4247

FIRST-TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case reference	:	**LON/00BK/OLR/2015/1043**
Property	:	**Basement Flat B & Vaults, 34 Rutland Gate, London SW7 1PD**
Applicant	:	**Rutland Gate 34B Limited (tenant)**
Representative	:	**Mr Piers Harrison, counsel, instructed by Pennington Manches**
Respondent	:	**Ellward Estates Limited (landlord)**
Representative	:	**Mr Alan Tunkel, counsel, instructed by Blandfords Law**
Type of application	:	**Section 48 of the Leasehold Reform, Housing and Urban Development Act 1993**
Tribunal members	:	**Judge Timothy Powell** **Mr Ian Holdsworth FRICS**
Date of determination and venue	:	**13 January 2016 at 10 Alfred Place, London WC1E 7LR**
Date of decision	:	**21 January 2016**
Corrected & reissued	:	**3 February 2016**

DECISION

<u>Summary of the tribunal's decisions</u>

(1) The tribunal determines that both clause 6 and amended clause 4 in the 2006 deed of variation should be retained in the new, extended lease.

(2) The tribunal also determines that the payment due to the landlord under clause 6 constitutes "rent" within the meaning of section 56 of the Act, and it should therefore be commuted to a peppercorn.

(3) Accordingly, the tribunal accedes to the submission at paragraph 31 of Mr Tunkel's skeleton argument and directs that the new lease should omit clause 6 of the 2006 deed of variation, but should retain the amended clause 4 set out in its schedule.

(4) The premium payable is **£196,390**.

Background

1. This is an application made by the applicant leaseholder pursuant to section 48 of the Leasehold Reform, Housing and Urban Development Act 1993 ("the Act") for a determination of the terms of acquisition and the premium to be paid for the grant of a new lease of Basement Flat B & Vaults, 34 Rutland Gate, London SW7 1PD (the "property").

2. By a notice of a claim dated 12 January 2015, served pursuant to section 42 of the Act, the applicant exercised the right for the grant of a new lease in respect of the subject property. At the time, the applicant held the existing lease to the flat granted on 10 January 1975 for a term of 99 years from 24 June 1971. The applicant also held the existing lease to the vaults granted on 12 April 1976, also for a term of 99 years from 24 June 1971. The applicant proposed to pay a premium of £90,178 for the new lease.

3. On 20 March 2015, the respondent freeholder served a counter-notice admitting the validity of the claim and counter-proposed a premium of £301,683 for the grant of a new lease.

4. On 8 June 2015, the applicant applied to the tribunal for a determination of the premium.

The issues

Matters agreed

5. The following matters were agreed:

   (a) The subject property is a self-contained flat on the lower ground floor within a converted Georgian terraced house constructed in about 1857 and containing seven flats of similar kinds;

   (b) The gross internal floor area is 61.69 square metres, which equates to 664 square feet. The vault is 14.31 square metres or 154 square feet;

   (c) The valuation date: 12 January 2015;

   (d) Unexpired term: 55.48 years;

   (e) Ground rent: currently £170 pa rising to £255 pa in 2037;

   (f) Long leasehold (unimproved) value: 99% of the freehold (unimproved) value;

(g) Capitalisation of ground rent: 6% per annum;

(h) Deferment rate: 5%;

(i) Agreed net rental value of the flat and vaults under clause 6 of the 2006 deed of variation: £350 per week; and

(j) Freehold vacant possession value: £850,000.

Matters not agreed

6. The following matters were not agreed:

(a) The basis of valuation (dependent on the new lease terms);

(b) Relativity to existing lease;

(c) Relativity to proposed lease; and

(d) The premium payable.

7. At the date of the hearing, the issue between the parties had resolved to whether and, if so, to what extent the new lease should retain two clauses in a 2006 deed of variation of the original 1975 lease; including whether an original version of one of those clauses should be reinstated. The premium was also at issue.

8. There are two original leases. The lease of the flat is dated 10 January 1975 and was amended by deeds of variation dated 5 January 1995 and 20 January 2006, respectively. The original lease was for 99 years from 24 June 1971. In addition, the tenant holds a lease of the vaults dated 12 April 1976, also for a term of 99 years from 24 June 1971.

9. The lease of the vaults is on the same terms and subject to the same covenants as the lease of the flat, save that the vaults must be used only for storage of property belonging to the tenant in connection with their use and occupation of the flat; and the lease of the vaults must not be assigned, sublet or transferred unless contemporaneously with an assignment, subletting on identical terms or transferred of the lease to the flat.

10. The lease to the flat contained a clause 4 in the following original terms:

> "The tenants shall not assign demise underlet or otherwise part with possession of the flat or any part thereof for any part of the said term PROVIDED ALWAYS that the tenants may with the lessor's written consent underlet the entirety of the flat on a furnished tenancy for which the agreement shall be in writing in a single occupation only to a respectable and responsible under-tenant for a specified period not exceeding six consecutive months in every calendar year during which the said term shall subsist".

