

BRIEFING REPORT
HUFC
GOSC 18TH FEBRUARY 2015

Purpose of briefing - To examine what happened around the lease restructure in 2013/14 and identify any lessons learned overall and from recent events.

This briefing will set out the history, the reasons for the lease restructure, the lessons learned from the process, and the interim arrangements currently being pursued.

Key questions

- Was the lease restructure robust and effective?
- What was the purpose of assigning development rights?
- What alternative options were considered and why were they not pursued?
- What is different about the interim short term lease arrangement?
- What can be done to ensure that leases are managed in the public interest in the future?
- Are there any additional provisions that need to be included in the leases?

Current status

- In November 2014 an application was made to court for forfeiture of the club's leases. Following on from the issue and service of proceedings all monies owed to the council were repaid.
- On 22nd December 2014 following on from the making of a winding up order against HUFC (1939) Ltd, the leases were forfeited by peaceable re-entry. The development agreement was terminated on the making up of the winding up order.
- The official receiver is the current liquidator of the club and has indicated no desire to appeal against that forfeiture and has no grounds to do so.
- The council is now inviting expressions of interest for an interim lease of the stadium.

Background

The old leases

Two leases were granted in 1982 by the then Hereford City Council to Hereford United Football Club (1939) Ltd (“the club”).

Lease 1, the football ground lease:

Granted 12th August 1982 for a term of 33 years expiring 11th August 2015. Subsequently this was extended by a deed of variation to a term of 38 years to 12 August 2020.

Key terms

- Full repairing obligation;
- Tenant to insure premises (against fire only);
- Permitted use as athletic sports and football ground and for ancillary purposes connected with raising of funds for the club or other charitable purpose;
- Obligation to promote and encourage promotion of high class football matches and athletic sporting events professional and amateur;
- No assignment without consent not to be unreasonably withheld;
- Subletting permitted without consent provided to for promotion of football/to certain bodies including the Herefordshire British legion;
- Forfeiture – rent arrears, breach of covenant, winding up;
- Security of tenure;
- 5 yearly market rent reviews

Lease 2, the East Stand:

- Term - 75 years from 12th August 1982 expiring 1st August 2057;
- Tenant to insure premises (against fire only);
- Full repairing obligation;
- Permitted use as social, restaurant or licensed or sporting facilities or combination with shop and offices associated with sporting facilities;
- Assignment permitted with consent not to be unreasonably withheld;
- Underletting permitted but no obligations about what lease to contain;

- Maintenance obligations on landlord - areas coloured brown on plan;
- Forfeiture - rent arrears, breach of covenant, widening up;
- Security of tenure;
- 5 yearly market rent reviews.

The move to new leases

As part of the programme of activity relating to the Old Livestock Market site regeneration, and in response to an approach from the then owners, negotiations commenced with the club in 2011 to restructure the leases. The aim was to facilitate the securing of investment into improvements of the Edgar Street ground at no cost to the council.

This was against the backdrop of the then anticipated development of the adjoining Old Market site and the longer term aspiration to create the urban village. Both these projects adjoin the stadium.

Heads of Terms for the surrender of the old leases and re-granting of new were agreed in September 2011 and signed off by the club and the council in April 2012. Negotiations then took place with the leases finally settled in February 2014. The club had been a tenant of the council for some years and as such as with any other longstanding tenant, their financial situation was known to the council as their landlord. With an existing tenant already entitled to occupy under current leases no new financial checks would have been undertaken or necessary as they would not tell the council what it did not already know. The council wished to help this tenant improve their situation and also improve the ground via investment.

The leases were modern form leases linked to a development agreement to enable the club to develop the ends of the ground and in doing so generate income to carry out improvements to it. They were designed so that the club could seek and obtain investment.

The 2014 leases

Key terms

- Area 1 - football pitch and stadium
- Area 2 - Blackfriars end
- Area 3 - Merton meadow end
- 30 year term;
- Tenant to insure against all usual insurable risks;
- Repair obligation limited by reference to schedule of condition evidencing condition at start of lease but in the event practical completion of redevelopment did not occur within timescales fixed in the development agreement the tenant would become liable for full repairing of the premises;

- Right to request an additional 15 years on the expiry of the term;
- No security of tenure;
- Alienation - the leases prohibit assignment of part only of each lease;
- They allow assignment of the whole subject to consent, which cannot be unreasonably withheld but tenant must have paid all outstanding sums before any assignment and assignee to be assigned membership of the FA;
- No underletting of whole or part without consent. Provisions as to the terms of those underleases including no security of tenure;
- Charging of whole permitted but subject to various conditions including landlord not to unreasonably withhold consent if borrowing is to improve the stadium;
- Forfeiture on rents arrears (including rates), breaches of covenant, CVA, winding up, appointment of receiver/liquidator/administrator. Any charge to have chance to remedy.

