The Real Estate M&A and Private Equity Review

Seventh Edition

Editors

Adam Emmerich and Robin Panovka

The LawReviews

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THE REAL ESTATE M&A AND PRIVATE EQUITY REVIEW

Seventh Edition

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This article was first published in July 2022
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Adam Emmerich and Robin Panovka

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Published in the United Kingdom
by Law Business Research Ltd, London
Meridian House, 34–35 Farringdon Street, London, EC4A 4HL, UK
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www.TheLawReviews.co.uk

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Enquiries concerning editorial content should be directed
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ISBN 978-1-80449-098-3

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

ALLEN & GLEDHILL LLP

BINDER GRÖSSWANG RECHTSANWÄLTE GMBH

BIRD & BIRD (INTERNATIONAL) LLP

CHIOMENTI

DARROIS VILLEY MAILLOT BROCHIER

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PREFACE

For real estate investment trusts (REITs), the covid-19 pandemic was a tale of two cities, of boom and bust, with the seismic changes in the world leading to strength in some sectors of commercial real estate and huge market dislocations and disruptions in others. In general, companies with assets that service the digital economy – cell towers, logistics and industrial properties, and data centres – benefited from the pandemic's acceleration of the digital economy. However, several traditional sectors confronted difficult issues involving liquidity, rent collection, dividend payouts, disclosure and guidance, as well as having to navigate the uncertain and sometimes shifting guidance from regulatory authorities regarding the timeline of reopening. While the distribution of the vaccine to many individuals in the United States and certain other countries has blunted the pandemic in some areas, inequitable distribution has yielded an uneven economic recovery internationally. Still, even with hopefully the worst of the pandemic behind us, we are unlikely to see a return to a pre-pandemic world, as the pandemic has changed the way that we interact with real estate, and compressed a decade or more of digitisation into a matter of months, with the new normal involving fewer, or at least different, in-person work or shopping. While vaccine rollouts have enabled many regions to fully reopen stores, offices and restaurants, we still have longer to wait to find out how many of the pandemic shifts (work from home and hybrid work arrangements, massive growth in online retail) are permanent, and which will fade with time. The eventual new normal that emerges will likely have rippling effects throughout the REIT industry for years to come. As always, strategic planning and risk management will be critical to adjust to changing times. Covid-19 aside, 2022 has brought some storm clouds, with war in Europe, rising interest rates and inflation running hot. While opportunities within real estate are unlikely to dry up, there may be increased volatility in the near term, and the complex macroeconomic backdrop will likely have disparate impacts on different subsectors and different geographies within the industry.

Stepping back from recent global events and market dislocations, publicly traded real estate companies and REITs, with help from real estate private equity, have steadily transformed the global real estate markets over the past 25 years. Their principal innovation, and 'secret sauce', has been liquid real estate. Unlike traditional property ownership, equity in publicly traded real estate vehicles is highly liquid, and can be bought and sold in large volumes, literally in minutes, on numerous global exchanges. Indeed, during the pandemic, REITs issued more than US$10 billion in public equity, taking advantage of the massive amounts of liquidity washing over financial markets beginning in the spring of 2020. In 2021, public REITs raised approximately US$27 billion in follow-on equity offerings.

Publicly traded real estate vehicles have an aggregate market capitalisation of over US$1.6 trillion globally, including over US$1 trillion in the United States and approximately

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US$200 to US$280 billion in each of Europe and Asia. As public REITs and other vehicles have aggregated these properties and grown in scale and sophistication, so too have real estate-focused private equity funds, playing an important role catalysing hundreds of billions of dollars of REIT and real estate merger and acquisition (M&A) transactions and initial public offerings.

However, despite that massive growth and despite the pandemic, potential growth is far larger both in long-standing REIT markets and in newer REIT jurisdictions, where the trend is more nascent. With increasing development and urbanisation, the world is producing more and more institutional-grade properties, and a growing percentage of this expanding pool – an estimated US$5 trillion and counting – will inevitably seek the advantages of liquidity by migrating to the publicly traded markets. The growth is expected to be both local and cross-border, with nearly 40 countries already boasting REIT regimes. Despite this potential for growth, it remains to be seen whether Russia's invasion of Ukraine and the associated energy and supply chain disruptions will spur a wider backlash against globalisation and cross-border investment.

REITs and other publicly traded vehicles for liquid real estate have grown because they are often a superior vehicle for stabilised assets. Greater liquidity and transparency – and often superior governance – are attractive to investors, resulting in a lower cost of capital and superior access to vast amounts and varieties of capital in the public markets. In addition to cheaper capital, REITs and other public vehicles benefit from efficiencies of scale, sophisticated management and efficient deal structures, to name just a few advantages. With these advantages, the global march of real estate to the public markets seems unstoppable.

This publication is a multinational guide for understanding and navigating the increasingly complex and dynamic world of liquid real estate and the transactions that mostly produce it. The sea change in the markets, sometimes called the 'REIT revolution', has meant that major real estate transactions have migrated from 'Main Street' to 'Wall Street'. They now often take the form of mergers, acquisitions, takeovers, spin-offs and other corporate transactions conducted in the public markets for both equity and debt. They have grown exponentially in complexity and sophistication, and increasingly represent cross-border multinational transactions fuelled by the now-global real estate capital markets and M&A deal professionals. And they are often intermediated by international investment banks rather than local brokers, and financed with unsecured bonds or commercial mortgage-backed securities. In a fair number of cases, they are catalysed by private equity firms or similar actors, sometimes building portfolios to be taken public or sold to public real estate companies, and sometimes through buyouts of public real estate companies for repositioning or sale.

To create this publication, we have invited leading practitioners from around the globe to offer practical insights into what is going on around the conference tables and in the markets in their jurisdiction, with an eye to cross-border trends and transactions. As will quickly become evident, the process of liquefying real estate and transactions involving public real estate companies requires a melding of the legal principles, deal structures, cultures and financial models of traditional real estate, public company M&A and private equity. None of this, of course, happens in a vacuum, and transactions often require expertise in tax, corporate and real estate law, not to mention securities laws and global capital markets. Each of our distinguished authors touches on these disciplines.

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We hope this compilation of insight from our remarkable multinational authors produces clarity and transparency in this exciting world of liquid real estate and helps to further fuel the growth of the sector.

Adam Emmerich and Robin Panovka
Wachtell, Lipton, Rosen & Katz
New York
July 2022

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Chapter 13

UNITED KINGDOM

Richard Smith, Ed Milliner and Graham Rounce[1]

I OVERVIEW OF THE MARKET

Following the devastating global impact of the covid-19 pandemic, President Putin's brutal invasion of Ukraine has become the latest major world event to dominate the political and economic landscape. Global political risk and a hardening of the macroeconomic environment have overtaken the pandemic as the main factors affecting confidence in the real estate M&A and private equity sectors. In case we forget, the implications of leaving the EU also continue to rumble along in the background. Coming out of lockdown heralded a very welcome resurgence in activity as investors started to embrace a return to pre-pandemic conditions and take advantage of investment opportunities. However, on 24 February 2022, Russia's large-scale invasion of Ukraine served as a terrible reminder of the lurking menace of political instability and its effect on world politics and the global economy.

