

# legal update

YOUR UPDATE OF  
RECENT CHANCERY &  
COMMERCIAL LAW

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and all that!**



Kenneth Munro

## Leasehold enfranchisement: busy times

**Despite the parlous state of the residential property market, enfranchisement claims continue to exercise courts and tribunals. This article gives a flavour of what has been generating disputes.**

### 'House', 'flat' and 'block of flats'

Nearly 45 years after the Leasehold Reform Act 1967 became law we might be forgiven for thinking that either Parliament or the courts would have adequately defined a 'house', a 'flat' and a 'block of flats'. Not a bit of it. In the last decade the House of Lords considered houses twice, in *Malekshad* and in *Boss Holdings*. The Court of Appeal has recently revisited houses in *Prospect Estates Ltd v Grosvenor Estate Belgravia* [2009] 1 WLR 1313 and *Day v Hosebay Ltd* [2010] 1 WLR 2317.

### House

In *Prospect* a building designed as a house and resembling a house was required by the terms of the lease to be used predominantly as offices. The Court of Appeal held that the prescribed and predominant use of the building, not its design and appearance, was the overwhelmingly significant factor and held it was not a house. Surprisingly, *Boss* did not feature greatly. The House of Lords gave leave to petition but the parties had already settled when they were told of the leave.

If *Prospect* is right, the terms of the lease can be of fundamental importance. The lawful user under planning legislation may be relevant. The actual use to which the property is being put (or was put when last used) will also be important.

*Day v Hosebay Ltd* concerned buildings constructed as large houses. When the notices of claim were given, three were being used for short-term accommodation for tourists and other visitors to London and in one most of the building was being used as offices. Whilst claiming to accept that it was bound by *Prospect*, the Court of Appeal, in effect, reverted to a test that looked at the physical layout of the building and ignored everything else. The Supreme Court has given permission to appeal.

### Flat

In *Fardale Court Freehold Ltd v G & O Rents Ltd*, unreported, Judge Cowell had to consider a development in south-east London built to house "keyworkers". The premises had the look and feel of student halls of residence, consisting of 176 bedsits with toilet, shower and wash-hand basin, grouped in 30 self-contained units each containing a kitchen. Each bedsit had a lockable door. The rooms were advertised as "studio flats." The judge held that each of the 30 units was a flat. The lessees of the flats were therefore entitled to enfranchise. The freeholders are considering an appeal.

### Block of flats

In *Crafrule v 41-60 Albert Palace Mansions* [2011] 2 All ER 295 the Court of Appeal had to consider what is a block of flats. Tenants gave notice to enfranchise 20 flats, part of a long terrace. Each staircase of 10 flats was vertically divided from its neighbours. The Court of Appeal held that it was not necessary to limit the specified premises to the smallest self-contained part of a building. The decision means that tenants in similar situations have a choice of enfranchising the smallest self-contained part of a building or contiguous multiples of the smallest part.

### Deferment rates

Turning to valuation issues, deferment rates have occupied much of the Lands Chamber's time. *Sportelli* settled the deferment rate where leases have over 20 years unexpired. During the course of *Sportelli* it was clear that the Lands Tribunal wanted, in effect, to prescribe a rate to be applied for as long into the future as possible. The valuation dates in *Sportelli* are now all well over 5 years ago. This led to the LVT decision in *Wellcome Trust v 19/22 Onslow Gardens*, where the landlords sought to adduce financial evidence to prove that the *Sportelli* rate was now too high. The LVT refused to allow the evidence in. An application for permission to appeal is before the Upper Tribunal.

### 10 to 20 years unexpired

In *Cadogan Square Properties Ltd v Cadogan* [2010] UKUT 427 (LC) the Upper Tribunal adopted the approach it had followed in *Arbib* and *Sportelli*. It gathered together appeals in which the deferment rate was the common theme. The Upper Tribunal decided that where there were 10 to 20 years unexpired the parties to a notional sale of the reversion on the valuation date would take account of whether the market was perceived to be over- (or under-) valued. The formula adopted was the *Sportelli* formula plus an adjustment to reflect reduced growth potential because the market was perceived to be overvalued. This is a recipe for disputes. It requires valuers to adduce evidence and form a judgment as to where the market is in the cycle, when it might be expected to pass through "equilibrium" and what adjustment sellers and buyers would make to the deferment rate.

