
STRUTT
&PARKER
BNP PARIBAS GROUP
Telecommunications
Survey
2019

Telecommunications & Survey 2019

WELCOME

It is my pleasure to introduce you to Strutt & Parker's Telecommunications Survey 2019.

Whilst we will review the changes in the industry since our last survey it is important to note our own changes. In October 2017, Strutt & Parker and BNP Paribas Real Estate merged to offer a broad set of services to clients throughout the real estate life-cycle, across every type of asset in commercial, residential and rural. Our integration continues to flourish and we welcome the opportunities afforded under both brands.

The Telecommunications Industry continues to move at considerable pace and the intervening years since our last survey has proved to be no exception; that was until the new Code, introduced as part of the Digital Economy Act 2017, was enacted on 28th December 2017. Arguably this has been the biggest single event to hit the industry since the first mobile phone call was made in 1985.

This survey will reflect upon the market place as it once was and how the new Code has impacted upon the relationships between Land/Building Owners, Wholesale Infrastructure Providers (WIP) and Operators.

We have analysed our extensive database to spot trends and debunk any untruths about a market which affects us all. However, this may be a snapshot in time now that we have entered the brave new world where Operators use imposition rather than attempting to reach consensual agreements.

In this edition, we will also consider the issue of thousands more sites being required when the market is now unwilling to do deals at the consideration and terms previously offered and accepted as the norm.

ROBERT PAUL
Head of Strutt & Parker's Telecoms Group

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LEASE TERMS

Analysis of new leases agreed over the last three years revealed a reversal of the trend to Open Market Value (OMV) only reviews. OMV/RPI reviews remain the predominant review mechanism, representing some 54% of all new leases. Our survey indicates that RPI only reviews exist in only 8% of new leases over the past three years.

Likewise, there was a shift in the rent review pattern. In our last survey we suggested that just over 60% of leases were reviewed on a three-yearly basis, but analysis now shows that this has increased to 74% of new leases entered into in the last three years.

The majority of leases (94.7%) which were concluded in the three years prior to the introduction of the new Code restrict the number of antennae that can be installed. The usual format is a restriction to 10 items, (usually 6 antennae and 4 dishes).

Given the changes in the new Code we can confidently predict that the trend towards tightly specified equipment rights in agreements will increase. The Code entitles an Operator to upgrade the equipment to which the agreement relates so it is important that this is clearly specified.

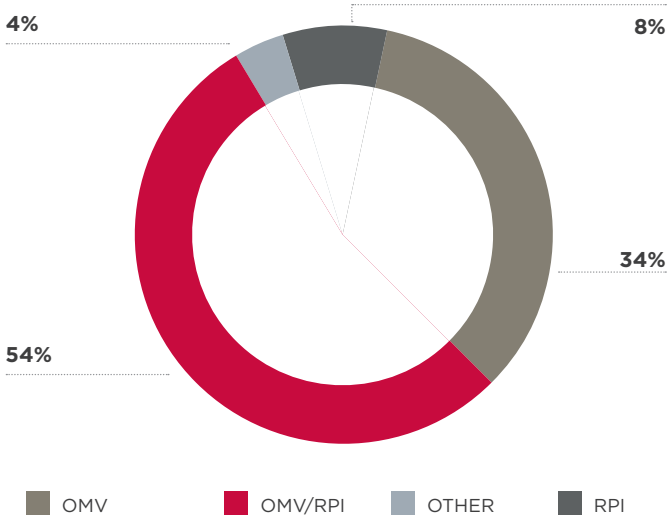
Most new leases restrict sharing but are granted in a manner that they can be used by both Operators in the present joint venture set ups (e.g. to CTIL for the joint use of Vodafone and Telefonica or granted to the joint names of EE and H3G).

The trend towards protecting Landlords against other site sharing continued prior to the 28th December 2017. 62% of new leases entered into in the last three years specify the Operators entitled to use the site. 19% provide that sharing can only occur with a Group company and only 12% provide for a payaway based on a percentage of the site share income enjoyed by the Operator. This is a considerable change from the 62% set out in our 2016 Survey. It is noteworthy that over half of the leases which provide for a percentage payaway also include provisions for a minimum sum, this is to ensure that Landlords are not penalised for non-market transactions between tenants and their licensees.

