



Law
Commission
Reforming the law



Commercial Leasehold: overcoming barriers to transactions

Summary of Consultation Paper

Our consultation

Who are we?	The Law Commission of England and Wales is an independent body established by statute to make recommendations to the Government to reform the law in England and Wales.
What is it about?	<p>(1) The right of first refusal (contained in the Landlord and Tenant Act 1987) which, in many cases, requires a landlord who plans to sell, grant a lease or otherwise dispose of its interest in a block of flats to a third party, to offer it first to the residential leaseholders.</p> <p>(2) An anti-avoidance provision contained in the Landlord and Tenant (Covenants) Act 1995, which can adversely impact commercial leasehold transactions (such as assignments and guarantees) between members of the same group of companies and within partnerships.</p>
What are we doing?	<p>Conducting a public consultation on targeted reforms to facilitate commercial leasehold transactions. In particular, we are consulting on:</p> <p>(1) whether the right of first refusal for residential leaseholders should be triggered on the grant of a commercial lease in mixed-use premises; and</p> <p>(2) whether assignments and guarantees should be permitted when they involve members of the same group of companies, partnerships and other closely connected parties.</p>
Why are we consulting?	We are seeking views on whether the law needs to change. Consultation is essential to our work. We want any recommendations we ultimately make to have as strong an evidence base as possible.
Who do we want to hear from?	We would like to hear from as many stakeholders as possible, including business tenants, landlords, representative groups, property professionals, judges, academics, researchers, and members of the public. We are also interested in hearing from residential leaseholders and representative bodies, particularly in relation to our proposals regarding the right of first refusal.

Where can I find the Consultation Paper?	The full Consultation Paper is available on our website: https://lawcom.gov.uk/project/commercial-leasehold .
When is the deadline?	The deadline for responses is 16 September 2026.
Are there other consultations?	In parallel to this consultation, we are running another consultation on reform to security of tenure for business tenants under the Landlord and Tenant Act 1954. That consultation is available at: https://lawcom.gov.uk/project/business-tenancies-the-right-to-renew .
What happens next?	After reviewing all responses, we will publish our recommendations about whether the law should change in a final report. It will be for the Government to decide whether to implement our recommendations.
How to respond	<p>We encourage you to submit your response to the Consultation Paper using the online form available at: https://consult.justice.gov.uk/law-commission/commercial-leasehold-consultation. If possible, please use this method.</p> <p>Otherwise you can respond to us:</p> <ul style="list-style-type: none"> • by email to: BusinessTenancies@lawcommission.gov.uk • by post to: Business Tenancies Team, Law Commission, 1st Floor, 52 Queen Anne’s Gate, London, SW1H 9AG. <p>For further information about how the Law Commission conducts its consultations, and our policy on the confidentiality and anonymity of consultees’ responses, please see page ii of the Consultation Paper.</p>

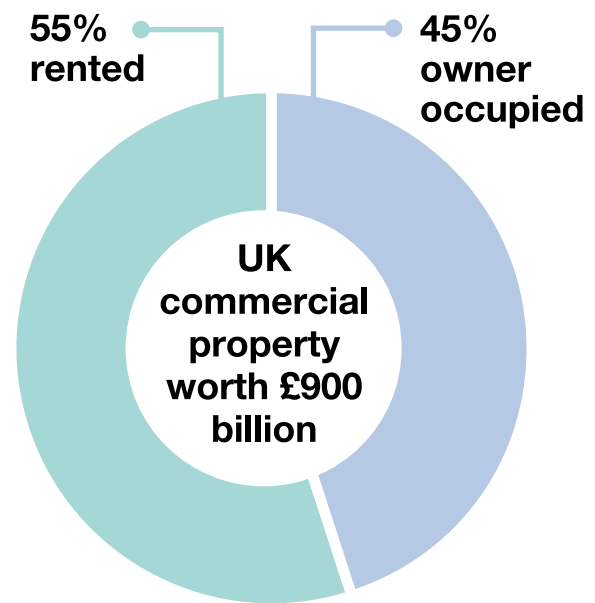
Introduction

There are around 5 million businesses in England and Wales. Some trade from the owner's home or garage, or provide services at a customer's place of business. But, for many, the business will have its own base, for example a shop on a high street, a workshop on an industrial estate, an office in a city centre, or a warehouse at the junction of a motorway. Some businesses trade from just one property. Other businesses have many locations from which they operate.



While some businesses own the freehold of the properties from which they operate, many occupy their premises as tenants, renting them from a landlord. Leasing can offer flexibility, reduce capital outlay, and allow businesses to adapt to changing circumstances.

