



**FIRST-TIER TRIBUNAL  
PROPERTY CHAMBER  
(RESIDENTIAL PROPERTY)**

**Case Reference** : LON/00BK/OLR/2015/0913

**Property** : Flat 42, Eaton House, 39/40  
Upper Grosvenor Street, London  
W1 X 9PF

**Applicants** : Odense International Holdings SA  
(leaseholder)

**Representative** : BACI LLP (solicitors)

**Respondents** : Grosvenor West End Properties  
(first respondent and the  
reversioner) and Chesterfield  
Properties Limited (second  
respondent and intermediate  
leaseholder)

**Representative** : Mr M. Pryor of counsel instructed  
by Boodle Hatfield LLP solicitors  
with valuation evidence from Ms  
S. Samios of Gerald Eve chartered  
surveyors; Mr T. Jefferies of  
counsel instructed by SBP law,  
solicitors with valuation evidence  
from Mr K. Buchanan of Lamberts  
chartered surveyors

**Type of Application** : Application made under section  
48 of the Leasehold Reform,  
Housing and Urban Development  
Act 1993 ( ' the Act' ) to determine  
the amount payable by the  
applicant to the second respondent.

**Tribunal Members** : Professor James Driscoll (Judge) ,  
Duncan Jagger MIRCS

**Date of Hearing** : 8 and 9 September 2015

**Date of Decision** : 7 October 2015

## **DECISION**

## **Summary**

1. The proportion of the premium payable for the grant of a new lease to the immediate landlord under the existing underlease of the flat is the sum of £ 51,463
2. Our valuation is appended to this decision.

## **Preamble**

3. This matter concerns a claim for a new lease where the parties dispute an aspect of the valuation of the premium and additional amounts payable to the landlords. Issues relating to the premium and other amounts payable are set out in schedule 13 of the Act.
4. The claimant is Odense International Holdings SA which has an underlease of a flat in a block of 28 flats at Eaton House, London W1X 9PF. The first respondent is the head leaseholder of the block who is the 'competent landlord', for the purposes of the claim. The second respondent has a lease intermediate between the underlease and the head lease of the building and it is the immediate landlord of the flat underlease. The freeholder (which is not a party to these proceedings) is Grosvenor Properties Limited.
5. There are, therefore, three parties to the application.
6. At the valuation date (which the parties agree is 18 September 2014) the underlease had an unexpired term of 20.26 years, the intermediate lease an unexpired term of 20.1 years (that is just three days longer than the underlease term) and the competent landlord had an unexpired term of 169.51 years. (The 'competent landlord' is defined by section 40 of the Act as either the freehold owner, or an owner of a lease who has the capacity to grant a new lease 90 years longer than the claimant's current term. Given the shortness of the intermediate lease the claim for a new lease is made of the head leaseholder).
7. The claimant, who has a qualifying lease under the Act, has the right to be granted in substitution for the existing term, a new lease for a term 90 years longer than the current term paying a nominal rent. Thus once the new lease is granted no rent is payable and the reversion to the flat by the intermediate and head leases diminishes in value. As the nominal rent applies from the start of the new lease the immediate landlord loses a rental income that would have been paid during the remainder of the current term.
8. The valuation issues involved are straight - forward to state: the claimant leaseholder must pay the competent landlord a premium for the grant of the new lease. Where, as in this case, there are one or more intermediate leases, the claimant must also pay additional sums to the intermediate leaseholder. In both cases the sums payable are to reflect the loss in value once the new lease is granted plus a share of marriage value.
9. Another way of putting it is that the dispute is over how the sums payable are to be divided between the two superior landlords.

## **The claim and the proceedings**

10. A claim notice was given on or about 17 September 2014. An amount of £ 9 ,450 was proposed for the intermediate lease. In a counter-notice given on or about 25 November 2014 an amount of £ 850 was proposed for the intermediate lease.

11. The three parties have agreed on almost all of the elements of the claim. However, there is a difference of opinion between the first and the second respondents as to how much should be paid by the claimant to the second respondent. By the date of the hearing, the head leaseholder contends that the sum of £ 1 ,800 (out of a total premium of £ 1 ,111,550) is payable, but the intermediate leaseholder considers that the larger sum of £6 5,418 should be paid (out of a total premium of £ 1 ,217,887). It will be recalled that at the valuation date the immediate lease had an unexpired term just three days longer than the underlease.

12. Under schedule 13 to the Act (Part II) the premium payable is the aggregate of (a) the diminution in value of the landlord' s interest in the flat and (b) the landlord' s share of any marriage value (and in certain cases, but not this one, additional compensation).

