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Feature

KEY POINTS

- A charge over a lease of commercial premises may secure part of the goodwill of a business carried on at those premises, even if goodwill is not expressly mentioned in the charge.
- The extent and value of any goodwill adhering to a lease depends on factors such as the nature of the business and any agreed absence of local competition.
- The court placed little weight on the value ascribed to goodwill in the sale documents of the business, as such value was usually set for the convenience of the buyer.

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Securing a share of goodwill

What value is secured by a charge over a lease of commercial premises? A recent decision in the Companies Court in *Re Crosscastle (in liquidation)* (unreported) held that even though a lease may, on the face of it, have negligible value, when it is sold in connection with a business, a portion of the goodwill of the business carried on at the premises may adhere to the lease.

Crosscastle Ltd operated two “Spar” branded convenience stores in Battersea. Capper & Co had loaned money to Crosscastle secured by two charges over the lease of one of its two premises. There was no mention of goodwill in the charges.

In 2010, Crosscastle entered administration, and the whole business, including the leases of two premises, stock, chattels, intellectual property and goodwill was sold. Crosscastle subsequently went into liquidation.

The liquidator and Capper & Co could not agree the value of the charges and the liquidator applied for directions under s 112 of the Insolvency Act 1986.

There were two issues:

- what proportion of the goodwill of the business attached to the lease; and
- what was the value of the lease plus any adherent goodwill.

In *Chisum v Dewes* (1828) 5 Russell 29, the Master of the Rolls held that the goodwill of a business could not be separated from the lease of the premises in which the business was carried on. However, by the time of *Muller & Co's Margarine v Commissioners of Inland Revenue* [1901] AC 217, it was understood that goodwill arose not just from location, but also from other factors,

including the name and reputation of the person carrying on the business.

In *Crosscastle* the court was faced with the difficulty of separating out these different types of goodwill.

The court held that the proportion of goodwill adhering to a lease was primarily a question of fact. The business was a convenience store, with most customers coming from within a small geographical area. However, there were no restrictive covenants preventing competitors establishing themselves in close proximity. The business also had goodwill which did not adhere to the lease, such as that which arose from its right to use the Spar brand. The court held that, given the type of business operated by Crosscastle, 50% of the goodwill of the business carried on at the premises adhered to the lease.

The valuation exercise conducted by the experts was an unusual one, as the goodwill of a business is usually considered as a whole. The experts' assessments of value differed widely, but both agreed that the value of the lease of the premises, if sold separately as an empty unit, was nil or nominal. The only real value was in the adherent goodwill.

It is notable that, while the sale contract for the business assigned a value to the goodwill, the court placed little weight on that valuation, it being common ground between the experts

that such apportionment was usually done for the convenience of the buyer, and bore little relation to the real value.

The decision shows that, even where a lease has little or no value if sold by itself, security over such a lease may still be valuable. This will, however, depend on the facts. While a significant proportion of the goodwill of a business may adhere to the lease of a pub or convenience store, for other types of business, such as those operating principally or exclusively over the internet, it may be that no goodwill adheres to the business premises at all.

Further Reading:

- Willmott Growers from an English law perspective: should lenders with security over leases be concerned? [2014] 3 JIBFL 160.
- Cherry picking, break dancing and gaming [2014] 4 JIBFL 227.
- LexisPSL: Banking & Finance Practice note: Security in real estate finance transactions.

Biog box

Thomas Elias is a barrister practising at Serle Court, Lincoln's Inn and is recommended for Company Law in Chambers & Partners 2016. He also practises in insolvency, commercial law, civil fraud, trusts and intellectual property. Email: clerks@serlecourt.co.uk Thomas Elias was instructed by David Barker of Carrick Read, and acted for Jeremy Frost of the Frost Group as liquidator.