T2) with the tenant covenants of the tenancy. In practical terms therefore, there is no release at all for G1 in respect of its liabilities under tenant covenants. This is because the liabilities under the tenant covenants are simply re-assumed by the guarantor, but this time as an assignee (and not as a guarantor). Further, the liability re-assumed by G1 as T2 is the very same in a case such as the present, where the guarantor is also primarily liable in respect of the tenant covenants. The objective effect of the assignment is that G1 re-assumes precisely the same liability in respect of the tenant covenants as a result of becoming T2 pursuant to the assignment. It is that consequence which "frustrates" the operation of section 24(2)(b) and the assignment is rendered void by section 25(1)(a), an anti-avoidance provision which is to be interpreted generously. The guarantor is therefore absolutely precluded from becoming the assignee, on an assignment by the tenant whose tenant covenants he is guaranteeing.

92. She rejected the argument based on Morgan J's views:

"The difficulty I have with this argument is that there is nothing in the Act, which provides for there to be sequential steps in relation to the release of the guarantor from his liabilities under the tenant covenants, and the re-assumption of those very same liabilities on him as the assignee. Rather, sections 5(2), 3(2) and 24(2) provide that these events should all happen at the very same moment in time, which is "as from" the assignment. There is therefore no moment in time when a person who is the guarantor, and then becomes the assignee, is actually released from, or otherwise freed from, his liabilities in respect of the tenant covenants. This means that, whether as guarantor or as assignee, the liabilities in respect of the tenant covenants have continued unchanged. Indeed, the need for an actual period of release is clear from K/S Victoria Street at para [51]…"

93. As to the effect of section 25, she said that the Claimant's arguments "do not make any sense at all". The "obvious consequence" of section 25 in that case was that the assignment was void. It was "an agreement relating to a tenancy" which purported to make the guarantor liable in respect of the same covenants from which it had just

been released as guarantor. This frustrated section 24(2) and resulted in it being struck down.

J: Where are we now?-Clarity and cloud

94. Following these cases some things have been made clear. However other things remain unclear.

95. Firstly it is clear that the general rule is that an existing guarantor of an assigning tenant cannot be made to guarantee the liabilities of an assignee whether or not the obligation to do so is contained in the lease. If one postulates a situation in which T1 is the original tenant; G is its guarantor and T2 is the proposed assignee, then T1 cannot assign the term to T2 with G guaranteeing T2.

96. Secondly, however, it is clear that, if the landlord **can** lawfully impose an AGA liability on the assigning tenant, then, provided it is reasonable to do so, the existing guarantor can lawfully be made to enter into a sub-guarantee of the AGA. Thus T1 can assign to T2 and, if T1 can lawfully be made to enter into an AGA then G can lawfully enter into a sub-guarantee of T1's AGA liabilities.

97. However the limits of this exception are not clear. For example the court in K/S VICTORIA STREET expressly left open whether the exception applies when the obligation to enter an AGA is expressly set out in advance in the lease (see paragraph 50). As a matter of logic, it would seem that there *could* be a valid sub-guarantee in

such circumstances. As set out above, one of the conditions for a valid AGA under section 16 is that under the terms of the lease consent is required for assignment (section 16 (3) (a)) and:

> *"any such consent is given subject to a condition (lawfully imposed) that the tenant is to enter into an agreement guaranteeing the performance of the covenant by the assignee"*.

However by section 19 (1A) of the Landlord and Tenant Act 1927 act (introduced by section 22 of the act) a landlord is entitled lawfully to set out in the lease specific conditions subject to which any licence or consent to assign can be granted. Leases now commonly set out a requirement that the assigning tenant and its guarantor enter into an AGA (that was the case in Good Harvest). Thus, provided that the requirement for the assigning tenant to enter into an AGA is set out as a condition in the lease, then the landlord can require the guarantor to sub-guarantee it. What is not so clear is whether a specific requirement set out in the lease for both the tenant to enter into an AGA **and** for the guarantor to sub-guarantee it will be enforceable or whether any requirement for the guarantor to sub-guarantee must depend, for its lawfulness, upon whether such a requirement is reasonable in all the circumstances of the individual assignment

98. What also seems tolerably clear, despite the Tindall Cobham case, is that clauses (such as are frequently encountered) which allow inter-group assignments without landlord's consent but so long as the existing guarantor G (usually the PLC) guarantees the assignee **may** (on their own) effectively allow assignment by T1 to T2

without consent and without the need for the G's guarantee. AGA's can only lawfully be imposed where consent is required for assignment. Thus no AGA can be sought from the assigning subsidiary pursuant to such a clause. If there can be no lawfully imposed AGA, there can be no lawful requirement for a guarantor's sub-guarantee. This was the accepted effect of section 25 on clause 3.15(F) in the Victoria Street case. The message for those drafting leases is thus clear: any assignment must require consent.