11. For convenience, this term of the original lease will be referred to below as "the original clause 4". As will be seen, it constitutes an absolute prohibition on underletting for a period of more than six consecutive months in any calendar year. This is a very unusual clause, which the tenant's valuer described in his report as being "a restrictive covenant, which is rarely experienced." It is also the first time that this tribunal has seen such a clause.

12. The 1995 deed of variation is not relevant to the present dispute. Although its terms fall to be incorporated in the new lease, it will not be referred to further.

13. By a deed of variation dated 20 January 2006, the original clause 4 of the lease was varied by the new terms set out in the schedule to the deed of variation, which were substituted for the original clause 4.

14. The consideration for the variation is dealt with in clauses 5 and 6 of the deed of variation. Clause 5 reads:

> "5. CONSIDERATION
>
> In consideration of the Lease being varied as herein provided the Tenant hereby covenants to pay the Landlord the additional rent herein provided which shall be recoverable from the Tenant in the same manner as rent payable under the lease".

15. That additional rent is set out in clause 6 of the deed of variation, as follows:

> "6. ADDITIONAL RENT
>
> On completion the sum of £1,366 will be paid to the Landlord in respect of net additional rent due and once a year no later than 1 February the Tenant shall pay to the Landlord such sum as represents sixty per centum of the net rent receivable by the Tenant for any period of underletting exceeding six months during the twelve months from 1st January to 31st December of the preceding year. The net rent shall be calculated by deduction from the rent receivable for that period all letting agents' fees, and also the utility charges including council tax, water rates, gas and electricity charges if paid by the Tenant in respect of the same period and to be taken into account for this calculation for which receipted invoices are presented to the Landlord. If utility charges are not payable by the Tenant then net rent shall be calculated after deduction of letting agents' fees of no more than ten per centum (plus VAT) of the rent receivable from subletting by the Tenant for the said period in excess of six months also evidenced by receipted invoices".

16. For convenience, these two clauses will be referred to below as "clause 5" and "clause 6", respectively.

17. The schedule of the deed of variation contains the new terms, namely the new clause 4 of the lease:

> "(1) Clause 4 of the Lease:
>
> The tenants shall not assign demise underlet or otherwise part with possession of the flat or any part thereof for any part of the said term provided always that the tenants may with the lessor's prior written consent (such consent not to be unreasonably withheld) underlet the entirety of the flat on an assured shorthold tenancy for which the agreement shall be in writing in a single occupation only to a respectable and responsible undertenant".

18. For convenience, this clause will be referred to below as the "amended clause 4".

19. Apart from modernisation of amended clause 4 to make reference to an assured shorthold tenancy and to say the lessor's consent must not be unreasonably withheld, the important difference between amended clause 4 and the original clause 4 is that amended clause 4 does not include the following final words: *"for a specified period not exceeding six consecutive months in every calendar year during which the said term shall subsist"*. From this, it will be seen that amended clause 4 is no longer an absolute prohibition on underletting, insofar as any underletting may exceed 6 months.

20. The parties having failed to reach agreement on the terms of the new lease, the matter was referred to the tribunal for determination. In order to reflect the possible outcomes of the tribunal hearing, the parties' valuers prepared three separate valuations, to reflect all foreseen possibilities, as set out in the following comparison table:

No.	BASIS	GEORGE POPE (for tenant)	GARY FRENCH (for landlord)
1.	The new lease retains clause 6 of the 2006 Deed and the amended clause 4, as set out in its Schedule, i.e. same as existing lease terms. Landlord's primary submission.	£105,919	£120,797
2.	The new lease omits clause 6 of the 2006 Deed and the amended clause 4 set out in its Schedule and reinstates clause 4 of the 1975 Lease. Landlord's offer.	£112,040	£129,538
3.	The new lease omits clause 6 of the 2006 Deed but retains the amended clause 4 set out in its Schedule. Tenant's claim.	£175,150	£224,000

The hearing

21. The hearing took place on 13 January 2016. The applicant tenant was represented by Mr Piers Harrison of counsel, instructed by Penningtons Manches LLP. The respondent landlord was represented by Mr Alan Tunkel of counsel, instructed by Blandfords Law LLP. In addition to Mr Harrison and Mr Tunkel, also present were Mr David Masters, solicitor, from Penningtons, and Ms Juliet Waller, solicitor, from Blandfords, together with Mr Howard Michaels, director of the respondent freeholder company.

22. The applicant relied upon the expert evidence of Mr George Pope FRICS, and his valuation report dated 30 December 2015; and the respondent relied upon the expert evidence of Mr Gary French FRICS and his valuation report of 28 December 2015.

23. At the commencement of the hearing number of documents were handed up to the tribunal members, namely: a skeleton argument and bundle of authorities on behalf of the applicant, a witness statement of Mr Howard Michaels, "Tab 21" being a bundle of correspondence and draft leases, added to the applicant's bundle, and a comparison table of the parties' experts' valuation figures (reproduced above).

The tribunal's determination

24. The tribunal determines that both clause 6 and amended clause 4 in the 2006 deed of variation should be retained in the new, extended lease.

