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Implied terms that consent is "not to be unreasonably withheld" Time to reassess?

> *"Implications of good faith and rationality, and of lack of arbitrariness or perversity, are standard, for they represent the very essence of business, and other, relationships."*
>
> (Socimer International Bank Ltd v Standard Bank London Ltd [2008] 1 Ll Rep 558 *per* Rix LJ)

The aim of this short piece is to draw on commercial cases to inform, challenge, and perhaps provoke further thought.

The scenario

A grant of a property right – such as a lease or a conveyance imposing a restrictive covenant – requires that something cannot be done without the consent of one party (or its successor). It does not say that consent is not to be unreasonably withheld. Will the court imply a term to that effect?

The background

In the commercial context, the courts have long taken the approach that where one party to a contract has to make a decision (not involving the exercise of a contractual right e.g. to terminate), it cannot to do so arbitrarily, capriciously, in bad faith or for an improper purpose.

> *"Contractual terms in which one party to the contract is given the power to exercise a discretion, or to form an opinion as to relevant facts, are extremely common. It is not for the courts to re-write the parties' bargain for them, still less to substitute themselves for the contractually agreed decision-maker. Nevertheless, the party who is charged with making decisions which affect the rights of both parties to the contract has a clear conflict of interest. … The courts have therefore sought to ensure that such contractual powers are not abused. They have done so by implying a term as to the manner in which such powers may be exercised, a term which may vary according to the terms of the contract and the context in which the decision-making power is given.*
>
> (Lady Hale DPSJ in Braganza)

Various principles are available and have been deployed by the courts to achieve that result, depending on the circumstances. A decision may involve a derogation from grant, be contrary to a separate legal or equitable duty (e.g. those imposed on mortgagees and fiduciaries), or be regarded as not complying with what the contract requires on its true interpretation (e.g. where is it not, in substance, a true 'decision' or 'judgment' of the sort contemplated). Often, though, particularly where only a contractual duty will achieve this result, the courts have looked to the implication of terms.

The approach to implication is the same as for other terms, as reiterated in Marks and Spender plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd [2015] UKSC 72. Thus, the implication of a term as to reasonableness is not automatic, either in commercial cases (e.g. Gan Insurance Co Ltd v Tai Ping Insurance Co Ltd (No.2) [2001] EWCA Civ 1047 at [62]) or in property cases (e.g. Price v Bouch (1987) 53 P&CR 257 at 258; Cryer v Scott Brothers (Sunbury) Ltd (1988) 55 P&CR 183 at 202).

Whether to make an implication will depend on the circumstances of each case, but as a general proposition (*per* Leggatt LJ in Abu Dhabi National Tanker Co v Product Star Shipping Ltd (The Product Star) (No.2) [1993] 1 Lloyd's Rep 397 at 404):

> *"Where A and B contract with one another to confer a discretion on A, that does not render B subject to A's uninhibited whim. … the authorities show that not only must the discretion be exercised honestly and in good faith, but, having regard to the provisions of the contract by which it must be conferred, it must not be exercised arbitrarily, capriciously, or unreasonably. That entails a proper consideration of the matter after making any necessary inquiries."*

The basic principle was also put in typically straight-forward and pragmatic terms by Brooke LJ in Ludgate Insurance Company Ltd v Citibank NA [1998] Lloyd's Rep. I.R. 221 at [35]:

> *"It is very well established that the circumstances in which a court will interfere with the exercise by a party to a contract of a contractual discretion given to it by another party are extremely limited. … [The] cases show that provided that the discretion is exercised honestly and in good faith for the purposes for which it was conferred, and provided also that it was a true exercise of discretion in the sense that it was not capricious or arbitrary or so outrageous in its defiance of reason that it can properly be categorised as perverse, the courts will not intervene."*

The frequent underlying reasoning was summarised by Potter LJ in Horkulak v Cantor Fitzgerald International [2005] ICR 402 at [30]:

> *"… it is presumed to be the reasonable expectation and therefore the common intention of the parties that there should be a genuine and rational, as opposed to an empty or irrational, exercise of discretion."*

This has been given renewed impetus by the decision of the Supreme Court in Braganza v BP Shipping Ltd [2015] 1 WLR 1661, an employment contract case: see the extract quoted above. There is a second, potentially significant aspect to Braganza – the scope and effect of any implied term – but that is a separate question, not covered here.

Property contracts

Does the same approach apply to contracts relating to property? There is no reason in principle to distinguish between property contracts and commercial contracts. The context may be different, but the same principles for the implication of terms apply to both, and recent cases confirm the lack of difference in principle. Indeed, the principles identified in such cases as in International Drilling Fluids Ltd v Louisville Investments (Uxbridge) Ltd [1986] Ch 513, Iqbal v Thakrar [2004] EWCA Civ 592 and Ashworth Frazer Ltd v Gloucester City Council [2001] UKHL 59 have been applied or seen as a useful analogy in other contexts, such as when considering a commercial contract adopting the "not to be unreasonably withheld" formulation: e.g. Porton Capital Technology Funds & others v 3M Holdings Ltd [2011] EWHC 2895 (Comm).