It is extremely unfortunate that this edition of *The Real Estate M&A and Private Equity Review* is once again dominated by bad news. After more than two years of the pandemic, and its heart-breaking toll of more than six million deaths, the world is now faced with the devastating reality of war in Europe. Tragically, it has become increasingly difficult to see a satisfactory and peaceful resolution to the conflict in the short to medium term. In addition to the humanitarian crisis, Putin's invasion of Ukraine has, of course, had a significant effect on the European economy. Real estate investment confidence has been knocked, and there has been a marked decrease in real estate M&A and private equity activity. The UK has arguably been less affected than mainland Europe, where Germany and those countries closer to the conflict have borne the brunt. In addition to any direct exposure to Russian real estate, there is also the more complicated issue of extricating deal structures from Russian-backed ownership and financing. The war has led to a number of sanctions and other measures aimed at economic crime. The Economic Crime (Transparency and Enforcement) Act 2022 provides for a new beneficial ownership register for overseas entities holding UK real estate, the strengthening of unexplained wealth orders and the more effective enforcement of sanctions. Although the introduction of the new legislation was accelerated by the war in Ukraine, much of it had been planned for some time. All overseas companies owning UK property will need to register details of their beneficial ownership. However, this is not expected to create an onerous burden for legitimate overseas investors seeking to acquire UK property and is unlikely, of itself, to deter investment. The UK's real estate markets have traditionally proved to be remarkably resilient in difficult times, offering a safe haven to investors in times

1 Richard Smith is a partner, Ed Milliner is a senior counsel and Graham Rounce is a professional support lawyer counsel at Slaughter and May.

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of political and economic instability. In particular, non-listed real estate companies tend to weather geopolitical uncertainty relatively well and real estate is often considered to be a good hedge against inflation. Russia's invasion of Ukraine has created a humanitarian crisis, and a major global economic shock that is yet to make its full mark on real estate markets and the wider economy. Norman Foster's offer to rebuild Kharkiv is indicative of the overwhelming support for Ukraine and the desire for a meaningful peace.

Real estate has been hit extremely hard by covid-19, with a sharp decline in values across all sectors. Retail and leisure were already in serious decline and have suffered the most, as footfall fell off a cliff. Any increase in online activity fell well short of compensating for the collapse in overall sales. Hopes of a swift bounce back have been thwarted by a brewing cost of living crisis that has threatened to crush consumer confidence. Surging prices and limited growth have raised fears of a return to the stagflation of the 1970s. Squeezed property companies have been caught in the middle with their tenants unable or unwilling to pay rent and their funders continuing to look for interest and loan repayments. A significant amount of arrears has already accrued since the start of lockdown in March 2020. In an attempt to move forward and draw a line under the issue, the government has confirmed the ringfencing of arrears accrued by tenants during periods of enforced closure and a new legally binding arbitration regime has been introduced to deal with those cases where a negotiated settlement cannot be reached. The Commercial Rent (Coronavirus) Act came into force in March 2022 and will amount to almost unprecedented government interference in commercial landlord and tenant relationships. The message remains that the situation is not the fault of any particular party and that the parties are expected to reach an agreement as to how to share the pain of the pandemic. The pain of an economic recession is perhaps a little harder for an already cash-strapped government to deal with.

On 31 October 2021, the eyes of the world were focused on Glasgow as COP26 took centre stage. Greta Thunberg and US presidents past and present convened on Scotland's biggest city to address climate change. Although the absence of a handful of key world leaders was disappointing, progress was made with pledges to fight global warming. The Glasgow Climate Pact was agreed at the last minute, subject to a controversial late amendment for the phasing down rather than phasing out of coal. There was also criticism that plans to limit a global temperature rise to 1.5°C do not go far enough. Climate change has a direct effect on all aspects of how we design, construct and use buildings. The increasing frequency of extreme climatic events and the resulting damage and devastation is of concern to us all. In addition to being an obvious casualty of climate change, buildings are also a major contributor to the problem. The built environment accounts for around 40 per cent of the UK's carbon footprint and yet there remains a sense that property was under-represented in Scotland. Nonetheless, there is now a sense that environmental, social and governance (ESG) has gained traction and is finally receiving the industry's full attention. Although there is still plenty of work to do, investors, landlords, tenants and their lenders are starting to pull together in the same direction. Collaboration, in particular the sharing of data, is essential. Although the focus has inevitably been on COP26, it is important to remember this was only part of the process and much remains to be done. One issue for real estate is the continued lack of a global baseline; the plethora of standards, while well-intentioned, can be confusing, particularly to overseas investors.

The office sector is in the process of a major reset. Covid-19 has had a profound effect on the market as occupiers across the spectrum have been forced to re-evaluate their UK and global office requirements. Unsurprisingly, the office letting market has been subdued and

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volumes are down significantly. Despite this, there are signs of stability, and larger corporates and professional firms have continued to see the need for a landmark headquarters building to identify with their brand. International law firms have been particularly active, and Slaughter and May is pleased to have helped fellow law firms Linklaters, Allen & Overy, Baker McKenzie, McDermott Will & Emery, Kirkland & Ellis, Skadden, Arps, Slate, Meagher & Flom, Travers Smith and others on their new London headquarters moves. The feared downsizing by corporate occupiers has failed to materialise and there is less vacant space than previously envisaged. Instead, the focus has been on using existing space differently. The return to the office must be a positive experience with attractive amenities and facilities to offset the appeal of working from home and the drudgery of the commute. The London office market offers flexibility to occupiers adjusting to new ways of working. In addition to landmark headquarters buildings, flexible short-term serviced office space will prove attractive as businesses settle on their preferred working model. Unsurprisingly, real estate investment volumes have also been adversely affected. Although there has been some resurgence in investment activity since the last edition, this follows record lows during lockdown and has slowed in recent months. Investment transactions have been dominated by overseas capital, while activity from UK buyers has tended to focus on smaller lots. Continued interest from overseas investors suggests that London and the wider UK remains high on the shopping lists of global investors.

