Enforcement of planning obligations

Matt Hutchings QC considers some of the lessons to be learned from his experience of acting for the London Borough of Southwark when enforcing s106 agreements

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'The use of third-party funding in the context of affordable housing obligations in s106 agreements has not obtained the same level of publicity it has in a right-to-buy context.'

I recently acted on behalf of the London Borough of Southwark, which brought claims in the Chancery Division to enforce affordable housing obligations imposed by s106 agreements. These claims were recently concluded by settlements approved by the High Court, and raised a number of legal issues of relevance to practitioners in this area, including:

- the interface between public and private law;
- drafting s106 agreements to counter avoidance schemes;
- the choice of remedies to enforce planning obligations; and
- the relevance of the public interest to enforcement by injunction.

Outline of the facts

The claims concerned mixed, predominantly housing developments at four sites within Southwark. The developers entered into s106 agreements with the local planning authority, the London Borough of Southwark (LBS), which included affordable housing obligations substantially based on the model agreement published by the Law Society's Planning and Environmental Law Committee in 2010.

The s106 agreements required the developers to construct a defined number of affordable housing units (AHUs) and for head leases of the AHUs to be granted to an approved registered provider to deliver the affordable housing. The agreements imposed affordable housing obligations, potentially in perpetuity, requiring the AHUs not to be used otherwise than as 'affordable housing' for households in need of it. 'Affordable housing' was defined as either intermediate rented or shared ownership housing. Income limits for potential tenants were prescribed by the s106 agreements, in order to ensure that the affordable housing went to households who could not afford to buy or rent on the open market.

For the uninitiated, shared ownership is an affordable housing model under which the tenant buys a notional share of the leasehold title (typically a minimum of 25%) and pays rent on the unowned share. The tenant can increase their share by buying a further percentage as and when they are willing and able to afford to. This process is known as 'staircasing'.

Each of the s106 agreements provided that the affordable housing obligations would not be binding on:

> ... any tenant staircasing to 100% pursuant to a shared ownership lease [and their successors in title and mortgagees]...

(the exception clause). In other words, once a tenant had staircased to 100% under a shared ownership

lease, the affordable housing obligations came to an end.

At each of the sites, purported shared ownership leases were granted to individuals selected by the appointed registered provider on the basis of qualifying under the prescribed income limits. It was claimed that these individuals had staircased to 100% ownership upon or shortly after the grant of the shared ownership leases. The leases were then sold at full market value either to property investment companies or to individuals buying them for use as ordinary market housing.

The above pattern of transactions is highly unusual in shared ownership housing. By definition, individuals eligible for shared ownership leases have a limited income and therefore require many years before they can afford to purchase their properties outright, if at all.

Upon investigation by LBS, it emerged that from the outset the individual tenants had held the shared ownership leases on trust for property investment companies (the companies), which had funded the (discounted) purchase prices. LBS obtained evidence that these individuals had never moved into the AHUs. It was admitted that the companies had paid the individuals to sign the relevant transactional documentation. Further, the declarations of trust that they executed gave the companies control over and responsibility for liabilities in respect of the properties. Once the shared ownership leases had apparently been staircased to 100% ownership, the companies (as beneficial owners) sold the leases to market-value purchasers, making a profit. In the context of an overheated London property market, such profits were substantial.

The net result was that the AHUs intended for use as affordable housing had never been used as such. However, the registered provider, the companies and the current owners of the AHUs claimed that these transactions were permitted by the s106 agreements and had successfully triggered the exception clause, so that the affordable housing obligations had come to an end.

In June 2015 LBS brought a claim in the Chancery Division of the High Court seeking declarations that the AHUs were still bound by the affordable housing obligations and injunctions requiring the AHUs to be used as affordable housing, or alternatively damages for breaches of the s106 agreements. At an early stage, LBS obtained interim injunctions or undertakings restraining further onward sales of the AHUs. The claim was later amended to bring in two further development sites and in June 2016 a further, similar claim was brought in respect of a fourth site.

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Following mediation, by a number of settlement agreements the claims were concluded with the return of a total of 26 flats to affordable housing use.

In March 2017, under the first settlement LBS reached an agreement with the registered provider, the companies and other property investment companies that had bought 18 of the AHUs, whereby 17 flats were sold to a new registered provider for use as affordable housing under the terms of a varied s106 agreement.

