


www.lease-advice.org

## LEASE CONFERENCES



Audio for the webinar will be through your computer speakers

Audio also available by telephone:  
Free phone no 0800 051 3810  
Free phone (int'l) +44 20 3478 5289

Access code: 950 315 133

For technical assistance please call Webex:

- 0800 389 9772
- Option 3
- Quote site reference: lease-advice.webex.com

Submit questions via the chat box

---

---

---

---

---


---

---

---

www.lease-advice.org Page 1

## Disclaimer



Whilst we make reasonable efforts to ensure it is accurate and up-to-date, information and guidance in this webinar does not and is not intended to amount to legal advice in any particular case

No responsibility for any consequence of relying upon the webinar material or presentations of the webinar is assumed by LEASE or any of our advisers

The law as stated during this webinar is as at 10<sup>th</sup> March 2015

---

---

---

---

---


---

---

---

www.lease-advice.org

## Collective Enfranchisement case law - valuation



Nicholas Kissen  
Leasehold Advisory Service  
10 March 2015

---

---

---

---

---


---

---

---

www.lease-advice.org Page 3

### A reminder of the key legislation



- Leasehold Reform Housing and Urban Development Act 1993
  - Part I Chapter 1
  - Section 1(1)(b) and Schedule 6

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 4

### A reminder of the key legislation



- Commonhold and Leasehold Reform Act 2002 changes
  - 80 years or more remaining on lease
    - Marriage value nil
    - Schedule 6, para.4(2A) of the 1993 Act

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 5

### Relevant date for valuation



- The date the s13 notice is given
  - s1(8) of the 1993 Act

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 6

### Which issues we shall be covering



- Capitalisation rate
- Deferment rate
- Relativity
- Treatment of development value

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 7

### Components of premium - Schedule 6 of 1993 Act



- Value of freeholder's interest
  - Paragraph 3
- Freeholder's share of marriage value
  - Paragraph 4
- Any compensation payable
  - Paragraph 5

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 8

### The landlord's interest



- Term and reversion method of valuation
- Capitalising the value of the ground rent
- Valuing the reversion

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 9

### Valuation of landlord's interest



- The amount which at the valuation date that interest might be expected to realise if sold on the open market by a willing seller.....

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 10

### Valuation of landlord's interest



- With neither the nominee purchaser or any tenant nor any owner of an intermediate interest buying or seeking to buy and on certain assumptions

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 11

### Assumptions



- Sale of estate in fee simple
  - Subject to relevant leases and
  - Any intermediate lease(s) or
  - Other leasehold interest(s)
- The 1993 Act confers no right to a lease extension or to take part in collective enfranchisement
- Improvements disregard
- Rights and burdens

---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 12

### The term

- Capitalised ground rent
- Application of yield rates
- Term should usually be considered separately from deferment rate for reversion



---

---

---

---

---

---


---

---

www.lease-advice.org Page 13

### *Nicholson v Goff [2007] 1 EGLR 83*

- Lands Tribunal decision of 8 January 2007
- Development outside Birmingham City Centre
- 11 flats above retail units
- Lease of three bed flat
  - Granted in 1931
  - 99 year term
  - Fixed rent of £50 pa
- Relevant valuation date
  - 8 April 2005



---

---

---

---

---

---


---

---

www.lease-advice.org Page 14

### *Nicholson v Goff [2007] 1 EGLR 83*

- **Factors relevant to the capitalisation rate**
- Length of lease term
- Security of recovery
- Size of ground rent
- Whether there was provision for rent review
- The nature of any such rent review



---

---

---

---

---


---

---

---

www.lease-advice.org Page 15

### Reversion - deferment rate



- “The rate of compound interest that would be needed to be earned on an investment made at the valuation date, in order to produce at the end of the term, the capital value which has been determined as being the value as at the valuation date of the interest, which value will however only accrue at the end of the term”
- *Arbib v Earl Cadogan [2005] 3 EGLR 139 para 87*

---

---

---

---

---


---

---

---

www.lease-advice.org Page 16

### *Earl Cadogan v Sportelli [2007]1 EGLR 153*



- Court of Appeal judgment of 25 October 2007
- Properties within SW1, SW3, SW7 and W1 postcodes
  - Prime Central London
- Conjoined appeals
- Mixture of enfranchisement and extension claims
- Issue of deferment rate applicable when valuing freehold interest with vacant possession