Although the construction pipeline is reasonably strong, much of the new office space has been pre-let, helping to maintain healthy competition for new space. Outside of London, the regions will continue to benefit from the government's levelling-up objectives. Continued decentralisation will benefit cities such as Manchester, Leeds, Edinburgh and Birmingham. The latter is hosting this year's Commonwealth Games, providing Birmingham and the wider Midlands area with the investment and regeneration opportunities that come with staging a major international event. The transition to legacy is now acknowledged as key to the medium and long-term success of such occasions. Those regional cities offering a strong talent pool combined with attractive amenities have proved particularly attractive for occupiers and investors. Appetite for UK property is no longer totally focused on London and knowledgeable overseas investors have continued to look further afield for opportunities. While London will undoubtedly retain its attraction as a key global city in which to live, work and do business, rapidly evolving technology and flexible working practices mean that not everyone needs to be in the office all of the time. While major businesses are still likely to look for a flagship central London headquarters building, that building may well be smaller than before and repurposed away from simply providing as much desk space as possible. Sustainability is becoming increasingly important as landlords, tenants and funders come under pressure to achieve ESG targets. As ESG strategies develop, occupiers have become more willing to contribute to the associated costs in order to protect brand reputation and attract and retain the best talent in a competitive labour market. This will focus demand on new developments allowing an occupier to impose its green credentials as part of its corporate identity. For example, the lease of Jones Lang LaSalle's new Docklands offices will contain the first legally binding green lease provisions on the Canary Wharf Estate, while the 67-acre Kings Cross Estate has become carbon neutral, with a commitment to renewable energy and a tree-planting scheme. The majority of new take up is for buildings with high sustainability credentials and a building research establishment environmental assessment method (BREAAM) rating of 'very good' or higher. Proptech has become a key part of the race to net zero, helping to make buildings smarter and better connected, as

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well as improving environmental efficiency. For example, digital twin technology will help predict the use, performance and energy requirements of buildings, new developments and, ultimately, towns and cities. This increased use of data and technology in turn emphasises the importance of cybersecurity and the sector's vulnerability to hacking, cybercrime and cyber warfare or terrorism. Consolidation is the proptech sector is likely to continue and we will see more proptech unicorns and listed companies, as well as M&A activity. Landlords, tenants and funders are now working together as meaningful green lease provisions and green financings start to become a reality, replacing earlier token statements of intent. A two-tier market has emerged with increasing vacancy rates in second-hand space and modern, safe and sustainable buildings with a broader social purpose and up-to-date amenities letting at a premium.

The co-working sector absorbed an immediate lockdown hit, particularly in central London. Rental values have since improved, initially in the wider market and ultimately in core office locations following the start of the back-to-the-office migration. The demand for flexible space will remain, and serviced offices have become an essential requirement for fledging businesses as well as a key part of the occupation strategy of larger occupiers needing flexibility and the ability to move staff quickly. However, in addition to connectivity and facilities, providers will need to ensure that they can offer a safe place in which to work. The co-working sector has become an established part of the market, including the development of sub-markets as operators have sought to establish niche appeal. The sector will continue to be driven by demand for good quality office space, available on flexible terms and in well-located, safe and sustainable office buildings.

The covid-19 pandemic has caused the UK population to rethink its relationship between home and work. For many, working from home has become the new normal. Rapid advances in technology mean that long commutes to and from the office have ceased to be an essential, and time-consuming, part of the working day. This has led to an increase in demand for larger residential properties with outside space, although the market for flats in urban areas has started to improve as workers return to city centres. Interest has been strong outside of urban areas with increased demand for those looking to upsize in traditional second home locations such as Cornwall, the Cotswolds and Norfolk. Enforced lockdowns have confirmed that the traditional office worker no longer exists. As the distinction between office and home life becomes increasingly blurred, workers and their employers, at least for the time being, have a choice as to where they live and work, and the market is changing to reflect this. The property industry will need to monitor working practices closely as the balance between working from home and personal attendance at the office begins to settle. It is no longer possible simply to move to new offices and expect the workforce to follow: push has become pull. The focus is now very much on what employees want and their individual wellbeing, both in terms of new developments and also the reinvention of existing space. To a certain extent offices have also started to come to the workers with, for example, new schemes in Elephant and Castle, Brixton, Vauxhall and other less fashionable parts of London. A long-term commitment to social values and the local community is essential if these neighbourhood working schemes are to prove successful in the long term.

Other than work–life balance, affordability is affecting the residential market with rising interest rates and a widening gap between wages and soaring inflation. Other factors include the government's ending of the stamp duty holiday, concerns about cladding and the safety of taller blocks of flats, and a shortage of properties coming to market. The country's housing crisis continues as successive governments have failed to meet new build targets.

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It has already been conceded that this year's target of 300,000 new homes is unlikely to be met. The UK's rising population will ensure that residential property will continue to provide opportunities for investors. Unfortunately, a combination of Brexit, covid-19 and war in Ukraine has led to increased building costs and slow construction progress, with delays in the supply of building materials and difficulties in ensuring the availability of a skilled and unskilled workforce. More affordable homes are urgently required, and there needs to be greater focus on social and economic factors in deciding where these should be built. Affordable housing and build to rent will make up a larger share of new developments and institutional investors are now alive to the opportunities. The anticipated growth of the retirement or later living sector could free up valuable housing stock as older owners are given the option of a dignified down-sizing. In difficult times, high-net-worth individuals have started to return to the capital's super-prime market, prompting optimism for the previously deflated central London investment market. This optimism seems well-founded, provided that international travel remains readily available and the UK tax regime remains relatively favourable. A plethora of new sanctions targeting wealthy individuals with links to Putin's regime and other economic crime measures may cool pockets of the market for the near future. Commentators will also keep a close eye on the UK political climate as we approach a general election in 2024. The wider residential market may become tougher in 2022 as economic pressures start to have a cumulative effect. Overseas investors in residential property are now also subject to a 2 per cent stamp duty land tax (SDLT) surcharge that comes on top of the existing 3 per cent surcharge for additional properties and the 15 per cent rate for those buyers using corporate vehicles. Environmental awareness has also permeated the residential market and energy performance certificate (EPC) ratings and energy improvement recommendations have become important factors for many buyers.

With the exception of the major supermarkets and established online retailers, it has continued to be a particularly difficult time for the UK's retail sector. A succession of household names have continued to join the seemingly endless list of casualties in a sector struggling even before the pandemic. Yawning gaps on the high street and empty shopping centres stand as testament to a sector that has changed beyond all recognition. Traditional retailers have been forced to adapt to the changing habits of their customers, while online retailers and delivery companies have benefited from a significant increase in custom. Technology has adapted rapidly to the situation and there has been a particular growth in e-commerce, including the use of data and development of online platforms. There are, however, signs that stretched consumers are beginning to cut back on online spending. Amazon's recent profit warning confirms the challenges faced in maintaining turnover at lockdown levels. Investors will continue to rethink how they see retail assets, and there will be a renewed focus on repurposing available space for residential, logistics and other more innovative uses. A number of major high street retailers have confirmed plans to diversify and to repurpose upper floors of flagship stores as offices or residential. The government has also proposed introducing powers to require landlords to let empty units to help rejuvenate high streets and town centres. Despite high vacancy rates, there is some cause for optimism as a number of value operators have confirmed plans to expand and smaller independent operators have the opportunity to take prime space vacated by larger chains on flexible and affordable terms. Pop-up retail and food outlets that can adapt quickly to events and demand have become an established part of the market. While London's West End has benefited from a gradual uptick in international and domestic visitors, the City remains much quieter as workers continue to stay at home. Those workers returning are at their highest concentration

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in the middle of the week, and the City is noticeably quieter on Mondays and Fridays. This has made it difficult for the coffee shops and other businesses dependent on a consistent flow of customers to build up a proper head of steam. It will be some time before footfall in the City returns to pre-pandemic levels. Overall, there is a sense that the retail market has bottomed out and values have stabilised in the worst performing shopping centre sector. Although opportunities remain for those looking for value, investors may have missed out on the bargains previously available. The London food and beverage sector is showing signs of recovery with a number of new openings beginning to fill the gaps left by operators unable to survive lockdown. London was reported to have welcomed 14 new international brands in 2021. Those restaurants and bars welcoming back customers have, however, struggled to find staff in a tight labour market. Despite emerging from lockdown, the pressure is back on for retail and leisure operators as discretionary consumer spending falls back.

