UPPER TRIBUNAL (LANDS CHAMBER)

UT Neutral citation number: [2011] UKUT 154 (LC)
LT Case Number: LRA/128/2007
LRA/17/2008
(Consolidated)

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LEASEHOLD REFORM – collective enfranchisement – price payable – whether hope value in respect of non-participating flats including caretaker's flat – relativity – use of graphs or adjustment to market comparables to allow for benefit of Act – effect of user restriction upon rental value of caretaker's flat – assessment of valuation evidence and of comparables – meaning of "taking into account" a section 42 notice served by a non-participating tenant – form of the covenant restrictive of user which should be imposed – meaning of "participating tenant" for purposes of marriage value – Leasehold Reform, Housing and Urban Development Act 1993 Sch 6 paras 3 and 4

IN THE MATTER OF APPEALS AGAINST THE DECISION OF THE LEASEHOLD VALUATION TRIBUNAL OF THE LONDON RENT ASSESSMENT PANEL

BETWEEN	**(1) THE EARL CADOGAN** **(2) CADOGAN ESTATES LIMITED**	**Appellants** **(LRA/128/2007)**
	and	
	CADOGAN SQUARE LIMITED	**Respondent**
AND BETWEEN	**CADOGAN SQUARE LIMITED**	**Appellant** **(LRA/17/2008)**
	and	
	(1) THE EARL CADOGAN **(2) CADOGAN ESTATES LIMITED**	**Respondents**

Re: 38 Cadogan Square, London SW1

Before: His Honour Judge Reid QC
and
A J Trott FRICS

Sitting at: 43-45 Bedford Square London WC1
on 11, 12, 15 and 16 November 2010

Kenneth Munro, instructed by Pemberton Greenish LLP, for The Earl Cadogan and Cadogan Estates Limited
Stephen Jourdan QC, instructed by Forsters LLP, for Cadogan Square Limited

The following cases are referred to in this decision:

Earl Cadogan v Sportelli [2007] 1 EGLR 153 (Lands Tribunal); [2008] 1 WLR 2142 (Court of Appeal); [2008] UKHL 71 (House of Lords)
Bircham v Clarke [2006] Lands Tribunal LRA/63/2005 (unreported)
Chelsea Properties Limited v Earl Cadogan [2007] Lands Tribunal LRA/69/2006 (unreported)
Blendcrown Limited v Church Commissioners for England [2004] 1 EGLR 143
31 Cadogan Square Freehold Limited v The Earl Cadogan [2010] UKUT 321 (LC)
Lloyd-Jones v Church Commissioners [1982] 1 EGLR 209
In re Shulem B Association Ltd's Appeal [2001] 1 EGLR 105
Culley v Daejan Properties Limited [2009] UKUT 168 (LC)
Arbib v Earl Cadogan [2005] 3 EGLR 139
Nailrile v Earl Cadogan [2009] RVR 95
Arrowdell Ltd v Coniston Court (North) Hove Ltd [2007] RVR 39
Plinth Property Investments Ltd v Mott, Hay & Anderson (1977) 38 P&CR 361 (CA)
Crammond v Theodore Gregory Limited [2004] LON/SC/00AW/NSI/2003/0076 (LVT) (unreported)
Sterling Land Office Developments Ltd v Lloyds Bank plc [1984] 2 EGLR 135
Earl Cadogan v Cadogan Square Ltd [2005] LON/ENF/1800/06 (LVT) (unreported)
McHale v Earl Cadogan [2010] EWCA Civ 1471
Moreau v Howard de Walden Estates Limited [2003] Lands Tribunal LRA/2/2002 (unreported)
Higgs v Paul [2005] Lands Tribunal LRA/2/2005 (unreported)
Peck v Trustees of Hornsey Parochial Charities (1971) 22 P & CR 789
Le Mesurier v Pitt (1972) P & CR 389

The following cases were referred to in argument:

*Donath and another v Second Duke of Westminster's T*rustees [1997] 1 EGLR 203
Cadogan v Pockney [2004] Lands Tribunal LRA/27/2003 (unreported)
Cadogan v Cecil [2001] Lands Tribunal LRA/10/2000 (unreported)
Sterling Land Office Developments Ltd v Lloyds Bank plc [1984] 2 EGLR 135
Dependable Homes Ltd v Mann [2009] UKUT 171 (LC)

DECISION

Introduction

1. In this case there are two appeals, one (LRA/128/2007) by the landlords, Earl Cadogan and Cadogan Estates Limited ("Cadogan") and the other (LRA/17/2008) by the nominee purchaser, Cadogan Square Limited ("the Nominee Purchaser"). The appeals are against the decision of the Leasehold Valuation Tribunal ("LVT") dated 3 July 2007, as corrected by a correction certificate dated 26 July 2007, in respect of the terms of enfranchisement of 38 Cadogan Square, London SW1 ("the Property"). By its corrected decision the LVT determined that the enfranchisement premium payable in respect of the freehold of the property was £1,836,419 and in respect of the intermediate landlord's interest was £52,266, making a total of £1,888,685. It also determined the terms of a restrictive covenant to be included in the transfer. These appeals relate to a number of issues arising from the LVT's valuation and as to the terms of the restrictive covenant.

2. Mr Kenneth Munro of counsel appeared for Cadogan and called Mr Cerian Jones BSc FRICS, a partner at Cluttons LLP. Mr Stephen Jourdan QC of counsel appeared for the Nominee Purchaser and called Mr Gavin Buchanan BSc MRICS, a partner in Knight Frank LLP.

3. We made an accompanied inspection of flats 1 and 2 of the Property and of flat 5 at 70-72 Cadogan Square on 15 November 2010. We also made unaccompanied external inspections of a number of comparables in Cadogan Square.

Facts

4. 38 Cadogan Square is a mid-terrace late Victorian building of traditional construction on basement, ground and four upper floors. It is located just off the north-west corner of Cadogan Square and has oblique views of the communal gardens in the centre of the Square. The building lies within the Hans Town Conservation Area and is Grade II listed. There is a raised garden at the rear of the property, which backs onto a rear mews house, 44 Clabon Mews, which is not included in the claim.

5. The building is approached via stone steps up from the pavement. The communal front door opens into an entrance hall leading to a lift and staircase to upper floors and basement. The lift serves all floors and it opens directly into the fourth floor flat (flat 5). The building has been converted into six self-contained units including a caretaker's flat in the basement.

6. The property is the subject of a headlease for a term of 62.5 years from 29 September 1960 expiring 25 March 2023, at a rent of £775 per annum without review. This lease is vested in the Nominee Purchaser.

7. The headlease requires the property to be used as a self-contained flat on each of the upper floors, a self-contained maisonette on the ground floor and rear of the basement, a self-contained flat for the caretaker in the front of the basement, and tenants' stores and boiler room in the basement.

8. In the underleases of flats 1, 2 and 3 the headlessee covenants to provide a resident caretaker but there is no specific provision enabling the headlessee to recover notional rent on the caretaker's flat. The service charge contribution payable by flat 1 is 3/11^{ths} of the total. The contribution of flats 2 and 3 is each 2/11^{ths} of the total expenditure.

9. The underlease of flat 4 permits the headlessee to provide such caretaking staff as it deems necessary and where accommodation is provided for the residence of such a person, a sum equivalent to the market rent of such accommodation can be recovered from the underlessee. The service charge contribution of this flat is such percentage as the lessor considers appropriate. It is agreed for the purposes of these appeals that the share of service charge applicable to flat 4 is 2/11^{ths} of the total expenditure.

10. In the underlease of flat 5, the headlessee covenants to provide a resident caretaker and can recover the rack rent letting value of the caretaker's flat. The service charge contribution of this flat is 2/11^{ths} of the total expenditure.

11. The headlease requires the headlessee to provide for the premises a full time caretaker who shall reside in the caretaker's flat on a service basis.

12. All of the underleases are on internal repairing terms and provide for the payment of a service charge relating to the maintenance, repair and insurance of the building.

13. By an originating application dated 8 November 2005 Cadogan sought determination by the LVT of the premium to be paid for the Property and the terms of the freehold transfer of the Property. It was stated that no terms had been agreed between the parties and that Cadogan considered the appropriate price to be a total of £3,366,225. This sum comprised £3,356,910 for the freehold of the specified premises, £5,000 for the freehold of appurtenant premises and £4,315 for the intermediate landlord’s interest.

14. The initial notice, dated 21 June 2005, had been served on Cadogan and on the intermediate landlord (named as 38 Cadogan Square Limited) by qualifying tenants of flats 1, 2 and 5 (being three of the six flats at the Property). The participating tenants were identified as Cadogan Square Limited (flat 1), Ms Sibel Erkman (flat 2) and Baron Renwick (flat 5). The notice claimed the freehold of No.38 itself (as the specified premises) and of basement vaults and the garden area (under section l(2)(a) of the 1993 Act). It also proposed acquisition of the headlease.

15. The purchase price proposed totalled £1,299,350, which sum comprised:

(i) £1,294,650 for No.38;

(ii) £200 for the vaults and garden; and

(iii) £4,500 for the headlease

The Nominee Purchaser was named as such but no other terms of acquisition were proposed.

16. Cadogan served a counter-notice dated 6 September 2005 on the Nominee Purchaser admitting the right to enfranchise of the participating qualifying tenants. The notice stated that the proposed purchase price was not acceptable and counter-proposed the price of £3,366,225. The counter-notice also contained proposals for the transfer to the Nominee Purchaser to include provisions as to certain rights, exceptions, reservations, covenants and declarations.

17. The then tenants of flat 1, Mr and Mrs Stille, had previously served on Cadogan a notice dated 29 March 2004 claiming a new/extended lease under section 42 of the 1993 Act and proposing a premium totalling £382,700. On 21 April 2004 they assigned their lease of flat 1 to the Nominee Purchaser together with the benefit of the section 42 notice. Cadogan served a counter-notice dated 3 June 2004 on the Nominee Purchaser admitting the claim but counter-proposing a premium totalling £605,800. The Nominee Purchaser became registered as proprietor of the leasehold interest in flat 1 on 18 June 2004 for a price stated as £792,500. This lease extension claim was suspended during the currency of the collective enfranchisement claim as was a similar claim relating to flat 2 (see section 54(2) of the 1993 Act).

18. Ms Erkman, the tenant of flat 2, served on Cadogan a notice dated 2 July 2004 claiming a new or extended lease under section 42 of the 1993 Act and proposing a premium totalling £299,100. Cadogan served a counter-notice dated 1 September 2004 admitting the claim but counter-proposing a premium totalling £529,300. By a transfer dated 25 May 2006, Ms Erkman assigned her lease of flat 2 to Amej Properties Limited (a company in which she and/or members of her family apparently had an interest) together with the benefit of the section 42 Notice. That company became registered as proprietor of the leasehold interest in that flat without any monetary consideration being stated. Subsequently, the Nominee Purchaser served a notice, apparently dated 22 November 2006, on Earl Cadogan notifying him of the assignment and that the assignee company had not become a participating tenant in accordance with section 14(8)(a) of the 1993 Act.

Agreed valuation matters

19. A number of valuation matters were agreed between the parties. They were as follows:

(i) Valuation date: 22 June 2005.

(ii) The Gross internal floor areas of the flats:

Flat 1	Ground floor and rear basement	1,550 sf
Flat 2	First floor	1,224 sf
Flat 3	Second floor	1,182 sf
Flat 4	Third floor	882 sf
Flat 5	Fourth floor	716 sf
Caretaker's flat	Basement	798 sf
Boiler room & corridor	Basement	295 sf

(iii) The capitalisation rate to be used for the headlessee's ground rent is agreed at 6%, 3% and 30% tax. The capitalisation rate to be used for the freeholder's interest is 6%.