### 0 to 5 years unexpired

The way in which the deferment rate should be calculated for leases with 0 to 5 years unexpired has been settled in *Trustees of the Sloane Stanley Estate v Carey-Morgan* [2011] UKUT 415 (LC), a collective enfranchisement. The Upper Tribunal decided that the deferment rate should be the net rental yield (NRY) plus an allowance for lack of vacant possession until term.

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... interesting times for  
enfranchisement practitioners



The NRY must be established by evidence. That will usually be property- and/or location-specific. Specific evidence of gross and net yields will be needed. Evidence of portfolio yields or references to published material on yields is unlikely to be persuasive, certainly where there is market evidence. The allowance for lack of vacant possession until term is said to be necessary to reflect the fact that the investor who buys a tenanted property does not have the same choices as one who buys with vacant possession. The Upper Tribunal fixed it at 5%. That was not intended to be a generally applicable figure: the figure will depend on evidence in every case.

#### 5 to 10 years unexpired

That leaves lease with 5 to 10 years unexpired. Do you start with *Sportelli* or *Vale Court*, a combination or something else? Whatever the method, the answer will have to avoid the discontinuities much discussed in the Cadogan Square appeals.

#### Other questions

Valuing existing leases continues to be a problem. In *McHale v Cadogan* [2011] 1 P & CR 313 the Court of Appeal confirmed the conventional wisdom that in a Schedule 13 valuation it is to be assumed that there are no rights under the 1993 Act. The Supreme Court has given permission to appeal.

As well as the claims noted above, the Court of Appeal considered the meaning of 'common parts' in *Cadogan v Panagopoulos* [2011] Ch 177 and may have to consider sham transactions in the Dolphin Square litigation. These are interesting times for enfranchisement practitioners.

**Kenneth Munro's practice consists almost entirely of real property related work and associated professional negligence. It is largely contentious but has a substantial non-contentious element. Of the cases mentioned, he appeared in *Arbib v Cadogan*, *Cadogan v Sportelli*, *Crafrule v 41-60 Albert Palace Mansions*, *Cadogan v Panagopoulos*, *Farndale Court Freehold Ltd v G & O Rents Ltd* and *Cadogan Square Properties Ltd v Cadogan*.**

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James Thom QC

## No smoke without fire

**It is well known that on exchange of contracts for the purchase of land, title to the property vests in the buyer in equity, so that the buyer is immediately at risk if there is damage to the property. This can be a trap. If, for example, the property is damaged by fire between exchange and completion, the buyer is bound to complete without reduction in price: *Poole v Adams* (1864) 10 LT 287.**

That is what occurred in *National Farmers Union Mutual Insurance Society Limited v HSBC Insurance (UK) Limited* [2010] EWHC 773 (Comm): a property was severely damaged by fire between exchange and completion; the purchasers completed, and claimed on their insurance policy issued by the Claimants ("NFU"). NFU, having paid out, then claimed a contribution from the Defendants ("HSBC"), the sellers' insurers, on the grounds of double insurance. The judge determined on a trial of preliminary issues that NFU's case failed.

#### General rules

If the HSBC policy had only covered the sellers, the NFU policy must have borne the entire loss, because even when a seller's policy pays out the buyer has no right to the money: *Rayner v Preston* (1881) 18 Ch D 1; further, on completion of the contract at the full price the seller has no claim, as he has suffered no loss, and if the insurer had previously paid out it can recoup its payment out of the purchase money by way of subrogation: *Chastellain v Preston* (1883) 11 QBD 380.

An attempt was made in section 47 Law of Property Act 1925 to reverse the effect of *Rayner v Preston*, but this attempt is generally regarded as unsuccessful: see the judgment in *NFU* at paragraph 18c.

The Standard Conditions of Sale provide that *if* the contract requires the seller's insurance to remain in force, the buyer is entitled to the insurance money (so far as not laid out on reinstatement) or, if it has not been paid, an assignment of the right to receive it. In this case the contract provided that the seller was not obliged to maintain insurance.

#### NFU's claim

How then did NFU claim contribution? They relied upon the fact that in certain circumstances the HSBC policy would not only cover the seller, but also extended cover to the buyer; they argued that this gave rise to a case of double insurance, so as to give them a claim for contribution.

#### HSBC's defence

The provision in the HSBC policy extending cover to a buyer stated that the policy would not cover "if the buildings are insured under any other insurance". There was also a general provision that wherever risks insured by HSBC were also insured elsewhere, the HSBC cover would take effect as excess cover. HSBC therefore contended that since the buyers had their own insurance with NFU, the extended cover under the HSBC policy never incepted.