25. The tribunal also determines that the payment due to the landlord under clause 6 constitutes "rent" within the meaning of section 56 of the Act, and it should therefore be commuted to a peppercorn.

26. Accordingly, the tribunal accedes to the submission at paragraph 31 of Mr Tunkel's skeleton argument and directs that the new lease should omit clause 6 of the 2006 deed of variation, but should retain the amended clause 4 set out in its schedule.

27. The premium payable is **£196,390**.

Reasons for the tribunal's determination

The counter-notice issue

28. The applicant's primary contention was that the respondent had already accepted the applicant's proposal to remove clause 6 from the new lease; and it was too late now for the respondent to seek to re-include it.

29. The notice of claim dated 12 January 2015 stated at paragraph 7:

"7. The new lease is to be granted on the same terms as the existing lease:-

(a) save for the extension to the term of 90 years in addition to the term remaining;

(b) the payment of the rent at a peppercorn (if demanded); and

(c) the removal of the additional rent introduced by the second deed of variation in 2006; and

(d) an amendment to the tenant's covenants affecting alterations, so that the landlord is allowed to make alterations to the flat, subject to obtaining the landlord's consent which should not be unreasonably withheld or delayed."

30. The respondent's counter-notice dated 20 March 2015 replied as follows:

"2. We accept the following proposals contained in your notice:

The terms that you propose in paragraph 7 (a) and (b) of the notice dated 12 January 2015.

The terms that you propose in paragraph (c) of the notice dated 12 January 2015, subject to clause 4 of the lease dated 10 January 1975 being reinstated.

3. We do not accept the following proposals contained in the notice dated 12 January 2015:

The premium in paragraph 5 of £90,178.

In paragraph 7 (d), an amendment to the tenant's covenants affecting alterations.

4. In respect to each proposal which we do not accept, our counter-proposals are as follows:

The premium in paragraph 5 is to be the sum of £301,683.

The tenant's covenants in relation to the alterations to the property are to remain as in the leases.

5. The new leases' terms should contain such modifications and amendments as we are entitled to under and/or as may be necessary to give effect to the requirements of Chapter II of Part I of the Act and without prejudice to the generality of the above such further reasonable modifications to be agreed."

31. The applicant submitted that the terms of paragraph 2 of the counter-notice meant that the respondent accepted the proposal in paragraph (c) of the notice of claim - i.e. the removal of clause 6 - so that the only matter for discussion between the parties and, therefore, the only dispute before the tribunal, was whether amended clause 4 or original clause 4 should go into the new lease. Mr Harrison relied on the wording of the sentence, its position in paragraph 2 which begins "we

accept the following proposals" and the subsequent conduct of the parties.

32. With regard to the contents of a counter-notice, Mr Harrison referred to section 45 of the Act, which, so far as material states:

> "45 (3) if the Counter-notice complies with the requirements set out in subsection (2) (a) [i.e. it admits the tenant's right to acquire a new lease] it must in addition -
>
> (a) state which (if any) of the proposals contained in the tenant's notice are accepted by the landlord and which (if any) of those proposals are not so accepted; and
>
> (b) specify, in relation to each proposal which is not accepted, the landlord's counter-proposal."

33. He also relied on dicta in the Court of Appeal decision in *Burman v Mount Cook Land Ltd* [2002] Ch 256, quoted at paragraph 21 of his skeleton argument, inter alia, that "The proper working of the statutory scheme requires that the tenant is left in no doubt as to what the landlord admits, how far the tenant's proposals are accepted, and what (if any) are the landlord's counter-proposals."

34. With regard to the parties' subsequent conduct, Mr Harrison referred to events occurring after the counter-notice dated 20 March 2015. Negotiations had taken place between the parties but, in default of agreement, an application had been made to the tribunal on 8 June 2015 and the tribunal's directions had been issued on 17 September 2015. The second of those directions required the landlord to submit a draft lease to the tenant for approval by 1st October 2015.

35. The landlord complied with that direction by email dated 22 September 2015 enclosing a draft lease. The email stated that the only outstanding point "... is the restriction on subletting as to which my instructions remain that my client would prefer that the provision (now in square brackets) be brought forward from the original lease, rather than from the deed of variation, the premium calculated accordingly." A copy of the September travelling draft lease appears behind tab 20 of the applicant's hearing bundle. The proposed clause 4 appears at page 229 of the bundle and repeats the terms of clause 4 of the original lease, with minor agreed changes.

36. The dispute in the travelling draft related to the final words of clause 4 "*for a specified period not exceeding six consecutive months in every calendar year during which the said term shall subsist*", which words appeared in the original clause 4, but not the amended clause 4 in the 2006 deed of variation.

37. It was not until 22 December 2015 that the landlord sought to change the wording of clause 4 (at page 189) with an amalgam of amended clause 4 and clause 6 from the 2006 deed of variation.

38. Mr Harrison said that until that point it had been perfectly clear what the parties' respective positions were: clause 6 was not to be included (because it had been accepted by the respondent); and the only issue was whether the wording of clause 4 should be that of the original 1975 lease or that of the 2006 deed of variation. Contrary to what had been stated in the counter-notice, the landlord "has now spun away" from that position and was now seeking to introduce terms that it had not asked for in the counter-notice.