(iv) The open market rental value of the caretaker's flat without the user restriction is £15,600 pa. It is agreed that with a restriction limiting the use to that of a caretaker's flat the rental value is £7,800 pa.

(v) Values are to be adjusted for time using the Savill's Prime Central London South West Flats Index ("the Savills Index"). The agreement to use this index only extends to comparables sold no later than June 2006.

(vi) The following freehold values are agreed:

Flat 3: £1,070,750

Flat 4: £772,500

Flat 5: £595,000

Although it did not appear in the agreed statement of facts the parties have also agreed the freehold value of the caretaker's flat at £411,049.

Issues on the appeals

20. The parties identified the subsisting issues in the appeals as being the following:

18.1 *Cadogan's appeal*:

(1) Hope value in respect of the non-participating flats

(2) Relativity and the value of rights under the Act

(3) Hope value in relation to the caretaker's flat

(4) The letting value of the caretaker's flat

(5) The valuation date used for flat 1

(6) Whether tenants' improvements and/or Act rights are to be disregarded in valuing the existing leases of participating flats for the marriage value calculation

(7) The freehold value of flat 1

(8) The freehold value of flat 2

18.2 *Nominee Purchaser's Appeal*

(9) The deferment rate

(10) The terms of the restrictive covenant as to user to be inserted in the transfer

(11) Valuation of flat 2: whether the s.42 notice given before the s.13 notice should be taken into account.

Issue (1): Hope value in respect of the non-participating flats

21. The parties agreed that flats 3 and 4 are non-participating flats. There is no such agreement about flat 2 which is considered separately under issue (11) below. Our conclusion on that issue is that, for the purposes of Schedule 6 paragraph 3 of the 1993 Act, the tenant of flat 2 is a participating tenant.

22. The LVT considered the issue of hope value as a point of law, following the decision of this Tribunal in *Earl Cadogan v Sportelli* [2007] 1 EGLR 153, as subsequently upheld by the Court of Appeal ([2008] 1 WLR 2142). The LVT excluded hope value from valuations under Schedule 6 of the 1993 Act. The House of Lords ([2008] UKHL 71) reversed the decision of the Court of Appeal and held that, in valuing the freeholder's interest under Schedule 6 paragraph 3 of the 1993 Act, it is possible to take into account the hope of granting new leases of individual flats to non-participating tenants and thereby releasing marriage value. The House of Lords at paragraph 69 of *Sportelli* agreed with the Lands Tribunal's method of calculating hope value which the Tribunal said should be based upon a proportion of marriage value rather than an adjustment to the deferment rate. It is therefore necessary to consider whether there is any hope value attributable to the freehold interest in flats 3 and 4 but not in flat 2 which we find to be a participating tenant for these purposes.

Evidence

23. Mr Jones said that hope value existed and he took it as 25% of the marriage value, namely the difference between the freehold vacant possession value of flats 3 and 4 and the sum of the freeholder's, intermediate landlord's and underlessees' current interests. He calculated the marriage value to be £241,219 and the hope value £60,305.

24. Mr Jones relied upon the sale of two major residential estates to support his figure of hope value. Firstly, he referred to the evidence of Mr Roland Cullum in *Bircham v Clarke* [2006] Lands Tribunal LRA/63/2005 (unreported), one of the conjoined *Sportelli* appeals. This showed that the Wellcome Trust had included 20% hope value in the price it paid to acquire the South Kensington Estate in 1995. This figure was accepted by the Tribunal.

Secondly, he referred to the sale of the Thurloe Estate in South Kensington in 2007 where his firm, Cluttons, had acted for an unsuccessful purchaser. That purchaser offered a price which included 30% hope value. On Cluttons' analysis the winning bid indicated hope value of approximately 50% of marriage value.

25. Mr Jones considered that there was every likelihood that the non-participating tenants would seek lease extensions "in the not too distant future". Purchasers of short leaseholds commonly required the vendor to submit a section 42 notice under the 1993 Act and he said that it was almost unheard of that a tenant would allow his lease to expire.

26. In cross-examination Mr Jones explained that he had increased his allowance for hope value by 5% to 25% to reflect the prospect that a purchaser of the freehold interest would be able to secure more than 50% of the marriage value in negotiations with the tenant. He said that there was no cap on the amount of marriage value that a freeholder could obtain in the no Act world and that it was a "potential goldmine" for a freeholder to deal with tenants who had no right to extend their lease.

27. Mr Jones accepted that the Lands Tribunal in *Chelsea Properties Limited v Earl Cadogan* [2007] Lands Tribunal LRA/69/2006 (unreported) did not accept the evidence of the sale of the South Kensington Estate. He also acknowledged that he had not been a party to the bid that Cluttons had prepared for the Thurloe Estate. In 2009 he had read the report that his colleague, Mr Glover, wrote to the client in 2006/07, recommending a purchase price. He was unable to verify the eventual sale price of £42 million, details of which he had obtained from another colleague, Mr Simon Scott-Barrett, who, he said, had "tracked the sale".

28. Mr Buchanan said that the decision of the House of Lords in *Sportelli* to allow hope value in respect of non-participating tenants was one of law and that hope value should only be allowed if there was evidence to support it. He was unaware of any such evidence in this appeal and he did not consider it appropriate to add any hope value.

29. He referred to this Tribunal's decision in *Chelsea Properties* where he gave evidence for the appellant tenant (although not on this point). That appeal was factually similar to the present appeal in several respects. It involved the grant of a new lease of a first floor flat at 70-72 Cadogan Square which was subject to a lease with an unexpired term of 18.7 years. The valuation date was 2 July 2004. The Tribunal, His Honour Judge Huskinson and N J Rose FRICS, found on the evidence that the respondent landlord had not proved the existence of any hope value in the landlord's reversion on the existing underlease.

30. Flat 4 was held on a lease with an unexpired term of more than 80 years so there would be no marriage value payable and no expectation of hope value. Flat 3 was sold to the current owners in 2005 by a tenant who was qualified to serve a section 42 notice. No such notice was served and the new owners, who themselves became qualifying tenants in 2007, had still not served one. Mr Buchanan concluded that they had no interest in extending the lease. He was aware of a number of short leases in Cadogan Square where tenants had neither claimed

a new lease nor joined in a collective enfranchisement and where they seemed intent on living out their days without making any such claim.

Discussion

31. We begin our discussion of this aspect of hope value by considering whether there is likely to be any such value included in the price a purchaser would pay for the freehold interest in flat 4 which had an unexpired term of nearly 108 years at the valuation date.

32. We accept Mr Munro's submission that Mr Buchanan's reference to 80 years as a cut-off point is not relevant in the context of the assessment of hope value in this appeal. That cut-off point only applies to marriage value in respect of participating tenants in the Act world. But Mr Munro's submission that a tenant with a lease of 108 years unexpired would be interested in seeking a lease extension was an assertion which was not supported by any evidence from Mr Jones. Although he did not provide a separate calculation of the hope value attributable to flat 4, the amount of such hope value, even taken as 25% of the marriage value, would have been insignificantly small. We do not accept that the tenant of flat 4 would have been interested in extending his lease further and we make no allowance for hope value in respect of it.

33. Mr Buchanan assumes that because a section 42 notice was not served either before or after the current owners purchased flat 3 in 2005 they had no interest in extending the lease. We do not accept that conclusion. As Mr Munro pointed out, the benefits to a tenant consist of more than a share of the potential marriage value and comprise a "bundle of advantages to the tenant", some of which, such as the desire to retain one's home or to benefit fully from improvement expenditure, are likely to increase as the length of the term declines.

34. In *Blendcrown Limited v Church Commissioners for England* [2004] 1 EGLR 143 the Tribunal, P H Clarke FRICS, said at [77F]:

> "I cannot accept Mr Maunder Taylor's view [*the expert for the nominee purchaser*] that, because he found no indication that non-participating tenants might wish to extend their leases and did not wish to participate in the collective enfranchisement, this shows the absence of hope value. What we must consider is the subjective view of a hypothetical purchaser. If Mr Maunder Taylor's approach is correct, it is unlikely that hope value could ever be attributed to the flats of non-participating tenants. The fact that a tenant does not wish to participate in acquiring the freehold or extend his lease at the time of collective enfranchisement does not mean that he (or his successor in title) will not be interested in paying for a lease extension at some time in the future."

Mr Buchanan essentially is making the same argument as Mr Maunder Taylor and we reject it for the same reasons as the Tribunal did in *Blendcrown*. The evidence suggests that it is rare for a tenant to allow a lease to run to term. No specific examples of such an event were given by Mr Buchanan, although he said he could "identify a number of cases in 1997 in Cadogan Place." In our opinion the hypothetical purchaser would consider it probable that the tenant

of flat 3 would seek a lease extension before the expiry of the term in 2023 and would include hope value in his bid.

35. There is no dispute between the parties that, if hope value is to be allowed, it should be quantified by taking a percentage of the potential marriage value and not by adjusting the deferment rate. Mr Jourdan, on his alternative case, argues that any hope value should, in effect, lie between 5% (*Blendcrown*) and 10% (Miss Frances Joyce's evidence on behalf of Cadogan in *Chelsea Properties*) of the potential marriage value. Mr Munro seeks 25% of such marriage value as supported by the evidence of Mr Jones.

36. Mr Jones assumes that the landlord would be able to negotiate more than 50% of the marriage value and he adds 5% to his original figure of 20% to allow for this. We can see merit in this argument (although not necessarily the amounts) where the lease is very short; the marriage value will be reducing towards zero and the tenant will have an increasing incentive to protect his home and any capital investment that he has made in it. The landlord will be well placed, in the no Act world, to negotiate a high percentage of the (reducing) marriage value to make it worth his while to grant a lease extension rather than wait a short while for vacant possession. But we are not persuaded that that point, with 17.75 years of the lease unexpired, has been reached in this appeal.

37. In *31 Cadogan Square Freehold Limited v The Earl Cadogan* [2010] UKUT 321 (LC) the Lands Chamber, His Honour Judge Huskinson and A J Trott FRICS, described the characteristics of the hypothetical purchaser as willing (but not over-eager), diligent and reasonably behaved. The Tribunal concluded at [83] that "the hypothetical purchaser is prudent rather than rash". We agree with Mr Jourdan that no sensible and prudent purchaser of the freehold would expect to achieve more than 50% of the marriage value of flat 3. This conclusion is also consistent with the Tribunal's decision in *Lloyd-Jones v Church Commissioners* [1982] 1 EGLR 209 where the Member, W H Rees FRICS, accepted the evidence of Mr Hopper of Gerald Eve in relation to 57 settlements on the Grosvenor and Cadogan Estates under the no Act assumption under section 9 (1A) of the Leasehold Reform Act 1967. The parties in those settlements agreed that, on the sale of a freehold of a house to the tenant, the landlord and tenant would divide the marriage value equally.

38. In *Blendcrown* the Tribunal gave two reasons why a purchaser would include an element of hope value in the price. Firstly, the relatively short unexpired terms of the flats of 46.5 years. The Tribunal considered that there may well be problems of funding (mortgageability) in the future as the unexpired terms reduced, leading to requests for lease extensions. There was no evidence that mortgageability was a factor in this appeal and, indeed, we consider that the acquisition of flats in Cadogan Square will largely, if not exclusively, be non-mortgage dependent. Secondly, there was a significant number of non-participating flats (15 flats comprising 17.2% of the aggregate value) which the Tribunal said was sufficiently large to give the expectation that some would seek lease extensions in the future. In the present appeal there is only flat 3 (see below for our decision on the caretaker's flat and flat 2) so the hypothetical purchaser will not have the comfort of expecting at least some of the tenants to seek lease extensions; instead he is faced with an "all or nothing" position.

