DechertOnPoint

Summer 2011 / Issue 23

Editor: gillian.baxter@dechert.com

Real World

Finance and Real Estate News

In this issue

p1 HEADNOTE
Olympic Countdown

p2 BRIBERY
The Bribery Act and the Real Estate Industry

p5 SEWERS
Automatic Adoption of Private Sewers

p6 LANDLORD AND TENANT
Vacant Possession and Break Rights

p7 CRC ENERGY EFFICIENCY SCHEME
CRC Simplified

p8 PLANNING
Planning Update

HEADNOTE

Olympic Countdown

by **Andrew Hutchinson**

As we count down to London 2012, I have found myself comparing and contrasting the "greatest show on earth" with our real estate market.

The Olympic Games brought globalisation to sport. For two weeks in 2012, London will be the focus of the world's attention in rather the same way that it has been for ever greater numbers of overseas investors in real estate.

It is likely that the 2012 medal haul will further evidence the shift in power from west to east.

Team GB will have to plan meticulously and execute flawlessly to deliver success. I worry whether our education system is now capable of delivering talent in the numbers that UK plc will require in the future.

98 per cent of the Olympic facilities will have been delivered by UK companies, though.

The Olympic Games are big business. I am not sure that the mantra: "it's the taking part that counts" remains true any longer. Similarly, in business, does there remain a place any more for second best?

This hunger for success requires the authorities to be vigilant in the fight against cheats; anti-doping in sport for example, and anti-corruption in the world of business. Those who use corrupt practices in sport or business and, in the latter case, those who fail to implement systems to prevent it, will be for the "high jump".

In these days of austerity, it is to private enterprise that the UK government looks to help revive the UK economy. It remains to be seen whether, like a weight lifter, it can achieve the necessary "clean and jerk", never mind whether it can subsequently lock its knees to prevent the economy from tumbling down.

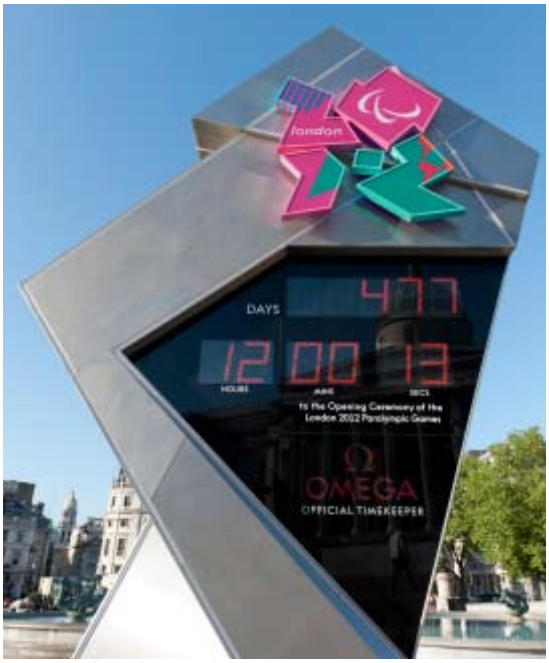
The availability of debt remains an issue as banks struggle with impaired loans and changing capital adequacy requirements. In the absence of debt, the traditional investor model based on gearing is as hopeless as a pole-vaulter without a pole.

Success, whether in sport or business, is typically the culmination of a vast collaborative effort. I wonder who, amongst our 2012 Olympians, will emerge as champions to stand alongside our great Olympians of the past. And I speculate about whether new industry leaders will emerge from the crash to help drive UK plc forward and help London maintain its pre-eminent position as a place to do business.

Come on Team GB! Come on UK plc!

And to continue the competitive theme, I'll send a £50 Marks and Spencer voucher to the reader who e-mails me a list of the 10 greatest British Olympians which matches or most closely matches my own list—good luck!