The trend to restrict ability to share is likely to continue. The new Code grants rights to share equipment for which the agreement was granted, not for a third party to introduce its own equipment. Additional sharers increase the impact on the Landlord.

Operators usually seek wide rights to break but were only partially successful in obtaining these. Conditional break rights formed the majority of new leases (57% conditional on the tenant's loss of licence). There was no right to break in 6% of new leases.

RENT REVIEW MECHANISM



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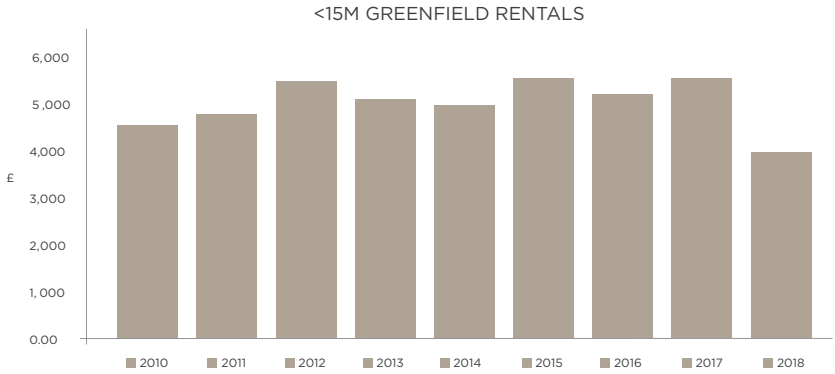
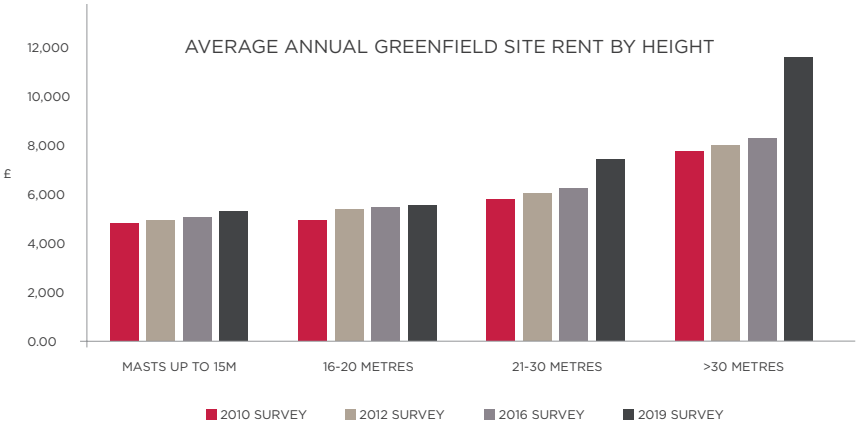
GREENFIELD SITES

Since 2010 and prior to the introduction of the new Code, analysis of rents for greenfield site rentals pointed towards a fairly stable market across the UK.



Indications from our record of transactions suggest that the value of a Greenfield agreement has reduced on average by 26% from our 2017 figures.



This is still pertinent to valuations under paragraph 24 of the new Code in that it does not require any existing planning consent to be ignored.

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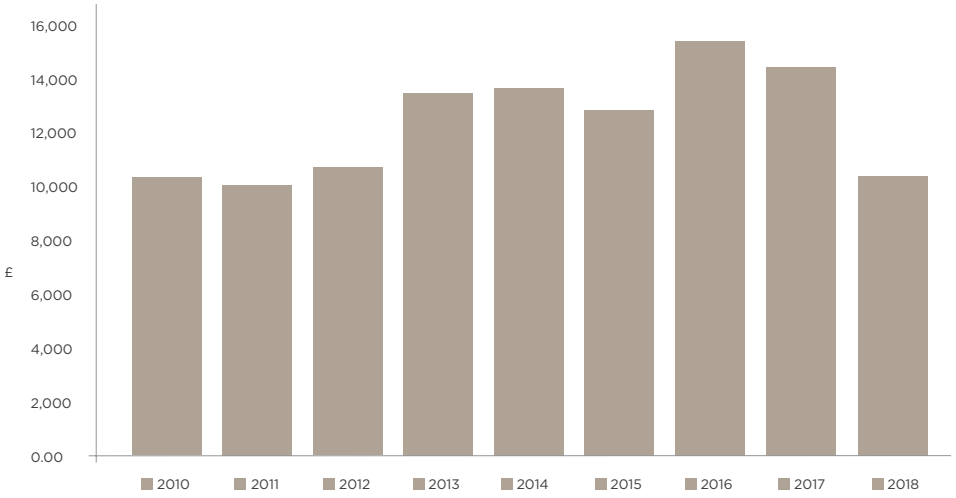
ROOFTOP INSTALLATIONS

Over the years, rooftop installations had stabilised and the London market continued to outstrip the national average. Again this market has changed dramatically since December 2017.