If there is no difference, why should property contracts not also be subject to the "standard" implications to which Rix LJ referred in the quotation at the start of this article?

Property lawyers are used to seeing the conventional phrase "not to be unreasonably withheld" in property contracts, as well as property grants. The degree to which, and ways in which, this might differ from the sorts of term implied in commercial contracts (including in the light of Braganza) is debatable, but there are obvious similarities.

In Cryer, the Court of Appeal approved the comment of Millett J in Price v Bouch that:

> *"there is no general principle of law that, whenever a contract requires the consent of one party to be obtained by the other, there is an implied term that such consent is not to be unreasonably refused"*

That no doubt still holds good in principle, but over 30 years later, might it be a little too emphatic? Does it reflect current commercial expectations?

Property grants

Grants of property rights commonly include **partially qualified covenants** (i.e. those subject only to obtaining consent). Property lawyers are used to treating these differently from **fully qualified covenants** (i.e. where consent is not to be unreasonably withheld); but how far does that distinction still hold good?

In most leases which require the landlord's consent to disposals, a requirement that consent is not to be unreasonably withheld is implied by statute (Landlord and Tenant Act 1927 s.19(1)(a)).

It is generally assumed that the situation is different in relation to covenants against alterations or changes of use "without the landlord's consent", and that the court will not imply a requirement that consent is not to be unreasonably withheld as a matter of contract.

That assumption may have arisen following two first instance decisions: Guardian Assurance Co. v Gants Hill Holdings [1983] 2 E.G.L.R. 36 (Mervyn Davies J) and Pearl Assurance plc v Shaw [1985] 1 E.G.L.R. 92 (Vinelott J). Both cases concerned clauses prohibiting changes of use without consent. In both, the judges identified that there were both partly and fully qualified provisions in the lease. That was a major factor which led them to refuse to imply a full qualification into a partly qualified covenant.

That will often be the position in a modern lease, with a mixture of fully and partially qualified covenants. If so, then that may well be a strong factor against implication; but is it enough? And what about leases or other grants without such a contrast? Will the use of this form of words always lead to the same conclusion?

The assumption may also derive in part from the court's refusal to imply a similar limitation in Lord Tredegar v Harwood [1929] AC 72 (a lease case concerning the landlord's approval of an insurance company), applied by the Privy Council in Hang Wah Chong Investment Co v AG of HK [1981] 1 WLR 1142 (a case of covenants in conditions of sale in an agreement for lease). In neither case was the analysis extensive, but for Lord Shaw (one of the 3:1 majority) in Tredegar, the failure to adopt the standard wording seems to have been an important consideration:

> *"The forms of contract, under which the reasonableness of withholding consent is made a term, are perfectly familiar, and they were not adopted in the present case; and the condition of the lessor's consent is a condition precedent in absolute terms."*

Does this now need to be reconsidered?

Those cases, and the long-standing approach to partially qualified covenants in this sort of situation (especially in leases), are likely to mean that the courts will continue to be reluctant for some time yet to imply a proviso that any required consent is not to be unreasonably withheld (except where statute requires it). The long-term nature of property grants, and the proprietary relationships that they create, may also be an important point of difference from ordinary contracts. Nevertheless, the following points may be worth thinking about:

1. These sparingly analysed decisions do not undermine the general approach to the implication of terms, as applied in other cases in the 1980s such as Price v Bouch and Cryer. Indeed, in Cryer at pp.192-194 and 202, the Court of Appeal said that the judge (who relied on Tredegar and Gants Hill) was wrong not to imply a proviso as to reasonableness. Neither Cryer nor Price v Bouch encourages the making of implications as a matter of course, but they emphasise the importance of the context.

2. Both judges in Gants Hill and Pearl Assurance rejected an *obiter dictum* of Shaw LJ in Bocardo SA v S&M Hotels Ltd [1980] 1 WLR 17 at 22:

> *"… the [statutorily] deemed proviso, 'such … consent is not to be unreasonably withheld,' applies only if and to the extent that the covenant or agreement in the lease, by its terms, provides for assignment with consent. Such a provision would, in strict law, be meaningless or ineffective, unless it were to have implied in it some such term as 'such … consent is not to be unreasonably withheld.' For if the landlord was entitled to refuse consent at his own entirely unrestricted discretion, the provision for assignment with consent would add nothing to, and subtract nothing from, the effect in law of the contract as it would be without those words being included. For a contracting party is entirely free to agree to a variation of the contract at the request of the other party. That applies equally where, as here, the variation of the contract would constitute a novation. It seems to me to follow that the effect of section 19(1) of the Act of 1927, on its true analysis, was merely to make statutory an implied term which must already have been implied, if the express words were to have any sensible purpose."*

Nearly 40 years on, more attention might be paid to that *dictum*, even though it may give too little weight the point that a partial qualification enables consent to be given without a variation or novation (or, indeed, a waiver).