Andrew Hutchinson
Partner
+44 20 7184 7428
andrew.hutchinson@dechert.com



Dechert LLP

BRIBERY

The Bribery Act and the Real Estate Industry

by **Jonathan Pickworth** and **Deborah Williams**

The Bribery Act 2010 came into force on 1 July 2011 and has serious implications for the real estate industry. The Act has wide extra-territorial reach and will affect both individuals and commercial organisations with a UK connection, even if the act of bribery occurs overseas. For commercial organisations, the scope is even wider—the act in question might take place abroad and by someone who has no connection with the UK, yet can still result in criminal liability for the organisation. Convictions for offences under the Act may lead to 10 years in prison, unlimited fines, confiscation orders, debarment from tendering for Government contracts across the EU, disqualification from acting as a director and, of course, serious reputational damage, not to mention the high cost and devastating impact of a protracted and public investigation. Clearly the Act must be taken very seriously.

The Scope of the Act

The Act defines the offences of bribery very widely and includes the general offences of bribing another person and being bribed, as well as a separate offence of bribing a foreign public official. The test for commercial bribery is different to that for bribing a foreign public official, where the offence can be committed even where there is no intent to induce improper performance. Probably the most significant aspect of the Act is the new strict liability corporate offence of failure to prevent bribery, where the only defence available to commercial organisations is for them to have "adequate procedures" in place to prevent bribery.

Extra-territorial Reach

Importantly, under the Act, the bribery does not need to have occurred in the UK for an offence to have been committed. In relation to the offences committed by individuals of bribing, being bribed or bribing a foreign public official, provided the person committing the offence has a close connection with the UK, for example they are a British citizen or are ordinarily resident in the UK, the physical act of bribery can occur inside or outside of the UK.

The corporate offence of failure to prevent bribery is not confined to the UK either. Provided the organisation is incorporated or formed in the UK, or that the organisation carries on a business or part of a business in the UK (wherever in the world it is incorporated) then the organisation is within the ambit of the offence. There has been consternation in some quarters as to the broad territorial reach of the Act. Surprisingly, much of this reaction has come from US companies even though the US Foreign Corrupt Practices Act (FCPA) has had, until now, the longest arm in terms of global anti-corruption enforcement. The only requirement under the new UK law is that the commercial organisation must do business or *any part of* its business in the UK which means that compliance programmes of international companies need to be updated across their operations, not just in the UK.

Bribing Another Person and Being Bribed

The offence of bribing another person includes an individual offering, promising or giving a financial or other advantage intending to induce or reward improper conduct, or knowing or believing its acceptance to amount to improper conduct. "Improper" here means breaching an expectation of good faith, impartiality or trust. So, for example, an individual who is a developer and has applied for planning permission to build an office block and car park next to the council offices and who offers to allow the members of the planning committee to park free in the car park, could fall foul of this offence.

The bribe does not actually have to be given; just offering it, even if it is not accepted, could fall within the offence. Additionally, the offer does not have to be explicit—a "nod and a wink" will be enough and an offer made through a third party will also be caught.

An individual being bribed is also an offence under the Act. This includes requesting, agreeing to receive or accepting a financial or other advantage where that constitutes improper conduct, or intending improper conduct to follow, or as a reward for acting improperly. Therefore, the act of asking for a bribe is an offence, even if the bribe is not actually given. So, for example, if an individual who is a developer suggests to a building contractor that he will be awarded the building contract for a development if he also builds a swimming pool at the developer's house, the developer may commit an offence even if the contractor does not agree.

Bribing a Foreign Public Official

There is a separate offence under the Act of bribing a foreign public official to gain or retain a business advantage. Unlike the general bribery offences above, this separate offence does not require evidence of an intention on the part of the person bribing to induce improper conduct, or knowledge or belief its acceptance will amount to improper conduct; only that the person bribing intends to influence the official acting in his official capacity.