39. Later, Mr Harrison proposed this test: what would you expect to see if the parties were asked to prepare a contract based on the counter-notice as it was? He suggested that that you would expect to see the clause 4 at page 229 of the hearing bundle; and no-one was suggesting at the time the clause 6 should be included as part of the terms of the new lease. He argued that the landlord was stuck with the proposals made in the counter-notice and was not now able to change its position.

40. For the landlord, Mr Tunkel rejected any suggestion that the counter-notice had failed to deal with the tenant's proposals or to state the landlord's counter-proposals. The counter-notice was perfectly clear: the landlord was saying to the tenant, in effect, "Let's tear up the deed of variation and go back to the wording of the original lease." The full wording of clause 4 of the travelling draft lease (at page 229) represented the landlord's offer in the counter-notice, which, Mr Tunkel said, the landlord would be entirely happy with, should the tenant accept it. However, as the tenant had not accepted the landlord's counter-proposal, the default position was as stated in paragraph 5 of the counter-notice, namely that the matter would be left to the tribunal to decide under its jurisdiction to resolve disputes as to the terms of acquisition under section 48 of the Act.

41. Having considered the documents, weighed up the respective submissions, reviewed the statutory provisions and read the authorities, the tribunal is satisfied that the counter-notice is not only valid and compliant with section 45 of the Act, but that the respondent landlord has not accepted unequivocally the tenant's proposal in paragraph (c) of the notice of claim.

42. Although there is no prescribed form, as a matter of common practice, it is usual to find that a counter-notice is structured in the following way: paragraph 2 sets out those tenant's proposals which the landlord accepts, paragraph 3 sets out those proposals that the landlord does not accept, and paragraph 4 sets out the landlord's counter-proposals.

43. While the common format has not been followed strictly in the present case, the tribunal is satisfied that on a true construction of the counter-notice it does comply with the requirements of section 45, i.e. to state which of the tenant's proposals are accepted and which are not; and to specify the landlord's counter-proposals. Such an approach is supported by the dicta of Chadwick LJ in *Burman v Mount Cook Land*

Ltd where, at the bottom of paragraph 29 of the judgement, he states "I accept, of course, that it would be enough if, upon a true construction of the notice, it could be found to contain such a statement or statements."

44. One of the tests is whether the counter-notice makes an offer that is capable of being understood by the tenant and capable of being accepted by him. This follows from a more recent Court of Appeal decision in *Bolton v Godwin-Austen and others* [2014] EWCA Civ 27, where McCombe LJ, giving the leading judgement, stated at paragraph 52: "In my judgement, however, if the counter proposals could not be converted into agreement of 'terms of acquisition' by acceptance, then difficulties arise in saying that the counter-notices complied with the requirements of section 45." He went on in paragraph 54 to say: "I do not see how a counter-notice whose proposals cannot be accepted in the terms expressed in it can be a valid notice within the criteria laid down by Chadwick LJ in the *Burman's* case in the passages which I have just quoted."

45. Furthermore, in his judgement in *Bolton*, Sir Stanley Burnton, at paragraph 60, said "I do not think that the court should be astute to hold that what was clearly intended to be a valid counter-notice was invalid." This was particularly so where any modifications that the landlord requires are "objectively ascertainable", as they were in that case; and where the counter-notice in that case contained a landlord's counter-proposal, which almost exactly mirrored the terms of paragraph 5 of the counter-notice in the present case.

46. It may have been better for the respondent not to have put its response to the tenant's paragraph (c) proposal in paragraph 2 of the counter-notice, but rather in paragraph 4 as a counter-proposal; and, equally, it may have been better for the respondent to have said that the paragraph (c) proposal was not accepted, in paragraph 3 of the counter-notice. Nonetheless, the sense of the counter-notice is clear. This was a conditional offer: the landlord would accept the tenant's paragraph (c) proposal if, in return, the tenant would agree to the original clause 4 being imported into the new lease terms.

47. In the tribunal's view, one cannot sever the sentence to say that the paragraph (c) proposal was accepted and, therefore, the dispute is only over the form of clause 4. That stretches the natural meaning of "subject to" to an unacceptable degree. The offer made by the landlord was in terms that the tenant could have accepted; and the tenant would have known exactly what it would receive, had it done said so. If the counter-notice had been accepted, clause 6 in the deed of variation would have vanished, that the original clause 4 from the 1975 lease would have been imported into the new, extended lease.

48. To that extent, the counter-notice is not ambiguous.

49. The tribunal is reinforced in this view by the fact that the applicant did not question or challenge the counter-notice prior to the application to the tribunal; and, in particular, did not issue county court proceedings to challenge the validity of the counter-notice, which incidentally the tenant had done in the *Burman* case.

50. As the tenant had not accepted the terms proposed by the landlord in the counter-notice, what then is the meaning of the sentence containing the landlord's response to the paragraph (c) proposal? It means: the paragraph (c) proposal is not accepted - so that clause 6 must be imported into the new lease terms - but the landlord counter-proposes that it would accept the paragraph (c) proposal, in return for the tenant agreeing to import the original clause 4 into the new lease.