39. The Tribunal in *Blendcrown* described hope value as speculative, uncertain and incapable of precise assessment. It must, therefore, be a matter of valuation judgment in each instance. Such judgment should be informed by evidence wherever possible. Mr Jones relies upon the sales of the South Kensington and Thurloe Estates. But that evidence is hearsay and is untested in this appeal. Mr Jones relies upon the evidence of Mr Cullum regarding the former sale. That evidence was not accepted in *Chelsea Properties* and we were given very few details about it. No supporting documents were produced. The evidence of the latter sale was even less substantial. It comprised solely of Mr Jones's recollection of reading, eighteen months ago, an analysis of the sale by one of his colleagues. We place little weight on either sale.

40. The only assistance as to the amount of hope value given to us by the Nominee Purchaser, bearing in mind Mr Buchanan's view (which we have rejected) that no allowance for hope value should be made, comes from *Blendcrown* (5% of marriage value) and *Chelsea Properties* (10%). Mr Munro referred us to *In re Shulem B Association Ltd's Appeal* [2001] 1 EGLR 105 (15%) and Mr Jones referred us to *Bircham* (20%).

41. We have already distinguished the facts of *Blendcrown*. The use of 10% by Miss Joyce (acting for the landlord) in *Chelsea Properties* was not based upon evidence. The Tribunal said at [62(1)] that:

> "She accepted that the 10% figure that she had used was a 'spot figure' and that she had adopted that figure 'to see what happens – it seemed a possibility and it seemed to make sense'"

In that appeal the Tribunal concluded that the landlord had not proved the existence of any hope value in the value of the landlord's reversion on the existing underlease. We obtain no assistance from Miss Joyce's evidence in *Chelsea Properties*.

42. *Shulem B* was concerned, inter alia, with the hope value to be attributed to a flat owned by a single non-participating tenant with an unexpired lease term of 60.75 years in a block of four purpose-built maisonettes. The nominee purchaser did not respond to the appeal and the only valuation evidence on the point was given by Mr Eric F Shapiro FRICS whose evidence was based largely upon the sale in 1994 of a ground rent estate of 34 maisonettes in Loughton, Essex. Mr Shapiro's analysis of that sale, accepted by the Tribunal, showed that the average price paid for the 27 leases that had not been extended included hope value that represented 13.81% of the marriage value. The Tribunal found that a purchaser would have paid 15% of marriage value for the non-participating flat. We distinguish the present appeal from *Shulem B* on four grounds. Firstly, there was no respondent and the evidence was not tested under cross-examination by the nominee purchaser. Secondly, the unexpired term, at 60.75 years, was very much longer than the 17.75 years in this appeal. Thirdly, the sale of the Loughton Estate took place shortly after the 1993 Act was enacted and, as the Tribunal recorded Mr Shapiro's evidence at [107J]:

> "the level of premium that would be determined or agreed was therefore uncertain, as was the level of potential activity."

Fourthly, Mr Shapiro's analysis was dependent upon the adoption of a deferment rate of 9%. A different result would have obtained had the 5% *Sportelli* rate been used. We do not find the facts or the decision of *Shulem B* to be of assistance in this appeal.

43. *Bircham* was uncontested by the nominee purchaser and was heard under the written representations procedure. We do not place weight upon it.

44. Several of these cases were considered by the Tribunal, the President and P R Francis FRICS, in *Culley v Daejan Properties Limited* [2009] UKUT 168 (LC). The Tribunal said at [62]:

> "Considerable care needs to be exercised before any weight is attached to specific percentages adopted in other cases both for the reasons expressed by the Member in *Blendcrown* …and because, in the light of *Sportelli*, the correct approach now is to approach hope value and the deferment rate quite separately…
>
> There are in our judgment two particular valuation matters to be borne in mind in the determination of hope value. Firstly, it is likely to be greater if the proportion of non-participating flats is relatively large. Secondly, it will be lower if the unexpired terms are particularly long."

The Tribunal went on to assess hope value at 10% of marriage value.

Conclusion

45. Our analysis leads us to the following conclusions about hope value:

(i) A purchaser of the freehold reversion at the valuation date would think it probable that the tenant of flat 3 (or his successor) would seek to extend the lease before the expiry of the term.

(ii) But there is no certainty that the tenant of flat 3 would seek to extend the lease or, if he did decide to do so, when this would take place. The fact that the tenant did not participate in the collective enfranchisement and had not served a section 42 notice by the valuation date suggests that no such action was imminent. In *Sportelli*, Lord Neuberger considered this to be a relevant factor. He said at [107]:

> > "Where a non-participating tenant has served such a [section 42] notice, the hope value attributable to his flat may well be increased because he has made it clear that he is interested in acquiring a new lease of his flat."

(iii) The purchaser is mainly concerned with the possibility of sharing in the marriage value. This declines at an increasing rate as the lease shortens. The longer the tenant delays in seeking to extend his lease the more the marriage value, and with it the hope value, will diminish. The purchaser is at risk of a loss if he were to pay a significant proportion of the marriage value as hope value. Mr Munro

disputed Mr Jourdan's submission that if a purchaser paid hope value for the freehold interest in a flat with an unexpired lease term of 17.75 years he would lose a substantial amount of money if the tenant did not seek to extend his lease until much later. Mr Munro argued that the freeholder's interest would benefit from the *Sportelli* real rate of capital growth of 2% in any event which would in turn lead to an increase in marriage value for any given length of unexpired term.

(iv) Whilst we accept that long term growth in capital values may reduce the rate at which the marriage value declines and would thus have a buffering effect against the loss over time of the money paid in hope value by the purchaser, the marriage value will eventually, and inevitably, disappear. The purchaser will lose all the money that he paid as hope value if the tenant does not proceed with a lease extension. Any increase in capital values in the meantime will not prevent or lessen the actual loss of the hope value paid at the valuation date. As the Tribunal said in *Blendcrown* such hope value is speculative and not susceptible to objective assessment. Its payment is, in a sense, a gamble and the stake can be lost either in whole or in part.

(v) The tenant is not solely concerned about marriage value. Other factors influence his decision about whether and when to seek a lease extension. Generally, those factors will encourage him to do so.

(vi) The purchaser is considering the prospect of a single tenant seeking to extend his lease. There is no opportunity to spread the risk across a large number of non-participating tenants.

The combined effect of these factors suggests that a purchaser will be particularly cautious about attributing significant hope value to the prospect of the tenant of flat 3 seeking to extend his lease in the near future. Under these circumstances we conclude that such a purchaser would only make a small allowance to reflect such limited hope value. We assess this allowance at 5% of the potential marriage value. Our valuation is given in Appendix 3 and the amount of hope value for flat 3 is determined in the sum of £9,863.

Issue (2): Relativity and the value of rights under the Act

Evidence

46. The LVT accepted Mr Buchanan's view that the appropriate method to assess the relativity of an existing lease was to make a percentage deduction (said by the LVT to be "at least 10%") from the market value of the lease to allow for the benefit of 1993 Act rights.

47. Mr Jones did not favour this method of assessing the benefit of the Act, describing it as pure conjecture that was not supported by any market evidence. Market transactions in the Act world were tainted and unreliable evidence (as the Lands Tribunal had found in both *Arbib v Earl Cadogan* [2005] 3 EGLR 139 and *Sportelli*). The LVT had used an arbitrary 10% to adjust the Act world evidence of short lease sales used by Mr Buchanan and had arrived at a relativity of 59.1% for flat 1 and 55.1% for flat 2. They had then wrongly said

that Mr Jones's method (which gave a relativity of 38%) was a "useful check". There was no consistency in the percentage adopted by the LVT when adjusting for the benefit of rights under the Act and no evidential basis for adopting any particular figure. He noted that in *Chelsea Properties*, a case involving a lease with 18.7 years unexpired, Mr Buchanan had also argued for a deduction of 10% to represent the benefit of the Act. The Lands Tribunal rejected that figure and adopted 15% instead.

48. Mr Jones preferred to rely upon published graphs of relativity. There were several such graphs in existence and these were summarised in an RICS Research Report entitled "Leasehold Reform: Graphs of Relativity" published in October 2009. Mr Jones was a member of the RICS Working Group that produced the report.

49. Mr Jones relied upon three of the graphs of relativity. Firstly, he used the John D Wood/Gerald Eve (1996) graph. This was based on open market sales of non-enfranchisable leases on the Grosvenor and Cadogan Estates before the enactment of the 1993 Act and settlements reached in relation to claims on the Grosvenor and Belgravia Estates, most of which pre-dated the 1993 Act. Mr Jones considered this to be the most reliable indicator of no Act world values in this location. He supported this with the Savills (1992) graph, a graph showing relativities in the no Act world that was produced in a Research Report entitled "The Impact of Leasehold Reform on the Central London Residential Market" in summer 1992. Finally, he referred to the graph first produced in 2001 by W A Ellis and based on data from the mid 1980s onwards. The graph was based upon local market knowledge and the firm's experience of managing the Trevor Estate which lies on the northern boundary of the Cadogan Estate.

50. Mr Jones said that the relativities derived from these graphs were based on historic evidence at a time when the deferment rate used to calculate the value of the freeholder's reversion in prime central London was 6%. Following a number of Lands Tribunal decisions including, most significantly, *Sportelli*, the appropriate deferment rate for flats in prime central London was now 5%. This had increased the price payable for collective enfranchisement and lease extensions such that the value of short and medium term leasehold interests had declined. The three graphs upon which he relied therefore "somewhat overstated" the relativities that were appropriate.

51. The relativities indicated by the three graphs were:

(i)	John D Wood/Gerald Eve (1996)	39.4%
(ii)	Savills (1992)	40.5%
(iii)	W A Ellis (2001)	34.0%

52. Mr Jones concluded, in the light of the reduced deferment rate referred to above, that the appropriate relativity to use in respect of the existing leases in this appeal was 38%.

53. As a cross-check Mr Jones relied upon the sale of the short leasehold of flat 1 at No.38 in March 2004 for £792,500. The lease then had 18.5 years unexpired. He indexed this price to the valuation date to produce a value of £820,734. Using Mr Buchanan's method he made a deduction in respect of the benefit of the Act which Mr Jones said was "at least 20%". This indicated a no Act world value of £656,587. Comparing this to his freehold valuation of flat 1 at £1,513,000 gave a relativity, when adjusted for the unexpired term of 17.75 years at the valuation date, of 41.6%. He said that the 2004 sale was at a time when the deferment rate was still 6% and that therefore the result gave "good support" for the relativity of 38%.

54. Finally, Mr Jones referred to market evidence of no Act world values. This comprised the sale of an unenfranchisable 10 year lease in 2-4 Hans Crescent (on the Cadogan Estate) for £1 million in June 2006. Mr Jones estimated the freehold value of the property at that time to be £13.6m (based upon the sale of 20 Hans Crescent in September 2006 for £13.4m). This gave a relativity of 7.35% for the 10 year lease compared with a range of 25% to 36% as shown in the "graph of graphs". Mr Jones concluded that this confirmed that the Gerald Eve graph did not underestimate relativity in this location and that actual no Act world relativities might be lower than indicated by any of the graphs.

55. Mr Buchanan said that "it has become common practice, and it is my standard practice" to value a lease without rights under the Act by using evidence of open market sales of short leases with the benefit of rights under the Act and deducting an allowance for those rights. In this appeal he considered that the appropriate deduction was 10%. He acknowledged the difficulties of the method but felt that there were greater difficulties associated with the use of graphs.