Given the scale of the commercial leasehold market, even modest inefficiencies in the law can generate substantial cumulative costs in terms of time, expense, and uncertainty. In addition, uncertainty about the validity of (or legal requirements for) routine transactions is bad for business, creating a barrier to productivity and growth.



Our project

This project examines specific issues affecting commercial leasehold transactions that arise from two pieces of legislation:

The right of first refusal under Part 1 of the Landlord and Tenant Act 1987 (“1987 Act”): where a landlord proposes to make a disposal of all or part of its interest in a block of flats – for example, by selling its freehold interest, or granting a lease of the non-residential parts – it is often under an obligation to give residential leaseholders the option to acquire the interest before disposing of it to a third party. This is called the “right of first refusal”. We have heard that the right of first refusal may be operating inappropriately in developments where there is a mixture of residential and commercial premises.

The Landlord and Tenant (Covenants) Act 1995 (“1995 Act”):

after a lease is granted the landlord or the tenant may transfer – or assign – their interest in it, for example a tenant who owns a shop might sell its interest in the lease to another shopkeeper. The main reason the 1995 Act was introduced was to avoid an original party to a lease, in particular a tenant, being bound by its terms after assigning its interest. In doing so, the 1995 Act corrected an unfairness in the then existing law. However, we understand that provisions in the 1995 Act are causing unnecessary practical problems in commercially important and sensible arrangements.





Scope of our project

The 1995 Act applies to many types of leases, including residential and commercial leases, and the right of first refusal in the 1987 Act is intended to benefit residential leaseholders. However, our project is focussed on the operation and impact of these Acts only in the commercial leasehold context. We are aware that there remain problems and concerns relating to the 1987 Act and 1995 Act either generally, or specifically in the residential leasehold sphere, on which we do not consult. This is unavoidable bearing in mind the scope of this project.

It is an important part of our work that we do not adversely affect residential leaseholders by any recommendations that we make.

The project is technical and targeted. It does not aim for wholesale reform of commercial leasehold law, nor does it question the fundamental policy objectives that underpin either Act. Instead, it considers whether particular aspects of these regimes are operating as intended so far as commercial leasehold transactions are concerned, or are generating unintended consequences, uncertainty, delay, and cost.

Relationship to other Law Commission work

This project runs alongside the Law Commission's Business Tenancies project. The Business Tenancies project focuses on Part 2 of the Landlord and Tenant Act 1954 ("1954 Act"), which gives business tenants "security of tenure" - the right to renew their tenancies when they would otherwise come to an end (subject to landlords and tenants agreeing that the right should not apply). We published a first consultation paper on that project in November 2024 and have recently published a second consultation paper, which is available, together with a summary, at <https://lawcom.gov.uk/project/business-tenancies-the-right-to-renew>.

Both projects share the objective of improving commercial leasehold law and are being progressed in tandem, with the intention that our final recommendations will be presented together.

Where we refer to the Consultation Paper in this Summary, it is a reference to the Consultation Paper "Commercial Leasehold: overcoming barriers to transactions".

Our consultation

We have published a detailed Consultation Paper (available at <https://lawcom.gov.uk/project/commercial-leasehold>) that asks questions and makes provisional proposals to reform the law, that we think will have benefits in the commercial leasehold sphere. This Summary sets out, at a high-level, an overview of the key provisional proposals. In this Summary, we include cross-references to the chapters of the full Consultation Paper and to some key consultation questions (“CQs”) to help consultees navigate between this document and that one. Before responding, consultees are encouraged to read our full Consultation Paper, or the relevant parts of it. We invite consultees to respond to all the questions in the full Consultation Paper, or as many as they are able. Our work benefits from hearing from as broad a range of perspectives and experiences as possible, and we welcome receiving as much or as little information as consultees feel able to contribute.

Impact

We are keen to hear whether we have addressed the issues (given the scope of the project explained above) that are most in need of being addressed by law reform from the perspective of commercial leasehold law.

We are also asking consultees to provide us with their views and evidence on the potential impacts of our provisional proposals and the consequences of the potential reforms. This could include the financial impact but may also include other impacts which are not easy to monetise, such as environmental impact or changes in market behaviour.

Bearing in mind the scope of our work, we have been careful not to make provisional proposals which might cause adverse impact to residential leaseholders or the residential leasehold market. However, we are keen to hear consultees’ thoughts about that.

(See **CQ 1**, **CQ 2** and **CQ 4**.)