We are now encountering offers from Operators at £50 per annum for city centre rooftops which, before the introduction of the new Code, would have commanded rents between circa £15,000- £30,000pa. It is therefore hardly surprising that Operators are now experiencing difficulties in the rollout of rooftop sites or in renewing agreements. This is particularly evident given the impact of the new Code in respect of a Landlord's ability to redevelop or improve their property and the impact of access issues etc. Landlords are understandably unwilling to enter into agreements at such paltry levels.

ROOFTOP RENTALS



Indications from our record of transactions suggest that the value of a 2018 Rooftop agreement saw a reduction in average value of 28% from 2017 figures. We expect that as more transactions are logged a clearer picture will develop of an average payment on both Greenfield and Rooftop sites but early indications are that the fall in value is consistent.

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MARKET SUMMARY

The Code provides Operators and WIPs with a plethora of rights which they sought from the Government.

Unfortunately, the consensual basis of earlier Codes, which led to the initial roll out of the mobile network across the UK, looks to have been replaced with the imposition of rights by the Lands Tribunal as owners shun the highly advantageous terms demanded by Operators.

Operators have seemed quick to resort to compulsion. In some cases, Code Notices have been served within four weeks of initial approaches to Occupiers with minimal attempts being made to negotiate. This could hardly be described as the making of 'every effort' for a consensual agreement as set out in the Ofcom Code of Practice.

Recent decisions have highlighted weaknesses in the valuation methodology adopted by Operators from the outset, but unless there is a marked change in approach from Operators, consensual agreements are unlikely to be achieved and more cases are likely to come before the Tribunal.

While the old Code was denigrated, the new Code is proving even less workable. Rather than addressing 'not spots' Operators are seemingly targeting existing sites and the direct benefit to the public of granting such agreements is questionable. The number of new lettings since the Code was enacted has plummeted. It would seem therefore that the new rollout and network improvements that were so forcefully argued as being the driver for Code Reform have failed to materialise, in favour of cost cutting endeavours impacting on Landlords which the Operators so obviously need to rely upon.

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THE NEW CODE

The 2017 Code is set out as Schedule 1 of the Digital Economy Act 2017 but actually takes effect under s.4 of the Act as a new Schedule 3A of the Communications Act 2003.

The Code came into effect on the 28th December 2017 and comprises 108 paragraphs (replacing 29 in the 2003 version). The Code is a statutory scheme of rights and obligations which enables Operators to enter land against the landowners wishes in order to install, erect, maintain and use any form of electronic communications apparatus together with any ancillary equipment for the purposes of an electronic communications network. It operates in parallel with any contractual arrangements and may, in many instances, override any agreement.

The central tenet of the Code is that it confers upon an Operator the right to come onto land, if necessary by order of the Court, against the will of the Landowner, to exercise "Code Powers".

Every agreement entered into after the 28th December 2017 falls under the jurisdiction of the new Code. There are far reaching implications for any person entering into a Code agreement. Subsisting agreements are also affected to a limited extent as set out in the Transitional Provisions of Schedule 2 of the Digital Economy Act.

What are Code Rights?

The new Code specifies nine Code Rights which Operators may obtain via the Lands Tribunal if a consensual agreement cannot be reached: -

(a) to install electronic communications apparatus on, under or over the land,

(b) to keep installed electronic communications apparatus which is on, under or over the land,

(c) to inspect, maintain, adjust, alter, repair, upgrade or operate electronic communications apparatus which is on, under or over the land,

(d) to carry out any works on the land for or in connection with the installation of electronic communications apparatus on, under or over the land or elsewhere,

(e) to carry out any works on the land for or in connection with the maintenance, adjustment, alteration, repair, upgrading or operation of electronic communications apparatus which is on, under or over the land or elsewhere,

(f) to enter the land to inspect, maintain, adjust, alter, repair, upgrade or operate any electronic communications apparatus which is on, under or over the land or elsewhere,

(g) to connect to a power supply,

(h) to interfere with or obstruct a means of access to or from the land (whether or not any electronic communications apparatus is on, under or over the land), or

(i) to lop or cut back, or require another person to lop or cut back, any tree or other vegetation that interferes or will or may interfere with electronic communications apparatus.