56. He said that the John D Wood/Gerald Eve graph was prepared in 1996 when the market was different to that at the valuation date. John D Wood had dissociated itself from the graph because it now considered it to be unreliable.

57. Mr Buchanan considered Lands Tribunal decisions in which it had adopted his method of deducting a percentage to reflect the benefit of the Act. He noted that in *Nailrile v Earl Cadogan* [2009] RVR 95 the Lands Tribunal had made a deduction of 7.5% (for a lease with an onerous ground rent) in respect of an unexpired term of 44 years. He expected the discount for rights to be higher where the unexpired term was between 30 to 40 years because marriage value was then at its greatest. Mr Buchanan also referred to *Chelsea Properties* in which the Lands Tribunal made a deduction of 15% for the benefit of rights.

58. There was no shortage of market evidence and Mr Buchanan said that both extended and existing lease values should be the exclusive product of comparable market sales. His witness statement continued:

> "The values which are produced should not then be trumped by settlements or graphs based on the opinions of valuers at some time in the distant past."

59. He supported his conclusions on relativity by reference to two leasehold sales at 29 Eaton Square, referred to as the "well matched pair". One was the sale of a 20 year unenfranchisable lease and the other was the sale of a 75 year long lease. Mr Buchanan said that the analysis of the sales showed that the 20 year lease had a relativity of between 68% and 72%.

Discussion

60. It is first necessary to consider the scope of this issue in this appeal. Relativity is relevant to calculating the marriage value in respect of participating tenants (flats 1 and 5) and when considering hope value in respect of non-participating flats (flat 3). The Nominee Purchaser submits that flat 2 should be valued in the same way as flat 1 and therefore contends that the section 42 notice at flat 2 should be taken into account. For the reasons given in our conclusions on issue (11) below we consider that flat 2 is a non-participating tenant for the purposes of Schedule 6 paragraph 4 of the 1993 Act but is a participating tenant for the purposes of Schedule 6 paragraph 3. The issue of relativity is therefore not relevant to this flat and we do not consider it further in this context.

61. We begin our analysis of the evidence by rejecting the LVT's view that the 38% relativity used by Mr Jones was "a useful check" against the results obtained by Mr Buchanan. In his final valuation Mr Buchanan's method produces relativities of 56%, 55% and 53% for the short leasehold interests in flats 1, 2 and 5 at No.38 respectively. A relativity of 38% cannot sensibly be considered to be a useful check of a relativity which is nearly half as much again. The methods used by the two experts in this appeal give very different results and, in our opinion, neither one lends support to the other.

62. Since the decisions in *Arrowdell Ltd v Coniston Court (North) Hove Ltd [2007] RVR 39* and *Nailrile* the RICS Research Report into Graphs of Relativity has been published. This gives brief details of how those graphs were prepared and was supplemented at the hearing by more detailed evidence about their history and construction. We are mainly concerned with three such graphs; the John D Wood/Gerald Eve (1996) graph, the Savills (1992) graph and the W A Ellis (2001) graph. The Nominee Purchaser directed cogent criticisms at these graphs. The 1996 graph is heavily dependent on houses (more than 90% of the data) and relies upon settlements (and opinion) rather than transactions. John D Wood & Co, the co-author of the graph, withdrew their support for it in 2000. Less than 1% of the data that supports the 1992 graph comprises leases with less than 20 years to run, ie less than 10 leaseholds out of 1,000. In our opinion that is a weak foundation upon which to build general conclusions about the relativity of short leaseholds under 20 years. The 2001 graph gives anomalously low figures for leaseholds with unexpired terms of less than 20 years when compared with the other graphs considered by the RICS. Although it is based on 200 transactions during the mid 1980s, all of these were house sales.

63. While we recognise the limitations of the graphs' source data when applied to the facts of this appeal, such data is nevertheless the only contemporary evidence of (in some cases) transactions that took place in the no Act world and which therefore exclude the benefits of

the Act. The experience of experts in recent years has necessarily been gained in the Act world, and reflects the market's views in hypothesising the absence of the benefits of the Act rather than direct no Act world evidence of transactions. Nevertheless Mr Buchanan supported his conclusions by reference to two transactions in Eaton Square ("the well-matched pair"). During cross-examination Mr Buchanan said that his knowledge of these transactions was based upon the evidence of a witness, Mr Robertson, who appeared before the LVT in a case involving 26 Bourne Street and who Mr Buchanan then contacted. Mr Buchanan accepted that the LVT in that case had not accepted the evidence of this pair of transactions and he agreed that he should have qualified his evidence in the light of the LVT's conclusions. Mr Jourdan submitted that the 26 Bourne Street case may have had factors that do not apply to Eaton Square but if there were any they were not identified to us. We accept Mr Munro's submission that Mr Buchanan effectively abandoned reliance upon the sales in Eaton Square and we give them no weight.

64. For his part Mr Jones introduced evidence of no Act world values in the form of the sale of an unenfranchisable 10 year lease at 2-4 Hans Crescent. He compared this with the freehold value of the property, derived from the sale of a comparable at 20 Hans Crescent, to give a relativity of 7.35%. Mr Buchanan gave a detailed criticism of the comparison between these two properties which we find to be persuasive and we do not find the transactions in Hans Crescent to be of assistance in this appeal.

65. The alternative approach to the use of graphs, and the one used by Mr Buchanan and favoured by the LVT, is to ascertain the existing leasehold value in the Act world (derived from comparables) and then to make a percentage adjustment to reflect the benefits of the Act. Mr Munro rejected the method, and Mr Buchanan's adoption of a 10% discount, as being arbitrary.

66. The Tribunal has been faced many times in recent years with similar arguments about relativity. The hope expressed by the Tribunal in *Arrowdell* that it might be possible for the RICS to produce standard graphs on the basis of a survey of assessments made by experienced valuers addressing themselves properly to the hypothetical no Act world remains unfulfilled. The members of the RICS Working Group formed to consider whether such definitive graphs could be prepared were unable to reach a consensus. The problem seems to be intractable.

67. In both *Arrowdell* and *Nailrile* the Tribunal did the best it could with evidence of transactions, even though such transactions took place in the Act world. It also had regard to graphs of relativity. These two leading cases did not opt for one approach in preference to the other; they considered all the available evidence. The difference between the present appeal and *Nailrile*, which involved an exhaustive analysis of several approaches to assessing relativity, is that in *Nailrile* the various approaches gave broadly similar results; the use of graphs gave a relativity of just over 69% and the use of a percentage adjustment gave answers varying from approximately 71% to 75% (the analysis being complicated by the existence of onerous ground rents). But in the present appeal the two methods produce significantly different answers; 38% (graph) and 53% to 56% (percentage adjustment). They cannot both be right.

68. A relativity of 55% for a lease with an unexpired term of 17.75 years is approximately the figure that is shown in Savills 2002 enfranchisable graph, ie before the benefits of the Act are deducted. Mr Buchanan accepted that elsewhere his colleagues at Knight Frank had adopted lower figures of relativity for short leaseholds based upon the use of graphs and upon settlement evidence. In *31 Cadogan Square Freehold Limited* the valuation experts were also partners at Cluttons (Mr Simon Scott-Barrett for Earl Cadogan) and Knight Frank (Mr Robert Orr-Ewing for the nominee purchaser). In that appeal the experts agreed that the relativity for 31 Cadogan Square (for a lease with 15.56 years unexpired) was 37% and for 37 Cadogan Square (for a lease with 16.07 years unexpired) was 38.5%. The fact that Mr Buchanan has adopted a much higher relativity for a lease with an unexpired term of 17.75 years does not make him wrong but it does, in our opinion, invite careful scrutiny of his approach.

69. In his final valuation Mr Buchanan adopts the LVT's determination of £697,683 (excluding improvements and Act rights) as the value of the short leasehold interest in flat 1 at No.38. That valuation is based upon the sale of that flat in March 2004 for £792,500.

70. We agree that this sale is good evidence of the value of flat 1 at No.38. Adjusting the sale price to the relevant date (June 2005) using the Savills Index gives a figure of £820,734 which must be further adjusted for the length of the lease and to exclude the value of improvements. When the leasehold interest in the flat was sold in March 2004 it had 19 years unexpired. At the relevant date in June 2005 it had 17.75 years unexpired. Using the Savills enfranchisable graph the reduction in value between the two lease lengths is 3.2% which gives a value adjusted for lease length of £794,471. The improvements to the flat were old (1980) and limited in scope and we consider Mr Buchanan's allowance of 5% to be reasonable. This gives an unimproved value at the relevant date, adjusted for lease length, of £754,747 including Act rights (£487 psf using the agreed floor area of 1,550 sf).

71. Mr Buchanan also relies upon the sale of two other ground/lower ground floor flats at No.23 and No.50, both of which were unimproved. No.23 had an unexpired term of 19 years and was sold in April 2004 for £988,500 (£492 psf). It is better located on the Square than No.38 and has a superior entrance but it lacks a garden. We consider that these factors are value neutral when considered together. Adjusting for time and lease length gives a value of £986,781 including Act rights (£491 psf).

72. There were three sales of the ground/lower ground flat at No.50 and Mr Buchanan relies upon the first such sale in May 2002 when the property was still unimproved. The lease had an unexpired term of 20.8 years and was sold for £905,000 (£471 psf). This flat is better positioned in the centre of the Square, for which we adjust by 5%, and, when further adjusted for time and lease length, gives a value of £818,682 (£426 psf) including Act rights.

73. Giving most weight (60%) to the sale of flat 1 at No.38 and equal weight (20%) to each of the other two comparables gives a rounded value for the existing lease at flat 1 at No.38, including Act rights, of £737,000 (£475 psf) as at the relevant date.

74. Relativity is also relevant in the valuation of the existing leasehold interest of the participating tenant at flat 5. Mr Jones takes the relativity at 38% of the agreed freehold value of £595,000 to give £226,100. Mr Buchanan gave no oral evidence to us about the value of the existing leasehold interest in flat 5. His evidence was confined to the existing leasehold interests of flats 1 and 2. Mr Buchanan adopts the figure of £352,809 (including Act rights) determined by the LVT. In the light of the Court of Appeal decision in *McHale v Earl Cadogan* [2010] EWCA Civ 1471 Mr Buchanan now deducts 10% from that figure to reflect the benefit of the Act, giving a net of rights value of £317,528 and a relativity of 53%.

75. In its decision the LVT says that it accepted four comparables used by Mr Buchanan at Nos.15, 17, 30 and 42, although it preferred Mr Jones's adjustments which gave a higher average rate of £492.75 psf. None of this evidence was heard or tested by or before us. But Mr Buchanan includes in Schedule 3 to his witness statement summarised details of the four comparables that he used before the LVT to calculate the value of the existing lease at flat 5 as well as copies of sales/auction particulars. Unfortunately Mr Buchanan does not provide a correct summary of the transaction at No.17. In his Schedule 3 he describes the sale as that of "$4^{th}/5^{th}$ floor flat, 12 Cadogan Square" and says that it was sold on 15 December 2005 for £415,000. The area is given as 1,460 sf. The LVT refer at one point in its decision to "Flat 12 at No.17" and at another to "Flat 12 at No.12". Mr Buchanan provides sales particulars of flat 12 at No.17 at tab 13 of his Schedule 3. Those details describe a flat with an area of 786 sf. It appears that Mr Buchanan has referred to the wrong flat in his summary and we therefore do not have accurate details of its sale price or date of sale. Nor do we have any details of improvements to these flats other than what appears in the sales particulars. From these it is clear that flat 5 at No.15 was unmodernised while flat A at No.30 and flat 4 at No.42 are not described as modernised or improved. The LVT made no deduction for improvements.