The industrial sector continued to attract investment, and well-located, high-specification distribution centres in the right locations continued to benefit from the boom in e-commerce. Logistics has been a rare success story with online retailers looking to expand their distribution networks as the pandemic accelerated the demise of traditional retail. The sector has proved to be an attractive target for investment capital with logistics assets high up on the wish lists of a range of overseas and domestic investors. Even Amazon's recent reassessment of its expansion plans has failed to dampen enthusiasm for the sector and the UK still needs greater warehousing capacity, although the Amazon news does serve as a timely reminder of the inherent value of a diverse portfolio and the risks of over-reliance on a single business occupier for constant growth. Further logistics development is essential to serve the UK's supply chain, manufacturing and renewable energy sectors. In addition to good road and rail connections, an acute labour shortage means that the availability of a pool of skilled and unskilled workers has become an important factor in choosing viable locations. The process of onshoring production capability and shortening supply chains should also enhance the UK industrial market and boost local economies. The UK offers plenty of opportunities for specialist manufacturing businesses seeking to take advantage of rising costs associated with existing supply chains, as well as helping customers to reduce their carbon footprint. It has been a boom time for the TV and film industry looking to catch up on a backlog of content. This has led to strong demand from the likes of Netflix, which has taken significant new space at Pinewood. Out of adversity comes opportunity, with large vacant retail units offering opportunities for repurposing as studio space. Generous tax breaks combined with production facilities and available expertise continue to make the UK an attractive filming location. Although pressures on disposable income may mean that new take-up peaked in lockdown, a huge amount of new material is still required just to keep pace with existing schedules. There has also been an increase in hyperscale data centres, although the UK and Europe remain significantly behind the US and China in this sector.

Alternative assets have become an established part of the investment market, alongside the traditional office, retail and industrial sectors. The build-to-rent boom continued as institutional investors looked to increase their market share, and there has been an increase in the number of new projects in the construction pipeline, both in London and the regions. A number of high profile private equity-backed investment vehicles have signalled an intention to develop and operate new tech-enabled build-to-rent neighbourhoods, underlying the growing significance of technology-led platforms in the sector. Despite operational difficulties, confidence remains high for operators in the specialist retirement living and student housing sectors, where major institutional investors are looking to increase

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their portfolios. Purpose-built student accommodation has largely weathered the storm now students have returned to campus. Although demand from private equity and institutional investors remains high for quality stock in strong regional cities, compressed yields are leading to more speculative development funding as investors look for value in the student accommodation market. The retirement living sector has much further to go if it is to emulate the North American, Australian and New Zealand models. Later living developments must provide an attractive community in which to live that adapts to provide care as the need arises. Perhaps not surprisingly, there has been a surge of interest in the life sciences sector, with the Oxford–Cambridge arc attracting the most attention. Innovation hubs thrive on shared technology and a dynamic talent pool and must compete on a global platform. Once established, they in turn boost investment in housing, ancillary offices, infrastructure and leisure facilities. Next generation science, innovation and technology will become a key part of the real estate market as well as the wider economy. The hotel and leisure sector has been desperate for a return to healthy occupancy rates. Last year this was met, at least in part, by domestic travellers in dire need of a post-lockdown holiday. More recently, there has been a gradual increase in overseas visitors as passenger planes returned to the skies. Confidence in the travel industry is essential, with a steady flow of foreign tourists required to fill an increasing number of available beds, particularly in London where a number of major new hotel projects are planned. Opportunities can be found in the pub sector, where some leading pub chains have expressed an interest in expanding their estates and have taken advantage of buying opportunities. The long-suffering nightclub and live entertainment sectors, although now open, have had to cope with confusing health and safety requirements, as well as local authorities and communities that have become accustomed to a quieter life. Alternative real estate assets seem likely to offer opportunities as investors are forced to be more flexible in their quest for growth in this rapidly evolving and increasingly important sector.

It has been a difficult year for the UK lending market with an increase in defaults, restructurings and refinancings. The retail and leisure sectors have been particularly badly hit. Banks are anticipating problem loans and have reconstituted their bad bank structures to work out portfolios of non-performing loans. Businesses will struggle with increased levels of debt and face liquidity problems, particularly if interest rates continue to increase in line with expectations. Borrowers have become accustomed to historically low interest rates and even a relatively gentle uptick is likely to be painful. Landlords and developers have found themselves squeezed in the middle as rental arrears have accrued, making it difficult for borrowers to meet their loan obligations. Development loans have been adversely affected by delays and defaults on construction contracts where shortages of labour and materials, as well as persistent supply chain issues, have led to significant delays and cost overruns. This has also fed into an increase in lending costs. Despite caution in the banking sector, it is hoped that an already diverse lending market will help maintain liquidity. A significant development has been the emergence of green financing to support developments and activities with a green or broader social purpose. Sustainable finance has become an established component of lender and corporate business strategies. Inevitably, a protracted period of economic stress will prove to be too much for a number of borrowers and there will be increased opportunities for investors in distressed assets and mortgage debt.

The world has become a very different place over the past couple of years. We have not witnessed global events of this magnitude in modern times. As lockdowns finally eased, the significant increase in activity across all sectors has been stymied by Russian hostility in Europe. However, it is not all doom and gloom as UK real estate traditionally provides

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investors from around the world with a relatively safe haven for their capital. In particular, private equity funds sitting on substantial firepower continue to be attracted by low valuations and take private opportunities, particularly in currently unfashionable sectors. Ukraine notwithstanding, global markets have been buoyed by positive news regarding the development and rollout of covid-19 vaccines. Despite this remarkable scientific achievement in such a short period of time, it is clear that covid-19 is not going to go away, and it has become a question of bringing it under control and managing its human and economic consequences. The world continues to face an enormous logistical challenge as millions of doses of effective vaccines need to be manufactured, distributed and administered around the world. There will inevitably be more ups and downs, with large numbers of people around the world still unvaccinated. Although cost and resources are factors in the varying vaccination rates around the world, vaccination has also become a social and political issue leading to protests and civil unrest. On a more positive note for the industry, inflation, relatively low interest rates and the attraction of a secure yield will ensure the continued attraction of UK real estate for global investors.

