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RESIDENTIAL PROPERTY TRIBUNAL (WALES)

LEASEHOLD VALUATION TRIBUNAL

TRIBUNAL

D J Evans LLB LLM
Ceri Trotman Jones MRICS
Roger Baynham FRICS

In the matter of 4A Downing Street, Newport NP19 0JJ
In the matter of an application under S.21(1)(a) of the Leasehold Reform Act 1967

APPLICANTS: Alun David Copeman, Leslie Roy Parfitt and Alan Collett

RESPONDENT: Person Unknown

DECISION

INTRODUCTION

1 We convened as a Leasehold Valuation Tribunal under the provisions of the Leasehold Reform Act 1967 (as amended)(the Act) on the 12th September 2012. We had before us an Order of the Newport (Gwent) County Court dated the 29th May 2012 transferring an application made by Mr Copeman, Mr Parfitt and Mr Collett (the Applicants) to the Leasehold Valuation Tribunal to make a determination of the value of the freehold interest in 4A Downing Street Newport NP19 0JJ (the Property).

BACKGROUND

2 The Applicants are the leasehold proprietors of the Property and wish to acquire the freehold pursuant to the Act. After exhaustive enquiries made on the Applicants' behalf, the freeholder of the Property cannot be found. On the 27th April 2012, the Applicant made an application to the Newport (Gwent) County Court claiming the right to purchase the freehold and on the 29th May 2012, the Court made the order referred to in paragraph 1.

LEASE

3 The Lease of the Property is dated the 28th August 1933. It was made between Rutherford Joe Bath (1) and Tom Henry David Higgs (2). It is for the term of 99 years from the 25th March 1933 at a yearly ground rent of £3.25 payable half yearly. The unexpired term is just under 20 years from the date of the application to the Court. The lease contains a requirement for the lessee to build a dwelling house together with the usual covenants for the lessee to pay the outgoings, insure the Property and maintain it.

INSPECTION

4 Prior to hearing the application, we inspected the Property internally and externally. We were accompanied on our visit by Mr Copeman. The tenants of the Property were also present. The Property is a semi -detached house constructed approximately 80 years ago. A small walled forecourt sets the house back slightly from the pavement. The building has cavity walls, a spa-dash rendered exterior and a hipped concrete tiled roof. The chimneys have been removed. There is a ground floor extension at the rear with a pitched roof. The plot upon which the house is built is relatively small.

5 The Property is located in a residential area on the eastern side of Newport with some local shopping and a supermarket reasonably close by. Most of the other houses on both sides of Downing Street are terraced.

6 Downstairs in the house, there is a living room as well as a large fitted kitchen and dining area which incorporates the original back room of the house and the extension. The stairs lead from the hallway to the landing. Upstairs, there are two bedrooms, one double and one single, and a bathroom. The property is double glazed and centrally heated. There is an enclosed very small rear garden which backs on to the rear garden of a property in the next street.

REPRESENTATIONS

7 The Applicants indicated that they wished the application to be dealt with by way of representations and without a hearing. We had before us a report from Mr Stephen Parker FRICS of Nuttall Parker, Chartered Surveyors, Newport. The report is dated the 10th July 2012. In it, he has followed the methodology adopted in the recent decision of the Upper Tribunal in Clarice Properties Limited [2012] UKUT 4(LC)(the President and Mr N J Rose FRICS) (Clarice). We had invited Mr Parker to consider the manner in which this Tribunal had followed Clarice in the case of 19 Plasmarl Terrace, Plasmarl, Swansea SA6 8LU (Plasmarl). Having applied the Plasmarl methodology, he considered that it made little difference to the final figure, although he did not provide us with either the breakdown or the final figure.

8 In his report, Mr Parker has capitalised the ground rent at 6½% and applied the three-stage valuation process - what is sometimes referred to as the Haresign approach (named after the Lands Tribunal's decision in Haresign –v- St John the Baptist's College Oxford (1980) 255 EG 711). He has put the entirety value of the Property at £70,000, used the Clarise rate of 5½% for de-capitalisation, recapitalisation and deferment and deducted 20% from the standing house value to take account of the possibility that the reversioner may not obtain vacant possession at the end of the lease. Mr Parker's resulting figure is £8,075.

CONSIDERATION

9 Section 9(1) of the Act makes it clear that our role is to determine "the amount which at the relevant time the house and premises, if sold in the open market by a willing seller (with the tenant and members of his family...not buying or seeking to buy) might be expected to realise..." We are required to make certain assumptions one of which is that the Property is being sold freehold but subject to the lease which, if it has not already been extended, has been extended. In other words the assumed term expires 50 years after the contractual term date. Here, the contractual term ends in 2032 so that assumed date when the lease will expire is in March 2082.

