

the problem of the sub tenancy dispute

Our casebooks are drawn from the chronicles of the Pensions Ombudsman and are designed to draw from these cases, perhaps in a light-hearted and easily digestible way, points that might be of relevance to advisers who work with self-invested and self-administered pensions.

so... what happened?

Two clients, whom we shall call Mr A and Mr B, found themselves in business together. They decided to further cement (no pun intended) their relationship with bricks and mortar: in other words, jointly purchasing a property via their pensions and then complete the circle by letting that property to their business.

All went rather well until, suddenly, it didn't.

Mr B owned the lion's share of the property (no, it wasn't a circus, or a zoo). He decided, however, that enough was enough, and parted company with Mr A on not so amicable terms. Trouble started brewing.

Now, these clients had entered into a syndicate agreement setting out the terms under which the property would be managed. The lease and syndicate agreement called for unanimous decision-making by the owners and, among other things, the sub-letting of the property by the company was prohibited.

Following Mr B's departure, it subsequently transpired that Mr A unilaterally allowed sub-letting of the property contrary to the agreements in place. Once Mr B was aware, he invoked his right to make his views known. Vociferously.





what was the outcome?

Mr B directed his grievances at the SIPP Provider alleging it was negligent in allowing the situation to evolve as it did. Chief amongst these were arguments that the SIPP Provider:

- had knowingly allowed sub-letting, contrary to the prohibition in the lease;
- was negligent in allowing a SIPP to be established without anticipating the consequences of a falling out between Mr A and Mr B;
- Discouraged Mr A and Mr B from taking separate legal advice when the transaction took place;
- Caused financial detriment to Mr B's benefits from increased wear and tear on the property, plus the potential of four sitting tenants (and one assumes standing, and generally moving around also) if the company as primary tenant failed.

In its reply, amongst many other relevant and useful comments (yes, really), the Ombudsman made the following main observations:

- The fact that the agreements that existed between Mr A, Mr B and the SIPP Trustee did not cover the eventuality of a falling out was not, in itself, maladministration. Further, there was no legal requirement for Mr A and Mr B to take separate legal advice before proceeding with the original purchase, nor for the SIPP Trustee to advise this course of action. In other words, it was up (or down, depending on your perspective) to the individuals.
- The promotion of the use of a panel solicitor to assist with the purchase did not amount to discouragement to take separate legal advice;
- Three of the sub-tenancies occurred without the knowledge of the SIPP Trustee, and it is therefore difficult to see how they could have prevented them. The fourth sub-tenant was, however, a different matter and it was felt that the SIPP Trustee should have taken steps to mitigate the conflict of interest that existed between Mr A and Mr B.
- The question of potential financial detriment was discounted by a counter argument (or, rather, a counter suggestion, as it was politely delivered) that despite being a breach of the lease, the sub-tenancies may well have bolstered the financial position of the company. So, though the sub-tenancies were wrong, they actually mitigated the potential financial detriment of the loss of the primary tenant (who in recent times had fallen into arrears but was now able to make good on the rent).

The matter was finally resolved when Mr B agreed to sell his share of the property (one assumes to Mr A, otherwise we'd start all over again...).

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what do we learn?



Disputes between individuals will sometimes arise no matter how amicably the position is at outset. It is important to recognise this and to try and build this into the purchase process. Solicitors are key here, but so is educating the protagonists (sorry, participants). Where there is an agreement that sets out how the property is to be managed, that agreement should also contain provisions that deal with what happens should there be a dispute. For example, that both parties agree to the appointment of an independent arbitrator.



Majority ownership does not create, in and of itself, greater voting rights. Unless the parties have specifically agreed that one individual 'out ranks' another, each party will have an equal say in relation to the property.

Arguably, even where individuals try to operate by majority rights, the Trustee would potentially still have the final say if the actions were seen to be detrimental to the minority owner's pension.



Claims for financial loss need to be actual rather than theoretical. So, for example, it is not enough to suggest that financial loss occurs because it is possible that something might happen in the future to devalue the property (such as sitting, standing, or otherwise aggressively active, tenants) because it has not actually occurred.



A serious conflict of interest is, in a nutshell, not easy to resolve. In this case, neither party acted as a Trustee of the other's SIPP, and therefore recourse to the Ombudsman was limited to taking exception to the actions (or inactions) of the SIPP Trustee, rather than the activities of the individuals themselves (which are usually the cause of the issues in the first place).

Serious disputes can lead to the unavoidable time, cost and effort of employing solicitors rather than assuming that there is, or might be, an easy solution written into pension law.

It is worth pointing out that in an extreme case, the Ombudsman would expect the SIPP Trustee to step aside from the conflict by potentially arranging the appointment of an Independent Trustee or even closing down the SIPP in question. Thus, the unintended consequence of a dispute could lead to a nightmarish scenario for the individuals, who suddenly find themselves without assets to fight over...