The law in Wales

Our consultation covers the law in England and in Wales. Under the Government of Wales Act 2006, the power to change the law in Wales is “devolved” and exercised by the Senedd (the Welsh Parliament), unless a topic is “reserved” to the UK Parliament. It is not clear whether any reforms to the 1987 Act and the 1995 Act would be devolved to Wales. Nevertheless, we want to consult stakeholders about reform of the 1987 Act and the 1995 Act in Wales specifically.

We invite consultees to tell us about any particular considerations or experiences in Wales, which consultees think are relevant to potential reforms of the 1987 Act and the 1995 Act as set out in the Consultation Paper.

(See **CQ 3**.)



The right of first refusal contained in the 1987 Act

Chapter 2 of the Consultation Paper sets out a detailed analysis of the right of first refusal and the way in which it may sometimes adversely affect mixed-use developments and commercial leasehold transactions.

Key definitions

- **disposal:** the creation or transfer of an interest in land which includes the grant of a lease and the sale of a freehold.
- **mixed-use premises (or developments):** premises (or developments) which are used for residential and commercial purposes. For example, a development with retail units on the ground floor and residential flats above.
- **qualifying tenant:** a tenant of a flat under a tenancy (which is not an excluded tenancy under section 3 of the 1987 Act). Not all qualifying tenants will have the right of first refusal. There are other requirements which include (a) the qualifying tenants must, between them, own at least two flats in the premises, and (b) the number of flats held by those tenants must exceed 50% of the flats in the premises.
- **relevant disposal:** a disposal by a landlord (under section 4 of the 1987 Act) to which the 1987 Act applies and which will trigger the right of first refusal.
- **right of first refusal:** a right given to certain residential leaseholders (see the definition of qualifying tenants) by the 1987 Act. Where a landlord intends to make a relevant disposal, it is required to offer the residential leaseholders the right to acquire the interest, before disposing of it to a third party.

The background to the right of first refusal

The right of first refusal was introduced at a time when the residential leasehold landscape was very different. It predated the introduction of other leaseholder rights, including collective enfranchisement and the right to manage, both of which now provide more direct mechanisms for residential leaseholders to acquire ownership or management of their buildings. We published a series of reports in 2020 in respect of both of these regimes, as well as the commonhold regime.

In addition, the nature of residential development has evolved since the right of first refusal was introduced. For example, mixed-use developments have become increasingly common.

The current law

In order for the right of first refusal to arise, certain requirements must be satisfied. These requirements relate to the nature of the premises, whether there are enough “qualifying tenants”, the identity of the landlord, and the type of disposal the landlord proposes to make. For example, the grant of a lease of a single flat does not trigger the right of first refusal.

Where the right of first refusal is triggered, landlords must comply with detailed procedural requirements set out in the 1987 Act, including the service of offer notices on the leaseholders. The leaseholders then have the right to acquire the interest that the landlord is proposing to dispose of.

The consequences of non-compliance with the right of first refusal are serious. If landlords do not comply (and do not have a reasonable excuse), they commit a criminal offence. In addition, leaseholders are given various rights that enable them to investigate, and potentially to unravel, a disposal.

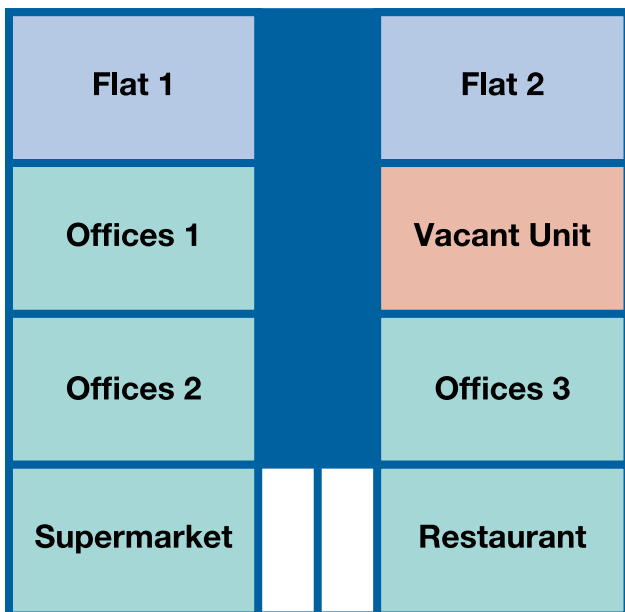


The problem with disposals of commercial units in mixed-use premises

The right of first refusal does not apply to premises that are solely used for commercial purposes. Furthermore, where premises are predominantly comprised of commercial space (with some residential flats), the right of first refusal will generally not operate. This is because the right of first refusal does not apply where more than 50% of the floor area of the premises is occupied for non-residential purposes, which we call the “50% Rule”.