II RECENT MARKET ACTIVITY

a Workspace Group acquired McKay Securities for £271 million;
b Capital & Counties acquired a 26.3 per cent stake in Shaftesbury for £436 million;
c Morrisons acquired McColl through a pre-pack administration;
d Macquarie Asset Management has agreed to acquire Roadchef from Antin Infrastructure Partners;
e LXI REIT acquired Secure Income REIT for £1.36 billion to create a top 10 UK REIT with assets of £2.4 billion;
f Starwood Capital acquired RDI REIT for £468 million;
g Sigma Capital was acquired by Pine Bridge Benson Elliott for £188.4 million;
h The Scape Living – iQSA consortium has acquired a 87.9 per cent stake in GCP Student living for £1.1 billion;
i Life Sciences REIT raised £100 million;
j Tritax Big Box REIT's £300 million capital raising;
k Home REIT's £350 million capital raising;
l Welcome Trust's acquisition of Urban & Civic for £506 million;
m Lone Star acquired McCarthy & Stone for £647 million;
n Blackstone Group acquired St Modwen Properties for £1.5 billion;
o Land Securities Management has acquired U&I Group for £190 million;
p Derwent London has agreed to acquire the City Road Island site, including Moorfields Eye Hospital, for £239 million;
q Brookfield Asset Management has acquired Arlington Business Park Partnership for £714 million;
r Fortress Investment Group has agreed to sell Paratus AMC to Athene Holding;
s Värde has sold Bizspace to Sirius Real Estate for £380 million;
t Barratt Development has acquired Gladman Developments for £250 million;
u LendInvest raised £186 million;
v Blackstone has acquired LS Harbour Exchange from Land Securities for £196.5 million;
w Terra Firma Capital Partners acquired Hopkins Homes for £300 million;

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x Berkeley Group Holdings has acquired the remaining interest in ST William Homes for £582 million;
y Office Group acquired Fora Space from Brockton Capital to create a combined entity valued at £412.5 million;
z Greystar Real Estate Partners acquired Fizzy Enterprises, with a portfolio valued at £400 million, from Metropolitan Thames Valley Housing;
aa AEW Europe has acquired 50 per cent of AEW UK Investment Management; and
ab SEGRO European Logistics Partnership's £500 million issue.

III REAL ESTATE COMPANIES AND FIRMS

i REITs

The UK REIT regime came into force in January 2007. It exempts from corporation tax the income and capital gains of a UK REIT's property rental business. The income and capital gains of any other business, including from acquiring or developing property for sale, is taxed at the main corporation tax rate. While not all property companies are REITs by any means, the largest corporate real estate groups are structured as REITs to benefit from these tax advantages. As a result, M&A involving UK REITs will have specific considerations that will need to be taken into account.

Main conditions

A UK REIT can consist of either a single company or a group of companies. The basic conditions that must be met by the company or parent company of a group are:
a it must be resident only in the United Kingdom for tax purposes;
b it can have only one class of ordinary shares, which (generally speaking) must be admitted to trading on a recognised stock exchange, and either listed or actually traded on such an exchange;
c it must not be a close company (a company that is controlled by five or fewer shareholders), although close companies that are controlled by certain institutional investors, such as pension funds, charities, certain collective investment schemes and other REITs, are allowed; and
d the property rental business must constitute at least 75 per cent of the total profits and assets of the company or the group.

There are also diversification rules requiring a business to hold at least three properties, each representing no more than 40 per cent of the total value of its portfolio.

To ensure that the property income generated by a property rental business is ultimately taxed, at least 90 per cent of the income profits of the business must be distributed annually by way of dividends. A UK REIT is subject to a tax charge to the extent that it falls short of this.

A leverage requirement is also imposed such that the gross income of a UK property rental business must cover the external financing costs of the entire property rental business by a ratio of at least 1.25:1. Again, a tax charge is imposed on UK REITs to the extent of any excess financing cost.

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Takeover of a UK REIT

If a UK REIT, whether a single company or a group, becomes part of another REIT, it will remain within the UK REIT regime as long as the conditions continue to be met. A takeover may well cause the company (or parent company of a group REIT) to become a close company unless the terms of an acquisition are such that at least 35 per cent of the ordinary shares remain in public hands. UK and equivalent foreign REITs are now recognised as institutional investors, which should deal with that point in most cases – however, it will not always be the case that a foreign entity labelled as a REIT will be equivalent to a UK REIT, so a degree of circumspection is required. In a cross-border context, the impact of the leverage requirement – in that it looks at gross income of the UK property rental business only but takes into account the external financing costs of the worldwide property rental business – will need to be considered.

ii Recent developments

The introduction of UK REITs in 2007 coincided with the beginning of a major downturn in the commercial real estate market. UK REITs were conceived during a UK property boom and consequently faced challenges during the financial crisis.

However, as property prices recovered, there emerged a renewed interest in UK REITs as a tax-efficient investment structure, especially following the abolition of a 2 per cent entry charge on seeding assets in 2012. The introduction of the UK REIT regime was a significant improvement to the tax environment for UK real estate companies and has since developed in a broadly investor-friendly way, leading to a positive impact on the UK-listed real estate sector. That said, the introduction of the indirect chargeable gains charge in 2019 (discussed in more detail below) has possibly soured things a little by making disposals by non-residents of holdings in UK REITs subject, in principle, to UK tax. The UK REIT sector now includes some of the United Kingdom's largest real estate companies, such as Land Securities, Derwent London, British Land, SEGRO, Great Portland Estates, Hammerson and Canary Wharf Group. The number of UK REITs has grown significantly in recent years (including externally managed UK REITs) to nearly 100.

iii Real estate private equity firms

Structure

In the United Kingdom, real estate private equity firms can be structured in a number of ways. As a result of regulatory and tax issues, which affect the operation of a fund and its investors, the most common structure in the United Kingdom is an English (or Scottish) limited partnership. Generally speaking, these vehicles have no legal status in their own right (although Scottish limited partnerships do have separate legal personality); in essence, they exist only to allow the partners to act collectively. Each partnership:

a has a finite life (usually 10 years with a possible two-year extension, although some have investors with rolling annual commitments);

b has one general partner with unlimited liability for the liabilities of the partnership;

c has a number of limited partners (LPs) whose liability is limited to the amount of their equity investment in the partnership; and

d is managed by an investment manager on behalf of all the partners.

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The investment manager is a separate entity (owned collectively by the private equity fund managers). It is structured as a partnership (then an offshore limited partnership). The manager receives a fee from each fund it manages.

The general partner is a company owned by the investment manager and, in compliance with the Limited Partnerships Act 1907, must have unlimited liability for the liabilities of the private equity fund. However, the individual partners cap their liability by investing through a limited company. Individual partners of the private equity fund manager are required to invest their own money directly in the fund (usually between 1 and 5 per cent of the fund).

External investors are LPs. Their total liability is limited to the amount of capital they have invested. LPs themselves may be structured as corporations, funds or partnerships.

Footprint

Private equity firms have been major investors in UK real estate in recent years. Investment has been made across a wide range of sectors including hotels, residential schemes, housebuilding, healthcare, student housing, restaurants, serviced offices, logistics and retail.

Private equity firms have continued to raise large amounts of capital for investment in UK and European real estate, and investment activity has been buoyed by the relatively low risk opportunities afforded by real estate in terms of a reliable income stream and capital growth.