51. For all of these reasons, the tribunal is satisfied that the counter-notice is a valid notice under the Act.

The "rent" issue

52. Mr Harrison's fall-back position, if the tribunal were to find that clause 6 was to be incorporated in the new lease, was that the rent reserved by clause 6 constituted "rent" within the meaning of section 56 of the Act, so that it should be commuted to a peppercorn. It will be recalled that clause 6 provided for the tenant to pay the landlord 60% of the net rent receivable by the tenant for any period of underletting exceeding 6 months during the 12 months of the preceding year.

53. The question posed was whether the money payable by the tenant under clause 6 could be characterised as "rent". Both counsel dealt with the arguments for and against the clause 6 payment being considered as "rent" under section 56 of the Act, both in their skeleton arguments and in their oral submissions.

54. Mr Tunkel set out verbatim extracts from *Woodfall: Landlord and Tenant*, i.e. paragraphs 7.001 (which starts with the mediaeval view of rent), 7.005, 7.006, 7.016, 7.024 and 7.025 (though not in that order), from which he extracted a series of arguments for and against.

55. While, in his view, it appears in principle that "a payment based on the net underletting rent received may be regarded as rent", not surprisingly, he considered the other factors identified weighed against such a result, so that "it is submitted that any payments that may fall due under clause 6 of the 2006 deed should not be regarded as rent."

56. Mr Harrison relied on several factors to say that the underletting payment should be considered as "rent". He pointed first to the express terms of the deed of variation. First, clause 5 refers to "the additional rent herein provided which shall be recoverable from the Tenant in the same manner as rent payable under the Lease"; and this is immediately

followed by clause 6 headed "Additional Rent". Mr Harrison agreed that heading was to be ignored by reason of clause 2.7 of the deed of variation, which stated that "the clause headings shall not be taken into account for the purposes of its construction or interpretation." However, he pointed to the wording of clause 6 itself, which starts by requiring payment to the landlord of the sum of £1,366 "in respect of net additional rent due" (which appeared to be due to the landlord as a result of a past breach by the then tenant of the underletting restriction in the lease) and, thereafter, an annual "sum as represents 60% of the net rent receivable by the tenant..."

57. He also drew parallels with the situation before the Court of Appeal in *Bolton v Godwin-Austen and others*, where the tenant's obligation to pay a sum equivalent to the rent that the head lessor had to pay to the freeholder was considered "rent", whatever the parties may choose to call it. Finally, he said, the payment under clause 6 was a form of turnover rent, assessed by reference to the profits of the land.

58. Mr Harrison accepted that if clause 6 were not incorporated into the terms of the new lease, or that it were incorporated but the payment under it was considered as "rent" under section 56 and therefore commuted to a peppercorn, the landlord would lose something. However, he said, that is why the valuers were present: to assess the premium to be paid to the landlord consequent upon the loss he suffered as a result of the operation of the Act.

59. Mr Tunkel accepts and, from a careful reading of the authorities, it must be the case that payment based on the net underletting rent may be regarded as "rent". While clause 6 does not provide that a certain sum is to be paid to the landlord, it does provide a formula that would enable the sum to be reduced to a certainty at the time of payment. Turnover rent is, the parties accept, capable of being considered "rent".

60. The tribunal considers that the payment is one arising from the occupation of land by the tenant; and, to the extent that the tenant's occupation is dependent upon a contract comprising the original lease and the 2006 deed of variation, it is paid in return for the occupation of land.

61. The issue, and Mr Tunkel's main argument, is whether or not payment should be considered as consideration payable under a "collateral agreement", which, according to *Woodfall* is not part of "rent". Paragraph 7.016 of *Woodfall*, headed "collateral consideration" reads as follows:

> "A consideration payable under a collateral agreement to enable the tenant to do on the demised land an act which otherwise he could not lawfully do (e.g. under a licence for change of use) is not part of the rent, even though so called by the parties." Reference being made in the footnote to the case of *Westminster (Duke) v Store Properties* [1944] Ch 129.

62. In paragraph 19 of his skeleton, Mr Tunkel puts it this way: "... had the clauses in the 2006 deed been included in the 1975 lease from the outset, then it would appear that the payment could indeed have been regarded as rent. However, the 1975 lease allowed underletting only for 6 months of the year. The 2006 deed permitted something that was otherwise forbidden by the 1975 lease. Had such permission being granted in return for a lump sum payment, then such payment would have been regarded as "consideration payable under a collateral agreement to enable the tenant to do on the demised premises an act which otherwise he could not lawfully do" (Woodfall para 7.016), so it would not have been rent."