76. We have adjusted the sale prices for the three flats for which we have details for time (Savills Index), lease length (Savills enfranchisable graph), position on the Square (add 5% to the value of No.30 which is off Square) and other known factors (deduct 5% from the value of No.42 which has a roof terrace). The results are summarised below (with the equivalent LVT values shown in brackets):

Flat 5 at No.15:	£501 psf (£527 psf)
Flat A at No.30:	£407 psf (£397 psf)
Flat 4 at No.42:	£488 psf (£536 psf)
Average:	£465 psf (£487 psf)

On the limited information that we have available, and acknowledging that neither expert was cross-examined on the evidence, we consider that the unimproved existing leasehold value of flat 5, including Act rights, was £335,000 (£468 psf) as at the valuation date in June 2005.

77. The freehold values of flats 1 and 5 at No.38 are £1,370,000 (see issue (7) below) and £595,000 (agreed by the parties) respectively. We have determined the existing leasehold values of the two flats, including Act rights, as £737,000 and £335,000 respectively. The relativity, including Act rights, of the flats is therefore 53.8% for flat 1 and 56.3% for flat 5.

Both leases had unexpired terms of 17.75 years as at the valuation date. The relativity for leases of this length of unexpired term is shown in the Savills enfranchisable graph (2002) as just over 55%.

78. Mr Jones takes the relativity excluding Act rights as 38%. Using that figure and the freehold values that we have referred to above gives existing lease values, excluding Act rights, of £520,600 for flat 1 and £226,100 for flat 5. To obtain these figures, using our existing lease values including Act rights, means that there would have to be a deduction for Act rights of 29.4% for flat 1 and 32.5% for flat 5. This compares with Mr Buchanan's allowance of 10%.

79. There is a piece of evidence that, to a limited degree, assists in deciding the order of magnitude of a deduction for Act rights. We understand from the evidence that both parties use the Savills 2002 enfranchisable graph to adjust for lease length (although in cross-examination Mr Buchanan expressed reservations about its construction and its use to adjust leases with unexpired terms of less than 60 years). The Savills 2002 graph (unlike the Savills 1992 graph) was not criticised by the Nominee Purchaser in submissions. Mr Jones also relies upon the John D Wood/Gerald Eve (1996) graph to determine directly the relativity net of Act rights. The difference in the relativities for equal unexpired terms shown in those graphs should (theoretically) represent the value of the Act rights. We make such a comparison in Table 1 below using the information available to us in the evidence and restricting the comparison to unexpired terms of between 5 and 50 years:

TABLE 1

UNEXPIRED TERM (yrs)	**RELATIVITY INCLUDING ACT RIGHTS[1] (%)**	**RELATIVITY EXCLUDING ACT RIGHTS[2] (%)**	**% DEDUCTION FOR ACT RIGHTS**
5	23.7	15	36.7%
10	40.9	25	38.9%
15	50.9	35	31.2%
20	58.0	43	25.9%
25	63.6	50	21.4%
30	66.1	56	15.3%
35	71.9	61	15.2%
40	75.2	66	12.2%
45	78.1	70	10.4%
50	80.7	74	8.3%
Notes: [1] Savills 2002 enfranchisable graph [2] John D Wood/Gerald Eve 1996 Graph			

80. This analysis shows that the benefit of the Act increases the shorter is the unexpired term (at least until 10 years). This suggests that the amount of marriage value, which is highest where the lease has an unexpired term of between approximately 30-50 years, is not necessarily the dominant factor in determining the value of Act rights. The ability, inter alia, of a tenant to call for a new lease at a time of its choosing as the unexpired term approaches zero also appears to be important. This cushions the effect of the lease as a wasting asset. We do not rely exclusively upon this analysis and we recognise the limitations of a comparison between these two graphs. However we do consider that it lends support to Mr Jones's argument that Mr Buchanan's allowance of 10% is inadequate. We are not satisfied that Mr Buchanan's conclusions are consistent with the totality of the evidence and, having carefully scrutinised his arguments, we conclude that his deduction for Act rights is significantly too low. We make a deduction of 25% for Act rights in this appeal. Applying this to the existing lease value of flat 1 gives a figure of £552,750 net of Act rights, or 40% of the freehold value. Applying it to the existing lease value of flat 5 gives a figure of £251,250 net of Act rights, or 42% of the freehold value.

Issue (3): Hope value of the caretaker's flat

81. The second aspect of hope value raised related to the caretaker's front basement flat. Although the headlease and four of the underleases contain covenants requiring, in effect, that the flat should be occupied by a resident caretaker, Mr Jones expressed the opinion that a hypothetical purchaser would see the opportunity of coming to an early agreement with the headlessee and the relevant underlessees to agree to vary their leases so as to dispense with the services of a resident caretaker.

82. Accordingly, in his revised valuations, he included £18,511 as "Hope value for early release of caretaker's flat". His figure presupposed that the notional purchaser would assume that he would have to make a payment to the headlessee and all the lessees (though in fact that might not be necessary as the lease of flat 4 did not oblige the landlord to provide a resident caretaker). He calculated the landlord's share of the marriage value to be released by this exercise as £37,021 and then discounted the figure by 50 per cent to allow for the risk.

83. Mr Jones did not allow for that value in his valuation of the headlease interest and in cross-examination accepted that this was an error. However in final submissions on behalf of Cadogan it was submitted that the figure for hope value remained the same because it presupposed that the notional purchaser would assume that he would have to make a payment to the headlessee and all the lessees.

84. He said in cross-examination that some tenants liked a resident caretaker but others did not. The Cadogan Estate was, he had been informed, regularly approached by leaseholders asking whether it would be possible to dispense with the services of a resident caretaker so as to reduce the service charge. The functions of a resident caretaker could easily and more cheaply be performed by an outside contract cleaning company, but the Cadogan Estate as a matter of policy would not dispense with the services of resident caretakers in their buildings because of concern that if basement flats were released into the market they might be used for

illegal or immoral purposes, causing a nuisance to residents and detrimentally affecting values on the Estate. Once the freehold had been transferred the Cadogan policy would no longer be applicable and the caretaker's flat could be released onto the market.

85. He identified two cases, 4 Draycott Place and 62 Pont Street, in which he had acted for the freeholders on collective enfranchisement cases and had agreed a sum as reflecting the potential early release of such a covenant. In one case the nominee purchaser had revealed there was already an agreement in place to sell the caretaker's flat on completion of the enfranchisement. Thus there had been cases in which a deal had been struck for the release of such a covenant, and the concept was not far-fetched.

86. For the Nominee Purchaser Mr Buchanan made no such addition. His view was that any one tenant could effectively veto the proposed variation and that a resident caretaker added value to the flats which would have to be offset.

87. Counsel for the Nominee Purchaser also submitted that in any event it would not be permissible, when valuing the freehold interest under Schedule 6 paragraph 3 of the 1993 Act to take account of possible variations of the terms of the leases. The valuation under Schedule 6 paragraph 3(1)(a) was on the assumption that the vendor was selling for an estate in fee simple subject to any leases subject to which the freeholder's interest in the premises was to be acquired by the nominee purchaser, but subject also to any intermediate or other leasehold interests in the premises which were to be acquired by the nominee purchaser. Thus, it was submitted, the valuation must reflect the terms of those leases, without regard to the possibility of their variation or surrender. He referred to *Plinth Property Investments Ltd v Mott, Hay & Anderson* (1977) 38 P&CR 361 (CA) concerning a rent review by an arbitrator where the lease in question restricted use of the premises to offices for consulting engineers and it was held not to be open to him to assume that the restriction might not be enforced.

88. The LVT accepted this submission of counsel for the Nominee Purchaser, observing that the statutory valuation provision required that the sale assumptions be applied as at the relevant date, which was the valuation date, so that even an actual but subsequent variation of the existing leases would, in its view, have to be disregarded. Accordingly, the LVT decided that, as a matter of law, no addition should be made for hope value in respect of the caretaker's flat.

89. On behalf of Cadogan it was submitted that the LVT had been wrong to conclude that the paragraph 3(1)(a) assumption and *Plinth* precluded the inclusion of hope value in relation to the caretaker's flat. The hope value under consideration was for the hope of doing a deal after the notional sale. It is a deal that releases obligations contained in covenants and no more. *Plinth* was nothing to the point, as it dealt simply with the construction of a rent review clause in a lease. The Nominee Purchaser's argument did not explain why a rent review hypothesis should apply to the valuation of a freehold reversion.

90. So far as the point of law is concerned, we accept the submission made on behalf of Cadogan that *Plinth* does not assist the Nominee Purchaser. It was a decision based on two

grounds: (1) the uncertainty in that case of assessing the sum a landlord would require to release the covenant and (2) the terms of the rent review clause. There is nothing in Schedule 6 paragraph 3(1)(a) which precludes the assessment of the hope value of obtaining a release of the covenant as to the provision of a resident caretaker when determining the appropriate value or requiring the hope value to be excluded.

91. However on the evidence before us we are satisfied that Mr Buchanan was correct in not allowing any sum in respect of the marriage value which might be released. Mr Jones's evidence as to two cases in which he had negotiated a figure for the potential release was unpersuasive. In one case there were clearly special circumstances, in that it was plain that the proposed release was already effectively a "done deal" and the lessees were willing, presumably for a price, to release the covenant. In the other we were given no adequate information as to the background of the transaction. In the present case, even assuming that Mr Jones's valuation as to the prospective marriage value capable of being released is correct, we are not satisfied that any prudent purchaser would pay good money for the chance of obtaining the release of the covenant at some uncertain future date from each of the six relevant leaseholders.

92. We therefore conclude that no element of hope value should be included in the valuation under this head.

Issue (4): Letting value of caretaker's flat

93. This issue arose from the terms of the headlease. Mr Jones contended that: (a) clauses X and XII of the headlease require that the caretaker's flat be used by a full-time caretaker who is to reside in it on a service basis; (b) the "market rent" or "rack rent letting value" must therefore be the value of the flat for letting to a resident caretaker; and (c) this value would be half of the open market letting value of the flat. The parties agreed that if the rental value of the flat is to be reduced because of the provisions of the headlease limiting the user to that of a caretaker's flat, effect should be given to the restriction by reducing the agreed rental value of £15,600 pa by 50%, which produces a figure of £7,800 pa. The LVT did not accept that argument.

94. The LVT held that although superficially it seemed inconsistent with the Court of Appeal decision in *Plinth*, that decision should be distinguished and that it should recognise that service charge provisions are essentially designed for compensation, or better reimbursement of cost, rather than rental valuation purposes.

95. Accordingly, the LVT held that the agreed market rental should not be reduced for the purpose of the valuation exercise. In doing so it relied on the LVT decision in *Crammond v Theodore Gregory Limited* [2004] LON/SC/00AW/NSI/2003/0076 (LVT) (unreported) (referred to as *109 Cadogan Gardens***)** where the expression was "an annual sum equivalent to the market rent". In that case, unlike earlier LVT cases, the point was argued by counsel, and the LVT held that the rent had to be arrived at on an unrestricted basis, not on the basis that the flat had to be occupied by a caretaker, saying at [49]:

> "We are satisfied, first, that the underleases require us to arrive at a rent on the basis of unrestricted user, and not on the basis that the flat must be occupied by a caretaker. We accept that the purpose of the provision is not to arrive at a rent for the flat as it is and must be used, but to compensate the landlord for the fact that he cannot let it in the open market. We think the present situation is clearly distinguishable from *Plinth Property Investments*, where the function of the arbitrator was to arrive at a rent for the property as it was required to be used."