13. The diminution in value is the difference in value between the landlord' s interest in the flat before and after the new lease has been granted.

14. Marriage value is payable where the current lease has an unexpired term of less than 80 years. It is divided equally between the landlord and the leaseholder.

15. Additional amounts are payable to any intermediate leaseholder under Part III of schedule 13 on the basis of its diminution in value before and after the grant of the new lease (and in certain cases, but not this one, additional compensation).

16. Those advising the parties agree that the value of the remaining term of the intermediate lease is nil and that the capitalised value of the ground rent (which will be lost to the intermediate leaseholder once the new lease is granted) is the sum of £ 801. Given the shortness of the intermediate lease this is hardly surprising. Approaching the valuation exercise on the basis of what a hypothetical purchaser would pay, this modest sum is all that would be paid.

17. However, the underlease has provisions that apply during the last seven years of that lease which forbid the assignment or underletting of the flat. How would this influence the hypothetical purchaser? If it makes the investment in the flat lease less attractive would the hypothetical purchaser pay a premium to the landlord to agree to a variation of the lease so as to remove the restrictions on during the last seven years of the lease? And if the answer to this question is in the affirmative, what is the correct way of valuing this hypothetical premium?

18. Thus the disagreement lies in what value (if any) can be attributed to the fact that during the last seven years of the underlease there is an absolute

covenant against assignment or subletting. What would a hypothetical purchaser of the remainder of the term pay for a variation of the lease to delete these clauses? Without such clauses the under leaseholder could sublet at a market rent or sell the remainder of the lease free of the current restrictions. It is this potential payment that is at the heart of this dispute.

19. The relevant restrictions in the lease may be summarised in the following way. First, under clause 2(xxxvi) and the fourth schedule there is a user covenant by the leaseholder ' . . . *to use and occupy the flat as a private dwelling house for the sole occupation of the lessee and his/her family and servants and in particular not to carry on any trade or profession therein* ... ' .

20. Second, there is the right to assign or to sublet the whole of the flat subject to the landlord's prior written consent (clause 2(x) of the lease). This applies during that part of the lease term preceding the last seven years.

21. Third, there is an absolute prohibition against assigning or subletting part of the flat (clause 2 (viii) of the lease).

21. Fourth, during the last seven years there is no right to assign, transfer, underlet or part with or share with possession (clause 2 (ix) of the lease). Should the leaseholder wish to, he or she can offer to surrender the remaining term at no consideration to the landlord.

22. To summarise, the dispute is over how to value the flat before and after the new lease is granted. The valuers and counsel quite correctly focused on the last seven years of the lease when the absolute restrictions on subletting and assignment come into play.

## **Hearing of the application**

23. An application was made under section 48 of the Act to the tribunal on 15 May 2015. Standard directions were given on 1 June 2015 . It was agreed between the parties that Boodle Hatfield LLP, the solicitors for the first respondent, would produce the bundle for the hearing. They instructed Mr Prior of counsel for the hearing and he called Ms Samios of Gerald Eve LLP to give valuation evidence.

24. As there is a coincidence of interest between the claimant and the first respondent no valuation evidence was produced on behalf of the claimant who was content for the hearing to proceed on the basis of the valuation evidence proffered by the first respondent's valuer.

25. Mr Pryor prepared a written statement of his submissions. He considers that the claimant leaseholder could circumvent the assignment restrictions by selling its shares either before or during the final seven years of the lease. In his opinion, officers or shareholders of the claimant company could themselves satisfy the user provisions in the lease. He elaborated on these submissions during the hearing which lasted two days. (The parties agreed with the tribunal that an inspection of the premises was unnecessary).

26. The valuers signed a statement of the facts and the issues that are agreed. These are referred to in their respective reports and they do not need to be

repeated in full in this decision. As noted above the valuation date is agreed to be 18 September 2014.

27. Mr Jefferies of counsel appeared on behalf of the second respondent. He was instructed by SBP Law, solicitors. He called a Mr C. Knighton a director of second respondent to give evidence about other transactions in the block. Mr Buchanan was called to give valuation evidence.

28. A lengthy written set of submissions was prepared for the tribunal by Mr Jeffreys. He argues that the claimant as a corporate entity cannot itself occupy the flat. If it continues to hold the lease it would have to take steps to assign to sublet to an individual for exactly seven years. He also submits that the claimant company could not circumvent the restrictions which apply during the last seven years of the lease by selling the shares in the company. Mr Jefferies expanded on these submissions at the hearing.