These form a 'shopping list' from which Operators can choose which rights they wish the tribunal to apply if a consensual agreement cannot be reached.

Ofcom has published a Code of Practice on behaviour, negotiation and the provision of information as well as model notices and suggested standard terms. This can be found on their website. The Code of Practice seems to endorse the approach taken by previous Court decisions that the agreement should be voluntarily sought in the first instance. It states "one of the principal purposes of this Code of Practice is to establish a voluntary process, which avoids recourse to the courts". Parties are required to make *'every effort'* to reach a consensual agreement. It would seem however that Operators are quick to resort to the Code to have an agreement imposed.

The need for a substantial public interest/benefit in overriding Landlord's rights is well-established in case law. This is the test that the Operator must satisfy in order to obtain such rights.

Before imposing Code rights on a landowner or property owner, the court must be satisfied that the prejudice to the landowner or property owner caused by the making of the order can be adequately compensated by money and is outweighed by the resulting public benefit. Public benefit is defined as *"access to a choice of high quality electronic communications services"*.

The Operator is merely the means of delivering public benefit; any benefit to them is not the test for the grant of Code Rights.

Realistically Operators will want wider rights than they are entitled to under the Code. These include (but are not limited to), the grant of exclusive possession, allowing other Operators to install equipment and to add equipment to the existing installation and so on.

New rights to assign, upgrade apparatus and share sites

Whereas the old Code was bilateral, enabling the use of such powers for that Operator's own network, the new Code introduces rights to share and assign. The following will apply to any new agreements entered into after 28th December 2017 regardless of what has been agreed:

- Any provisions that prevent or limit assignation to another Operator, or make it subject to conditions (e.g. payment of a sum to the property owner) will be void.

- Any provisions that prevent or limit upgrading or sharing of apparatus, or are specified as subject to conditions, are also void – subject to particular caveats. The caveats are that an owner can refuse this consent if the upgrading/sharing would (1) have an adverse (or more than a minimal adverse) impact on a site's appearance, (2) would impose an additional burden on the owner. The tribunal is still to determine what a minimal adverse impact, or additional burden might be.

- The Operators will undoubtedly argue that these provisions prevent the need for site sharing payment(s) to be paid to the Landlord albeit they will still be free to use sharing rights to generate additional income.

Termination under the new Code

To end any telecoms agreement, an owner must serve a notice on the Operator which states (1) the Owner wishes to terminate the agreement, (2) the statutory ground on which the owner proposes to terminate (these grounds are very restricted), (3) the steps that may be taken by the Operator in relation to the notice, and (4) the intended termination date.

Operators can then serve counter-notices (meaning the owner then has to ask the Tribunal to sanction the removal of the Operator's equipment).

Under the new Code:

- the expiry date is to be the later of (i) any relevant expiry date provided for within the agreement and (ii) 18 months' prior notice being given to the Operator;

- only the property owner can now seek the removal of the apparatus, i.e. not the occupier tenant – so even though a tenant can grant (whether intentionally or inadvertently) Code rights to Operators in respect of a property and can terminate a telecoms agreement, it cannot necessarily seek removal of the equipment itself; an owner must do that; and

- the owner must give a further notice requiring removal of the apparatus and a reasonable period of time in order for the Operator to do so.

Termination is a two stage process involving; firstly 18 months' notice under part 5 and then, if the Operator fails to remove, an action to remove under part 6. This may have a considerable impact on the Landlords reversionary interest.

We estimate that it could now take up to 3 years to remove electronic communications apparatus under the new Code. Given this, it is important for property owners to engage and negotiate up-front with Operators who have apparatus on a property if the owner is likely to want to redevelop (or sell it to a third party for redevelopment) or to carry out work to a building and where the apparatus needs to be removed to enable this.

Compensation & Consideration

If an agreement is imposed, the consideration payable under the agreement is to be "market value" with specified disregards.