In July 2017, under the second batch of settlements LBS reached agreements with individual purchasers of the leases at the fourth site and their banks, under which injunctions were granted requiring the nine flats to be used as affordable housing, suspended for a period of one year, and LBS was granted options to purchase the flats within this period at their agreed affordable housing value. The High Court judge approved these settlements and granted declarations against the leaseholders and banks that the AHUs were bound by planning obligations requiring them to be used as shared ownership housing.

The interface between public and private law

The legal basis for the imposition of planning obligations under s106 of the Town and Country Planning Act 1990 lies in planning legislation and policy, the enforcement of which is a matter of public law. Planning obligations may be subject to challenge in judicial review proceedings on a wide range of public law grounds. However, once the period for a public law challenge has expired, their enforcement is primarily a matter of private law.

Thus, s106 agreements are treated by the courts in a similar way to other contracts, albeit contracts which are, by virtue of s106(3), enforceable against successors in title. To what extent is the planning background admissible as an aid to construction of a s106 agreement?

In *Stroude v Beazer Homes* [2006], a case about the implication of terms into a s106 agreement, Warren J stated at para 38 that:

> ... first and foremost, the section 106 Agreement is a contract between the parties to it which, in my judgment, falls to be construed according to ordinary principles of construction. The fact that the section 106 Agreement is made in the context of the statutory provisions is, no doubt, part of the factual matrix against which it has to be construed; accordingly, it should be construed, so far as possible, in a way which enables the statutory provisions to operate.

In the Southwark cases, the affordable housing obligations had been imposed in accordance with the development plan at the time of the grant of each planning permission, in particular the London Plan (2011), the Southwark Core Strategy (2011) and saved policies from the Southwark Plan, which identified the provision of affordable housing as a key strategic and local planning objective. These policies were expressly identified as reasons for the imposition of the planning obligations within the decisions granting planning permission. The transactions described above were designed as an avoidance scheme, which, if successful, had the

effect of undermining these policy objectives.

There is authority that clauses of a contract should not be interpreted in such a way as to undermine its main purpose (alternatively, a similar result may be achieved by the implication of a term into the contract). *Bankway Properties Ltd v Dunsfold* [2001] was a case about a clause in an assured tenancy agreement, drafted as a device whereby the landlord could increase the rent to £25,000 per annum and thus remove the tenant's security of tenure. At para 68 Pill LJ stated that the clause in question:

> ... is, in my judgment, inconsistent with the statutory purpose which it was the main object of the agreement to achieve. In the *Glynn* case [1893] AC 351, 357 Lord Halsbury stated:
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> > 'Looking at the whole of the instrument, and seeing what one must regard... as its main purpose, one must reject words, indeed whole provisions, if they are inconsistent with what one assumes to be the main purpose of the contract.'

LBS argued that the exception clause should not be interpreted in such a way as to defeat the main aim of the affordable housing provisions of the s106 agreements, which was illuminated by the planning policies, which they were intended to implement. In particular, it would defeat their aim if the exception clause was triggered by transactions which were devices whose only commercial purpose was to avoid the affordable housing obligations.

In the event, LBS did not need to rely heavily on the above line of argument. This was because it obtained compelling evidence that the shared ownership clauses of the leases, and the purported staircasing transactions, were a sham. This evidence was obtained through non-party disclosure applications brought against the solicitors that acted for the registered provider and the tenants in relation to the grant of the shared ownership leases. The solicitors' ledgers showed that the full premiums for the leases had been paid before completion, and that no staircasing transactions had in fact taken place.

Nevertheless, the interesting question for practitioners is whether or not, if the avoidance schemes had been operated in accordance with the transactional documents, they would have achieved their purpose.

Drafting s106 agreements to counter avoidance schemes

Avoidance schemes present a dilemma for the draftsman of s106 agreements. On the one hand, it is desirable to include express provisions to counter any well-known avoidance schemes. On the other hand, detailed anti-avoidance clauses may simply lead to more sophisticated avoidance schemes. Further, the existence of express anti-avoidance clauses may add force to the argument that, the s106 agreement having expressly forbidden a particular kind of avoidance scheme, a differently designed scheme is permitted.

In these cases, the defendants' defence was that the literal requirements of the exception clause had been complied with and therefore it simply followed from the wording of the s106 agreements that the affordable housing obligations had ceased. Further, the defendants argued that there was nothing in the s106 agreements that prohibited the tenants from having recourse to third-party funding or executing declarations of trust in favour of the funders, and nor was there any express requirement that the tenants should occupy the AHUs for any minimum period before 100% staircasing took place.