96. Cadogan argued that the LVT was wrong to follow the decision in *109 Cadogan Gardens*. *Plinth* was said to be binding authority for the proposition that in assessing the rental value of a property, the valuer had to give effect to the terms of the letting. The lessees contributing to a notional rent of the caretaker's flat contributed on the basis of a restricted user of the flat. The lease of flat 4 referred to recovery of a proportion of a "market rent of such accommodation," being any accommodation provided for a resident caretaker. The lease of flat 5 obliged the landlord to provide a resident caretaker and referred to a proportion of the "rack rent letting value" of "the flat occupied by the caretaker." The headlease required the caretaker's flat to be used as a self-contained flat for the caretaker. The recoverable rent therefore had to reflect the fact that the notional rent could only refer to the notional rent of a flat being resided in by a caretaker.

97. The issue is what is meant by "market rent" and "rack rent letting value".

98. The terms of the relevant underleases are designed to compensate the headlessee for the rental income he could receive from the caretaker's flat. The decision in *109 Cadogan Gardens* "to compensate the landlord for the fact that he cannot let it in the open market" does not assist the Nominee Purchaser's argument because the reason the headlessee could not let on the open market without restriction of user is the covenant in the headlease. There is no justification for asserting that if he were not using it to provide a resident caretaker in accordance with his obligations in the underleases he could use the caretaker's flat in a way inconsistent with his obligation under the headlease so as to let it out on the open market.

99. Although the normal meaning of "rack rent" is the rent which represents the full annual value of the holding and "market rent" means the same as "open market rent": see *Sterling Land Office Developments Ltd v Lloyds Bank plc* [1984] 2 EGLR 135, that does not assist the Nominee Purchaser. The headlessee could not offer the caretaker's flat for rent on the open market, whatever the position vis a vis the underlessees because of the terms of the headlease, and the words must be construed accordingly. An analogy would be if there was a restrictive covenant restricting user of the flat. It could not then be argued that the rack rent or open market rent should be assessed ignoring the limitations imposed by the covenant.

100. It follows that in our judgment the LVT was wrong to reject Mr Jones's argument and consequently the agreed market rental should be reduced by 50% to £7,800 pa.

Issue (5): The valuation date used for flat 1

101. The tenant of flat 1 served a section 42 notice on 29 March 2004. The LVT concluded that where the benefit of a section 42 notice is assigned by a non-participating tenant to a participating tenant, the valuation date should, as the Nominee Purchaser contended, be the date of the section 42 notice. Cadogan contended for 22 June 2005, the date the section 13 notice was given.

102. The effect on the valuation of the giving of a section 42 notice was discussed in the House of Lords in *Sportelli.* Lord Neuberger said at paragraph 107:

> "That suggests to me that the purpose of sub-paragraph (b) [in paragraph 3(1) of Schedule 6] is to entitle the landlord to argue that the section 42 notice is evidence that the tenant concerned is interested in acquiring a new lease of his flat. Where a non-participating tenant has served such a notice, the hope value attributable to his flat may well be increased because he has made it clear that he is interested in acquiring a new lease of his flat. In other words, by serving a section 42 notice, a non-participating tenant has, in my view, assisted any contention that he would be in the market, because he has evinced a desire to acquire a new lease of his flat at market value, which is what Schedule 13 effectively means that he would have to pay."

103. Counsel for Cadogan argued that no statutory contract is created by the giving of a section 42 notice. If, as Lord Neuberger made clear, the purpose of sub-paragraph (b) is to address the position at the valuation date for the collective enfranchisement, it cannot be possible to superimpose on that exercise, values based on earlier (or later dates): the tenant is assumed to be in the market at the valuation date for the collective enfranchisement and "has evinced a desire to acquire a new lease of his flat at market value." The whole valuation exercise and its component parts are predicated on values as at the valuation date. He observed that if the Nominee Purchaser was right, a section 42 notice served subsequent to the section 13 notice would require a valuation to the latter date, not the former. That could not be right as it would give potential to completely subvert the fixed valuation date now provided for section 13 notices.

104. Counsel for the Nominee Purchaser argued that the flat 1 section 42 notice was not given by a participating tenant, but by predecessors in title of a participating tenant. Accordingly, in valuing the freeholder's interest in reversion on the lease of flat 1, it is to be assumed that the assignee of the benefit of the notice is entitled to a grant of a new lease of flat 1 pursuant to the flat 1 section 42 notice, in relation to which the valuation date is 29 March 2004.

105. He pointed out that the assumptions by reference to which Schedule 6 paragraph 3(1) provides that the freehold is to be valued include:

> "(b) … that this Chapter and Chapter II confer no right to acquire any interest in the specified premises or to acquire any new lease (except that this shall not

preclude the taking into account of a notice given under section 42 with respect to a flat contained in the specified premises where it is given by a person other than a participating tenant)',

(c) … that any increase in the value of any flat held by a participating tenant which is attributable to an improvement carried out at his own expense by the tenant or by any predecessor in title is to be disregarded."

106. He submitted that the wording of these sub-paragraphs (b) and (c) revealed a clear distinction between a participating tenant, and a predecessor in title of a participating tenant. Paragraph (b) applies to a section 42 notice "where it is given by a person other than a participating tenant". That paragraph does not refer to a notice "given by a person other than a participating tenant or any predecessor in title". Where the Act intends predecessors in title to be taken into account, it says so in terms, as in paragraph (c). The Nominee Purchaser's counsel also referred to section 19(3). As to the meaning of "participating tenant", the term is defined in section14(l) as:

"(a) in relation to the relevant date, the qualifying tenants by whom the initial notice is given; and

(b) in relation to any time falling after that date, such of those qualifying tenants as for the time being remain qualifying tenants of flats contained in the specified premises."

107. In the present case, the qualifying tenants by whom the initial notice was given were the Nominee Purchaser (flat 1), Sibel Erkman (flat 2) and Baron Renwick (flat 5). They were the participating tenants. The flat 1 section 42 notice was not given by any of the participating tenants. It was given by Mr and Mrs Stille, the predecessors in title to the Nominee Purchaser, and they assigned the benefit of the flat 1 section 42 notice. Accordingly, in valuing the freehold under Schedule 6 paragraph 3(1), the flat 1 section 42 notice had to be taken into account.

108. Cadogan's argument was rejected by the LVT. It accepted the Nominee Purchaser's arguments and held that, as at the valuation date for enfranchisement (ie 22 June 2005), a hypothetical purchaser considering the effect of a section 42 notice would be advised to do so on the basis that, if the claim to a new or extended lease proceeded, it would do so with its own statutory valuation date (ie 29 March 2004). In doing so it followed the decision of the LVT in *Earl Cadogan v Cadogan Square Ltd* [2005] LON/ENF/1800/06 (unreported) in which at paragraph 6.9 the Tribunal said:

"6.9 The Act as amended by the Commonhold and Leasehold Reform Act 2002 provides that in collective enfranchisement claims the Valuation Date is the date of the tenants' initial S13 notice, in this case 3 October 2005. In valuing the freehold interest at that date however regard can be had to the earlier S42 notice served by a non-participator in the collective enfranchisement in respect of Flat A even though as Mr Munroe (sic) rightly points out S54(2) suspends the operation of that notice. A purchaser of the freehold would consider aborting his bid if he is faced with the

> prospect of having to accept shortly after his purchase a lesser premium on the grant of a new lease of Flat A than the sum he would otherwise have included in respect of that flat as part of the freehold."

109. The LVT rejected counsel for Cadogan's submission that this could not be right because a subsequent section 42 notice (ie one served at a later date than a section 13 notice) would require the LVT to value as at the later date, not the former and this would give the potential to subvert the fixed valuation date provided for section 13 notices. The LVT considered this submission misconceived. In its view the valuation of the freehold interest for enfranchisement purposes is required to be as at the relevant valuation date from which it followed that no account should be taken of any subsequent events such as the later service of section 42 notices. It considered that whilst it might be arguable that a later section 42 notice constituted a change of circumstances capable of affecting a vesting order within section 24(4)(b)(i) of the 1993 Act, this involved different issues not arising here and not justifying counsel's submission.

110. Lord Walker observed at paragraph 45 of his opinion in *Sportelli* that Schedule 6 paragraph 3 permits the inclusion of hope value, such as it is, in respect of new leases of the flats of non-participating tenants, but that is hope value in respect of deals which might be freely negotiated, rather than leases granted under any statutory right because paragraph 3(1)(b) excludes statutory rights (except where section 42 notices have already been served) but not the possibility of negotiated contracts. In our judgment, in valuing the Property under Schedule 6 of the 1993 Act, the rights and obligations created by the flat 1 section 42 notice are, in accordance with the view of Lord Walker, to be taken into account, pursuant to Schedule 6 paragraph 3(l)(b).

111. However, Lord Neuberger seems to express a different opinion about the exception contained in paragraph 3(1)(b). In paragraph 107 of *Sportelli* he says:

> "…the bracketed words in para 3(1)(b) require one to take into account the 'notice', not the rights and obligations which accrue pursuant to it. That suggests to me that the purpose of sub-para (b) is to entitle the landlord to argue that the section 42 notice is evidence that the tenant concerned is interested in acquiring a new lease of his flat."

In conclusion he says at paragraph 115:

> "Accordingly, for these reasons, as well as those articulated by Lord Walker, I consider that hope value can be taken into account under para 3 of Schedule 6, in so far as it is attributable to the possibility of non-participating tenants wishing to obtain new leases of their flats in the open market (and not pursuant to Schedule 13)."

112. Lord Hope says at paragraph 31 that he agrees with:

> "Lord Walker and Lord Neuberger for the reasons they give, that para 3 of Schedule 6 to the 1993 Act permits hope value to be taken into account in the valuation in so far as it is attributable to the possibility of non-participating tenants seeking new leases of their own flats."

Lord Hope says nothing about whether the rights and obligations created by a section 42 notice given by a non-participating tenant should be taken into account when considering hope value.

113. Lord Mance expressed "full agreement" with the reasoning given in the speeches of both Lord Walker and Lord Neuberger while Lord Hoffman issued a dissenting opinion in which he argued that hope value should be excluded for all tenants.

114. According to Lord Neuberger the valuation of the freeholder's interest under paragraph 3 of Schedule 6 can take into account the hope that a non-participating tenant would seek to negotiate a new lease in the open market. The amount that such a tenant would pay and the terms of the new lease that he might be granted are not constrained by the statutory provisions of Schedule 13 to the 1993 Act. It seems to us that Lord Walker takes the same approach in the absence of a section 42 notice. But where such a notice has been served by a non-participating tenant their Lordships appear to differ in the interpretation of its effect. Lord Walker, it seems to us, would take the rights under the section 42 notice into account but Lord Neuberger would not. Lord Neuberger considers that the service of such a notice should inform the purchaser's view of the possibility of the non-participating tenant wanting to extend his lease but he does not take account of the rights of the tenant under that notice.

115. We do not think that it is correct to characterise the valuation date in this appeal as being the date of the section 42 notice. The valuation date in respect of flat 1 is (as required by the Act) the date of the section 13 notice, but in valuing at that date the valuer will have to take account of the fact that a section 42 notice was served at an earlier date by a non-participating tenant. This could result in the grant of an extended or new lease at a price ascertained at that earlier date "at market value, which is what Schedule 13 effectively means he would have to pay", to use Lord Neuberger's words. The valuer will have to form a view as to the likelihood of the section 42 notice being followed through to the grant of a new lease. In our opinion "the taking into account" of the section 42 notice must reflect the facts and circumstances at the valuation date for the collective enfranchisement. In this appeal the non-participating tenant who served the section 42 notice assigned the benefit of it shortly afterwards to the Nominee Purchaser who was a participating tenant for the purposes of the initial notice under section 13. We therefore agree with the LVT when it said at paragraph 41 of its decision:

> "Nevertheless the reality is that the s42 notice will not proceed re flat 1, because the present tenant is participating in the enfranchisement …"

Consequently we consider that the section 42 notice will have no effect on the value of the freeholder's interest as at the valuation date (22 June 2005).