It is worth highlighting that, unlike the FCPA, facilitation payments (i.e., small bribes made to secure or expedite the performance of a routine or necessary action to which the payer has a legal or other entitlement) are not permitted under the Act. All companies operating globally should adopt a zero tolerance approach to all bribery, including facilitation payments. US companies in particular need to take care that there is no permissive language in their current policies or codes of ethics regarding facilitation payments, or else they could fall foul of the Bribery Act even though they might be compliant with the FCPA.

Failure to Prevent Bribery

It is possible for a corporate body (and its senior officers) to be found guilty of any of the general offences of bribing, receiving a bribe and bribing a public foreign official listed above. However, the difficulty for the prosecution in proving corporate liability is that it must show that the necessary mental element can be attributed to the "directing" mind of the corporate body. Therefore, it is of major significance that the Act has introduced a new strict liability corporate offence of failure to prevent bribery, where the prosecution will not have these evidential problems in taking action against corporate entities.

The new offence is committed by a commercial organisation where a person "associated" with it bribes a person with the intention of obtaining business or a business advantage for that organisation. The only defence available to the commercial organisation is that it had "adequate procedures" in place to prevent bribery.

For example, if an architect offers a bribe to a member of the planning committee to obtain planning permission for a client company's development, the client company may fall foul of this offence if the client company does not have "adequate procedures" in place.

Who is an associated person?

An "associated" person for the purposes of this offence is widely defined as a person who performs services for or on behalf of the commercial organisation. Therefore it could include not only employees and agents such as managing and letting agents, but also, depending on the particular circumstances, subsidiaries, joint venture partners, contractors, consultants such as architects, surveyors, mechanical and electrical engineers, and intermediaries or brokers who are paid a fee for putting together a deal or finding a site. Where a joint venture is conducted through a separate legal entity, that entity might be treated as "associated" with its members for this purpose, but will not automatically be; it will depend on the degree of control the member has over the entity. A supplier or contractor who is merely acting as a seller of goods is unlikely to be regarded as an associated person.

What are adequate procedures?

Guidance issued by the Ministry of Justice sets out the following key principles:

- **Proportionate procedures.** The procedures to prevent bribery should be proportionate to the bribery risks faced by the organisation and the nature, scale and complexity of the organisation's activities.
- **Top-level commitment.** Senior management should be committed to preventing bribery and a senior person should have overall responsibility for the programme.
- **Risk assessment.** The organisation should carry out periodic, informed and documented assessments of its exposure to bribery and act on them.
- **Due diligence.** Appropriate checks should be carried out on persons performing services for the organisation and those persons should in turn be required to carry out similar checks on the persons they deal with.
- **Communication.** Bribery prevention policies should be clearly communicated internally and externally and there should be continuous training.
- **Monitoring and review.** The risks and procedures should be regularly monitored and reviewed.

Every commercial organisation should have procedures in place that are proportionate to their business and their risk profile, but which above all must be "adequate".

Corporate Hospitality

The guidance makes clear that the Act is not intended to criminalise bona fide hospitality or promotional expenditure. It is advisable to have transparent internal guidance and an appropriate policy firmly in place to guide employees and directors. When assessing corporate hospitality, the following general questions should be considered:

- Is the hospitality offered for a legitimate purpose or is it intended to influence decision making?
- Is the level of hospitality proportionate and therefore considered to be a routine business courtesy, or is it excessive?

An organisation should have policies and procedures in place to ensure that there is adequate clear guidance to enable associated persons to know what is acceptable and that there are appropriate procedures for securing approvals and reimbursement.

By way of example, a managing agent taking a client to a sporting event would not normally be caught by the Act. However, the scale or timing of the hospitality could allow an inference to be drawn under the Act—for example if the sporting event is abroad and the client and his wife are accommodated at a five star hotel for a week, or if the agent's contract is up for renewal.

An architect providing reasonable travel and accommodation to allow a prospective client to inspect a previous project is unlikely to fall foul of the Act because the hospitality is both for a legitimate purpose and proportionate.