10 Until Clarice, the standard practice was to apply the two-stage approach unless the three stage approach produced a valuation which was "significantly higher" (per Mr N J Rose FRICS in Freehold Properties Ltd's Appeal [2009] UKUT 172 (LC)) or where the circumstances "warrant this exception" (per Mr P H Clarke FRICS in Marlodge (Monnow)'s Appeal (LRA/28/2002)). The two stage

approach would generally be used where there were, say, over 50 years to run on the lease so that the deemed expiry date was over 100 years into the future. The decision in Clarice was a conscious decision on the part of the President and Mr Rose to change "the standard practice in section 9(1) valuations and to apply instead the three-stage approach". Its reasons for so doing are set out in paragraph 36: "As a matter of good valuation practice, where a price has to be determined, every element of value should in general be separately assessed unless there is some good reason not to do so....The only relevant question is whether the reversion does have a significant value". As there were only approximately 20 years from the valuation date to the end of the term, it was always likely that the market would adopt the Haresign approach as opposed to the two stage approach when valuing the reversion.

DETERMINATION

Date of Valuation

11 We have considered our decision on the basis that the valuation date is the 27th April 2012 being the date when the application was made to the Court. The lease is for 99 years from the 25th March 1933 which means therefore there were approximately 20 years unexpired. For the ease of calculation and use of the tables, we shall employ the figure of 20 years rather than the 19 years 11 months used by Mr Parker.

Capitalisation Rate

12 Mr Parker has used a capitalisation rate for the ground rent of 6½ %. An investor purchasing the asset will bear in mind that the return of £3.25 is very small and there are administrative costs associated with the collection of the ground rent which will need to be factored in. In our view, a figure of 6½% is not unreasonable and in keeping with other decisions of this Tribunal. This produces a value of £35.81.

Entirety Value of the Property

13 Although we are acquainted with the cost of development land as well as single plots, we had no comparable evidence of land values relating to properties of this nature within the Newport area. We agree with Mr Parker that it is appropriate to proceed by way of the "Standing House" method. In his report Mr Parker provides two comparable properties in Downing Street as evidence to assist us. Following our inspection of the Property, we took the opportunity to look at these comparables from the outside only. Number 17 Downing Street was sold for £54,000 in April 2012 and number 34 for £70,000, again in April 2012. The lower priced property was a part exchange property sold by a national builder, something which will have influenced the price. Both properties were terraced but with gardens larger than that at 4A which had the advantage of being semi- detached. Number 17 had three bedrooms, but no forecourt, and the bathroom was on the ground floor. Using our knowledge and experience, we agree with Mr Parker that the entirety value of the Property on the basis that the house was modernised, in good condition and with the site fully developed, was £70,000 as at the valuation date.

Plot Value

14 Mr Parker suggests a plot value of 30% of the entirety value. For many semi-detached properties in this area, that would be appropriate. However, we must take into account the size of the plot. There is very little of the plot which is not built upon. The building cost would represent a relatively higher proportion of the entirety value in the market than a house built on a larger plot.

We consider 27½ % of the entirety value to be appropriate. This is in line with the decision of this Tribunal in the case of 5A Downing Street, the next door property. We therefore determine the plot value to be £19,250.

De-capitalisation/Recapitalisation/Deferment Rates

15 Mr Parker has applied a rate of 5½ % for de-capitalisation, the process to ascertain the modern ground rent. In doing so, he has adopted the rate used in Clarice. Although he provides no evidence to support that rate, as a general rule it does not matter what rate is used for de-capitalisation provided the same rate is used for recapitalisation in perpetuity. However, in the three stage approach, where the modern ground rent is only recapitalised for 50 years, the rate used can be significant. Further, it is important that whatever rate is determined for de-capitalisation must be used for recapitalisation. (See Lord Denning MR in Official Custodian for Charities and Others –v- Goldridge (1973 26 P & CR 191): "They should adopt the same percentage for re-capitalisation as for de-capitalisation. This is a better way of finding 'fair terms'"). Using a different rate for recapitalisation produces an unfair advantage to one side or the other – sometimes known as an adverse differential. Deferring the recapitalised value is a different step in the process. Different considerations can apply. Indeed, for many years, Tribunals used a different rate for deferment than that used for de-capitalisation and recapitalisation. In Clarice, however, the Upper Tribunal suggested that the deferment rate determines all three rates. It is important point to note that the Upper Tribunal provides "guidance" as part of its function in order to maintain a consistency of decision making throughout England and Wales (see the comments of Carnwath LJ in Cadogan –v- Sportelli [2007] EWCA Civ 1042 (Sportelli)). It is, nonetheless, "guidance" and not a "constraint". Leasehold Valuation Tribunals (LVTs) comprise local professionals and lay members who have knowledge and experience of the areas in which they sit. It is simply not possible for the Upper Tribunal to cater for every situation which arises in the diverse communities covered by all LVTs. In Plasmarl, this Tribunal considered the proposition that the deferment rate determined the other two rates but was not persuaded that the process for determining the modern ground rent – which can be independent of the acquisition of a freehold reversion – should be governed by the deferment rate. As the Tribunal pointed out in Plasmarl, the effect could be that two identical properties are assessed as having different modern ground rents simply because one is a basic modern ground rent calculation and the other is part of a freehold purchase. Such matters must always be a question of fact and depend on the circumstances of the case. Rates of return in the market are currently at a low level, although they may not always remain this low. Returns from property are affected by economic conditions and landlords are accepting lower rents in order to keep premises tenanted. On the other hand, the modern ground rent is fixed for a long period and so the market will adopt a rate which will factor in the possibility of higher returns at some point in the future. Using our knowledge and experience, we consider that a rate of 5% for de-capitalisation and recapitalisation is both in line with the market as well as other decisions of this Tribunal. In our view this produces a fair assessment of the modern ground rent attainable for the Property.