HSBC's alternative case was that its cover took effect as excess over NFU's cover, and as the case had been settled within NFU's policy limits the HSBC policy did not answer to the claim.

#### Overlapping policies

Many insurance policies contain clauses which modify the cover provided in the event that there is other insurance covering the same risk. In one of the American cases (*Jones v Medox Inc* 430 AR 8.3d 488) they are analysed as usually taking one of three forms:

- > escape: a clause that if there is any other insurance covering the same risk the subject policy will not cover;

- > pro rata (or rateable proportion): a clause that the subject policy will only pay a proportion of the total amount of cover; or
- > excess: a clause that the subject policy will take place as excess to other existing cover.

NFU argued that because there was a pro rata clause in the NFU policy, a trilogy of English cases (*Gale v Motor Union* [1928] 1 KB 359; *Weddell v Road Transport and General Insurance Co* [1932] 2 KB 563; *Austin v Zurich* [1944] 2 All ER 243 (Tucker J), [1945] 1 KB 250 (CA)) compelled the court to hold that both NFU and HSBC were liable to indemnify in respect of the damage, with the result that HSBC should meet half of NFU's payment.

The issue which arose in two of those cases was that when two insurance policies each provide that they will not apply if another policy also covers, there is the potential absurdity expressed by Rowlatt J in *Weddell* (at p 567) as, “the result that, on the ground in each case that the loss is covered elsewhere, it is covered nowhere”.

HSBC argued that there was no conflict between the policies. Although the property passed to the buyer in equity on exchange, the seller retained an insurable interest, because the buyer might not complete the purchase, in which case the seller would suffer a real loss, which the seller's policy would indemnify: *Castellain* at 385. The extension of cover to buyers was provided for the benefit of HSBC's insured, by providing cover to an otherwise uninsured buyer so that he could complete. If the buyer had other insurance this benefit was not required.

#### Judge's decision

The judge upheld HSBC's primary case.

At paragraphs 19 to 26 he accepted HSBC's submissions that apart from authority the natural meaning of the HSBC policy was that an insured buyer was not indemnified by the HSBC policy. There was no conflict with NFU's pro rata clause, since there was no cover under the HSBC policy, and so no reason why NFU would not be liable in full.

Turning to the trilogy of cases relied on by NFU, at paragraphs 29 to 40 the judge pointed out that both *Weddell* and *Gale* were cases where there were conflicting escape clauses, which could not be given their literal effect because to do so would give effect to the absurdity stated above. They gave no assistance in this case.

Turning to *Austin*, in paragraphs 41 to 48 he pointed out some of the conceptual difficulties in that decision. At paragraphs 49 to 52 he preferred the approach of the New Zealand Court of Appeal in *State Fire Insurance v Liverpool and London and Globe Insurance* [1952] NZLR 5, which was that the policies should be given their natural meaning except in the case of mutually stultifying clauses, whether escape or excess. There was no absurdity in giving effect to the qualification to the HSBC extension, and holding that NFU's policy was solely responsible for providing indemnity. The result was that HSBC's primary case succeeded.

The judge made it clear that the approach in *State Fire* supported HSBC's alternative case if it had been necessary for HSBC to rely upon it.

The judge was clearly right to construe the policy according to its commercial purpose and natural meaning, rather than adopting an artificial construction, used in relation to other policies and in other circumstances, where both the policy terms and the circumstances were different.

**James Thom QC has a broad-based Chancery practice covering two main areas: first, property advice and litigation and, secondly, company law and insolvency. He appeared for the successful defendants in the NFU case.**

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Gerard van Tonder

## Signed, executed and all that!

**The decision of the Court of Appeal in *Hilmi & Associates Ltd v 20 Pembridge Villas Freehold Ltd* [2010] 1 WLR 2750 (CA) highlighted the strict requirements of s 36A of the Companies Act 1985 (and hence the similarly-worded ss 43-47 of the Companies Act 2006 now in force) about companies signing and executing documents. The decision concerns a claim for leasehold enfranchisement, but is of wider importance and is a reminder, assuming that any is required, that statutory notices are very much all or nothing.**

#### The facts

The holders of four long leases of a block of flats in Notting Hill served notices under s 13 of the Leasehold Reform, Housing and Urban Development Act 1993 (“the 1993 Act”) exercising their rights as qualifying tenants to acquire the freehold of the building by way of collective enfranchisement. Each of the participating tenants has to serve an individual notice. Three of the qualifying tenants were individuals and each duly signed a notice. The fourth was a company and its notice was signed by its director for the company. The question was whether that signature of the notice amounted to a valid signature on behalf of the company. The significance was that if the company's notice was not valid then the exercise of the collective enfranchisement failed, as the remaining three tenants represented fewer than half of the flats in the building.