In Building A below, the 50% Rule means that the right of first refusal does not apply. The landlord is therefore free, for example, to grant a commercial lease of the Vacant Unit in the premises without first offering it to the residential leaseholders.

Building A



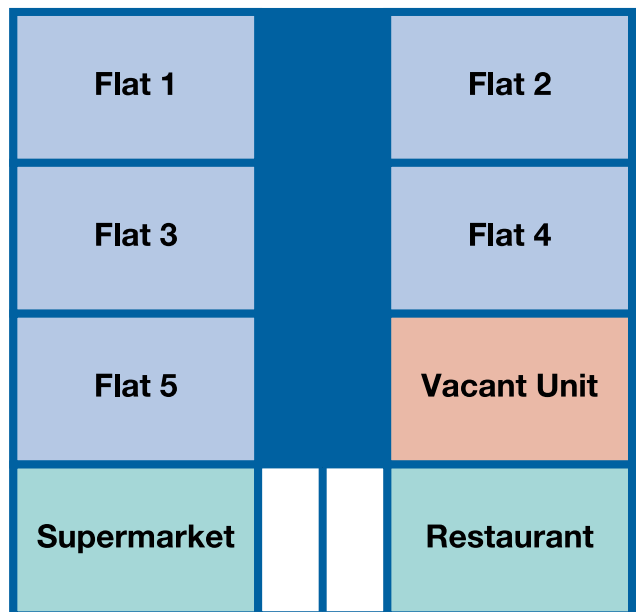
However, where premises predominantly comprise residential space (with, for example, fewer commercial units), and assuming all the other requirements in the 1987 Act are satisfied, it is our view that the right of first refusal is likely to apply to the grant of leases of commercial (i.e. non-residential) space.

In Building B below, the 50% Rule does not apply. The landlord cannot, therefore, grant a commercial lease of the Vacant Unit without first offering it to the residential leaseholders.

We understand the effect of the current law can be increased complexity in developing mixed-use properties and expense, delay, and risks in what might otherwise be straightforward transactions.

We are not aware that residential leaseholders are keen to exercise the right of first refusal in the circumstances described above. Furthermore, we believe it is unlikely that Parliament deliberately intended the right of first refusal to apply to the grant of a commercial lease in mixed-use premises.

Building B



Our provisional proposals and consultation questions

We provisionally propose that the grant of a lease of a part of the premises which is (or is to be) exclusively used for non-residential purposes should not trigger the right of first refusal.

This proposal is subject to a limited exception for areas shared by residential leaseholders which are ancillary to their residential use.

(See **CQ 5**.)

Preserving residential leaseholders' rights

Our provisional proposal is limited to the grant of leases that are exclusively non-residential. It is designed to preserve the core protection that the right of first refusal affords to residential leaseholders, while preventing it from applying to transactions that are unlikely to be of benefit to them and which may, instead, interfere with commercially desirable arrangements.



Facilitating commercial transactions and the 1995 Act

Chapters 3, 4 and 5 of the Consultation Paper set out a detailed analysis of the 1995 Act and some of the challenges it poses in relation to commercial transactions.

Key definitions

- **assignee:** the person who acquires the property which is being assigned. Also referred to as the “incoming tenant” below.
- **assignment:** the transfer of a property (such as a lease) from one person (the assignor) to another person (the assignee).
- **assignor:** the person who transfers the property which is being assigned. Also referred to as the “outgoing tenant” below.
- **authorised guarantee agreement (AGA):** a special type of guarantee which satisfies requirements that are set out in the 1995 Act. It requires the assignor to guarantee the performance, by their immediate assignee (but no future assignee), of the obligations in the lease.
- **guarantor:** a person who promises to perform a tenant’s obligations under the lease if the tenant fails to do so.

Key features of the 1995 Act

Where a tenant (the “outgoing tenant”) assigns a lease to a new tenant (the “incoming tenant”), it is a central feature of the 1995 Act that the outgoing tenant is automatically released from liability for the obligations it owed to the landlord under the lease. (Key provisions of the 1995 Act do not apply to leases that were granted before the 1995 Act came into force).

The 1995 Act also provides that, where an outgoing tenant is released, any guarantor of that tenant is released to the same extent.

The principal exception to the automatic release of an outgoing tenant is the authorised guarantee agreement (“AGA”). An AGA requires the outgoing tenant to guarantee the performance of the tenant obligations in the lease by the incoming tenant. If the incoming tenant breaches those obligations, the outgoing tenant may be liable for that breach under the AGA. Depending on the terms of the lease, a landlord may, when giving consent to an assignment of a lease, require the outgoing tenant to enter into an AGA.