63. He goes on to rely on the *Westminster* decision, quoting the short head note and the judgement of Bennett J in full, at paragraph 20 of his skeleton argument. In that case, a lease to premises contained a covenant by the lessees not to use them for any trade or business, but only as a private dwelling-house. The lessor granted to assignees of the lease a licence to convert the house into office premises in return for a yearly rent of £50 in addition to the rent reserved by the lease, so long as the premises, so converted, were in use as office premises. Bennett J held that the annual sum of £50 payable under the license was not "rent reserved" within the meaning of the War Damage Act 1943, basing his decision on the usual technical meaning of "rent" and not on any special meaning in the Act. The key part of the judgement is where Bennett J states:

> "The truth is that the sum in question is not the consideration for the demise of the land comprised in the original lease, but is the consideration payable under a collateral agreement to enable the tenant to do on the land then vested in him an act which otherwise he could not lawfully do. [...] ... the rent to which the section refers is something which arises on the occasion of a demise and is the subject of a reservation out of the subject of a demise. The sum payable to a landlord by a tenant by virtue of a collateral agreement containing no demise cannot, I think, properly be referred to as a rent reserved."

64. Mr Harrison seeks to distinguish the *Westminster* case stating, quite simply, that what was under consideration there was a licence (so-called by the parties), which was explicitly acknowledged to be a "collateral agreement"; whereas the lease restriction in that case (use only as a private dwelling-house) remained and, but for the licence, would have prevented office use.

65. The present case was different: this was not a "collateral agreement" but a deed of variation; and it matters not the reasons why the deed came about. Whereas a licence benefits only an individual tenant, a deed of variation affects the very interest in land itself and is assigned with the original lease on sale. In Mr Harrison's submission, the execution of the deed of variation acts as surely as a surrender and re-grant, so that clause 6 has become just as much a part of the lease as the original terms (although the tribunal accepts, following *Woodfall*

paragraph 17.026, that a mere increase in rent does not operate as a surrender and re-grant of the original lease; and, neither, it is considered, does the mere variation of a user covenant).

66. Accordingly, there is no longer an absolute prohibition of underletting for more than 6 months in any year: the deed of variation has done away with that. It is now permitted, subject to the payment of the turnover rent. That payment is not under any collateral agreement, but it is under the lease itself, as varied. It could have been under a collateral agreement - as with the license granted to the assignee tenant in *Westminster* - and had it been so, the payment would not have been considered as "rent".

67. Mr Tunkel emphasised that Bennett J in *Westminster* had talked about rent being in connection with the demise of the land comprised in the "original" lease, but that interpretation is too restrictive, especially when one looks back at the nature of rent in paragraph 7.001 of *Woodfall*, which states: "in modern times it has been said that rent in its correct sense is (1) a periodical sum, (2) paid in return for the occupation of the land, (3) issuing out of the land, and (4) for non-payment which a distress is leviable" (though the latter common law right to distrain for arrears of rent has now been abolished).

68. In the non-technical language of the Oxford English Dictionary, rent is "a periodical payment made by a tenant to an owner or landlord for the use of land or buildings." The original use under the 1975 lease was owner-occupation as a private residence for at least six months in each year, given the absolute restriction in the original clause 4 not to underlet the premises from more than six months a year.

69. That use was changed for all time following the execution of the 2006 deed of variation. Now, the tenant can underlet for more than six months a year. This is a different use.

70. The payment to the landlord, or rent, for the original use was contained in clause 2(1) of the lease ("to pay the reserved rent..."), in clause 2(2) ("to pay ... by way of further and additional rent ... "the service charge"...) and in the Third Schedule, being the yearly ground rents rising every 33 years.

71. The payment to the landlord, or rent, for the changed use are the sums referred to in clauses 2(1) and (2) and the Third Schedule of the original lease, plus the turnover rent in the deed of variation, called "net additional rent due".

72. The tribunal accepts, on the strength of the obiter comments of Sir Stanley Burnton in *Bolton v Godwin-Austen and others* at paragraph 61, that "what rent is for the purposes of Chapter II cannot depend on what the money or the obligation is called" by the parties. However, the payment due under the deed of variation is not a service charge and nor

is it a licence fee; it is a turnover rent and properly described as "additional rent due". This is not at all surprising: the changed user is more useful and more valuable to the tenant; the tenant is willing to pay an additional rent for it; and the landlord also wants to benefit from the changed, enhanced use of the property. That much was clear from the correspondence at tab 1 of the respondent's bundle, which pre-dated and led to the creation of the 2006 deed of variation.

73. In the *Westminster* case, the lease user restriction remained, but a collateral agreement allowed the tenant to do otherwise; and he paid consideration for it. In the present case, by amending clause 4, the deed of variation changed the user for all time - i.e. changed the lease itself - and the consideration payable was for the new, changed user in the now combined lease and deed of variation (which is to be treated as one whole), not for a concession in a collateral agreement which, by definition, is a side-agreement, not merged with the original lease.

74. Accordingly, the tribunal determines that the payment to the landlord in clause 6 of the deed of variation is "rent" within the meaning of section 56 and it is therefore to be commuted to a peppercorn, with an attendant adjustment (i.e. a compensatory increase) to the premium payable to the landlord on the grant of an extended lease under the Act.