116. In the light of our decision it is not necessary for us to reach any conclusion about the apparent differences in the opinions of their Lordships regarding how to take into account section 42 notices. However, we would reiterate the note of qualification given by the Tribunal in paragraph 116 of its recent decision in *Earl Cadogan v Betul Erkman* [2011] UKUT 90 (LC) in which it noted that in another case it may need to be decided whether or not regard should be had to the rights and obligations arising under a section 42 notice which falls to be taken into account under paragraph 3(1)(b) of Schedule 6.

Issue (6): McHale

117. In *McHale v Earl Cadogan* [2010] EWCA Civ 1471 the Court of Appeal decided that the rights under the 1993 Act should not be taken into account when valuing the existing leases for the purposes of marriage value. It is a necessary consequence of this decision that the Tribunal must allow Cadogan's appeal on this issue.

Issue (7): The freehold value of flat 1

Evidence

118. Both experts valued flat 1 as a participating tenant and therefore valued the flat in its unimproved condition.

119. Mr Jones relied mainly upon 7 of the 24 comparable sales of ground/lower ground flats that he identified in Cadogan Square. He adjusted these for time using the Savills Index and used the Savills 2002 enfranchisable graph to adjust for lease length.

120. He identified two sales of the subject flat; one in November 2001 and the other in March 2004. Before the LVT he gave less weight to the second sale because it appeared to show that the flat had lost 29% of its value in less than 3 years and he suspected that it may have been a sale to a connected person. But the evidence produced by the Nominee Purchaser at the LVT showed that the sale was at arm's length. Mr Jones said that he now gave the most weight to the second transaction in March 2004. However it did not form one of his chosen 7 comparables. Table 2 below summarises Mr Jones's analysis of those comparables:

TABLE 2

FLAT	DATE OF SALE	SALE PRICE (£)	AREA (sf)	PRICE (£/psf)	LEASE LENGTH (Yrs)	VALUE (INC. ALL ADJUSTMENTS) AT 22/6/05 (£/psf)	SUMMARY OF ADJUSTMENTS[1]
Flat A at No.2	3/06	1,600,000	2,100	762	70	974	Add 20% for unmodernised condition, inferior location, no garden.
Flat 1 at No.11	12/05	1,430,000	1,861	768	39	1,016	–
Ground/lower ground at No.21	10/04	4,700,000	3,931	1,196	110	996	Deduct £250 psf for improvements.
Flat 2 at No.22	6/06	3,400,000	2,528	1,345	124	1,006	Deduct £250 psf for improvements
Flat E at No.30	11/02	1,113,000	1,601	695	49	909	Onerous ground rent allowed at £10 psf before adjustment for time/lease length.
Flat 1 at No.44	2/03	2,500,000	2,098	1,192	110	996	Deduct £250 psf for improvements.
Flat 10 at No.78	1/07	2,000,000	1,418	1,410	Share of freehold	1,007	Add 5% for poor layout, deduct £250 psf for improvements.
Average						986	
Notes: [1]All comparables adjusted for time and lease length							

121. Mr Jones also took account of two LVT decisions involving other ground/lower ground flats in Cadogan Square; No.23 (valuation date October 2005, adjusted rate £958 psf) and No.42 (valuation date November 2005, adjusted rate £986 psf).

122. Mr Jones concluded that the appropriate rate to use for the valuation of flat 1 was £960 psf which gave a total value of £1,513,000. At the hearing it was agreed that the correct floor area was 1,550 sf. This gives an amended total value of £1,488,000. However Mr Jones continued to use an area of 1,576 sf in his final amended valuation. We use the agreed (lower) floor area in our analysis.

123. Mr Buchanan analysed 9 comparable sales of ground/lower ground flats in Cadogan Square. He distinguished between sales of improved and unimproved properties and said that there were different markets for each. Two properties (Nos.21 and 58) had been sold twice; once unimproved and once following improvement. Mr Buchanan said that the unimproved sales of these properties provided the best comparable evidence. They were supported by settlement evidence of a lease extension at flat 1 at No.44 (unimproved). Table 3 below summarises Mr Buchanan's analysis of his 3 preferred comparables:

TABLE 3

FLAT	DATE OF SALE	SALE PRICE (£)	AREA (sf)	PRICE (£/psf)	LEASE LENGTH (Yrs)	VALUE (INC. ALL ADJUSTMENTS) AT 29/3/04 (£/psf)	SUMMARY OF ADJUSTMENTS
G/LG at No.21	7/02	2,900,000	3,877	748	111	734	Add 2.5% for layout, deduct 2.5% for separate entrance.
Flat 1 at No.44	4/02	1,275,000	1,761	724	112	734	NONE
Flat 1 at No.58	4/02	1,825,000	2,560	714	119	780	Add 8.5% for garden, deduct 5% for position

Adopted value as at March 2004: £776 psf
Adopted value as at June 2005 (+3.5%): £803 psf
Adjusted for relativity at 99% (March 2004): £784 psf
Adjusted for relativity at 99% (June 2005): £811 psf

124. Mr Buchanan valued to 29 March 2004 which was the valuation date for the section 42 notice served in respect of flat 1. "For the purposes of providing an alternative valuation" he adjusted his final valuation to June 2005 by adding 3.5%. Mr Buchanan's respective freehold valuations were £1,214,462 (£784 psf) as at March 2004 and £1,256,968 (£811 psf) as at June 2005. He said in his witness statement that he adopted the freehold figure determined by the LVT (£1,140,236 as at March 2004 and £1,180,859 as at June 2005). In his original valuation he used £1,142,646 (as at June 2005) and in his final (amended) valuation he used £1,256,965 (as at June 2005). Neither figure is that adopted by the LVT, even allowing for the fact that the LVT was using an area of 1,576 sf.

Discussion

125. The LVT preferred Mr Buchanan's comparables and relied in particular upon the sale of the unimproved flat at No.58. The LVT recorded Mr Buchanan's analysis of this sale as producing a rate of £768 psf after adjustments for the garden and the position on the Square. The LVT made a smaller (5%) adjustment for the garden and derived a figure of £742 psf as at June 2005. Applying this to an area of 1,576 sf, and using a relativity of 99%, gave a freehold value for flat 1 at No.38 of £1,180,859. Using this rate and the agreed floor area of 1,550 sf gives a freehold value of £1,150,000.

126. Four of Mr Jones's comparables have been modernised. In each case he allows for this by deducting £250 psf which he said he had agreed with other valuers as the appropriate adjustment for improvements in the market at that time and a figure that he had used successfully when negotiating settlements. He accepted that if he had underestimated the value of modernisation then his resultant valuation would be too high. Mr Buchanan's evidence was that an allowance of £250 psf for improvements was too small. He compared the sales of the three pairs of unimproved/improved flats, Nos.21, 44 and 58, and concluded,

having adjusted for time, that the percentage uplift due to improvements was 38%, 49% and 32% respectively. Using Mr Buchanan's adjustments the difference between the unimproved and improved values of these three comparables at the relevant date in June 2005 was £474 psf, £729 psf and £334 psf respectively.

127. Flat 1 at No.44 shows a much higher uplift than the other two flats relied upon by Mr Buchanan and we are not satisfied that his analysis of the first (unimproved) sale is reliable, based as it is upon a sale of a short lease in 2001 followed by a lease extension in April 2002. It was not an open market transaction of a long leasehold interest and we exclude it from our analysis.

128. We note that all three of the unimproved sales relied upon by Mr Buchanan took place before any of the improved sales. By the relevant date in June 2005 the market would have known about the results of all of the improved sales and was therefore aware of the potential profits to be made from modernising such flats. In our opinion this market knowledge would be reflected in a higher value for flat 1 at No.38 (unimproved) compared with the rates derived solely from the sales in 2002 upon which Mr Buchanan relies.

129. In the light of all the evidence we consider that Mr Jones's allowance for improvements is too low and we adopt a figure of £300 psf. We do not accept Mr Buchanan's sole reliance upon unimproved sales three years before the relevant date and we see no justification for the LVT's apparent reliance upon a single comparable at flat 1 at No.58 (unimproved).

130. The ground/lower ground flat at No.21 is two and a half times the size of the subject flat and we reflect this by placing a lower weighting on the two sales involving this property.

131. Of the 10 flats which form the main comparable evidence upon which the experts rely we have already rejected the first sale of flat 1 at No.44 (unimproved). We also reject flat A at No.2. This flat is remote from the Square and fronts onto Pont Street. Similarly we exclude Flat 2 at No.22 which is located north of Clabon Mews and well away from the Square. We do not consider it to be a useful comparable. Flat 1 at No.11 and flat E at No.30 are much closer in size to the subject flat but both were held on relatively short leases, being 39 years and 49 years respectively. Mr Jones adjusted them for lease length using Savills enfranchisable graph. Mr Jourdan said that this gives huge, unreliable adjustments. Mr Jones said they were large, but not unreliable, adjustments and that the market uses the method. Flat E at No.30 is further complicated by the presence of an onerous ground rent. We use these two comparables in our analysis but give them a reduced weight.

Conclusion

132. We have valued flat 1 at No.38 by reference to 7 of the comparables that were preferred by the experts. Details of our analysis are given in Appendix 1 and the results are summarised in Table 4 below together with the weightings that we attach to each transaction. We have given separate weightings to the two transactions at No.21 since these were more

than two years apart. We have given the second sale a lower weighting to reflect the requirement to adjust for improvements.

TABLE 4

FLAT	VALUE (£/psf)	WEIGHTING (%)	WEIGHTED VALUE (£/psf)
1 at No.11	1,041	10	104.10
G/LG at No.21 (sold 7/02)	766	15	114.90
G/LG at No.21 (sold 11/04)	937	12.5	117.12
E at No.30	921	10	92.10
1 at No.44	937	17.5	163.97
1 at No.58	777	17.5	135.97
10 at No.78	890	17.5	155.75
			883.91
	Weighted average, say		£884

133. The weighted average rate (rounded) is £884 psf and we determine the freehold value of Flat 1 at No.38 at, say, £1,370,000.

Issue (8): The freehold value of flat 2

Evidence

134. Mr Jones explained that he valued flat 2 as a participating tenant (notwithstanding that he said the opposite in his witness statement) and had therefore adjusted his comparables to unimproved values. He adjusted for time using the Savills Index and for lease length using the Savills (2002) enfranchisable graph. He made further adjustments for location and for second balconies. Mr Jones relied mainly upon 6 leasehold comparables, of widely differing length of unexpired term and all of which were sold after the Schedule 6 valuation date. Details of these comparables are summarised in Table 5:

TABLE 5

FLAT	UNEXPIRED TERM (Yrs)	DATE OF SALE	PRICE (£)	AREA (sf)	VALUE (£/psf)	FREEHOLD ADJUSTED VALUE (£/psf)
1 at No.9	16	6/06	1,100,000	1,228	896	1,450
1st floor at No.5	16	9/06	995,000	1,282	776	1,250
1st floor at No.69	17	12/06	1,165,000	1,169	997	1,424
1st floor at No.69	43	4/07	1,970,000	1,169	1,685	1,510
3 at No.53	107	11/06	3,053,777	1,778	1,718	1,233
2 at No.50	107	1/07	3,350,000	1,578	2,123	1,504
Average						1,395

135. Mr Jones took a rate of £1,348 psf to value flat 2 at No.38 (less than the average rate of £1,395 psf). This gave a freehold value of £1,650,000.