---

---

---

---

---


---

---

---

www.lease-advice.org Page 17

### *Earl Cadogan v Sportelli [2007]1 EGLR 153*



- Lands Tribunal applied general deferment rate of 4.75% for houses and 5% for flats
- Court of Appeal decided it was appropriate for LT to lay down guidelines as to deferment rate applicable in future cases
- In future cases involving property outside PCL the deferment rate adopted by LT would be the starting point, although evidence might be called to show that a different rate should be applied

---

---

---

---

---

---


---

---

www.lease-advice.org Page 18

### Components of Sportelli rate

- Risk-free rate (RFR)
- Real growth rate (RGR)
- Risk premium (RP)



---

---

---

---

---

---


---

---

www.lease-advice.org Page 19

### Risk-free rate

- *The return demanded by investors for holding an asset with no risk, often proxied by the return on a government security held to redemption*
- Why **2.25%** chosen?
- *Average index-linked yields on a five year rolling basis over the last decade suggested that a more stable market based risk-free rate would be in the range 2.0 per cent - 2.5 per cent*



---

---

---

---

---

---


---

---

www.lease-advice.org Page 20

### Real growth rate

- **2%** adopted as assumed growth rate
- Note fluctuation in house prices
- Note substantial difference over a long period that can arise from different rates



---

---

---

---

---

---

---

---

www.lease-advice.org Page 21

### Risk premium

- The additional return required by investors to compensate for the risk of not receiving a guaranteed return
- Volatility
- Illiquidity
- Deterioration
- Obsolescence
- LT considered **4.5%** was appropriate rate

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 22

### Components of Sportelli rate

- RFR=2.25%
- RGR=25
- RP=4.5%

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 23

### What does the 5% deferment rate comprise?

- RFR-RGR+RP
- 2.25%-2%+4.5%
- **4.75% deferment rate for houses**

---

---

---

---

---

---

---

---


---



www.lease-advice.org Page 24

### And the deferment rate for flats...

- 4.75% plus additional 0.25% for flats
- **5.00% deferment rate for flats**



---

---

---

---

---

---


---

---

www.lease-advice.org Page 25

### The Sportelli rate

- Applies where unexpired terms of 20 years or more
- With leases of less than 20 years deferment rate would need to take account of property cycle at valuation date
- Applying universal deferment rate irrespective of location
- Court of Appeal leaving open the possibility of further evidence in areas outside PCL
- Sportelli still the starting point



---

---

---

---

---

---


---

---

www.lease-advice.org Page 26

### Marriage value

- Recognises those participating can grant themselves new long leases at peppercorn ground rent
- Excess value bought about by merger on interests
- Only payable in respect of participating lessees and remain so until binding contract entered into
  - Hope value?
- 50% marriage value paid
- Only paid where leases have less than 80 years term unexpired when s13 notice served



---

---

---

---

---

---


---

---

www.lease-advice.org Page 27

### Marriage value

- Everyone's interest after minus
- Everyone's interest before



---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 28

### Valuing the current leasehold interest

- The importance of relativity



---

---

---

---

---

---

---

---


---

www.lease-advice.org Page 29

### Relativity

- The value of a dwelling held on an existing lease at any given unexpired term divided by the value of the same dwelling in possession to the freeholder, expressed as a percentage

*(RICS Research October 2009, Leasehold Reform Graphs of Relativity)*



---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 30

### Relativity



- Value freehold vacant possession value
- Work out what proportion of that value remaining lease should be
- Percentage/proportion = relativity

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 31

### Relativity



- Actual transactions
- Graphs based on tribunal decisions and settlement evidence
- Doing the best you can

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 32

### How to approach relativity?



- *Kosta v Carnwath (Trustees of the Phillimore Estate)* [2014] UKUT (LC)
- Leasehold Reform Act 1967

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 33

### Kosta - the facts



- Valuation date -13 October 2011
- 47 Phillimore Gardens
- 52.45 years unexpired
  - Importance of marriage value

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 34

### What did each side want?



- Lessee - 87.04% relativity
- Landlord - 75.5% relativity

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 35

### Relativity - what did the lessee rely on?



- Dr Bracke's statistical study
- Hedonic regression analysis of several market transactions between 1987 to 1991
- Resulted in higher relativity than relying on graphs

---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 36

### Relativity - what did the lessee rely on?

- Graphs published by the RICS



---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 37

### The lessee's argument

- Graphs prepared by others much less reliable than Dr Bracke's study
- Landlord produced no valuation evidence based on comparables