The "clause 4" issue

75. This was a straightforward question whether the new lease terms should incorporate the original clause 4 in the 1975 lease, or the amended clause 4 in the schedule to the 2006 deed of variation. Mr Harrison's submission was that the respondent was not able to introduce, at this stage, the original clause 4. He founded his argument on the wording of the counter-notice, which contained no freestanding counter-proposal to reinstate the original clause 4, bolstered by an assertion that it would be contrary to the terms of section 57 of the Act - which requires the new lease to be on the same terms as the existing lease, but with such modifications "as may be required or appropriate" to take into account the omission of property, alterations to the property since the grant of the existing lease, or the combined effect and differences in any terms where the existing lease derives from more than one separate lease.

76. Section 57(6) allows the parties to reach agreement on new terms (which they have done, to a limited extent) and allows either of them to require that any term of the existing lease be excluded or modified insofar as it is necessary to remedy a defect in the existing lease or it would be unreasonable in the circumstances to include, or include without modification, the term in question in view of changes occurring since the date of commencement of the existing lease, which affect the suitability of the provisions of that lease.

77. Mr Tunkel submitted that the provisions of section 57 were such that the tenant could agree to include the original clause 4 in the new lease; but, otherwise, none of the provisions of this section were applicable so as to enable the landlord to require or the tribunal to direct that the original clause 4, as opposed to the amended clause 4, should go in the new lease.

78. The tribunal is satisfied that there are no grounds under section 57 for requiring the original clause 4 from the 1975 lease to be in the new, extended lease; and it appears that the parties do not dispute this.

Conclusion

79. The tribunal determines that both clause 6 and amended clause 4 in the 2006 deed of variation should be retained in the new, extended lease. However, as the tribunal has determined that the payment due to the landlord under clause 6 constitutes "rent" within the meaning of section 56 of the Act, it is commuted to a peppercorn.

80. Accordingly, the tribunal is willing to accede to the submission at paragraph 31 of Mr Tunkel's skeleton argument and direct that the new lease should omit clause 6 of the 2006 deed, but should retain the amended clause 4 set out in its schedule.

81. The tribunal also considers that the landlord should be compensated under the Act by way of a higher premium, to reflect the loss of rental payments that would otherwise have fallen due under clause 6. Of the three possible valuations set out in the comparison table before the tribunal, valuation No. 3 will be the appropriate one, whereby "The new lease omits clause 6 of the 2006 Deed but retains the amended clause 4 set out in its Schedule." As at the hearing, the respective valuations for this eventuality were £175,150 for the tenant (Mr George Pope's valuation 1) and £224,000 for the landlord (Mr Gary French's valuation 3A).

Valuation issues

82. The agreed valuation matters are listed at paragraph 5, above. The tribunal is required to determine the relativity and the likely benefit arising to the freeholder from the inclusion of clause 6 within the lease prior to the calculation of the premium payable for a new lease.

83. Both valuers confirmed the subject property was sold in November 2014, subject to the current lease provisions, for £600,000. Mr Pope, the applicant's surveyor, proposed a relativity of 78.3% based upon the adjustment of this sale price through the use of the FPD Savills Enfranchisable Rights index and Gerald Eve relativity graph statistics. Mr French, the respondent's surveyor, argued for a relativity of 74.74%. He reduced the sale price by 10% to reflect the benefit of "Act Rights" to

produce a "No Act Rights" current lease value of £540,000, adopting 10% by reference to two cases referred to in paragraph 14.08 of his report. He then relied upon the Agreed Freehold Value of £850,000, to which he applied a 15% reduction to reflect the onerous sub-letting clauses contained within the lease. This adjustment produces a freehold value subject to the current lease of £722,500 and a derived relativity of 74.74%. Mr French corroborated this outcome against published relativity graphs in his evidence.

84. The tribunal was mindful of the guidance offered by the Upper Tribunal in *Nailrile Ltd v Cadogan* [2009] 2 EGLR 151, which emphasised the use of all available relevant information in determining relativity, including published relativity graphs as well as transaction evidence. The reliance upon a single transaction, albeit the subject property by both surveyors was of concern to the tribunal.

85. The tribunal preferred the evidence of Mr French, because he relied less upon third party statistics in the calculation of relativity than Mr Pope, he sought to rely on authority and there was more transparency in his figures. The construction and reliability of the FPD Savills and Gerald Eve indices were not explored at the hearing by the applicant. The tribunal accepted the use of these statistics as material to the accuracy of the outcomes. Accordingly, a relativity of 74.74% was adopted by the tribunal.

86. The lease currently provides for an additional rent to be paid to the freeholder should subletting occur for more than 6 months of any 12 month period. The tribunal determines at paragraph 74 above that any sum payable is rent under the terms of section 56 of the Act. It falls upon the tribunal to decide how often the freeholder is likely to receive these monies in calculating a commuted sum as compensation. Mr French told the tribunal he expected the freeholder to receive a receipt every 6 months for the remainder of the term, amounting to a capital sum of £87,400. Mr Pope argued that the freeholder would receive £13,650 spread throughout the 55 year remaining term, having taken the agreed annual rent potentially receivable by the landlord and multiplied it by 2.5. In his view, the prospect of the landlord receiving a share of such rental payments was "remote"; and this was essentially an "owner-occupier's" flat. However, there was no evidential basis for either opinion.