16 In Clarice, the Upper Tribunal endorsed a deferment rate of 5½% and Mr Parker has adopted this in his report. In Clarice this was the rate which the parties had agreed should apply as the deferment rate when the matter came before the Leasehold Valuation Tribunal. The Upper Tribunal used the Sportelli deferment rate of 4¾% as its starting point (see Cadogan –v- Sportelli [2007]1EGLR 153). Accepting the evidence of Mr Geraint Evans, the Appellant's surveyor, the Upper Tribunal determined that the prospects for capital growth were lower in the West Midlands than in Prime Central London (PCL) and increased the Sportelli rate by ½% to 5¼%. It regarded this as being in line with the Upper Tribunal decision in Zuckerman –v- Trustees of the Calthorpe Estate [2010]1 EGLR 187 (Zuckerman). However, it then added a further ¼% to the deferment rate because there was no reason why the risk of deterioration was less in respect of the appeal property than was the case in Zuckerman. It determined a deferment rate of 5½%. It justified departing from its decision in

Mansal Securities Ltd (LRA/185/2007)(Mansal) because it was now deferring to a standing house value and not, as in Mansal, a site value.

17 In Mansal, the Upper Tribunal (Mr Rose) had increased the Sportelli rate by ¼% on the grounds that "since the reversion in the case of a section 9(1) is to ground rent only, a potential purchaser is likely to require a higher risk premium to compensate for the increased volatility and illiquidity than if the reversion also included a house standing on the site" (paragraph 27). The difference between Mansal and Clarice is that in Clarice, the Tribunal accepted the evidence on the issue of growth. In Mansal, the Sportelli rate is increased to provide for the illiquidity factor when selling a ground rent or plot; in Clarice, it is increased to cover the possibility of greater deterioration relative to value for properties outside PCL. In Mansal, although the Appellants had argued that the prospects for growth in the West Midlands were less than in PCL, Mr Rose was not persuaded on the basis of the evidence adduced.

18 In the present case, we have no evidence concerning the different rates of growth between Newport and PCL and in the absence of such evidence, as in Mansal, we do not consider it appropriate to depart from the Sportelli rate for that reason alone. We do accept, however, that properties in the Newport are at greater risk of deterioration relative to value than properties in PCL and, following Clarice, that the market would adjust the deferment rate by ¼% to accommodate this. We therefore adopt the rate of 5% as the rate to defer the recapitalised ground rent to the contractual end of the lease term (20 years). This has the effect of valuing what is sometimes referred to as the first reversion at £6,622.44.

Standing House Value

19 The final stage in the valuation process is to determine the value of the Property and defer that figure for the period of the contractual term plus the deemed 50 year extension as prescribed by the Act. For this we use the value of the Property in its existing form as at the valuation date. The entirety value is based upon the assumption that the Property is in good repair and condition. In reality the Property is in good condition having undergone a recent refurbishment. Mr Parker uses the same figure as for the entirety value and we agree with that approach. We determine that the standing house value is £70,000.

Schedule 10 of the Local Government Act 1989 (Schedule 10)

20 The last issue which the Upper Tribunal dealt with in Clarice was to assume that Schedule 10 of the Local Government and Housing Act 1989 (the 1989 Act) would apply to the tenancy created by the lease. Under the 1989 Act, the original tenancy automatically continues until notice is served under paragraph 4 of Schedule 10. The lessee is then entitled to an assured tenancy under the Housing Act 1988 at a market rent. The reversioner will therefore not be certain that it will obtain vacant possession. In Clarice, the Upper Tribunal held that that uncertainty would have a depressing effect upon the value of that reversion. It commented that whilst "the purchaser of the freehold reversion would have no means of knowing whether vacant possession would be gained at the end of the 50 year lease extension"..."the fact that there can be no certainty of obtaining vacant possession would have a significant depressing effect on value..." Without the benefit of comparable evidence, the Upper Tribunal deducted 20% from the "full standing house value" of the Property.