Legal Documents

As part of an organisation's "adequate procedures" suitable provisions will need to be included in legal documentation with "associated persons". The terms of engagement of agents, consultants and service suppliers should include provisions requiring them to comply with the organisation's anti-bribery policies and to have and implement their own policies which they must require their own associated persons to comply with. There should also be provision for the immediate termination of the contract if those requirements are breached.

There should not be any need to insert anti-bribery provisions in sale and purchase contracts or in leases or licences, as the parties to those documents do not perform services for each other and so would not be "associated". However, it may be appropriate to include such provisions in a development agreement where the developer will be providing services such as the construction and letting of the development for the land owner. The developer would then include corresponding provisions in the agreements with its associated persons, such as the building contract.

Impact of the Act

It is clear that the Act is going to have a significant impact in the UK and overseas. In particular, the corporate offence of failure to prevent bribery means that commercial organisations in the real estate sector need to take immediate action and carefully consider what procedures need to be implemented to limit their exposure to criminal liability.

Jonathan Pickworth
Partner
+44 20 7184 7608
jonathan.pickworth@dechert.com

Deborah Williams
Associate
+44 20 7184 7680
deborah.williams@dechert.com

SEWERS

Automatic Adoption of Private Sewers

by **William Fryzer**

Most private sewers and drains will automatically be transferred on 1 October 2011 to the ownership of water and sewerage companies, which will take over responsibility for their maintenance.

Which Pipes Are Affected?

The scheme applies to pipes on both residential and commercial premises in England and Wales. It affects private sewers and lateral drains that were connected to the public sewerage system on 1 July 2011. Private sewers are pipes which serve more than one property; lateral drains are pipes which serve only one property but lie outside the boundary of that property. Pumping stations will also be transferred but not until 1 October 2016.

The scheme does not apply to pipes which serve only one property and lie within the boundary of that property. The legislation refers to the "curtilage" of the property but does not define that term, so there is some uncertainty as to exactly which pipes will be transferred.

Sewers and drains owned by railway companies are excluded from the scheme. Those on land owned by the Crown or a government department are covered unless the Crown Estate Commissioners or the relevant government department has given notice to exclude them.

A further scheme is being developed which will apply to new sewers and lateral drains connecting to the public sewerage network after 1 July and will require them to be constructed to a specified standard.

Is There Any Downside?

In most cases this change will be beneficial to property owners and occupiers as it will clarify the responsibility for maintenance of the pipes and remove the burden from the property owners. Another advantage is that there will be a right to connect to the adopted sewers and drains subject to certain conditions. Water and sewerage bills, of course, will go up to cover the increased costs to the water and sewerage companies, but they estimate the increase will average less than ten pounds a year.

However, the operation of the scheme may be unwelcome if it interferes with existing arrangements for shared drainage on multi-let developments which are working well or if it prevents the use of "lift and shift" provisions which allow for pipes to be diverted to enable future redevelopment to take place. The transfer will also give the water and sewerage companies legal rights to enter private property for access to the pipes.

Can Property Owners Opt Out?

There is no right to opt out, but the owner, or anyone else affected, can appeal to OFWAT if the proposed adoption would be "seriously detrimental" to them, or it does not satisfy the relevant criteria (for example the relevant pipe is not a private sewer or lateral drain). OFWAT has issued draft guidance on how the appeal process will work and the issues it will have regard to in determining an appeal. The draft guidance is available at http://www.ofwat.gov.uk/consultations/pap_con110615privatesewers.pdf.

The water and sewerage companies must serve two months' notice on the owners of pipes affected by the scheme and must also place notices in newspapers. That means the notices must go out before August. Appeals must be lodged within that two month notice period. Because of the difficulty of identifying all the pipes affected and their owners, the companies will probably just serve a general notice on all their customers without identifying particular pipes. That would make it impossible to appeal on the ground that a particular pipe does not satisfy the criteria for transfer. It also means that notices going to customers might not come to the attention of the freeholder.

