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Legal alert

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Toxic rentcharge warning

Morgoed Estates Limited and others v Lawton and others [2016] UKUT 395 (TCC)

In the nineteenth century, rentcharges were popular with landowners as a way of earning additional money from the sale of land for housing. Freehold land sold to developers would be accompanied by a liability under a rentcharge to make fixed annual monetary payments in perpetuity to the original landowner.

These days, thanks to the Rentcharges Act 1977, rentcharges can no longer be created for the purpose of imposing standalone monetary payments. Instead, the 1977 Act says that the only type of rentcharge that can now be created is an "estate rentcharge", which is a device to make positive covenants (such as the payment of service charge contributions to the manager of a housing or industrial estate) run with the land burdened by the rentcharge.

Nevertheless, old historic monetary rentcharges still exist and remain valid. However, the 1977 Act provides that they will be automatically extinguished in 2037 and, in the meantime, the freehold owner of the burdened land is entitled to buy out the rentcharge by making a capital payment to the rentcharge owner calculated under a statutory formula. Moreover, the potential liability under old rentcharges has been substantially eroded by inflation. In the words of the judge in this case, "A rentcharge requiring a payment of £2 per annum imposed 150 years ago requires a payment of £2 per annum today." In most cases, therefore, the money has long since stopped being demanded by the rentcharge owner.

These considerations have led many solicitors, on encountering an old rentcharge during due diligence, not to give it a second thought. It was extremely unlikely to be bothersome.

Enter Morgoed Estates.

Morgoed Estates is a company that has acquired ownership of some 15,000 old rentcharges. It has spotted that section 121 of the Law of Property Act 1925 permits the owner of an unpaid rentcharge to grant a lease of the burdened land to nominees for the purposes of recouping the arrears. The lease can be granted without warning the freeholders and whether or not they been asked to pay up. The lease can then be mortgaged, sold or underlet to realise the amount owed.

The effect of the grant of a section 121 lease (of which Morgoed Estates has granted many) is that the freehold is held to ransom. The freehold is worthless unless the lease is surrendered. There's no right for the freeholder to bring the lease otherwise to an end, even if all arrears are paid, nor if the freeholder buys out the rentcharge, nor when the rentcharge itself comes to its statutory end in 2037.

Morgoed Estates' practice is to make an offer to the freeholder to surrender the lease in return for (among other things) payment of a £650 "administration charge" (an amount which dwarfs the arrears owed).

Unsurprisingly, Morgoed Estates' activities are being challenged in the courts by a number of disgruntled freeholders. In this particular case, the freeholders tried to argue (on a technicality) that the Land Registry should not register the leases. The judge disagreed. But challenges on other grounds will no doubt be forthcoming.

One such ground would be to claim that a rentcharge unpaid for 12 years is extinguished under the general law of limitation. This may well be successful in relation to unregistered rentcharges. But, unfortunately, thanks to new procedures brought in by the Land Registration Act 2002, it now looks virtually impossible to prove limitation of a rentcharge that has been registered at the Land Registry.

WARNING: Old rentcharges have become toxic. If you encounter any during due diligence, consider buying them out, or consider indemnity insurance (or both).