The issue of third-party funding being used to subvert tenants' rights is a familiar one in other housing contexts. Social tenants are given a right to buy a leasehold interest in their property at a substantial discount, usually on the basis that if they dispose of that interest within a period of five years, the discount is repayable. It is a common occurrence that third-party finance is offered to social tenants enabling them to exercise the right to buy on the condition that, after the period of five years has expired, the leasehold interest is conveyed to the finance company. While legally permissible, this type of arrangement undermines the aim of promoting home ownership by social tenants. The use of third-party funding in the context of affordable housing obligations in s106 agreements has not hitherto obtained the same level of publicity it has in a right-to-buy context.

The transactions were designed as an avoidance scheme, which, if successful, had the effect of undermining LBS's policy objectives.

The simplest way in which to inhibit avoidance schemes of the type employed in the Southwark cases would be to include in the s106 agreement a prohibition on dispositions, or contracts to dispose, of any legal or equitable interest in respect of the AHUs, save to individuals meeting the prescribed income limits. LBS imposed such a prohibition under the terms of the varied s106 agreement entered into with the new registered provider as part of the first settlement referred to above.

Given that it is not possible to anticipate every type of avoidance scheme that may be employed by enterprising property investors, even if such clauses are included, it is likely that there will remain a role for purposive interpretation along the lines discussed in the preceding section.

Choice of remedies to enforce planning obligations

Section 106 of the Town and Country Planning Act 1990 expressly provides for two methods of enforcement:

- an injunction under s106(5); and
- where the s106 agreement imposes an obligation to carry out operations, self-help under s106(6).

An injunction is normally viewed as the remedy of choice. Injunctions

are a flexible remedy that can cover a wide variety of situations, including pre-emptive injunctions restraining a threatened breach, injunctions requiring the effect of a past breach to be reversed, or specific performance enforcing positive obligations. It is normally axiomatic that the injunction must be sought from a current owner of the land, and it is usual for s106 agreements to provide that, once an owner has parted with their interest in the land, they are no longer bound by the relevant planning obligation.

Hitherto, the potential availability of damages for breach of planning obligations has not received much attention by the courts. The local planning authority will usually be the party enforcing the s106 agreement. Ordinarily, it will not own any relevant land and therefore will not suffer any financial loss caused by the breach. When granting injunctions in favour of local planning authorities, the courts have often stated that damages would not be an adequate remedy, precisely because the only damages recoverable would be nominal: see eg *Avon County Council v Millard* [1985].

LBS's case was that only an injunction would be an adequate remedy, because any damages recovered would be insufficient to enable it to replicate the public benefit secured by the s106 agreements, namely affordable housing within desirable developments in its area. However, as a fallback, and in case the court exercised its discretion to refuse an injunction, LBS advanced an alternative claim for substantial damages. These were claimed on a negotiation damages basis (often referred to as *Wrotham Park* damages), ie a reasonable fee for the release of the affordable housing obligations. Supported by expert valuation evidence, LBS calculated these damages as 50% of the profits made by the owners of the land by reason of their breaches of the planning obligations.

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Negotiation damages have in recent years received considerable attention from the courts and have been awarded with increasing frequency: see for example *Lunn Poly Ltd v Liverpool & Lancashire Properties Ltd* [2006] and *Pell Frischmann Engineering Ltd v Bow Valley Iran Ltd* [2009], and in the context of trespass *Stadium Capital Holdings (No. 2) Ltd v St Marylebone Property Company* [2011], *London Borough of Enfield v Outdoor Plus Ltd* [2012] and *Eaton Mansions (Westminster) Ltd v Stinger Compania de Inversion SA* [2013].

As a result, the principles applicable to the assessment of negotiation damages are well developed. However, although they are often claimed and awarded in respect of the breach of negative covenants affecting land, there are no reported cases in which negotiation damages have been awarded in respect of the breach of planning obligations. There appears to be no reason in principle why they should not be available in this context also.

Relevance of the public interest to enforcement by injunction

The defendant leaseholders at the fourth site argued that the grant of injunctions enforcing the affordable housing obligations against them would be oppressive. In particular, they had purchased leases at full market value in the belief that the transactions in respect of the AHUs had triggered the exception clause, as appeared on the face of the transactional documents. A number of them were individuals of limited means, who had taken out substantial mortgage liabilities on this basis.

The main thrust of LBS's response to this argument was that the affordable housing obligations had been established in the public interest; the provision of affordable housing was an important strategic objective of LBS and there was a great need for homes in London accessible to people on low and middle incomes. In short, the public interest outweighed any individual hardship that the grant of injunctions would cause.