An appeal can also be made against a failure to transfer a sewer or drain and in that case there is no time limit.

Source: The Water Industry (Schemes for Adoption of Private Sewers) Regulations 2011.

William Fryzer
Partner
+44 20 7184 7454
william.fryzer@dechert.com

LANDLORD AND TENANT

Vacant Possession and Break Rights

by **Gillian Baxter**

An obligation to give vacant possession is not satisfied if personnel remain at the property, even if the tenant has offered to return the keys to the landlord and would leave if asked to do so.

It is a well established rule that conditions attached to a right to terminate a lease, a "break right", must be strictly complied with. For that reason, a tenant would be well advised not to agree to a condition that it has complied with all its obligations under the lease, because there will inevitably be some breach, probably of the repairing covenant, which would prevent the tenant from exercising the break right. A condition requiring vacant possession to be given is very common but, as a recent Court of Appeal decision shows, it too can trip the tenant up.

The recent case concerned a lease of a warehouse in Rotherham. The tenant had originally taken an assignment of a ten year lease and when that ended it took a further two year term with a right to break after one year on six months' notice provided the rent was paid and the tenant had given vacant possession of the premises.

The tenant gave notice to exercise the break right and a few days before the lease was due to end some minor outstanding repairs were identified. The tenant made what the judge later described as a sensible proposal. It suggested that it would keep its security guard on site for a week after the break date while its workmen finished the repairs, but it would not pay rent or rates during that period and would hand over the keys on the break date so that the landlord would have full access. In effect the suggestion was that the tenant would give possession on the break date and return later to finish the repairs as the landlord's licensee.

The judge said that an arrangement along those lines would probably have made the litigation unnecessary. Unfortunately the landlord's surveyor could not get hold of the landlord before the break date to get a response to the tenant's proposal but the tenant unwisely went ahead with it in any event. When, a few days later, the landlord finally responded to urgent enquiries about handing back the keys, it discovered that the workmen were still on site. Instead of collecting the keys the landlord obtained legal advice and claimed that vacant possession had not been given so that the break right had not been properly exercised and the tenant remained liable to pay the rent.

The case went as far as the Court of Appeal, where a new definition of vacant possession was formulated (see box).

Applying that definition, it was clear that the tenant had not given vacant possession.

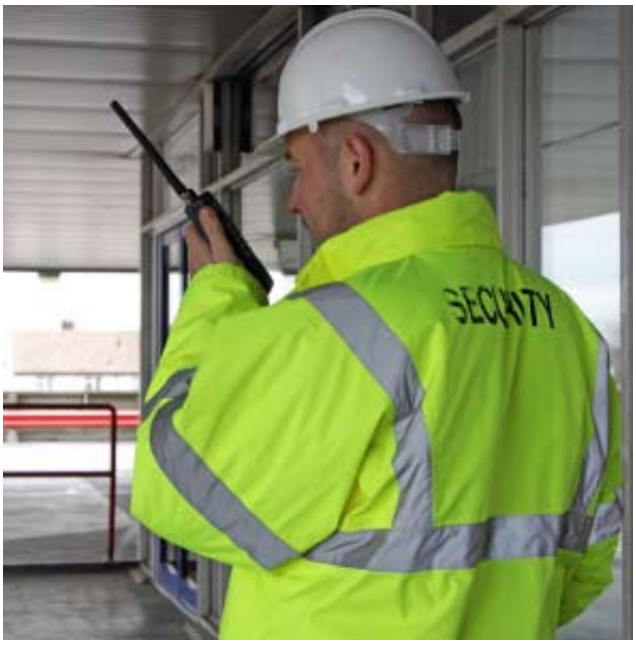
Definition of Vacant Possession

"It means that at the moment that 'vacant possession' is required to be given, the property is empty of people and that the purchaser is able to assume and enjoy immediate and exclusive possession, occupation and control of it. It must also be empty of chattels, although the obligation in this respect is likely only to be breached if any chattels left in the property substantially prevent or interfere with the enjoyment of the right of possession of a substantial part of the property."

