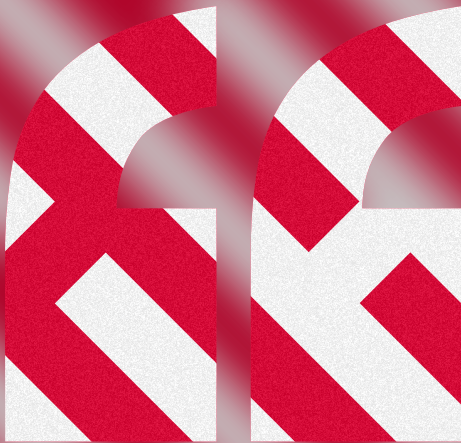


C L I F F O R D  
C H A N C E



**BREXIT-PROOFING  
CONTRACTS:  
EIGHT TIPS FOR  
LANDLORDS AND  
DEVELOPERS**



**— THOUGHT LEADERSHIP**

OCTOBER 2019



## **BREXIT-PROOFING CONTRACTS: EIGHT TIPS FOR LANDLORDS AND DEVELOPERS**

What can investors who are pressing ahead with expanding their UK property portfolios or commencing developments do to Brexit-proof their commercial leases and prelet agreements for lease? The laws governing these types of agreement in the UK will not change as a result of Brexit, and (thankfully) we know from the recent *Canary Wharf v EMA* case that Brexit is unlikely to result in frustration of these agreements.

But with continuing uncertainty around potential disruption to supply chains, currency fluctuations, and labour shortages as a result of Brexit, there are still some steps that prudent landlords and developers can take now to avoid the worst of any adverse consequences that could flow from a chaotic Brexit.

①

### **“Brexit clauses”**

Despite press reports to the contrary, clauses which allow a tenant to terminate their lease in the event of Brexit or a no-deal Brexit occurring are highly unusual, and have not become market standard in the UK. Unless there are deal-specific reasons for their inclusion, these should be strongly resisted by landlords as they are likely to negatively impact value.

②

### **Provision of services**

The lack of labour, power cuts or shortages of materials may result in certain elements of the building services being unavailable for periods of time. Appropriate limitation of liability language should be included in service charge clauses to relieve the landlord from liability for failures outside of its reasonable control.

③

### **Service charge caps**

Service charge caps should also be included in leases, with care given to the potential for supply chain disruption to drive the cost of providing the building services up. This could result in void costs for landlords where the cost of providing the services exceeds what can be recovered from tenants.

④

### **Be wary of index linking**

Shortage of goods due to trade barriers or unexpected tariffs could push up inflation, resulting in a large jump in payments linked to the retail prices index or the consumer prices index.

In many cases this will be in the landlord's favour, but where it isn't, collars and caps on annual indexation increases should be considered.

## **Tenant default**

Prolonged economic uncertainty could trigger a wave of insolvencies, so landlords should be mindful of tenant covenant strength from the outset and seek suitable security, such as rent deposits. Landlords should also be wary of granting leases to special purpose vehicles (SPVs) that don't come with parent company guarantees or other security, as this enables occupiers to cut loose their SPVs and refuse to continue to provide credit support. Whenever a lease is forfeited, landlords should assess whether they might be able to make a claim against a previous tenant if they provided an authorised guarantee agreement (AGA) when the lease was assigned.

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## **Sharing risks with building contractors**

Developers negotiating building contracts should think carefully about risk allocation relating to change of law, labour costs and delays in obtaining materials/components. Most building contracts put these risks firmly on contractors' shoulders, but that will be of little comfort if it leads to the contractor seeking to renegotiate the commercial deal to avoid insolvency. "Brexit clauses" are starting (perhaps belatedly) to make their way into the construction market, but these should be treated with caution as they tend to be drafted vaguely and have an uncertain legal effect.

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## **Force majeure**

Developers entering into development agreements with local authorities or landlords, or preletting space to tenants, should include longer buffer periods in build programmes to reflect the possible delays caused by labour or material shortages, disruption to supply chains, and possible contractor insolvencies. Any damages or LAD regimes agreed with these contractual counterparties should also include appropriate force majeure wording to limit the developer's exposure to risks outside of its control.

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## **Ability to act fast and flexibly**

Developers also need to be able to act quickly in terminating and replacing any insolvent contractors or suppliers, so approval rights given to landlords or prelet tenants should be minimised or capable of being expedited. Care should also be taken when agreeing to provide collateral warranties from contractors and sub-contractors, for example as a condition of the developer being released from its obligation to rectify defects, as this may be unachievable in the event of an insolvency.

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