
GETTING IN THE MIX: ENSURING SUCCESS WITH A MIXED USE DEVELOPMENT SCHEME

Here at Forsters, our experienced team of lawyers has compiled a three part guide to assist property developers with the effective planning and management of a mixed use development scheme.

A shortage of housing supply, particularly in London and the South East, the relaxation of planning controls on change of use under the permitted development rights and increasing interest amongst institutional investors in the private rental sector are just some of the reasons we are seeing an ever increasing emphasis on mixed use development schemes in the current market. In this, the first of three parts, we give an overview on:

- The legal considerations which should be tackled when acquiring a site;
- Funding the development; and
- Obtaining vacant possession.

ACQUIRING THE SITE

Documenting terms

- Having identified a suitable site, the parties will agree a set of heads of terms (HOT) outlining the principal terms of the deal.
- The more detailed the HOT are on the key points, the better – it will save lengthy negotiation later down the line.
- Consider the different options for structuring the purchase of a mixed-use development site. For example:

- Contracts may contain various conditions to be satisfied (such as one or other of the parties obtaining satisfactory planning permission) before legal ownership of the land is transferred.
- Sellers may look to impose overage obligations so that they can share in any value uplift which is realised only after the sale has completed.
- Once HOT are agreed, lawyers will circulate draft documents and negotiate them in detail.
- Further down the line, in addition to the sale agreement and transfer, there may be a development agreement, a building contract, various construction documents, and warranties given by contractors to other interested parties, all of which will need careful consideration.

Due diligence

- Carry out a comprehensive title investigation to ensure you are aware of any potentially troublesome title matters, such as rights of way over the development site or covenants which impact upon the use of the property for the intended purpose.

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- A full suite of searches will ensure you have as much information as possible about matters ranging from the planning history of the site to the location of any utility pipes, wires or other apparatus. The size and location of the property will impact on the cost of the searches. Depending on location or site-specific features, specialist searches such as a Canal and River Trust or HS2 search may also need to be undertaken.
- A physical site inspection should be carried out and comprehensive enquiries raised of the seller.
- Third party experts may need to be instructed to carry out site-specific assessments. This may include a building survey, environmental report and a flood risk assessment depending on the location and nature of the property.
- Third party rights have the potential to scupper development projects, so it is critical to identify them at the outset and budget for them accordingly. For instance, a rights of light survey will reveal the likelihood of a claim and any risks can then be fully addressed, perhaps by way of indemnity insurance.
- Consider not only the rights which the property will need once built out, but also those which are required for the construction phase of the development. Will an alternative access route be needed for construction traffic? Do the site dimensions necessitate swinging a crane over or placing scaffolding on a neighbour's land? Will there be building works which will engage the statutory party wall provisions? Try to ensure that all such matters are addressed as early as possible in the process.

FUNDING THE DEVELOPMENT

Money talks

- The initial site acquisition cost can be a small proportion of the overall cost of building a development. Often developers will seek third party funding for the works scheme, for instance from a bank or pension fund.
- A number of structures can be created between the parties – for instance, a “forward purchase”, where the developer builds at its own cost and is then reimbursed by a funder on completion, or a “forward funding agreement” where a funder will make monthly

payments towards the build costs as the project progresses, subject to a maximum commitment. There are pros and cons for each approach, and proper advice should be sought at an early stage.

- Many developers will want an exit strategy once the works are complete, and the value of the land once fully let will partly determine the profitability of the project, so most funders and developers will be keen to secure rack-rented pre-lets of commercial parts and off-plan sales of long leasehold interests in the residential parts as soon as possible.
- Tying tenants into a contract at an early stage will give future landlords peace of mind but, where possible, try to ensure that tenants cannot terminate their agreements except in very specific and defined circumstances.

OBTAINING VACANT POSSESSION

- If you need to demolish a building (or part of it), you may have to deal with the removal or relocation of incumbent businesses or residential tenants. Whether or not a developer will be purchasing the site with vacant possession (VP) will be part of the commercial terms of the acquisition.
- Where the site is being acquired with incumbent tenants, a developer-landlord will need to consider the terms of the existing leases on the site, and the method and likely cost of obtaining VP of each of the units.
- Whilst acquiring a vacant site removes the need for a developer to expend such time and energy in securing VP, incoming developers may wish to ensure an interim rental income stream from the site pending the development commencing. Is it possible to move existing tenants over to a more flexible short-term tenancy or licence arrangement whilst development plans are finalised?
- Early strategic advice should be sought, particularly if there are any existing residential tenants who can enjoy extensive statutory rights to remain in the property. This can otherwise prove fatal to a buyer's plans to acquire and/or develop. Our real estate litigation team

is experienced in working together with clients and their other professional advisors to deal effectively with these sorts of issues.

TERMINATING EXISTING BUSINESS TENANCIES

Is there a landlord break?

- When seeking to rely on a contractual landlord's break right to bring existing tenancies to an end, the usual care should be taken to ensure absolute compliance with the provisions of the lease as to service of notice and any break conditions.
- Additional difficulties can arise where the lease has not been excluded from the statutory security of tenure provisions of the Landlord and Tenant Act 1954 (the Act) so always seek advice before serving a break notice – if you don't get it right first time, you may lose your right to break!

Can a surrender be agreed?

- Any commercial tenancies which either do not expire before the date on which VP of the site is required, or which do not contain a landlord's right to break the lease before that date will probably need to be surrendered.
- This will require the tenant's consent and is likely to mean payment of a premium to the tenant.
- Surrenders will need to be carefully timed in order to ensure that a developer is not left with one tenant on an otherwise vacant site, who can effectively hold them to ransom.

Impact of the 1954 Act

- The landlord will then need to consider whether any remaining commercial tenancies are protected by the Act, which gives business tenants statutory rights to renew on expiry of their lease.

- Ending those tenancies which are not protected by the Act on their contractual term expiry dates should be relatively straightforward.
- However, bringing tenancies which are inside the Act to an end is more complicated as the landlord will need to follow the procedure for opposing renewal under the Act. This will mean serving either a notice or a counter-notice, specifying one or more statutory grounds of opposition. Counter-notices must be served within two months of receiving a tenant's request for a new tenancy, so advance planning is crucial.
- Depending on the grounds relied upon, the landlord may need to pay the tenant statutory compensation upon it quitting the premises.
- Either party may apply to Court to determine whether the landlord can prove the ground(s) which it has relied on. The tenancy will remain on-going until the Court application is disposed of, and so an application made late in the day can cause significant delays to a development programme. A pro-active landlord can manage this risk by serving the relevant notices in a timely fashion, and either seeking to agree surrenders or issuing its own Court application at an early stage.

GROUND (F) OPPOSITION

The most common ground of opposition in these circumstances is "Ground (f)" which provides that, on termination of the current tenancy, the landlord intends to demolish or reconstruct the premises, or a substantial part, or that it intends to carry out a substantial work of construction on the holding.

This briefing is the first of a series of three, the second edition will focus on navigating the planning process and setting up contractual arrangements with the construction team.

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This article offers general guidance only. It reflects the law as at January 2015. The circumstances of each case vary and this briefing should not be relied upon in place of specific legal advice.