Was the lease restructure robust and effective?

The leases sought to achieve a balance between helping the club and protecting the landlord. They were a better protection for the landlord than the old leases. The restructure was effective - the development agreement also comprised an agreement for surrender and grant allowing for the old leases to be terminated and the new ones put in place and for a contribution to legal costs.

With hindsight a question has been raised as to whether these leases should have included a landlord's break clause allowing the council to terminate them triggered by the change of control in the club.

It would be unusual for a commercial lease to contain such a clause. A tenant would resist it as allowing the landlord to interfere in its company and trigger termination not based on its default.

Even if such a clause had been in the leases all this would have allowed is earlier termination by the council but such termination would not have resulted in repayment of any of the monies owing and this would not have operated in the interests of the public.

A break clause is not a mechanism for the rectification of a tenant's default i.e. unpaid rents or breach of repair obligations. Recourse for such default lies in forfeiture. This recourse was used in this instance to gain repossession of the sites occupied pursuant to leases and to get repayment of monies owed.

A break clause is also not the correct mechanism for control of who occupies leased areas. The mechanism for this is the alienation clauses which ensured that if HUFC wished to pass on the leases to another party they had to get the consent of the council to do so. The change of control of the tenant did not change their status as being HUFC (1939) Ltd and therefore did not trigger this.

What was the purpose of assigning development rights?

The council wanted to secure the club's long term future in the football league and create an environment whereby it could either directly or with an external funder/developer undertake commercial development of surplus land at the Blackfriars and Merton Meadow ends to generate income for investment in new stadium or improvements to the existing facilities.

Key terms:

- Provisions concerning the development of the areas at the Merton meadows and Blackfriars ends of the football ground with obligations on HDC to grant long (250 year unless residential use in which case 999 year leases to enable units constructed on the sites to be sold).
- Before any development can commence payment is to be made into an escrow account in the names of the landlord and tenant. What is to be paid is calculated based on the proposed heads of terms for any development with a proposed developer/buyer and what the tenant is going to be paid for that and the lease. Costs incurred by the tenant are deductible from this sum.
- Before actual completion of the grant of the new lease the tenant must notify the landlord the final actual receipts that the buyer is to pay for the grant of the lease and the receipts subject to deduction of all costs incurred in obtain the planning permission and documenting the sale terms and other costs incurred either the terms or development (with the landlord to approve the deduction of such costs) the receipts are to be paid into the escrow account. The tenant is to use such sums for investment into the ground and associated purposes.
- Pre-agreed investment plan for all income generated from the development.
- Pre-approval by the council to the development terms in advance of any legal agreement between Club and funder/developer.
- A timescale by which the development must be undertaken after which development rights lost.
- Long term leases only granted on completion of the new development.
- The agreement was personal to the tenant and therefore not assignable to a third party.

What alternative options were considered and why were they not pursued?

- Do nothing and the Club would be unlikely to secure any significant funding for further investment in improvements to the stadium.
- The council agree terms to take part area 2 & 3 as a partial surrender of original leases and take direct control the redevelopment. Financial cost to council, receipt to the Club insufficient to deliver required investment, potential state aid risk.

What is different about the interim short term lease arrangement?

- There will be one lease of the ground only with limited rights to use other areas for access and collecting footballs only. Route can be altered by landlord;
- Short term - only runs from March 2014 - July 2017 and no renewal rights;
- No alienation - no assignment or subletting permitted at all;
- Tenant must at all times be a member of the FA;
- Change of control termination clause. Neither the old leases nor the new leases continued a provision allowing the landlord to terminate - a landlord's break clause - on the change of control of the company comprising the tenant. This is a clause used in commercial contracts but unusual in commercial leases. It would if in the leases have allowed for earlier termination but it would not have resulted in any payment to the council which the standard forfeiture route used did;
- This is to be included in the interim lease now being offered and may be included in a future long term lease which will be the subject of a separate report at that time;
- Forfeiture wider so any insolvency event triggers the right;
- Obligation on tenant to maintain lighting rig;
- It is being dealt with in house led by the asset management team with in house legal representation.

What can be done to ensure that leases are managed in the public interest in the future?

The council has now taken control of all sites leased to the club. The council will lease the ground only and retain control of the ends of the ground leaving it open to the council to develop itself or seek other opportunities as to the sites in the public interest and in accordance with its duties and powers.

Are there any additional provisions that need to be included in the leases?

There is only one lease and additional terms include those items listed above.