21 This issue had been considered previously by the Lands Tribunal in Vignaud –v- Keepers and Governors of John Lyon's Free Grammar School (LRA/9 & 11/1994)(Vignaud) and by the Upper Tribunal in Sillvote Ltd –v- Liverpool City Council [UKUT] 192 (LC) (Sillvote). In the former case, HH Judge Rich accepted a deduction of 10% to reflect "the remote risk that [the leaseholder] or some assignee in the last ten months of the term might" exercise her rights under Schedule 10 and remain in possession even though he was "virtually certain" that the leaseholder would not exercise those

rights. In his decision, HH Judge Rich stated that "the proper deduction for this right must be a matter of evidence or agreement". In Sillvote, where there were 11 years remaining on the lease, Mr P R Francis FRICS stated that the question was "whether, as a matter of evidence, there is a likelihood that the lessee will exercise that right". He held that there was no evidence and consequently made no deduction. Following that decision, in Cardiff County Council –v- The Estate of Alice Zelia David (3 Ovington Terrace, Cardiff)(reference QA 976565) this Tribunal also held that it had no evidence upon which to base a deduction from the house value to take account of the lessee's Schedule 10 rights. After the decision in Clarice, however, this Tribunal, in Plasmarl, did not consider that the market would factor in a deduction as high as 20% to take account of the possibility that a lessee might retain possession with the benefit of an assured tenancy. It considered the appropriate deduction to be 10% - significant enough to take account of the possibility of those rights being exercised, but not such as to over compensate bearing in mind that the rights were only exercisable in 66 years' time and indeed might not be exercised at all.

22 Mr Parker has followed Clarice and applied a 20% deduction, but he has not provided any justification or evidence to support his contention. In this case, the extended lease term ends approximately 70 years after the valuation date. Following the Upper Tribunal's guidance, we conclude that a significant deduction needs to be made from the standing house value in order to take account of the lessee's Schedule 10 rights. The amount of such deduction is preferably to be based upon evidence, but, as with Clarice, we have none. We must therefore rely upon our knowledge and experience. The value of the Schedule 10 rights is essentially a question of judgment. Whilst there is a wait of 8½ years less than in Clarice before the Schedule 10 rights take effect, the value of the property in this case is less than half that in Clarice. We do not believe that the market would make an adjustment as high as 20%. As with Plasmarl, we consider 10% to be the appropriate figure. This produces an adjusted standing house value of £63,000.

23 Applying the same deferral rate of 5% as above, the second reversion is valued at £2,070.57 to which we add the capitalised current ground rent of £3.81 and the value of the first reversion of £6,622.44 making a total of £8,728.82, say £8,730. We have set out the figures below.

DECISION

24 Freehold Valuation

Applying the findings that we have made above, we calculate the value of the freehold of 4A Downing Street, Newport, NP19 0JJ as follows:

Ground Rent	£3.25		
20 years purchase @ 6.5%	11.0185		£35.81
Entirety value	£70,000.00		
Plot value @27½ %	£19,250.00		
Modern Ground Rent @ 5%	£ 962.50		
Yrs. Purchase 50 yrs @ 5%	18.2559	£17,571.30	
Present value of £1 in 20 years @ 5%		0.3768895	£6,622.44
Standing house value	£70,000.00		
Less Schedule 10 rights @ 10%	£7,000.00		
Adjusted value	£63,000.00		
Present value of £1 in 70 years @ 5%	0.0328662		£2,070.57
			£8,728.57
		Say	£8,730.00

25 Ground Rent Arrears

We respectfully draw the attention of the County Court to the provisions of Section 27(5)(b) of the Act, substituted by section 149 of the Commonhold and Leasehold Reform Act 2002, which requires the leaseholder to pay "the amount or estimated amount ....of any pecuniary rent payable for the house ...which remains unpaid". The amount so payable can only be the amount for which the freeholder can enforce payment. If it were otherwise, a leaseholder of an untraced freeholder would be required to pay more than a leaseholder whose freeholder's identity was known. The maximum recoverable is £3.25 a year for the period of 6 years, namely £19.50. However, this was not an issue referred to us and so the actual amount of ground rent payable by the Applicant is a matter for the County Court.

Dated this 19th day of September 2012

Chairman