IV TRANSACTIONS

i Legal frameworks and deal structures

Legal frameworks

When investors acquire or dispose of real estate in the United Kingdom, the majority of deals do not involve a transfer of title to the relevant property from the seller to the buyer. While smaller deals may involve the direct transfer of real estate assets, for a number of reasons (the main driver is often tax, as outlined below) the acquisition or disposal of real estate assets is made through share purchases of corporate vehicles that own the property in question. It is unusual for there to be a direct transfer of real estate.

Various structures are used to acquire and hold real estate. The optimum structure will depend on, in each case, a number of factors and considerations (including funding, tax and exit routes (for private equity funds)). Typical structures include:

a companies limited by shares: body corporates with a legal personality distinct from those of their shareholders and directors: these companies are governed by the Companies Act 2006;

b limited partnerships: discussed above in relation to private equity firms;

c limited liability partnerships (LLPs): bodies corporate with a legal personality distinct from those of their members. Members have limited liability in that they do not need to meet the LLP's liabilities. They are governed by the Limited Liability Partnerships Act 2000 and the Companies Act 2006;

d joint ventures: there are no laws relating specifically to joint ventures under English law; their structure will be determined by the nature and size of the enterprise, the identity and location of the parties and their commercial and financial objectives. The relationship between the parties will be subject to, depending on the structure, general common law rules, the legislative provisions of company and partnership law and the provisions of the joint venture agreement;

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e trusts of land: any trust that includes land as part of a trust property will be a trust of land. Trustees have the power to sell the property, but no obligation to do so, unless this is expressly provided for. They are governed by the Trusts of Land and Appointment of Trustees Act 1996; and

f REITs.

Deal structures

Share acquisitions with cash consideration remain the predominant form of real estate transaction structure. This is likely attributable to the relative simplicity of completing a transaction structured as a share acquisition and, from a valuation perspective, the certainty of receiving cash consideration.

Fixed-price transactions (often in the form of locked boxes) are the structure of choice for private equity sellers, although they are increasingly used by trade sellers conducting auctions. Earn-outs and deferred consideration are not common features of the UK real estate M&A market.

Post-completion adjustments to the purchase price are also a common feature, particularly where there is a delay between signing and completion (see below). Adjustments are most commonly made to account for variations in working capital and net debt.

The use of escrow structures has also increased in the real estate private equity M&A market as a way to make contractual claims in respect of warranties and post-completion purchase price adjustments.

Acquisition agreement terms

As previously noted, typically real estate assets will change hands through a sale of the shares in a corporate vehicle that owns those assets. As with any share deal, the buyer will take on the target's existing liabilities and commitments and the seller will provide warranties and certain indemnities. The title to the real estate assets will usually be certified by the seller's counsel. The extent of the sales and purchase agreement (SPA) provisions will vary depending on the nature of the transaction, the real estate assets in question and the due diligence undertaken. However, there are a number of aspects to consider.

Conditionality

A number of conditions may need to be satisfied before a real estate transaction can complete (such as obtaining planning permission, third-party consents or even practical completion of a property development). Any such conditions must be satisfied or waived before the real estate transaction can complete.

Splits between signing and completion

For any split between signing and completion, several practical matters should be considered, including whether:

a shareholder (or equivalent) approval is required by either party;

b EU merger clearance is required;

c any warranties given at signing need to be repeated at completion;

d rescission is possible between signing and completion;

e any deposit paid at signing should be returned to, or forfeited by, the buyer if the transaction does not complete; and

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f management of the underlying properties is required and, if so, whether the buyer will exercise control.

Rescission

Where there is a split between signing and completion, this may affect whether a buyer is able to negotiate a rescission right, as mentioned above, during that time.

Where sellers are required to obtain shareholder approval for a real estate transaction after signing but before completion, it will be difficult for them to argue that during this period the buyer should face the potential risks and be unable to rescind.

In contrast, where the reason for a split is as a result of the time required by the buyer (e.g., to procure debt finance), it is less likely the buyer will be able to negotiate a rescission right for anything other than material breach of any restrictive conduct provisions.

Buyer protections

In UK real estate acquisitions, buyer protections are particularly important as the buyer is not afforded any statutory or common law protection on acquisition; caveat emptor (buyer beware) applies. Where a buyer purchases a target group and is to inherit all related obligations, liabilities and commitments, a robust package of warranties and appropriate indemnities will be required from the seller. These will normally be limited to the corporate vehicle and taxation matters; the buyer will usually be expected to satisfy itself on title to the real estate assets through a normal due diligence exercise or reliance on certificates of title issued by the seller's lawyers. Recently we have seen a move towards title insurance as a way for buyers to deal with title due diligence, sometimes in combination with purchaser due diligence or certificates of title, or both of these. A combination of approaches is not uncommon on portfolio deals with properties of various values or significance.

Warranties

Although sellers (particularly private equity sellers) will not want to provide a large number of warranties on the sale of real estate assets, they are important to provide buyers with some contractual protection. An SPA will not generally include long-form property warranties; the buyer's property enquiries will be answered by the seller in the form of representations.

Buyers are increasingly succeeding in extending the scope of warranty coverage, although sellers often succeed in disclosing all due diligence information against such warranties. Private equity sellers have also conceded business warranties on occasion (however, these tend to be in respect of identified issues that cannot be addressed through further diligence or otherwise reflected in the price).

The repetition of warranties at completion is usually limited to core warranties regarding title to shares or real estate assets and the capacity and authority of the seller to enter into a transaction.

Indemnities

Where a buyer identifies (through due diligence) a particular risk or liability that it is unwilling to assume (e.g., environmental risks or planning liabilities) and that risk is not easily quantifiable, specific indemnities will be sought, shifting the exposure to the seller.

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Warranty claims are difficult to make in practice, so indemnities are preferable from the buyer's perspective. Sometimes title insurance to protect against a specific title defect can be obtained.

Seller protections

The limitations on a seller's liability under an SPA will be dependent on the particulars of each transaction. In practice, however, the parties will agree that certain warranties (i.e., core warranties) will be capped at the overall consideration for the deal. Depending on commercial and competitive pressures, there may be a different cap on liability for other warranty breaches (e.g., 15 to 20 per cent of the overall consideration).

General warranties are likely to have a duration of 18 months to two years, while tax warranties are more likely to have a duration of four to six years. There is also likely to be a *de minimis* threshold that must be reached before a claim is brought.

As previously noted, the seller's exposure under the warranties will be limited by the disclosures made in the disclosure letter (which the buyer will ensure are sufficiently detailed so that a view can be taken on its liabilities).

There is a growing tendency for both sellers and buyers to obtain warranty and indemnity insurance in the UK M&A market. Insurers such as Aon and Willis are increasingly marketing their willingness to offer warranty insurance, although they expect that careful due diligence will be carried out in the normal way by the buyer. This trend has been driven by sellers seeking a clean exit – a broader set of warranties can be presented with limited post-completion financial exposure. Similarly, buyers are arranging insurance to supplement or cover gaps in the protection provided by sellers – securing sufficient protection can allow buyers to proceed with a transaction without raising a seller's exposure and potentially prejudicing the competitiveness of any offer.

ii Financing considerations

Real estate investors are usually backed by a mixture of debt and equity. Lenders will require typical security packages in relation to real estate lending, which will consist of:

- *a* charges by way of legal mortgages over real estate assets;
- *b* charges over rents receivable;
- *c* potential charges over bank accounts into which rents are paid; and
- *d* additional charges over certain contracts (such as leases, insurance policies and development and construction contracts).

