What is a virtual assignment?

"For those who do not gambol in this arcane field and have not previously encountered a "virtual assignment", let me endeavour to explain what it is. I cannot do better than repeat the Judge's description:

'a "virtual assignment" is an arrangement under which all the economic benefits and burdens of the relevant lease (including any management responsibilities) are transferred to a third party, but without any actual assignment of the leasehold interest or any change in the actual occupancy of the premises in question. It is typically employed where the relevant lease contains covenants against the assigning or parting with the possession of the demised property without the consent of the Landlord, and there are concerns either that the Landlord may be unwilling to consent to a legal assignment of the lease because of perceived concerns about the financial standing of the assignee, or that the Landlord's consent may not be available in advance of the scheduled date for completion of the transaction.'

"It has other uses: it can be employed as a means of removing lease liabilities from the balance sheet; capital can be released to be better invested elsewhere in the assignor's business; property risks can be transferred to a third party; the assignor's property liabilities can be more closely aligned to business needs because surplus property can be vacated before the term of the lease expires."

So said Lord Justice Ward in Clarence House Limited v National Westminster Bank plc. This was the Court of Appeal decision declaring that the virtual assignment to which National Westminster Bank plc had been a party was not a breach of the alienation provisions in the lease under which the Bank was tenant. This decision overturned the High Court's judgement to the contrary.

Are they here to stay?

Whether or not a particular virtual assignment contravenes the alienation provisions of a lease depends, of course, on the particular provisions of the Lease and of the virtual assignment. However this decision does give considerable support to the validity of such a transaction and the fact that it does not result in a breach of standard alienation provisions. Ward LJ quoted an Estates Gazette article on 23 May 2009, where it was said of a virtual assignment that it is "an invaluable mechanism which has facilitated a number of vital portfolio transactions for tenants without damaging Landlord's interests...it is here to stay and the market should be grateful". Now that the Court of Appeal has made this decision that comment may well prove true.

Having said that, landlords are already taking steps to prohibit virtual assignments; alienation provisions in many new draft leases make it quite clear that the tenant is not entitled to effect these.

Each landlord must make his own decision on whether to prohibit these. A tenant would certainly argue that the landlord is not prejudiced by such a transaction. He still has the same tenant and the person in occupation of the property will not change. In many situations, a tenant is unlikely to be in a position to contemplate effecting a virtual assignment. However, where a tenant might benefit from the right to make one but his lease prohibits him, then he might raise at rent review the argument that the lease is less valuable with a prohibition against such action. Perhaps then, a landlord will regret changing his precedent lease to include a provision prohibiting "a transfer to any third party of the economic benefits and/or burdens" of the lease.
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