Operators considered that new Code agreements would result in dramatic cost savings because of the unfortunate use of the words 'no scheme world' when the Code was first introduced and the implication such words have under Compulsory Purchase legislation. This is not borne out by the legislation as subsequently enacted. From the outset Operators adopted a "pro-rata existing use" approach, seeking to determine the annual rental value of a site for non-Code purposes using the freehold capital value or rental value as a starting point.

Property owners do and should have well founded reservations about allowing Operators to have relatively unrestricted rights over their properties. The impact of such rights weigh heavily in the valuation approach and, given the tiny sums currently being offered, there is an understandable reluctance of Property owners to give up control of their property to the extent that entry into an agreement for Code rights is likely to entail.

An owner of a £100 million building in central London may take a view on whether they want to entertain the potential blight and hindrance to repairs and redevelopment now created by the grant of rights to an Operator.

Our clients have received offers for new Code agreements on rooftops of £50p.a. and Greenfield sites where consideration for a 10-year term has equated to a total payment of £36.89. At such levels, land owners and property owners are simply unlikely to be interested in entertaining or accommodating an Operator's proposal given the impact of the rights being imposed.

As well as consideration, an Operator will be obliged to pay compensation on the basis of any loss or damage that has been sustained or will be sustained by a person, as a result of the exercise of the Code right to which the order relates. In an imposed agreement, this can be awarded at the time or any time afterwards (albeit a contractual agreement may override this). Operators are seeking to avoid the compensation provisions of the Code by limiting liability in the agreements demanded.

Transitional Provisions

There will be a number of Landlords who have agreements which have expired since the Code was enacted and where rent is still being paid or which are still within the term of the lease. These agreements will be classified as 'subsisting agreements' and are subject to the Transitional Provisions in Schedule 2 of the new Code.

Almost all activity in the market, save for the roll out of the emergency services network, appears to relate to Operators seeking to reduce rents of existing sites. Operators use the threat of the Code in respect of such agreements but appear not to take account of the procedure for modifying or renewing existing agreements under the new Code. Any request to replace a subsisting agreement for a new Code agreement must be carefully considered.

Any existing agreements should be reviewed to ensure that Landlords are adequately protected against and are aware of what rights the Operators are entitled to under the Code.

Any new approach from an Operator must be carefully considered. The new Code means that any agreement will be difficult and lengthy to terminate. Operators are seeking rights, under threat of the Code, that impose a considerable burden on the Landlords and are offering minimal consideration / compensation for such rights.

More than ever, specialist advice should be sought early in proceedings as Operators are exercising Code Powers shortly after commencement of negotiations. Operators are, however, suggesting specialist advice is unnecessary, despite this now being a highly technical Compulsory Purchase scenario.

Impact of the Code

Following the introduction of the new Code, Operators withdrew from almost all ongoing negotiations seeking instead to renegotiate terms offered, even if a new lease had been on the cusp of completion. Operators are generally seeking to exploit the opportunity to potentially reduce the sums they pay to Landlords through new Code agreements even in situations where it would appear that the public benefit test may not be satisfied.

Since 28th December 2017 the market has been in a period of flux, as Landlords and Operators come to grips with the new Code. Very few deals are being done (and most of these with confidentiality clauses). Anecdotal evidence suggests that rents agreed in such deals are not far short of previous levels but meaningful analysis is not yet possible given the small volume of transactions.

Telecoms agreements are essentially overriding interests capable of binding successors in title, even where they have not been registered at the Land Registry. Given the effect of the Code on the ability to obtain possession when acquiring land, it is important in land transactions to carry out suitable due diligence to establish whether there are any telecoms rights affecting the land – whether there are leases for telecoms apparatus or rights to lay cables underground or through property.

NEW ROLL OUT

Whilst the market appears to have ground to a halt in light of the new legislation, we are aware of initiatives to try to increase geographic and population coverage.

The advent of 5G is expected to be late 2019 or early 2020 and as such industry experts have proclaimed that an additional 400,000 locations will be required to house equipment.

The current networks operate from c52,000 sites, so the number of additional sites required highlights the need for a plethora of new agreements. We envisage that 'street furniture' may be adapted to provide small cell solutions but there will be an overwhelming number of new sites required upon privately owned buildings and land. Even street furniture is not without its problems given the impact of the new Code on local authorities (which is often overlooked). How new agreements will be forged (either by force or by consensual agreement) will determine the speed at which such roll out will take place.