In this situation, the only safe course for the tenant is to move everyone out of the property by the break date and return the keys. Simply offering to return the keys and being willing to leave if asked by the landlord is not sufficient. If necessary, the tenant can seek to agree with the landlord that it will be allowed access after the break date to finish repairs, but it must be clearly agreed that the tenant's presence at the property will be as the landlord's licensee and not as tenant. Luckily for the tenant in this case it had another break right just eight months later which it exercised correctly.

Source: *NYK Logistics (UK) Ltd v Ibrend Estates BV [2011] EWCA Civ 683*.

Gillian Baxter
Professional Support Lawyer
+44 20 7184 7450
Gillian.baxter@dechert.com



CRC ENERGY EFFICIENCY SCHEME

CRC Simplified

by **Alison Lympany**

In the winter issue of Real World *we reported on fundamental changes to the CRC Energy Efficiency Scheme ("the Scheme") including the scrapping of recycling payments following the Comprehensive Spending Review. In June 2011 the Department of Energy and Climate Change ("DECC") published proposals to simplify the Scheme in an effort to further reduce the administrative burden on businesses.* ***Interested parties have until 2 September 2011 to comment on the proposals.*** *DECC will consult on draft legislation in February 2012 and the changes will come into force from April 2013.*

Simpler Qualification Rules

DECC suggests a streamlined "one step" qualification process in place of the existing two step process. Participants will only be required to prove that they use a certain amount of electricity from a settled half hourly meter. If this proposal is accepted the 6,000 MWh threshold may need to be revisited to maintain the Scheme's current coverage.

Move from Cap and Trade to Fixed Price Allowance Sales

DECC suggests that, rather than capping the number of allowances and auctioning them annually, from 2014 (the start of the second phase of the Scheme) there will be two sales of fixed price allowances each year. The sales would be by uniform price sealed bids which, they say, avoids participants having to develop auctioning strategies. The first sale is intended to be at a lower price than the second retrospective sale. This allows participants to control their own compliance, by either forecasting energy use and purchasing cheaper allowances at the beginning of the year, or "buying to comply" in the second retrospective sale when they have reported on their actual energy use. Any additional allowances required could be purchased on the secondary market from participants with excess allowances. This would not affect the retrospective sales of allowances in the introductory phase for £12 per tonne.

Fewer Fuels Covered

Scheme participants must currently report on their emissions from 29 different fuels. On the basis that 95% of emissions covered by the Scheme come from just four fuels, it is proposed that only emissions from gas, electricity, kerosene and diesel will be covered by the Scheme. The objective is to reduce the administrative burden of the Scheme without compromising the emissions it captures.

Simpler Organisational Rules

DECC's proposal to allow organisations to participate as "natural business units", rather than in large CRC groups which do not reflect their structure, acknowledges that the existing rules do not readily translate to typical company or fund structures. Although the existing rules will be retained for Scheme qualification purposes, participants will have the option to disaggregate more flexibly thereafter to allow natural business units to monitor, manage and report their energy use separately, thus introducing greater flexibility. No detail has yet been provided as to what DECC regards or defines as natural business units.

Reducing Overlap with Other Schemes

DECC suggests that sites covered by Climate Change Agreements or within the EU Emission Trading System will automatically be exempt from the Scheme (by being regarded as "self supplies").

Landlord and Tenant

Importantly, DECC proposes no change to the rule that landlords are responsible for supplies of energy to their tenants (unless the tenant arranges and receives the energy supply itself). DECC acknowledges that "the split between landlords and tenants is a difficult area - a classic case of split incentives", but states that alternatives, such as joint responsibility, would be difficult to operate. DECC takes the view that the landlord is in the best position to implement the most cost effective energy efficiency measures.