---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 38

### The landlord's argument

- Dr Bracke's study merely evidence of state of market in 1987 to 1991
- No grounds to believe study reflected present state of the market



---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 39

### What did the Upper Tribunal think?



- Dr Bracke's work stated to be "by common consent, a formidable piece of research"
- Point estimates of relativity for certain periods of unexpired lease were unrealistically high
- Tribunal wary of graph which appeared to be flat between 50 and 80 years

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 40

### What did the Upper Tribunal think?



- Did not consider Dr Bracke's evidence accurately reflected market at the valuation date

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 41

### What did the Upper Tribunal think?



- Considered drawbacks of graphs in RICS report
- However...

---

---

---

---

---

---

---


---

---

www.lease-advice.org Page 42

### What did the Upper Tribunal think?

- The RICS Graphs were well known at valuation date and would constitute an important ingredient in decision of hypothetical buyers at the valuation date as to how much to bid for existing lease



---

---

---

---

---

---


---

---

www.lease-advice.org Page 43

### What did the Upper Tribunal decide?

- The LVT had correctly decided a relativity of 76%



---

---

---

---

---

---


---

---

www.lease-advice.org Page 44

### The buyer's margin and relativity

- *82 Portland Place (Freehold) Limited v Howard de Walden Estates Limited*
- [2014] UK UT0133(LC)



---

---

---

---

---


---

---

---

www.lease-advice.org Page 45

### The facts



- 1920s mansion block in Marylebone
- 25 flats on basement, ground and eight upper floors
- Harley Street Conservation Area
- 14 had unexpired terms of 11.82 years
- 11 flats had extended leases expiring in 2111
- Owners of two flats not executed participation agreement or given Section 13 notice

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 46

### What did the LVT decide?



- Premium of £21,340,923, calculated at the relevant valuation date in September 2009

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 47

### 82 Portland Place - three valuation issues



- The no act world assumption
- Approaches to relativity
- The purchaser's margin

---

---

---

---

---

---

---


---

---



www.lease-advice.org Page 48

### The no act world assumption



- McHale v Earl Cadogan
  - [2010 ] EWCA Civ 1471
- Judgment of the Court of Appeal dated 21<sup>st</sup> December 2010
- In calculating marriage value is the leasehold interest valued with a no Act world assumption?
- Parties bound by judgment in case that was settled after Supreme Court granted leave to appeal

---

---

---

---

---


---

---

---

www.lease-advice.org Page 49

### Approaches to relativity



- Real world relativity could help in valuing existing leases even though for purposes of working out marriage value leases had to be valued in the no Act world on assumption 1993 Act did not apply

---

---

---

---

---


---

---

---

www.lease-advice.org Page 50

### Approaches to relativity



Ascertaining relativity in no Act world complicated by

- Passage of time
- Limited availability of reliable valuation data

---

---

---

---

---


---

---

---

www.lease-advice.org Page 51

### Approaches to relativity



- Evidence available to establish relativity of short leases to freehold vacant possession value of same flat in current conditions

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 52

### Approaches to relativity



- One of valuation methods for short leases in no Act world was to undertake adjustment to real world relativity established by evidence of market sales of short leases

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 53

### In a nutshell.....



- a) Establish real world relativity at relevant lease length
- b) Adjust to reflect hypothetical no Act world

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 54

### What did Upper Tribunal decide?

- Parties agreed that in real world leases with 11.82 years left and enjoying 1993 Act rights worth 41.25% of FHVP of same flat
- Discount to reflect no Act world

---

---

---

---

---

---

---

---

www.lease-advice.org Page 55

### The appropriate relativity

- Look at available graphs in PCL
- Average of figures produced by graphs was 33.5%
- Reinforced parties' experts evidence as to proper no Act world reduction

---

---

---

---

---

---

---

---

www.lease-advice.org Page 56

### The appropriate relativity

- Upper Tribunal decided appropriate discount for 93 Act rights where 11.82 years unexpired was 20%
- Therefore appropriate no Act relativity was 33% for calculating marriage value
  - $41.25\% \times 80\%$
- Tribunal restated the Nailrile orthodoxy

---

---

---

---

---


---

---

---

www.lease-advice.org Page 57

### The Nailrile orthodoxy



- One must do the best one can with real world evidence of relativity allowing for the benefit of the Act and with regard to the various graphs of no-Act world relativity

