Restrictive Covenants Indemnity Insurance – important safety net or just another racket?

Authors: Catherine Stanbury & Andrew Cash

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The perversity of restrictive covenants has made the news again with The Sun recently accusing a well-known housebuilder of contrived snobbery in curbing parking arrangements at a new residential development in Essex. Oliver Smith, a tradesman who presumably would have been more than welcome on site in the construction stages, was unable to purchase a newly-built Persimmon Homes property as the development covenants meant that, as a resident, he would not have been allowed to park his commercial vehicle outside. In a way, Oliver Smith was lucky – he knew that the restrictions were unacceptable to him and so decided not to proceed. Far less fortunate are those buyers who are themselves happy to abide by a property’s restrictions, but are concerned about being punished for the breaches of their predecessors.

Of particular concern to conveyancers is the past breach of any covenant which has attempted to control the way in which a property may be developed in the future. Typically, such a covenant will be drafted with the purpose of either preventing any further building at all or prescribing the manner in which new buildings may be added or changed. What is feared is that the purchaser will somehow inherit a predecessor’s breach and then be liable to compensate the land owner who benefits from the covenant, should he chose to sue at a later date. Property lawyers have long been happy to recommend the purchase of indemnity insurance to ensure that neither buyer nor mortgagee is left to pay any damages, but, at an average cost of £200 per policy, are we really sure that this is necessary?

Liability for old covenants

It has been firmly established since Tulk v Moxhay (1848) 2 Ph 774 that, provided certain conditions are fulfilled, restrictive covenants may ‘run with the land’. By way of exception to the usual rules of privity of contract, where freehold land is made subject to a covenant which imposes a negative duty (typically, not to build additional structures on a property), that negative duty must be observed by future owners of that property even though they would have had no opportunity to negotiate the terms of that covenant when initially conceived. Future owners will be bound by a restrictive covenant where (1) the original covenant was designed to protect the land of the person creating it (2) that benefit is ongoing (3) the construction of the covenant is not such that it was only intended to bind the original parties (Morrells of Oxford Ltd. v Oxford United Football Club Ltd. [2001] Ch 459) applying s79 Law of Property Act 1925) and (4) it is registered pursuant to the appropriate unregistered or registered land regime.

A new beginning

Whilst a new owner must himself observe the stipulations of an old covenant, he should not be concerned about paying for past infringements. The seminal case of Powell v Hemsley [1909] 1 Ch 680, heard in the Court of Appeal, settled the point.
The defendant had purchased part of a freehold building estate. He had covenanted for himself and his successors that no buildings should be erected on the land save for private residences whose plans had been pre-approved by the seller. The defendant then granted a long lease to a tenant who went on to build residences in breach of the covenant. The tenant’s lease later came to an end on bankruptcy and the defendant, as freeholder, found himself back in possession of the land facing action for the tenant’s breach. For the purpose of assessing the defendant’s liability in equity under the Tulk v Moxhay principle, the defendant was treated as a successor in title (an assignee of the tenant).

In finding for the defendant, the Court held that the breach of a covenant which attempts to regulate building on a property, is not a continuing breach and so cannot be perpetuated by a successor. Once building has been carried out in contravention of such a covenant, there is a ‘breach complete at once’ (Farwell J.); a covenant not to erect does not additionally mean ‘nor allow to remain erected’ (Cozens-Hardy M.R.). Where the breach is complete, a successor is not burdened with liability for it simply by putting up with the product of the breach and not attempting to undo the harm caused.

The role of bad faith

Whilst a successor entirely innocent of the commission of the breach has nothing to fear, a successor who has in some way facilitated it, will not escape liability. In Powell v Hemsley it was made clear that a successor who has been ‘actively assisting … the real wrong-doer to do what he has done’ (Cozens-Hardy M.R.) will share some blame.

The circumstances in which a successor could have been embroiled in the initial breach, however, will be rare. More than sixty years after Hemsley, such facts did finally come before the Court of Appeal in Wrotham Park Estate Co v Parkside Homes Ltd [1974] 2 All ER 321.

The peculiar case of Wrotham Park

At auction, Parkside Homes Ltd purchased development land from the local authority which had itself acquired it approximately fifteen years before from the owners of a large estate generally known as Wrotham Park. The local authority was selling the property with planning permission but it was clear that the land was encumbered by an old restrictive covenant concerning development. The covenant had been created in April 1935 to control the character of the site where it was to be developed in the hands of new owners. It was intended to ensure that there would be no building ‘except in strict accordance with a lay-out plan to be first submitted to and approved in writing by the Vendor or his Surveyors’.

Following their purchase, Parkside had no intention of observing the covenant and, without any reference to the Wrotham Park Estate, began to work on the site and accept pre-exchange deposits from purchasers who were to buy their plots off plan. Parkside were then notified by the Estate owners that further development would contravene the covenant and that work should stop. Parkside immediately responded that they believed that the covenant was unenforceable and did

1 The defendant was not liable at law as the action was brought by a successor to the original covenantee who was not, under the terms of the covenant, entitled to sue for past breaches.

2 Today, such breaches are commonly referred to as ‘once and for all’ breaches.
not seek to negotiate any further. Preliminary building work followed and, in the face of a writ against Parkside seeking an injunction to prevent development otherwise than in accordance with the covenant, indemnity insurances were arranged to protect the purchasers and contracts were exchanged. Three months later, the properties were structurally complete and the buyers moved in. The road to the development remained in Parkside’s ownership.

So far as the buyers were concerned, the design covenant was irreparably breached well before their purchases were completed. If Powell v Hemsley were to be applied, liability for this ‘once and for all’ breach could not be imputed to them as Parkside’s successors.

Powell v Hemsley was however distinguished by the Court and the buyers were held liable. In Wrotham it was held that, whilst the breach was ‘once and for all’, it was only complete when the estate was fully developed. Accordingly, in exchanging contracts and paying over their deposits in the full knowledge that the development was prohibited, the purchasers were said to have participated in the breach. Using language usually reserved for describing criminal activity, Brightman J. scathed that, in providing monies at exchange which were then put to use in completing the building of the estate, the purchasers had ‘aided and abetted’ the breach.

The shadow of Wrotham Park

Regrettably, it is the ruling in Wrotham Park, decided in the context of all its peculiarities, that seems to underpin the modern compulsion to obtain indemnity policies wherever past breaches appear. Whilst Wrotham Park is a significant case in the context of a successor’s liability for freehold covenants, we must also appreciate the limit of its reach.

Although Wrotham, in the context of new developments, has perhaps stretched the period over which a ‘once and for all’ breach could be considered live, there is no sense in which it has changed this type of breach into a ‘continuing’ one for the purpose of fixing a successor with liability for it. Accordingly, the significance of the Wrotham finding on this point should not be over-blown. Where the possible breach of a building control covenant is concerned, as long as a purchaser only commits to buying the affected property after it has been finished, he will be a successor to the breach and not a party to it.

Post-Wrotham, Powell v Hemsley is still good law. A covenant aimed at restricting building is still one intended to prevent a single act and therefore its breach is still ‘once and for all’. A successor in title, remote from such a past breach, cannot be held liable for it.

Be bold!

Buy your next restrictive covenant indemnity policy advisedly – if the terms of the covenant itself do not expressly make a successor in title liable for past breaches (and it is highly unlikely that it will), consider whether there is any need for insurance at all.

Catherine Stanbury and Andrew Cash are non-practising solicitors and senior lecturers at the University of Huddersfield. www.hud.ac.uk