99. What one **can** say after the Permira, Tindall Cobham and UK Leasing cases, is that the courts will strive to apply section 25 in such a way as to leave the parties with a commercially workable contract.

100. Following the EMI case, it is clear that T1 cannot assign the term to G, his guarantor.

101. However, the Court of Appeal in the Victoria Street suggested that the guarantor can lawfully guarantee a second assignment. Thus T1 could assign to T2 who would then assign to T3 with G being able lawfully to guarantee T3. However the limits of this has not yet been tested. Certainly in the UK Leasing case Morgan J held that this scenario may well be avoided by section 25 if there is an agreement in advance for the G to re-assume liability on a subsequent assignment by T2 to T3. That I would suggest is clearly right. However, Morgan J did then allow a direct assignment back by T2 to T1 with the guarantor being released and then immediately giving a new

guarantee. I would suggest that this could only be regarded as lawful if the original assignment by T1 to T2 was **un**lawful. If the assignment was lawful, then such a reimporting of liability would run contrary to the reasoning and result in the EMI case.

102. Further, if section 25 applies to render an assignment void, what happens to the term which has been assigned to G? Some have said that both the assignment and the term are rendered void. The better view, as now confirmed in the EMI case, is that it is only the assignment which is (or are) rendered void.

103. Finally, given the reasoning and outcome of the EMI case, what happens if T1 assigns to T1 and T2 jointly? There is some force in the argument that, by reason of the combination of sections 5(2) and 25 (as explained in that case), section 25 would apply to avoid the assignment, certainly, so far as T1 is concerned: T1 has assigned the term and has to be released under section 5(2). In the same way as the guarantor is prevented from assuming a new liability on assignment so it might well be argued is T1. It might however be argued that, as T1 and T2 are joint tenants and, as such, are in the position of a single owner vis-à-vis the rest of the world (see e.g. MEGARRY & WADE (8th edition) at paragraph 13-002 and ff) then T1 is a different legal person from T1 and T2 jointly. As such, an assignment by T1 to T1 and T2 jointly would not frustrate the operation of the act.

J: The position of landlords

104. Landlords can (and no doubt will) argue that this outcome undermines the investment value of commercial reversions in that there is doubt as to the extent to which they can any longer rely on a guarantor's covenants once the term is assigned.

105. In addition to: requiring sub-guarantees instead of direct guarantees and ensuring that all alienation clauses require landlords consent there are still a number of methods by which landlords can seek to protect their position.

106. Landlords can still refuse consent to assign in circumstances in which it is reasonable to do so (at common law this can include a sensible diminution in the value of their reversion-see NCR V RIVERLAND PORTFOLIO (No.2) [2005] L&TR 25).

107. Further, and more importantly, they can (as a result of the addition of section 19(1A) of the 1927 Act) now lawfully impose conditions such as those in the clauses in the Good Harvest lease. In particular, the landlord can stipulate that it can withhold consent to assign unless:

(i) The assignee provides a guarantor of at least the same covenant strength as the existing guarantor;

(ii) The combined covenant strength of the assignee and its guarantor is the same as that of the existing tenant and its guarantor;

(iii) It reasonably believes that there will be no perceptible diminution in the value of its reversion on the assignment.

108. The PLC guarantor which wishes to assign the term from one SPV to another can either procure another group company to stand as guarantor or provide a rent deposit.

109. I would concede that, even so, the decisions may make landlords more reluctant to assign. Landlords will have to look more closely at the assignee's covenant strength, if possible ignoring any guarantors offered as the latter would fall away on the next assignment. Potential assignees (or original tenants) are much more reluctant to pay rent deposits than they are to provide guarantees.

110. Further, some particular alienation clauses may present a problem. For example take the wording such as this:

"the Landlord may withhold consent if the assignee (along with its guarantor) is of lesser financial standing than the tenant".

An argument could be made that the landlord in this situation is obliged to consider the assignee and the assignee's guarantor as a joint package and if their combined total covenant strength is sufficient, it would not be able lawfully to refuse consent. However, if the guarantor were 80% of that combined covenant strength and the assignee were only 20%, then the good covenant would fall away on the further assignment and the landlord would be powerless to prevent that.