

KEY LEGAL CONSIDERATIONS FOR OVERSEAS INVESTORS

As the UK continues to adjust to an economic environment of high interest rates and high inflation, opportunities are emerging for overseas investors in the UK real estate market.

In light of this, we look at some of the main legal issues overseas investors should be aware of when investing in real estate in England and Wales, as well as some of the hot topics for UK real estate in 2024.

Readers should note that the legal issues discussed in this note refer to the laws of England and Wales; the rules relating to Scotland and Northern Ireland may differ.

Legal ownership of real estate

Title to property is either freehold (essentially ultimate ownership) or leasehold (a lease granted out of the freehold or a superior leasehold). “Long leasehold” interests for investment purposes, usually for a term between 125 and 999 years, are common and are generally considered to be institutionally acceptable (provided the terms of the lease are acceptable). In many ways they are equivalent to a freehold interest.

Over 85% of property in the UK is registered at the Land Registry (and that figure is closer to 100% in cities, towns and built up areas). The Land Registry is a government department that guarantees title to registered interests and estates and records title and ownership information. Such records are held on a digitally and publicly accessible register. Title is usually

verified by due diligence by the buyer’s solicitors in the acquisition process, and any defects in the title are typically dealt with by contractual provisions and/or title indemnity insurance.

Title to property in the UK may benefit from and/or be burdened by ‘encumbrances’ such as rights (e.g. rights of way) and restrictive covenants (e.g. covenants not to use the land for a specific purpose). The existence and impact of any such encumbrances will be identified during the due diligence process, and any potential issues for a buyer’s proposed use can potentially be dealt with by, for example, an express release or variation of an existing restrictive covenant or through title indemnity insurance.

Investment structuring

Buyers will need to consider and select their preferred investment structure at an early stage, to be ready to move quickly when the

right asset becomes available. Key considerations include:

Asset purchase or share purchase

Should the buyer acquire the asset directly, or the shares in the selling entity that owns the asset?

This will largely depend on whether the seller is willing and able to sell the entity. Acquiring the asset directly typically requires less due diligence and therefore lower transaction costs, however the stamp duty land tax (SDLT) is likely to be higher compared to a share purchase. On a share purchase, the SDLT savings are likely to be attractive to buyers, although they should also be aware of potentially unknown liabilities within the property holding entity, as well as potentially limited recourse if the seller’s warranties are incorrect (risks that may be covered by warranty and indemnity insurance). Usually share purchases are therefore only attractive where the property value is sufficiently high.

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Choice of property-holding vehicle

Should the buyer acquire the property using a UK entity, or an offshore vehicle?

This will depend on a range of factors including whether the buyer is acquiring the asset or the shares (see above), how the buyer intends to fund and withdraw income from the investment, and its future plans for growth and exit. Since the UK announced changes to capital gains tax rules for overseas investors we have seen more overseas investors use UK entities as their holding vehicles (instead of offshore vehicles), but it will very much depend on a client's particular circumstances.

For example if an investor is acquiring a property owning entity based in a foreign jurisdiction, it might not be desirable (e.g. for tax or other financial reasons) to move to another jurisdiction. Similarly, if the property holding entity is already in a foreign jurisdiction, it might make financial and administrative sense to continue to base the entity in that jurisdiction.

New regulations came into effect in 2023 which require an overseas entity to register and annually update its beneficial ownership at Companies House in order to make a disposition (buying/selling/leasing) of a UK property – see our article [here](#) for further details. Consideration of

these requirements is needed at an early stage where an offshore vehicle is to be used to acquire, sell or lease property.

Transacting quickly

Real estate acquisitions in the UK are usually concluded fairly quickly, with legal due diligence and contracts typically concluded between 2 and 4 weeks from the date heads of terms are agreed on a straightforward commercial property purchase (timescales may vary depending on the complexity of the deal). Buyers should therefore make sure they are “ready to transact”, including having their investment structure in place, availability of funds for completion, and have lined up post-completion matters such as building insurance and the appointment of a competent asset manager for the property.

Occupational leases

Investors in UK real estate will need to understand the key features of occupational leases as they are likely to be the main source of income from commercial properties. A number of these features may be commonly found in leases globally, but some aspects specific to the UK market include:

- **“FRI” leases:** Most leases in the UK are full repairing and insuring (FRI), meaning the tenant is ultimately responsible

for all costs of repair, maintenance, insurance, and the provision of any services. This is similar to a “triple net” lease found in other jurisdictions.

- **Security of tenure/right to renew:** Occupiers of business premises under a lease for longer than 12 months will automatically have a statutory right to renew the lease when it ends, unless the parties have agreed otherwise before the lease was entered into and complied with the relevant statutory procedure. If a tenant does have a statutory right to renew, the landlord can only resist such renewal on specified grounds, some of which require compensation to be paid to the tenant.
- **Rent review:** As a matter of market practice, leases in the UK typically contain an ‘upwards only’ rent review, meaning that the rent will not be reduced at any time during the term but parties can review rent levels periodically (usually every five years) and increase the rent either to the open market rent at the date of the review or in line with inflation. In contrast with some other jurisdictions, there are no statutory restrictions on rent increases, which is a particularly attractive feature of real estate investment in the UK.

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Hot Topics for 2024

Overseas investors will no doubt be keeping a close eye on global and macroeconomic issues, such as higher interest rates, and some recent and upcoming changes which will potentially have a significant impact on the UK real estate sector in 2024.

Building safety regulations for higher-risk buildings

New regulations came into effect in 2023 which impose enhanced building safety obligations on any party (often landlords or superior landlords) that has an obligation to repair an occupied building which: (a) contains two or more residential units and (b) is 18 metres or higher, or has 7 or more storeys. This will not impact a building which only comprises commercial units, but many buildings in urban areas may contain a mixture of residential and commercial units.

Minimum energy efficiency standards for let commercial property

Current Government proposals will require all non-residential let properties to have a minimum energy performance certificate (EPC) rating of C by April 2027 and of B by April 2030. This is a standard of energy efficiency that many commercial properties in the UK do not currently meet, potentially requiring landlords to incur significant expenditure to bring their properties to the required level before they can be let. There has been a lack of clarity from the Government as to when these proposals may become law and, with an anticipated general election in the UK in 2024 (and potentially a change of Government), there remains uncertainty for investors as to how the UK will reach its aim to be 'net zero' by 2050.

National security regime

National security regulations introduced in 2021 allow the UK Government to intervene in certain acquisitions, including the acquisition of land and property, that could harm the UK's national security. This grants the Government the power to call in the transaction within the earlier of: (a) 5 years from the date of the transaction and (b) 6 months from the Government becoming aware of the transaction. If a transaction is called in, the Government may impose conditions on the acquisition or unwind/block the transaction in whole or in part. While the current guidance is not clear, the main factors in assessing the risk will be: (a) the identity of the buyer (b) the current/intended use of the property and (c) whether the property is located near a sensitive site.



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