Conclusion

It is clear that DECC has listened to calls for change and the proposals go some way to achieving its stated aims of providing greater business certainty, reducing complexity and administrative burden and increasing flexibility for participants.

Alison Lympany
Senior Associate
+44 20 7184 7611
alison.lympany@dechert.com

PLANNING

Planning Update

by **Justin True**

The Administrative Court has clarified the time limit for bringing judicial review proceedings and the Government has widened the definition of affordable housing to include affordable rented housing.

Time Limit For Judicial Review

The Civil Procedure Rules require an application for judicial review to be made "promptly and in any event within three months". What is "prompt" will depend on the particular circumstances, but it is clear from the cases that it can be less than three months.

Last year the European Court of Justice ruled, in a case dealing with public procurement, *Uniplex (UK) Ltd v NHS Business Services Authority*, that the requirement that a challenge must be made promptly was not compatible with the principle of certainty in the Procurement Directive and therefore a fixed three month time limit should apply. However, it was not clear whether the principle was restricted to public procurement cases or whether it applied more generally.

The Administrative Court has now answered that question in a case concerning the Environmental Impact Assessment Directive, *R (Buglife) v Natural England*. Buglife – The Invertebrate Conservation Trust was challenging the grant of outline planning permission for the development of a business park by National Grid Property Holdings Ltd on the Isle of Grain in the Thames Gateway. The site provides habitats for rare and protected invertebrates and Buglife considered the environmental statement submitted with the planning application to be inadequate.

Buglife's application for permission to bring judicial review proceedings was made two days before the end of the three month period. National Grid and the local authority argued that the application had not been made promptly. Buglife claimed that the *Uniplex* decision applied so that the application was in time as long as it was made within three months but National Grid and the local authority responded that the *Uniplex* decision was limited to public procurement cases.

The court decided that the *Uniplex* decision applies to proceedings arising out of *any* EU directive, not only the Procurement Directive. Therefore it did apply in this case. However, the court took the view that in the circumstances of this case the application had in fact been made promptly.

It appears that a challenge on planning, rather than environmental, grounds will still have to be made promptly because it is not based on a directive. This gives rise to the possibility that an applicant seeking to challenge a decision on planning grounds might try to include an environmental challenge too in order to extend the time limit to the full three months. It is not clear whether in such circumstances the challenge based on planning grounds could be struck out as being out of time, leaving the environmental challenge to go ahead alone.

Affordable Rented Housing

A revised version of Planning Policy Statement 3: Housing has been published including a new wider definition of affordable housing in Annex B. Affordable housing now includes social rented, affordable rented and intermediate housing.

Affordable rented housing is a new concept. It is let by registered providers of social housing to those eligible for social rented housing but the rent may be up to eighty per cent of the local market rent (including service charges). Local market rents are calculated using the RICS approved valuation methods and the Tenant Services Authority has issued an explanatory note on them. The tenancies may be fixed term or periodic.

Sources: *Uniplex (UK) Ltd v NHS Business Services Authority Case C-406/0; R (Buglife) v Natural England [2011] EWHC 746 (Admin). Planning Policy Statement 3: Housing (www.communities.gov.uk).*

Justin True
Head of Planning
+44 20 7184 7462
justin.true@dechert.com

About Dechert LLP

An international law firm with offices throughout Europe, the United States and Asia, Dechert LLP focuses on corporate and securities, business restructuring and reorganization, complex litigation and international arbitration, real estate finance, financial services and asset management, intellectual property, labour and employment, and tax law.

If you would like to receive any of our other *DechertOnPoints*, please click here.

Dechert LLP

www.dechert.com

EUROPE Brussels • Dublin • London • Luxembourg • Moscow • Munich • Paris • **U.S.** Austin Boston • Charlotte • Hartford • Los Angeles • New York • Orange County • Philadelphia • Princeton San Francisco • Silicon Valley • Washington, D.C. • **ASIA** Beijing • Hong Kong