Injunctions are a discretionary remedy. This suggests that there is some scope for the court to conduct a balancing exercise between the public interest and private hardship in relation to the grant of an injunction enforcing a s106 agreement. However, it is a given that a planning obligation lawfully imposed was enacted in the public interest and hence its enforcement is also likely to serve the public interest. The enforcement of a planning obligation cannot, without undermining the applicable statutory scheme, be the occasion for re-arguing the planning merits of the s106 agreement.

In *London Borough of Newham v Ali* [2014] the Court of Appeal held that the discretion of the court in this context was relatively limited. At para 20 Lord Dyson MR stated that:

> In my judgment, where there has been a substantial breach of a planning obligation under section 106 of the 1990 Act, an injunction will normally be granted unless the local planning authority has acted in a way which justifies withholding relief on ordinary equitable principles. The fact that there is an outstanding planning appeal will usually be irrelevant. That is because the matters to which a local planning authority must have regard when making a planning decision concerning matters of planning control (for example, determining an application for planning permission, seeking an injunction under section 187B of the 1990 Act or taking direct action under section 178 of the 1990 Act) are not matters to which a local planning authority is required to have regard when deciding whether to seek an injunction under section 106 (5) or to which the court should have regard when deciding whether to grant such an injunction.

Further, at para 23 Lord Dyson MR stated that it was not open to a defendant to argue that the planning obligation no longer served a valid planning purpose, for the following reasons:

> If a person wishes to contend that a planning obligation no longer serves a planning purpose, then it should seek to discharge or modify the obligation under section 106A or 106B. That is the route by which Parliament decided that a person might be relieved from its planning obligation.

Newham was a case in which the defendant himself had entered into the relevant s106 agreement, the obligations under which he resisted the enforcement of. Where the original contracting party seeks to resile from a planning obligation it entered into, it may easily be seen that it is seeking to retain the benefit of the planning permission while avoiding the attendant burdens: see *J A Pye (Oxford) Ltd v South Gloucestershire DC* [2001] at para 26. However, the same applies to subsequent owners of the land: by using the land in the way permitted by the planning permission they are benefiting from it; the planning obligations are the reverse side of the same coin.

The enforcement of a planning obligation cannot, without undermining the applicable statutory scheme, be the occasion for re-arguing the planning merits of the s106 agreement.

In entering into settlement agreements with LBS, the defendant leaseholders recognised that they could not establish that LBS had acted in a way which justified the court withholding relief on ordinary equitable principles, and that the public benefit secured by the affordable housing obligations prevailed over the individual hardship caused to them by their enforcement.

Conclusions

Drawing on my experience of the Southwark cases, I offer the following conclusions for the consideration of practitioners in this field:

- Caution should be applied when relying on an exception to a planning obligation. Even if the circumstances of your case satisfy the literal requirements of an exception clause, there may be scope for a purposive interpretation. This is particularly so if you are relying on artificial transactions designed to avoid the planning obligations.

- The potential use of third-party funding to get around affordable housing obligations, which diverts affordable housing resources away from those who need it, is an issue that merits specific consideration by those drafting s106 agreements.

- While an injunction remains the remedy of choice for the enforcement of planning obligations, there is no reason in principle why negotiation damages should not be available and this remains a relatively unexplored area of the law.

- Defendants seeking to resist the enforcement of planning obligations on the basis of oppression face a steep uphill task in the absence of unconscionable conduct by the local planning authority. ■

Avon County Council v Millard (1985) 50 P&CR 275

Bankway Properties Ltd v Dunsfold & anor [2001] EWCA Civ 528

Eaton Mansions (Westminster) Ltd v Stinger Compania de Inversion SA [2013] EWCA Civ 1308

J A Pye (Oxford) Ltd v South Gloucestershire DC & ors [2001] EWCA Civ 450

London Borough of Enfield v Outdoor Plus Ltd [2012] EWCA Civ 608

London Borough of Newham v Ali & ors [2014] EWCA Civ 676

Lunn Poly Ltd & anor v Liverpool & Lancashire Properties Ltd & anor [2006] EWCA Civ 430

Pell Frischmann Engineering Ltd v Bow Valley Iran Ltd & ors [2009] UKPC 45

Stadium Capital Holdings (No. 2) Ltd v St Marylebone Property Company & anor [2011] EWHC 2856 (Ch)

Stroude v Beazer Homes [2006] EWHC 2686 (Ch)