29. It was agreed that the first respondent would open the case. Mr Pryor called Ms Samios to give her evidence on valuation and she spoke to her report which is dated 28 August 2015 (to which she made a few minor changes). She also answered questions in cross-examination from Mr Jeffreys and from the tribunal. She was examined by Mr Prior. Her report refers to a decision of this tribunal on issues similar to those in this application (Flat 43, Eaton House, 39/40 Upper Grosvenor Street, (case number LON/OOBK/OLR/2011/0908) which was decided on 27 January 2012).

30. She is of the opinion that this valuation should be on a term of 3.5 years on the assumption that a diligent investor would have a tenant contracted to take up occupation at the commencement of that part of the term. Based on this term a net yield approach was preferred based upon *Vale Court* (that is the decision in *Carey Morgan v Sloane Stanley Estate* [2012] EWCA Civ 1181). In other words the valuation should be based on a net rental yield as the relevant term is less than five years.

31. As to the deferment rate she considers that the 6% rate should be used (instead of the usual 5% rate promulgated in *Sportelli v Cadogan Estate* [2008] 1 WLR 141).

32. Her evidence is that the restrictions over assignment and subletting during the last seven years of the current underlease would not be considered by a potential purchaser as onerous. This is because of two factors; first, a prudent purchaser or leaseholder would ensure that the flat was occupied long-term before the last seven years of the lease arises; second, her understanding of the legal position is that a leaseholder could in fact sublet or assign during the last seven years.

33. Ms Samios provided the tribunal with an alternative valuation based upon the assumption that the intermediate landlord's legal position is correct.

34. Mr Jefferies opened the case for the intermediate landlord. A Mr Knighton was called to give evidence and he spoke to his statement which is dated 7 September 2015 to which he attached various items relating to the grants of various consents. He was cross-examined by Mr Pryor and he answered questions posed by the tribunal. Mr Knighton told us that he has

been a director of the intermediate landlord for 'very many years', that he has managed the block and that he has dealt with many applications for the grant of licences. He spoke in support of an analysis of transactions in the subject premises which has been prepared.

35. Mr Knighton told us that when licences to assign are considered one of the conditions usually imposed is one forbidding a leaseholder which is a corporation from assigning its shares on or after the last seven years of the lease starts. Attached to his written statement are copies of emails passing between solicitors and copies of the standard form of a licence to assign. Unfortunately, it has not been possible to locate a copy of the document consenting to the assignment in this case.

36. Mr Jefferies then called Mr Buchanan to give his evidence on valuation. He spoke to his report which is dated 2 September 2015. Mr Buchanan made a few minor changes to the report. He was cross-examined by Mr Pryor, he answered questions posed by the tribunal and he was re-examined by Mr Jefferies.

37. His report starts by summarising the legal position so far as assignment and subletting is concerned. His position is that these restrictions which apply during the last seven years would make the property unattractive with the result that a prospective purchaser would seek a variation of the lease to rid it of these restrictions for which the intermediate landlord would expect to receive a premium.

38. As to how to value such a premium he considers the value of the seven year term held the claimant and then adjusts this to reflect the inability to assign or to sublet during the last seven years. He concludes that a 'blended approach' should be adopted in the valuation. By this he means taking an average of the published graphs of relativity and also a net rental approach. This is justified, he argues, as the seven year term is between the five year principle used in what is commonly known as the Vale Court decision (*Carey Morgan v Sloane Stanley Estate* [2012] EWCA Civ 1181) for leases with unexpired terms of less than five years. In such cases one should examine the net market rental income in valuing the freehold value. An alternative for leases between 10 and 20 years is the approach taken in *Cadogan Square Properties v Cadogan* [2010] UKHT 427 where a conventional valuation approach based on deferring the freehold value should be adopted.

39. Mr Buchanan then takes the average of the figure derived from the relativity analysis (which he would defer for the standard generic *Sportelli* rate of 5%) and the net rental yield approach. This produced an average figure of £225,000. He discounts this value to reflect the restrictions in the lease and he concludes that this difference in value would be divided between the claimant and the intermediate leaseholder. He also refers to the analysis of settlements in Eaton House in support of his figures.

40. We turn to the schedule of Eaton House transactions. During the hearing we were handed an analysis of transactions in Eaton House since 2010. This provided information on the grant of new leases and the sums paid. The schedule provided evidence of seven transactions where compensation was paid to the intermediate landlord by under-lessees who have sought to have the clause preventing alienation during the last seven

years of the term varied either by issuing a notice under Section 42 of the Act for an extended lease or by direct negotiations for a deed of variation. The schedule is self-explanatory and ranged from £16,810 for Flat 43, being the LVT decision through to £55,000 for flat 1.