A new Emergency Services Network (ESN) will replace the existing 'blue light' services network operated by Airwave which was due to be terminated on 31st December 2019. ESN is being delivered by EE, with sites being acquired in the name of EE and the Home Office, the latter under the Extended Area Services (EAS) programme.

The three emergency services and other public safety users in the UK will have use of the network which will be based on 4G/LTE technology which will deliver secure and resilient voice communication alongside broadband data services.

In practice, the programme has slipped and the delivery of new sites has taken considerably longer than originally expected. Airwave's contract will now not finish before the end of 2019, with an extension to at least the end of 2024 now secured. We are aware that Airwave have been reluctant to engage in any lease renewal negotiations, with many agreements now holding over or due to lapse. Any contract extension may offer the opportunity to renegotiate such agreements.

Roll out of 5G may be problematical with its increased power and back-haul requirements. There are also concerns about the larger exclusion zones for public health required for such installations. It is likely that there will need to be specialist training for those outside of the industry who will work within the zones. Personal safety equipment may also be required.

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DECOMMISSIONING

Decommissioning can be at the request of the Landlord or the Operator.

Decommissioning by Operators can occur for a number of reasons, the topography of the land may have changed, buildings will have been developed and in some cases network consolidation will render some cell sites redundant.

Despite thousands of new sites being required, decommissioning of existing infrastructure will still take place. Once a cell site has been integrated into a network, the replacement of such a site becomes more difficult without the need to tweak the other cell sites in close proximity to ensure that a similar or better level of coverage is maintained. For this reason, decommissioning levels are somewhat low.

While the changes to the Code make it more difficult for a Landlord to require an Operator to remove its apparatus, we are finding many Landlords now actively considering removal given the stance taken by Operators.

Operators are seeking to leave some, if not all, of the apparatus in place because of the costs of decommissioning. It is important to consider the implications of how the site will be decommissioned in its entirety (inclusive of any electric or fibre option cables). Requirements will be governed by the terms of the agreement and the provisions of the Code.

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FIBRE OPTICS

The desire for Ultrafast fibre optic broadband brings about more challenges.

To date, Openreach, which has separated from BT in March 2017, has been operating much of the UK's fibre optic network. The main method of connection still relies on copper wires to deliver broadband from a cabinet into a property. When 5G is deployed, the requirement for super-fast broadband speeds will continue to grow and it is now the Government's initiative to deliver full fibre service across all of the UK by 2033.

Historically, BT and Openreach have had a monopoly over its ducts and poles network, however, this is set to change. In July 2018 Ofcom published a set of measures aimed at reducing the cost of full fibre broadband in order to incentivise other telecoms providers to invest in their own full fibre infrastructure. Some of these measures include enabling unrestricted access to Openreach ducts and poles and a duty on BT to make its infrastructure and underground tunnels available to rival broadband service providers. Such changes are likely to increase the use of land upon which the equipment is situated-to the detriment of the Landowner.

We understand that the Government is set to publish consultations on legislative changes to streamline wayleaves and fibre connections in new build houses; however, there are no new recommendations for existing and future wayleaves in rural locations. As such, Operators continue to insist on agreeing their own standard set of terms, which do not provide sufficient rights to the Landowner. It is therefore imperative that Landowners seek professional representation when seeking to negotiate a wayleave agreement.

Fibre Optics, BT Cables, Poles etc all fall under the remit of the Code. As such, Operators, particularly BT, generally seek to insist on their standard wayleave agreements. These standard agreements often make no allowance for consideration or professional fees where it is considered by the Operator to be in the Grantor's favour, and therefore may not reflect the circumstances. It is recommended that careful consideration is given to such terms prior to acceptance.

About us

Following the enactment of the new Code telecoms is now firmly in the domain of true specialists.

We have dedicated Teams based in both the Shrewsbury and Banchory offices, our employees have a wealth of experience in the telecoms industry. We are able to offer advice tailored to our client's needs based on an expert knowledge and understanding of the marketplace. We are able to maximise the opportunities that the industry will continue to offer, whilst never ignoring the primary use of the building or land in question or the need for improved digital connectivity.

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