#### The statutory requirements

Section 99(5) of the 1993 Act provides:

Article continued >



## ... signing and executing documents



“Any notice which is given under Chapter I or II by any tenants or tenant must—

(a) if it is a notice given under section 13 or 42, be signed by each of the tenants, or (as the case may be) by the tenant, by whom it is given; and

(b) in any other case, be signed by or on behalf of each of the tenants, or (as the case may be) by or on behalf of the tenant, by whom it is given.”

The signature of the notice has to be that of the tenant and not of an agent (*St Ermins Property Co v Tingay* [2002] 3 EGLR 53) and the signature of one notice by a nominee purchaser on behalf of all the participating tenants is not a valid signature for the purposes of ss 13 and 99(5) (*Cascades and Quayside Ltd v Cascades Freehold Ltd* [2008] L&TR 367).

Section 36A of the Companies Act 1985 (“the 1985 Act”) was introduced in 1989 to give effect to the change in the law about the execution of deeds in s 1 of the Law of Property (Miscellaneous Provisions) Act 1989. Section 36A allowed a company to execute a document (other than a deed) either by affixing its common seal or by complying with sub-section (4):

“A document signed by a director and the secretary of a company, or by two directors of a company, and expressed (in whatever form of words) to be executed by the company has the same effect as if executed under the common seal of the company.”

Before s 36A came into force there was no requirement for the manner in which companies had to execute documents which were not required to be deeds.

### The first instance decision

In *Hilmi*, at first instance, the judge construed the requirements of s 99(5) of the 1993 Act in a purposive manner; he concentrated on the

requirement in s 13 that the tenant should give the notice personally, so that the tenant really knew what he was doing rather than have something done in his name. He accordingly held that the requirements of s 36A of the 1985 Act about the execution of documents were not applicable. He declined to follow the decision in *City & Country Properties Ltd v Plowden Investments* [2007] L&TR 225.

### The decision on the appeal

On appeal, Lloyd LJ (who gave the only substantive judgment) concluded that s 36A prescribed how a company registered under the Companies Acts could itself sign a document which was required for some legal purpose. He held that a notice under s 13 of the 1993 Act was such a document. The judge relied on the definition of ‘execute’ in the *Oxford English Dictionary* to overcome the difference in language between ‘execute’ in s 36A of the 1993 Act and ‘sign’ in s 99(5) of the 1985 Act and held that:

“... in the context where some degree of formality is required to make a document valid and effective for some particular legal purpose ... , it is appropriate and natural to speak of the execution of the document, as a matter of ordinary language. That is so even for a document to be made under hand rather than by deed. ... Not only is that, as it seems to me, a natural use of the word ‘execute’ as a matter of English generally, and supported by the OED definition. It also fits well with the context and language of section 36A.”

Lloyd LJ rejected the possibility that the change of the law brought about by the introduction in 1989 of s 36A left a further category of documents, such as simple notices, which could be signed merely by a duly authorised representative of the company.

By reference to the decision in *Burman v Mount Cook Land Ltd* [2002] Ch 256 the judge confirmed

that the issue was whether the tenants had complied with s 13 of the 1993 Act and s 36A of the 1985 Act as to the form of the notice and not what the reversioner might reasonably have thought about the notices. He held that the tenants had not done so: the notice should have been ‘signed’ either by the affixing of the company’s common seal or by the signatures of two directors or of a director and the secretary.

### The Companies Act 2006

The result of *Hilmi* would have been the same under the provisions of sections 43-47 of the Companies Act 2006 (which came into force on 8 April 2008). Section 44 does, however, introduce an additional method for the execution of a document by a company, which makes it easier for companies to comply with the requirements for execution of documents:

“(2) A document is validly executed by a company if it is signed on behalf of the company—

(a) by two authorised signatories, or

(b) by a director of the company in the presence of a witness who attests the signature.

(3) The following are “authorised signatories” for the purposes of subsection (2)—

(a) every director of the company, and

(b) in the case of a private company with a secretary or a public company, the secretary (or any joint secretary) of the company.”

**Gerard van Tonder’s practice is concentrated on property matters and includes landlord and tenant (business and residential premises), leasehold enfranchisement and disputes about title. Gerard appeared for the defendant in *Hilmi*.**

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