## Reasons for our decisions

41. We deal first with the legal issues. Inevitably the two competing set of legal submissions had a huge influence on the valuer's approaches to the valuation. In our view the scope of the leaseholder covenants on user and alienation are not difficult to interpret. Before the last seven years of the lease the leaseholder may occupy the flat provided he or she complies with the conditions in the fourth schedule to the lease. If the leaseholder choses to sublet instead of residing in the flat, they may do so with the landlord's consent, which, under the terms of the lease, may be given with conditions.

42. This type of user clause is, in our experience very common in flat leases. It restricts living in the flat to one family and forbids any non-residential use. For good reason landlords will want to have a considerable say on how the flats are occupied and by whom.

43. What is the position where the current leaseholder is a company? Mr Jefferies in both his written submissions and in his submissions at the hearing cites the case of *Falgor Commercial SA v Alsbahia Incorporated* [1986] 1EGLR 41 concerning a lease containing a similar covenant. In that case the Court of Appeal dismissed an appeal against the grant of an injunction against a company leaseholder of flats which had been letting the flats for payment. It dismissed the submission that that company was using the flats itself, as they were used by others (that is the persons to whom it let). The Court stated that it is '...impossible to make sense of that covenant, assuming the lessee to be a company' (at 43L).

44. Mr Pryor countered by noting that the Court also stated that 'It is not a case of a company using property for its directors its staff or its own guests' (at 42J) to support his submission that a company which lets a flat in this way does so in conformity with the user covenant.

45. We reject Mr Pryor's submission that a company can occupy through its directors or employees. As a matter of common sense a company cannot 'live' in a residential property. There can only be occupation by an individual. Where the leaseholder is an individual there can be lawful occupation by the leaseholder and members of their family. But where the leaseholder is a company we do not accept that the it can reside in the property in any meaningful sense.

46. In this case the company has the right to sublet provided it has the consent of the landlord. But once the lease has less than seven years unexpired the leaseholder cannot sublet at all.

47. Similarly the leaseholder can assign the lease until there are seven years unexpired with the landlord's consent but during the last seven years the leaseholder cannot assign at all.

48. To summarise, under the terms of this lease the leaseholder can sublet



or assign until the last seven years after which there can be no assignment or subletting at all. During this last period of the lease the leaseholder can offer to surrender the lease at no consideration but this is clearly not commercially attractive.

49. We conclude that a leaseholder with a short lease may try to sublet for a full seven year period before the last seven years (subject to the landlord consenting). However, we do not think that finding a tenant who would take a seven year assured shorthold tenancy would be very practicable. The hypothetical purchaser, in our opinion, would negotiate a variation of the lease to allow him or her to sublet or to assign with the consent of the landlord. We have no doubt that the landlord would expect a substantial premium for agreeing to this.

50. We also conclude that the possibility of a corporate leaseholder selling its shares is a way of avoiding the leasing restrictions. This is because the new owner of the shares in the company would also be bound by the terms of the lease including the final seven year restrictions.

51. As to the possibility that the consent to assignment was granted with a restriction on selling shares, Mr Jefferies admitted that the failure to produce the consent was unfortunate. However, we accept the evidence of Mr Knighton who impressed us as a well-briefed and a fair witness. We conclude that on the balance of probabilities that such a consent was given. However, we reiterate our conclusion that if the shares were sold, the new owner would also be subject to all of the terms of the lease.

52. This brings us finally to the valuation itself. Although the exercise of determining what a purchaser is in part a hypothetical one, in this case there is abundant transactional evidence of what leaseholders will pay for the grant of a new lease for the removal of the restrictions in the last seven years of the lease. We prefer Mr Buchanan's evidence to that of Ms Samios on this central issue.

53. Ms Samios told us that we should assume that an investor would arrange for the flat to be let for at least three years during the last seven. As such a letting would be granted before the start of the final seven year period it could be granted with the consent of the landlord.

54. We are far from convinced by this part of her evidence. Such a letting would have to be for a fixed term of at least three years. In our experience letting a property for a fixed term of this duration is far from common. Moreover, the leaseholder would have to obtain the consent of the landlord to the subletting.

55. Why would a landlord agree to such a sublet just before the seven year restrictions would start to apply? After all, if the landlord refused, the leaseholder would have no rights to sublet and could not assign once the final seven year starts. It could offer to surrender at no consideration but this clearly commercially unattractive. It is possible that a periodic tenancy could be granted. This too would require the landlord's consent and there is no guarantee that a periodic tenant would stay longer than one year. On balance, we agree with Mr Buchanan that the better approach is to value the whole of the seven year term.