87. It is a matter of speculation and, ultimately, judgment as to the likely rent that the landlord might receive from possible underlettings of the subject flat over the remainder of the term; and over the extended term. The tribunal determined a freeholder would reasonably anticipate a receipt in three 6-monthly periods every 10 years. This likelihood of sub-letting by the leaseholder reflects the property size, type and location, that is to say, it is a small basement flat, but in a good location. Under this frequency of sub-letting the freeholder would be due a payment of approximately £29,100. Compensation of around £1,190 was added to the premium payable to reflect the income loss

during the statutory 90 year extension. This is added as compensation under paragraph 5 of Schedule 13 because the potential receipt does not exist in the landlord's current interest, but it only arises after the statutory extension of the term is granted and as a reflection of the tribunal's determination that the rent under clause 6 should be commuted to a peppercorn.

The premium

88. The tribunal determines the appropriate premium to be **£196,390**. A copy of its valuation calculation is annexed to this decision.

Name: Judge Timothy Powell **Date:** 21 January 2016

Corrected & reissued: 3 February 2016

Appendix: Valuation setting out the tribunal's calculations

Rights of appeal

By rule 36(2) of the Tribunal Procedure (First-tier Tribunal) (Property Chamber) Rules 2013, the tribunal is required to notify the parties about any right of appeal they may have.

If a party wishes to appeal this decision to the Upper Tribunal (Lands Chamber), then a written application for permission must be made to the First-tier Tribunal at the regional office which has been dealing with the case.

The application for permission to appeal must arrive at the regional office within 28 days after the tribunal sends written reasons for the decision to the person making the application.

If the application is not made within the 28 day time limit, such application must include a request for an extension of time and the reason for not complying with the 28 day time limit; the tribunal will then look at such reason(s) and decide whether to allow the application for permission to appeal to proceed, despite not being within the time limit.

The application for permission to appeal must identify the decision of the tribunal to which it relates (i.e. give the date, the property and the case number), state the grounds of appeal and state the result the party making the application is seeking.

If the tribunal refuses to grant permission to appeal, a further application for permission may be made to the Upper Tribunal (Lands Chamber).

Property: 34B & Vault Rutland Gate London SW7 1PD
Reference No: NAT/LON/00BK/OLR/2015/1043

Lease and Valuation Data

Lease Term:		24 June 1971				
Lease Expiry date:		23 June 2070				
Unexpired term as at valuation date:		55.48	years			
Date of Valuation		12 January 2015				
Rent receivable by landlord:						
Payable from valuation date for 55.48 years	£	171				
Payable from valuation date for 145.48 years	£	256				
Values						
Agreed Freehold	£	850,000				
Long lease value without clause 4 and 6	£	841,500				
Freehold adjusted to reflect clause 4 and 6	£	722,500				
Abated long lease value with clause 4 and 6	£	715,275				
LHVP	£	540,000	Relativity		74.74%	
Capitalisation rate (%)		6.00				
Deferment rate (%)		5.00				
Value of Freeholders present interest						
Term 1						
Ground rent payable	£	171				
YP @ 22.48 years @ 6%		12.16915	£	2,081		
Term 2						
Ground rent payable	£	256				
YP @ 33 years @ 6%		14.23023				
Deferred @ 22.48 years @ 6%		0.26985	£	983		
Reversion						
Freehold in vacant possession	£	850,000				
Deferred @ 55.48 years @ 5%		0.06674	£	56,733		
	Total				£	59,797
Sub letting additional rent to freeholder during term						
Agreed annual rent payable	£	5,460.00				
Likelihood of occurrence		33.30%				
Additional rent p.a. based upon 6 months receipts	£	1,818.18				
YP @ 55.48 years @ 6%		16.00919	£	29,107.59	£	29,108
Less						
Freehold value after leasehold extension	£	841,500				
PV of £1 in 145.48 years at 5%		0.0008268	£	696	£	88,209
Freeholders interest value						
Calculation of Marriage Value						
Value of flat with long lease on statutory terms	£	841,500				
Landlords proposed interest	£	696	£	842,196		
Less						
Value of Leaseholders existing interest	£	540,000				
Value of Freeholders current interest	£	88,209	£	628,209		
Marriage value	Total				£	213,987
Division of Marriage Value equally between						
Freeholder					£	106,993
Leaseholder					£	106,993
Schedule 13 , para 5(1) losses						
Compensation for additional rent loss at extension						
Agreed annual rent payable	£	5,460.00				
Likelihood of occurrence		33.30%				
Additional rent p.a. based upon 6 months receipts	£	1,818.18				
YP @ 90 years @ 6%		16.57870				
Deferred @ 55.48 years @ 6%		0.03945	£	1,189.10		
Price payable to Freeholder						
Value of freeholders current interest					£	88,209
Share of marriage value					£	106,993
Compensation for loss of additional rent at grant of new lease					£	1,189
					Total	£ 196,391
					Say	£ 196,390