Depending on the circumstances, lenders may also seek protection against borrower default through conditions precedent and direct covenants in the facility agreement, property valuations, parent company guarantees and bonds, and cash collateral, and by obtaining floating charges from the parent company.

Where development and construction are anticipated, lenders may also require approval of material development documentation as a condition precedent to drawdown and may expect to receive collateral warranties or third-party rights from contractors, designers and key sub-contractors. Step-in rights may also be sought to take over a contract in the event of default.

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iii Tax considerations

Stamp duty land tax (SDLT) is payable by the buyer of commercial real estate and is a percentage of the purchase price, varying depending on the consideration paid for the property. SDLT is currently payable at 2 per cent on the portion of consideration between £150,001 and £250,000, and 5 per cent on the portion of consideration above £250,000. For investors to avoid paying high tax rates for individual real estate assets, it is better for the shares in the vehicles themselves to change hands. SDLT does not apply to the purchase of shares in companies holding real estate assets (at least, not yet – see below). The rate of stamp duty on the transfer of shares in a UK-incorporated company is 0.5 per cent.

If real estate assets are sold and purchased directly, the default position is that the sale or purchase in the United Kingdom is not subject to VAT, although owners can opt to tax property at the standard rate of 20 per cent. Generally, most owners opt to tax – the exceptional cases tending to be where the occupational tenant is one with restricted VAT recovery, such as a bank or insurer. Where a property is currently let or a letting has been agreed, VAT can be mitigated by ensuring the sale is treated as outside the scope of VAT as a transfer of a business as a going concern, provided the buyer continues letting the business and opts (and notifies HMRC that it has opted) to tax. Otherwise, even if the buyer can recover all of the VAT charged on the sale, the VAT amount will count as part of the consideration on which the SDLT charge is calculated and thus create an absolute cost in all cases.

Interest charges on borrowings are, generally speaking, deductible expenses for tax purposes, so gearing will generally result in tax efficiency. Many real estate investors introduce borrowing to achieve this result. In such circumstances, it is important that any loan arrangement is at arm's-length. To the extent that loans do not meet that commercial threshold, interest on them will not qualify as being deductible.

With effect from April 2017, the UK introduced a new restriction on the deductibility of debt finance for corporation tax purposes, similar to those that have existed for some time in other jurisdictions (such as Germany). The UK regime limits interest deductions to 30 per cent of a group's taxable EBITDA. The intention is more to discourage groups shifting a disproportionate amount of debt into the UK than to attack debt finance as such. Accordingly, groups that are highly geared on a worldwide basis may benefit from making an election that permits the use of a percentage based on the ratio of the group's net interest expense to its global accounting EBITDA. There is also an exemption for third-party debt incurred by infrastructure companies that, somewhat generously, extends to companies carrying on a UK property letting business (provided the leases in question are to third parties and do not exceed a duration of 50 years).

A significant change to the taxation of offshore investors in UK real estate was announced as part of the 2017 Budget. With effect from April 2019, non-resident companies became subject to tax on profits and gains arising from holding or disposing of UK real estate in the same way as UK-resident companies. Previously, non-resident investors paid only income tax on rents, and, although disposals of residential property by non-residents have been subject to capital gains tax since 2015, the new tax charge covers all forms of UK property. A more surprising part of this package was that non-residents that dispose of indirect interests in UK property (essentially, shareholdings in UK property-rich companies or collective investment schemes) became in principle liable to UK tax on any gain, subject to any exemption and the terms of any applicable double taxation treaty. A company will be UK property-rich if more than 75 per cent of its gross asset value is attributable to UK real estate (whether held directly or via subsidiaries). A non-resident will be subject to tax on any gain if it holds a 25 per

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cent or greater interest in the company, or has done so within the preceding two years and with interests held by connected parties being aggregated. However, investors in collective investment schemes (including UK REITs) do not benefit from this 25 per cent threshold unless the vehicle they invest in is widely held and is marketed as being invested as to no more than 40 per cent (by market value) in UK real estate.

The UK had not before attempted to tax non-residents in this way, and this change received much negative comment. It is also widely seen as a precursor to the introduction of indirect SDLT, similar to the German real estate transfer tax, although no formal proposals for this have yet been announced. Rather, the focus in terms of new real estate taxes shifted to the residential property developer tax, introduced with effect from April 2022. This tax has the rather specific object of raising at least £2 billion over a 10-year period in order to fund the remediation of unsafe cladding in residential apartment blocks, a policy brought about following the Grenfell Tower tragedy of 2017 and the realisation that a number of apartment blocks in the UK were fitted with cladding, previously considered to be safe, that was now understood to present a fire hazard. It is in effect a surtax charged at 4 per cent (subject to a £25 million annual allowance) on the profits of businesses undertaking residential property development in the UK, whether for investment or sale.

One noteworthy fiscal response to the pandemic was the decision taken in the 2021 Budget to increase the UK's corporate tax rate from 19 to 25 per cent with effect from April 2023. This represents a significant reversal of the policy first adopted by the last Labour government in 2007 of reducing the rate from its high point of 30 per cent – at that stage to 28 per cent – and further under the coalition and the current Conservative governments to its present rate of 19 per cent.

V OUTLOOK AND CONCLUSIONS

Recent events have confirmed that more than ever it is impossible to predict the future. Covid-19 has thrown much of what we know and trust into confusion. The pandemic has had a profound effect on how people around the world live and work. Despite positive news regarding the progress of vaccine programmes, it is very clear that covid-19 in some shape or form will remain with us for some time to come, and real estate and the wider economy will feel its legacy for longer still. Russian aggression has reminded a world emerging from lockdown of the importance of global political stability. The ongoing occupation of Ukraine has demonstrated the fragility of world peace and also the complexity of global economics as we continue to buy oil and gas from the aggressor (albeit not to the same extent as continental Europe). All of this sits against the backdrop that is the longer-term challenge of climate change and other ESG considerations, which businesses are coming under increasing pressure to take account of in their operating practices and investment decisions.

Although flexible working practices will clearly become a more accepted part of how we work, lockdown has also confirmed that face-to-face contact is a key part of our working lives. It is not just the existing workforce that needs to be catered for but the generations to come. Physical presence in the office has traditionally been an essential part of the learning curve for those starting out on their careers or changing jobs. Remote working may prove to be an unsatisfactory substitute, giving credence to those currently advocating greater attendance. It seems certain that employment lawyers and HR departments are going to be busy over the coming months and years as the tension between new employee expectations and traditional employer requirements continues on its journey towards a happy equilibrium.