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 58

### The purchaser's margin



- Difference in value between amount that a dealer or an investor (the purchaser) would pay on reversion for the freehold of the building with vacant possession of the short leasehold flats and the aggregate value of those flats if sold individually to an end user

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 59

### The purchaser's margin



- Should the margin be deducted from the aggregate of all freehold vacant possession (FHVP) values?
- Bulk discount
- Reducing FHVP values by deducting professional costs and disbursements from those values
- Reflecting likely costs which the nominee purchaser might incur on re-sales

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 60

### The purchaser's margin



- Upper Tribunal decided not necessary to allow a further allowance in FHVP values

*“There is no statutory requirement to assume a further sale upon expiry of the short leasehold interests and we see no justification for the assumption of such a sale. The only sale required to be assumed is the valuation date”*

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 61

### Development potential



- *Padmore v Official Custodian for Charities*
- [2012] UKUT 0211(LC)
- Decision of the Upper Tribunal (Lands Chamber) dated 31 December 2013

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 62

### Padmore - the facts



- Semi-detached property in Barnet EN4
- Two maisonettes on separate leases
- Each had 61 years unexpired
- Both owned by Miss Padmore

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 63

### The issue



- To what extent the prospect of reconversion to a house could be taken into account when decided the price for collective enfranchisement

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 64

### What did the LVT decide?



- Rejected landlord's argument that could be taken into account as "development marriage value" when deciding the landlord's share of marriage value, by including a sum reflecting the nominee purchaser's ability to convert premises to a house at the valuation date
- Applied *Themeline Limited v Vowden Investments Limited*
  - [2011] UKUT 168 (LC)

---

---

---

---

---

---


---

---

---

www.lease-advice.org Page 65

### What did the LVT decide?



- Chance of reconversion could be taken into account as "development hope value" when valuing the freehold interest
- Assumption that hypothetical buyer of freehold interest would pay premium because of prospect/hope of being able to reach agreement with owner of leasehold interests to acquire those interests to enable reconversion to happen
- Decided price payable on that assumption was £150k
  - Agreed between parties

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 66

### What did the LVT decide?

- Miss Padmore appealed and argued that she would not be willing to co-operate in developing the premises
- Cross-appeal by landlord who argued Themeline wrongly decided and including development marriage value would produce price of £194k

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 67

### Decision of the Upper Tribunal

- Not open to Miss Padmore to challenge LVT on ground that gave insufficient weight to her personal views
- Credible that buyer prepared to pay premium to reflect development value as circumstances and intentions of Miss P might change

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 68

### Decision of the Upper Tribunal

- Common ground between parties before LVT that intentions of Miss P herself relevant to deciding value of freeholder's interest using development hope value
- This assumption correct as valuing freeholder's interest
- Parties taken to have had Miss P's personal intentions in mind when reached agreement on appropriate discount to use in calculating development hope value

---

---

---

---

---

---

---

---

---

www.lease-advice.org Page 69

## Decision of the Upper Tribunal

- Development marriage value would not be excluded
- No legitimate portion of value should be left out when deciding price
- Development value would be released immediately when Miss P able to marry freehold and her existing leasehold interests
- So premium would be £194,000

---

---

---

---

---

---

---

---

www.lease-advice.org Page 70

## Upcoming LEASE training

|  |                                 |
|--|---------------------------------|
| <b>Classroom training</b><br>25 March 2015 – London<br>1 April 2015 – Manchester | <b>Webinar</b><br>19 March 2015 |
|--|---------------------------------|

**Right to Manage**  
The Right to Manage is a very popular option for leaseholders who want to take over the management of their building. This right contains pitfalls for the unwary, which can cause substantial problems. This full day training course will detail these problems, and provide you with the knowledge to take your clients through these procedures with confidence

**Basic introduction to park homes legislation**  
The Mobile Homes Act 2013 aims to improve standards in the industry and give greater protection to mobile home residents. This webinar will take you through the main changes brought about by the legislation. It will touch on the buying and selling process, the new licensing powers that Local Authorities now have, site rule making process and pitch fee reviews

---

---

---

---

---

---

---

---

www.lease-advice.org

## Questions?

The Leasehold Advisory Service  
020 7832 2500  
info@lease-advice.org  
www.lease-advice.org  
Fleetbank House, 2-6 Salisbury Square  
London EC4Y 8JX

---

---

---

---

---

---

---

---