56. This brings us to the approach of how to value the seven year part of the term. We conclude that this should be valued on the basis of the *Cadogan Square* approach rather than the *Vale Court* analysis. This is principally because the term under examination is for more than five years. We were not convinced by Mr Samios' evidence on this point when she submits that a rental approach should apply as the first two to three years of the last seven years amounts to valuing a term of less than five years.

57. We are also attracted to the approach taken by Mr Buchanan who has adopted the approach in *Cadogan Square* with blended approach based on net market rental yields.

58. The model adopted by Mr Buchanan is best suited to the approach taken by the tribunal in calculating the relativity of 22.5%. This was based upon an average of PCL RICS graphs discounting the W.Ellis graph. The tribunal took a dual valuation method with a 30% tax allowance.

59. The tribunal adopted a deferment rate of 5% based upon the conventional Sportelli approach as there was no compelling evidence provided to justify a departure from this rate generic deferment rate.

60. We preferred Mr Buchanan's evidence in connection with the assessment of an appropriate discount to reflect the inability to sublet and assign being 50%.

61. The tribunal considers that a discount of 40% is appropriate to access the likelihood of a tenant approaching the intermediate landlord in this matter.

62. Finally we must refer to the submission made on behalf of the respondents that we should follow the previous decision of this tribunal in *Flat 43, Eaton House, 39/40 Upper Grosvenor Street* [2012]. As we pointed out during the hearing previous decisions of this tribunal are not binding precedents. Even though that case concerned a property in the subject block of flats we have reached different conclusions to the other tribunal. Unlike the tribunal in the earlier case, where the intermediate landlord was not legally represented, we had the benefit of full legal submissions from all sides. As we have sought to demonstrate in this decision the key to the determination is to establish correct legal basis for the valuation.

63. In summary, we determine that the amount payable for the intermediate lease is the sum of £ 51,463 At the invitation of the parties we have prepared a full valuation which is appended to this decision.

**James Driscoll and Duncan Jagger**

7

**October,**

**2015**

**Flat 42, Eaton House, 39-40 Upper Grosvenor Street, London W1. APPENDIX 1**  
**The Tribunal's Valuation**  
**In accordance with Leasehold Reform, Housing and Urban Development Act 1993 (As Amended) Schedule 13**  
**LON/00BK/OLR/2015/0913**

**Components**

Valuation date:	18 <sup>th</sup> September 2014
Yield ground rent:	7.5%
Deferment rate:	5%
Freehold value:	£2,434,500
Relativity	80.55%
Unexpired term of intermediate lease	20.27 years

**(A) Value of Intermediate Lease Interest**

Agreed by both parties @ £801

**(B) Value to intermediate landlord of restrictions in lease during the last seven years**

(i) Gross rent per annum	£64,350	
Net rent: less 25%	<u>£48,262</u>	
YP 7 years @ 1.98%, 2.25%, 30% tax	£120,234	
(ii) Agreed freehold value	£2,434,500	
Relativity 22%	<u>£547,762</u>	
Deferred 13.26 years @ 5% 0.5262	£288,232	
Average of the two sums:	£204,233	
Assessment of discount appropriate to reflect inability to sublet and assign: 50%	£102,166	
Discount to assess the likelihood of tenant approaching intermediate leaseholder :40%		<u>£40,846</u>
		<b>£41,647</b>

**(C) Valuation of Head Lease held by GWEP**

Existing		
Value of freehold value £2,434,500@ 99%	£2,410,155	
Deferred 20.27 years at 5% 0.3720		£896,578
Proposed		
Freehold value	£2,434,500	
Agreed relativity @ 80.55%	£1,960,990	
Deferred 110.26 years	0.003	<u>£5883</u>
		<b>£890,695</b>
Total diminution in the value of GWEP's interest		<b>£932,342</b>

**(D)Marriage Value**

Value of proposed interest				
GWEP's interest		£5,883		
Chesterfield Properties Ltd		£2,385,800	£2,391,683	
Value of existing interest				
GWEP's		£896,578		
Chesterfield Properties Ltd		£40,846		
Tenants @ 42.36%	£1,055,599			
Less value of onerous lease	<u>£40,846</u>	<u>£1,014,753</u>	<u>£1,952,177</u>	£439,506
Landlords share of marriage value @ 50%				£219,753
Premium payable				<b>£1,152,095</b>

**(Apportionment)****To the intermediate leaseholder**

Diminution in value of interest				£41,647
Share of marriage value @ 4.467%				<u>£9816</u>
				<b>£51,463</b>
To GWEP				<b>£1,100,632</b>