AGAs are subject to strict constraints. An outgoing tenant may only guarantee the obligations of its own immediate assignee, and only for so long as that assignee remains the tenant. This means that AGAs cannot be used to impose liability on an outgoing tenant in respect of future assignees. Crucially, AGAs are the only means by which an outgoing tenant can remain liable for future performance of tenant covenants under a lease.

The 1995 Act contains a widely drafted provision – called an anti-avoidance provision – which causes any agreement to be of no effect to the extent that it excludes, modifies, or frustrates the operation of fundamental principles in the 1995 Act governing the release of an outgoing tenant and guarantor.



The 1995 Act – problems with the current law

The anti-avoidance provision underpins the operation of the 1995 Act. It is important to ensure the key aim of the 1995 Act is not avoided.

However, stakeholders have told us that the anti-avoidance provision, and its interaction with other elements of the 1995 Act, is preventing commercially sensible arrangements from being entered into, particularly in transactions involving closely connected parties. For example, it can adversely affect:

- assignments and guarantees within groups of companies;
- reorganisations within partnerships; and
- assignments from a tenant to their guarantor.

Our provisional proposals and consultation questions

In the Consultation Paper, we ask questions and make provisional proposals that are aimed at understanding and addressing problems with the operation of the 1995 Act.



Our provisional proposals would allow flexibility in specific circumstances, while maintaining the 1995 Act's fundamental objective of protecting former tenants and guarantors from ongoing liability.

Facilitating transactions involving group companies

We provisionally propose that the 1995 Act should facilitate, rather than prohibit, assignments and guarantees between members of the same group of companies (see **paragraph 4.138** of the Consultation Paper for a list of what transactions we consider should be permissible under the 1995 Act). This rule would apply to (1) the assignment and (2) any agreement to enter into the assignment, provided that the relevant parties were (at the time each is entered into) members of the same group of companies. We provisionally propose that the definition of a group of companies should be based on section 42 of the Landlord and Tenant Act 1954.

(See **CQ 6**, **CQ 7** and **CQ 8**.)

Facilitating transactions involving partnerships

We provisionally propose that the 1995 Act should facilitate (and be clear that it facilitates), rather than prohibit, assignments within partnerships, where the partners comprising the assignor and assignee are in substantially the same partnership (see **paragraphs 4.183** and **4.184** of the Consultation Paper for a list of what we propose should be permissible partnership transactions under the 1995 Act). We also provisionally propose that repeat guarantees should be permissible in these circumstances. A repeat guarantee would be where one person acts as a guarantor for the outgoing tenant and again for the incoming tenant.

We consult on whether the greater flexibility afforded by this provisional proposal risks tenants and/or guarantors (particularly those who are not advised) being put in a worse position than under the existing law.

(See **CQ 9** and **CQ 10**.)

Facilitating transactions involving persons with other substantial business relationships

We ask for consultees' views on whether the 1995 Act has an adverse impact on business relationships (beyond those involving group companies and partnerships) and seek evidence on the types of business relationships, the prevalence of them in the market, and the impact caused to them by the 1995 Act.

(See **CQ 11**.)

Facilitating assignments to guarantors

We provisionally propose that where a tenant under a lease has the performance of its obligations guaranteed by a guarantor, the 1995 Act should facilitate, rather than prohibit, the assignment of the lease by the tenant to the guarantor. This proposal would only apply to the assignment itself. To avoid undermining a key aim of the 1995 Act, it would not permit parties to agree in advance that the guarantor will take an assignment of the lease.

(See **CQ 12**.)





The 1995 Act – other issues

The main aspects of the 1995 Act that we are aware are causing problems in commercial leasehold transactions relate to the effect of the anti-avoidance provision and its interaction with other provisions in the 1995 Act.

Chapter 5 of the Consultation Paper considers some other issues with the 1995 Act that may be problematic. The issues we consider relate to: concurrent leases, covenants with management companies, agreements for lease, the registration gap and geographical limitations on the service of notices under the 1995 Act.

We do not make any proposals to reform the 1995 Act in respect of these issues, broadly because they do not appear to be causing significant difficulties specifically (or principally) for commercial leasehold transactions, or because reform may adversely impact the residential leasehold sector (which is outside of the scope of our project). However, we invite consultees' views on these issues and whether there are any other issues with the 1995 Act which are causing difficulties.

(See **CQ 13**.)

Conclusion

We encourage you to read the full chapters in the Consultation Paper and to respond to all or any of the questions in the paper.

Links to the full Consultation Paper and the online response form can be found at <https://lawcom.gov.uk/project/commercial-leasehold>.

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