3. A contrast with other, fully qualified covenants in the same document will often have considerable weight against implying a term into partially qualified covenants, but it will not be conclusive; and not every contract or grant contains contrasting covenants.

4. The nature of the clause makes a difference. The courts are already more open to making an implication into a clause which allows something but requires consent to a particular aspect of it (e.g. a clause which permits alterations only in accordance with approved plans or details): i.e. clauses which presume that something will or may be done, but give one party the power to consent to aspects of it. This is to be compared with a clause which prohibits something altogether unless consent is obtained (e.g. no alterations at all without consent): see Cryer. We may yet see more careful consideration of particular clauses, and more sophisticated analysis.

What about the existing cases and our assumptions? Should we now treat these with a little more caution? Perhaps we should.

In Lymington Marina Ltd v McNamara [2007] EWCA Civ 151, what was in issue was a mooring licence under which the licensee could allow others to exercise the rights for short periods, subject to the licensor's approval of the sub-licensee. The licensor accepted that it had to act honestly and in good faith, but rejected any wider duty. The licensor sought to argue that, in the light of Tredegar, the parties would have understood the law to be that there would be no wider implication. The Court of Appeal rejected this (at [32]-[34]):

> *"On [the licensor's] submissions, any terms to be implied into the licence must depend on the state of the law when the licence was executed in 1969. He submits that the parties are likely to have agreed their contract in accordance with the law as they then understood it. The law*

as it stood in 1969 was part of the factual matrix. The licence would have been drafted in the light of the law as it then stood.

In my judgment there can be no necessary implication that, where the parties come to an agreement, that agreement must be interpreted on the basis of the law as it stood when the agreement was made as if it were in some time warp. … If the parties have been content to leave a matter to the general law, they must be taken to have agreed that their agreement should be interpreted in the light of the general law from time to time.

[The licensor] did not submit that the Gan case is inconsistent with the Tredegar case. The issue in each case was the true interpretation of the contractual documents and therefore neither case establishes a rule of law to which the doctrine of precedent applies."

So, even in cases analogous to Tredegar, Gants Hill, Pearl Assurance, it would be wrong to assume that there will be no implication.

Assuming Lymington is right about the common law as part of the contractual context (as Lewison suggests: 'The Interpretation of Contracts', (6th edition), 4.06), it might still be arguable that there is an established interpretation of a standard form of covenant, at least in lease covenants governing disposals, alterations or changes of use : see Lewison, 4.07; and, e.g. Sunport Shipping Ltd v Tryg Baltica International (UK) Ltd [2003] 1 Lloyd's Rep 138 at [28] and Beaufort Developments (NI) Ltd v Gilbert-Ash NI Ltd [1999] AC 266 at 274D. But this, too, should not be pushed too far, particularly in relation to bespoke contracts and grants other than leases; and it is debatable whether it can really be applied with much force to many clauses in leases, at least beyond alterations and changes of use.

Recent cases

In Victory Place Management Company Ltd v Kuehn [2018] EWHC 132 (Ch) (the case of Vinnie the dog), Vos C had to deal with a provision in lease prohibiting pets in a flat "without the written consent" of the management company. Here, it was common ground (see [2]) that a term should be implied. (There was disagreement as to its scope.)

Most recently, in Hicks v 89 Holland Park (Management) Ltd [2019] EWHC 1301 (Ch), a term was implied into a clause referring to the approval of plans, drawings and specifications under restrictive covenants. (The implied term was decided in an earlier judgment (see [11]): the later decision dealt with the consequences of that implication.)

What might the future hold?

We are already having to wrestle more often with a contractually-orientated analysis – e.g. where a tenant's actions justify forfeiture of a lease but may also amount to a repudiation. The implication of reasonableness requirements might become another part of the same trend. Time will tell what effect this has, but might we start to see the following?

1) More willingness to imply terms in these types of case than in the past, even if the implication falls short of a 'full' obligation not to withhold consent unreasonably.

2) More frequent arguments that there should be an implication in partially qualified covenants in leases and other grants, if words such as "in its absolute discretion" have not been used.

3) More arguments about the effect of implied provisos, including the purposes for which the requirement for consent was imposed: i.e. the sort of grounds on which consent can be refused (as in Sequent Nominees Ltd v Hautford Ltd [2019] UKSC 47).

Whatever the future may hold, property lawyers should not allow commercial lawyers to dominate the arguments. If implied restrictions on the ability to refuse consent are gaining greater acceptance, then property lawyers need to shape this development in a way that works in property transactions: not just for landlords and tenants, but for all those involved in property investment, development, and funding.

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