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Although fewer workers may need to be in the office, those workers will be more conscious of what the office has to offer. The City has lagged behind the West End as office workers have been slow to return in significant numbers. Trends starting even before the pandemic have become established, as mid-week office attendees have left the City feeling empty on Mondays and Fridays with a knock-on effect on the dependant retail, food and beverage and leisure businesses. Corporate owners will need to focus on how space can best be used. It is no longer sufficient to simply build an office and expect workers to fill it. Architects have been forced to focus on purpose rather than simply appearance. Tenants have finally become customers and landlords need to become customer relationship managers with all parties actively engaged throughout the contractual term and beyond. The office has a key role in attracting staff and talent retention, it is no longer just a place to work. The gap between new-build product and second-hand office space will widen and this will result in a repurposing of redundant buildings. Hybrid working has shifted the purpose of the built office environment as employers seek to provide an altogether better workplace experience. Confidence is key and offices must be seen as attractive places to work and play, particularly in London, which thrives on large numbers of talented people from all over the world wanting to work and live in a world-leading financial and cultural hub.

The industrial sector has fared best in the current crisis. Demand for logistics space remains strong to meet the requirements of internet shopping and UK-wide distribution. The post-Brexit spike in demand for commercial storage space and a move to refocus existing buildings for distribution and storage use has continued. The industrial sector has become the top performer and a new safe haven for investors. The boom in life sciences also seems set to continue. There has been a surge of interest in film and studio space as the industry seeks to catch up with consumer appetite for new content. With the exception of the major supermarkets, the retail and leisure sectors face an uncertain future and we will see further insolvencies and restructurings. Discount and value operators will take up some of the space vacated and there will be opportunities for new entrants and independents to take previously unattainable space at affordable rents. The pub sector is an obvious target for bargain hunters and chains planning to expand their footprint. Rental structures are likely to evolve further to enable landlords and tenants to share the pain and gain, by reference to turnover and commercial success. The obtaining and sharing of data will become an increasingly important part of the landlord and tenant relationship, not only in relation to turnover rents but also to help meet respective ESG targets. It will be fundamental that people feel safe where they live, work and relax. The normally robust hotel sector may also take time to recover as confidence returns and global travel restrictions are lifted fully. Even then, it is likely that air travel will remain well below pre-pandemic volumes as rising costs and complex travel requirements continue to deter holidaymakers and businesses review their travel policies in the light of ESG strategies. The serviced apartment and holiday let sector may benefit as people prioritise their own personal space and facilities. The central London residential letting market has started to pick up as workers, students and tourists return to the capital. Demand for housing is likely to remain strong, although the pandemic may involve a rethink in the design and location of new developments. Those finding themselves working from home on a much more regular basis will continue to prioritise space over convenience.

A combination of covid-19 and Brexit had already led to intermittent problems in the supply chain, and issues associated with ensuring both a skilled and unskilled workforce have led to delays on construction projects. War in Ukraine has served to add to supply chain issues and increase costs further. Covid-19 will also cause a major rethink on major

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infrastructure projects as we re-evaluate our transport requirements and funding becomes stretched. Following significant delays and cost overruns, the Elizabeth line finally opened to coincide with the Queen's Platinum Jubilee. Crossrail 2, however, remains on ice as part of the funding agreement reached between the government and a cash-strapped Transport for London. The proposed expansion of Heathrow remains open to further political, environmental and economic debate. Supply chains are expected to shift to rail to counter an acute shortage of HGV drivers, a problem that has been brewing for a long time owing to declining pay and conditions in that sector. The UK's ongoing transport requirements will need a degree of re-evaluation once new patterns of living and working become established. As once-in-a-lifetime climatic events threaten to become more frequent, increased expenditure on flood defences and other infrastructure is required to limit the damage caused by such events and to enable much-needed development to occur on floodplains and in other vulnerable locations. Much will depend on the steps taken to stimulate the economy by a government saddled with increased debt and under pressure to address the cost of living crisis.

The covid-19 pandemic and war in Ukraine have put concerns about leaving the EU into perspective. Indeed, the all-encompassing effect of both events has to some extent levelled the post-Brexit playing field. In order for the recovery to continue, the market needs certainty, and that certainty will only arrive once peace is achieved in Europe and the covid-19 threat is contained. The much-anticipated surge in real estate M&A and private equity activity as the world lifted covid-19 restrictions has been hamstrung by war in Ukraine. Although there will inevitability be less activity than expected, opportunities in real estate undoubtedly remain. There is no shortage of global investment capital, and it is reasonable to believe that UK real estate will continue to receive more than its fair share. London in particular will retain its position as a leading global city. However, competition will be strong and the UK must work hard to ensure that it remains attractive as a place in which to live, invest and do business. The much-derided Marble Arch mound proved to be one of the UK's less successful initiatives to help achieve this.

Economic forecasts have been revised downwards for 2022 and 2023, reflecting political and economic uncertainty stemming from conflict and other risks to growth. The real estate industry is by no means immune and there has been an uptick in insolvencies in the property and construction sectors. Although stock markets have suffered their worst falls since June 2020 at the height of the pandemic, the FTSE 100 has just about managed to steady itself above the psychologically important 7,000 barrier. Conflict in Europe, a robust and mutating virus, rising inflation, higher borrowing costs, ongoing supply chain disruption, product and labour shortages and the withdrawal of pandemic-related government support are persistent headwinds facing the UK's recovery. These ongoing issues will ensure that every business will continue to re-evaluate how they operate and their property requirements.

The lifting of travel bans has encouraged activity from overseas investors looking for an attractive destination for their pent-up capital, and investment volumes in the last quarter of 2021 reached pre-pandemic levels. Interest from Asian investors has been strongest followed by the US, the Middle East and Germany. China has faced troubles of its own with the introduction of its 'three red lines' debt controls to address the issues in its own real estate market highlighted by Evergrande. This and existing exchange control measures may curb Chinese enthusiasm for UK real estate, at least for the time being. Although the appetite for deals remains strong, a greater understanding of each target sector and the underlying assets will be required. The skill is being able to identify those sectors of the market demonstrating chronic need combined with guaranteed demand. It is also important to remember that real

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estate remains a relationship-driven industry, and an ability to tap into property expertise is essential if investors are to blend successfully into the market. Some sectors have changed forever, and the real estate market will never be the same as it was before the pandemic. There has been a significant re-setting of the UK's property requirements and investors will need to show imagination and adapt to the new world order.

After a gloomy couple of years dominated by the covid-19 pandemic, it is sincerely hoped that next year's edition brings with it much more positive updates from the UK and the rest of the world. Those returning to Cannes for MIPIM earlier this year will have noticed a smaller but perhaps more focused event, reflecting the challenges as well as the opportunities ahead.

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Appendix 1

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Richard Smith has a broad corporate and corporate finance practice with particular experience in public and private M&A and equity capital markets work. His clients include Land Securities, Grosvenor, Equinix, Aviva, Reckitt Benckiser, United Utilities, Close Brothers, Countrywide and Stock Spirits.

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ISBN 978-1-80449-098-3

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