136. Mr Buchanan relied upon three main leasehold comparables to estimate the unimproved freehold value of flat 2, details of which are summarised in Table 6:

TABLE 6

FLAT	UNEXPIRED TERM (Yrs)	DATE OF SALE	PRICE (£)	AREA (sf)	VALUE (£/psf)	ADJUSTED VALUE FOR EXTENDED LEASEHOLD[1] (£/psf)
6 at No.70/72	23 (Plus 90 year lease extension)	7/05	1,650,000	1,446	1,441	887
3 at No.74	62	8/03	585,000	878	666	854
11 at No.78	72	4/04	795,000	958	830	927
Average						889
Notes: [1]Mr Buchanan adjusts the sales to July 2004						

137. Mr Buchanan took the average of the extended leasehold adjusted rates at £887 psf and multiplied the result by the agreed floor area of 1224 sf to give an extended leasehold value for flat 2 as at July 2004, the date of the section 42 notice, of £1,074,000. He then adjusted for time by 3.5% to give an equivalent figure as at the Schedule 6 valuation date (June 2005) of £1,112,000. He made a final 1% adjustment to give a freehold value of £1,123,000 or £917 psf. Mr Buchanan made several arithmetical errors when calculating this result (some of which were identified by the LVT) and the correct figure, using his analysis, is £1,137,000 or £929 psf. For the purpose of these appeals Mr Buchanan adopts the LVT's valuation of £1,145,994.

Discussion

138. The LVT preferred Mr Buchanan's evidence and rejected Mr Jones's comparables because they:

> "considered the adjustments necessary to the sales figures used by Mr Jones to be unacceptably complex. …"

The LVT relied upon "comparables with long leases". They made no comment about the date of the sales. They adopted a rate of £927 psf to value flat 2 at No.38, which was the adjusted rate that Mr Buchanan analysed from the sale of flat 11 at No.78. This gave an extended lease value of £1,134,648 and a freehold value, based on a relativity of 99%, of £1,145,994. Although this is higher than the valuation spoken to by Mr Buchanan before us he adopts it for the purposes of this appeal.

139. In our opinion the LVT made three mistakes when valuing flat 2. Firstly, Mr Buchanan adjusted the value of flat 11 at No.78 (and his other two preferred comparables) for lease length. Although he does not say in terms how he did this, judging from the results he used the Savills (2002) enfranchisable graph. The source data for that graph (produced in evidence by Mr Jones) shows that it gives the relativity of leaseholds of varying length to *freehold* values. But the LVT in adopting the rate of £927 psf to value flat 2 makes a further relativity adjustment of 1% to go from what it describes as "a long lease value" to the freehold value. Mr Buchanan says that he adjusts to an "extended leasehold value" and then makes a further 1% adjustment to derive the freehold value. But the second adjustment is unnecessary where the Savills (2002) enfranchisable graph is used and, in our opinion, both Mr Buchanan and the LVT have double counted the relativity adjustment.

140. Secondly, the correct analysis of the sale of flat 11 at No.78, upon which the LVT primarily relies, produces a higher value than was adopted by the LVT. The flat was sold in April 2004 for £795,000 (£830 psf) when the lease had approximately 72 years to run. At the relevant date (22 June 2005) it had, say, 71 years to run. Adjusting for time to the relevant date using Savills Index gives a value of £819,852 (£856 psf). Adjusting for lease length using the source data for the Savills (2002) enfranchisable graph gives a relativity of 89.4% and a final figure of £917,060 (£957 psf).

141. The figure of £927 psf calculated by Mr Buchanan and adopted by the LVT is the value at July 2004 which is the valuation date for the section 42 notice that was served in respect of flat 2 rather than the relevant date for the purposes of Schedule 6 of the 1993 Act. Mr Buchanan uses the £927 psf as part of his average rate of £887 psf (it should be £889 psf as noted by the LVT) which he then adjusts for time to give an "alternative value" at June 2005 (see paragraph 12.7 of Mr Buchanan's witness statement). The LVT make no such adjustment and use £927 psf as the value as at June 2005. In our opinion, if the LVT wished to rely (at least primarily) upon the sale of flat 11 at No.78 they should have used £957 psf which would have given a value of £1,171,368 as at the Schedule 6 valuation date.

142. Thirdly, both experts give a valuation for the freehold interest in flat 2 at No.38 which is for the property in its unimproved condition. Mr Jones said this in terms at the hearing. Mr Buchanan did not state this explicitly but we think that it is evident from the analysis of his comparables that this is what he has done (see, for instance, his analysis of the sale of flat 6 at Nos.70/72 in paragraph 12.5 of his witness statement). The LVT, by adopting one of Mr Buchanan's comparables, also value the property as an unimproved flat.

143. In their original valuation the LVT use the figure of £1,145,994 to value flat 2 as a participating tenant. In their revised valuation they use the same figure to value flat 2 as a non-participating tenant. Mr Buchanan adopts the LVT's figure and uses it to value flat 2 as a non-participating tenant and, adjusted only for time at 3.5%, uses it to value a lease extension under Schedule 13. As we have already noted the figure of £1,145,994 represents the unimproved value of flat 2. Whilst that figure (as corrected) is the appropriate starting point for a Schedule 13 valuation, the figure that should have been used when valuing as a non-participating tenant is the "as seen" value, ie the value of the flat as improved.

144. Mr Buchanan describes the improvements undertaken to flat 2 following a licence for alterations that was dated 25 April 1997. He says it "was fully refurbished and modernised". It was redesigned, re-wired and re-plumbed at a cost of £150,000. We have no doubt that such improvement works increased the freehold value of flat 2. That being so we consider that both the LVT and Mr Buchanan were wrong to use the unimproved value of flat 2 in their valuation of that flat as a non-participating tenant.

145. Turning to the evidence of the two experts, the Nominee Purchaser criticises Mr Jones's comparables for being short leases, modernised properties and sales which post date the valuation date.

146. Three of Mr Jones's comparables are short leaseholds (16 and 17 years unexpired). He converts these to equivalent freehold values by using the Savills (2002) enfranchisable graph. This leads to large adjustments with the 16 year leases being increased in value by over 90%. We have considered this criticism in connection with some of the comparables that Mr Jones uses to value flat 1 (see paragraph 131 above). The criticism is not directed at the construction of the Savills (2002) enfranchisable graph but its use in valuing freeholds by reference to short leaseholds. Mr Buchanan said in cross-examination that he did not think it appropriate to use it where the unexpired term of a lease is less than 60 years. The graph is commonly used before this Tribunal to adjust comparables for lease length. While its use in respect of the first three comparables in Table 5 above involves large adjustments, the short leasehold flats have areas that are significantly closer to that of flat 2 at No.38 than the comparables with longer unexpired terms. We therefore take the three short lease sales into account in our analysis but give them reduced weight.

147. The second criticism of Mr Jones is that he uses modernised comparables to derive an unimproved value. So far as we can tell from the details included with the evidence such modernisation and improvement is limited. The layout of the first floor flat at No.69 is unchanged between the two sales in December 2006 (with a 17 year lease) and April 2007

(with a 43 year lease). There would not have been time to complete any major improvements between these two sales and there is no reference in the sales particulars to any such work having been done. Flat 3 at No.53 was said in the sales particulars to have been "well presented". Mr Jones said that "this property had been modernised" but "not newly modernised" and he allowed £200 psf in respect of the works. He said that flat 2 at No.50 "would have benefitted from updating" but it appears from the sales particulars that between the two sales of this property in August 2003 (with a 21 year lease) and in January 2007 (with a 107 year lease) work had been undertaken to provide bedroom 2 with an en suite bathroom, to improve the layout of bedroom 1 and to create a new, separate WC. These are significant improvements but Mr Jones does not allow for them. Doing the best we can with the limited evidence available we allow 20% (£365 psf) for these improvements.

148. The third criticism of Mr Jones is that he uses comparables that all post date the valuation date (they range from June 2006 to April 2007). Details of these sales could not have been known at the valuation date, but the Tribunal has had regard in other appeals to post valuation date evidence. In this appeal the sales at Nos. 50 and 53 are the only direct evidence of the sale of long leasehold interests (107 years). This minimises the adjustment required for lease length. We consider that these transactions are relevant and we place weight upon them. Mr Buchanan opposes the use of the Savills Index beyond June 2006 at which time the market was rising rapidly. He considers that there is a greater potential for error under these conditions and declines to make indexed adjustments for time. This is not a view that has been shared by other experts appearing before this Tribunal. In *31 Cadogan Square Freehold Limited* experts from the same firms as those in the present appeal agreed to use the Savills Index across a wide range of dates, including those eschewed by Mr Buchanan. Mr Buchanan offers no alternative method of time adjusting comparables which are sold during such a volatile market. We do not accept that evidence from a rapidly rising market cannot be adjusted to a later (or an earlier) date. Savills Index is well regarded and commonly used by experts appearing before this Tribunal and we do not accept that its use should be circumscribed across any period that we are considering in this appeal.

149. Mr Buchanan relies mainly upon three comparables. He does not state how he adjusts these for lease length or other factors (apart from a 5% adjustment for the off square position of flat 2 at No.38 when analysing flat 6 at No.70/72). We mentioned this at the hearing and although Mr Buchanan provided us with some corrected pages for his witness statement, he did not provide further details, either then or subsequently, of his analysis of these comparables.

150. Flat 11 at No.78 is a relatively small rear flat with a reception room that faces west, away from the Square. There is no en suite bathroom and there are stairs between bedroom 2 and the other habitable rooms. Mr Jones says that it is dated by comparison with flat 2 at No.38.

151. Flat 3 at No.74 is a much smaller flat which Mr Jones says was poorly converted. The reception room is compromised by a partially open plan kitchen and a narrow second bedroom at the front. There is only a single bathroom (not en suite) and the sales particulars say that it required updating.

152. Mr Jones describes Mr Buchanan's analysis of the sale of flat 6 at No.72 as unconventional since it combines the sale of a short leasehold interest with the premium paid for a lease extension.

153. We do not agree with the LVT's heavy reliance upon the sale of flat 11 at No.78. In our opinion it is not a good comparable for the reasons given in paragraph 150 above.

154. The layout of flat 3 at No.74 is poor and the sales particulars recognised the need for the flat to be updated. But the appropriate comparison is between that flat and flat 2 at No.38 in its unimproved condition. Before flat 2 was improved it had a third bedroom, located between the bedroom at the rear of the flat and the kitchen. Between the kitchen and the largest bedroom was a separate bathroom. The improvements, for which a licence was granted in 1997, comprised the conversion of the bedroom next to the kitchen into a larger en suite bathroom for the rear bedroom which was itself enlarged. We consider flat 3 at No.74 to be a relevant comparable and we attach weight to it.

155. The sale of flat 6 at Nos.70/72 was a hybrid transaction involving the sale of a short (23 year) lease and a premium for a lease extension. Mr Buchanan says "At the time of the lease extension the unimproved value had been agreed at a figure of £1,350,000 which indicated a value of £933 psf". There are no details of this agreement. Apparently Mr Buchanan was not one of the parties involved. The analysis of this type of transaction is not straightforward (Mr Jones fairly describes it as unconventional) and without details of the component parts of the transaction we give it no weight.

156. We do not accept the LVT's view that Mr Jones's adjustments of his comparables are unacceptably complex. Mr Jones's adjustments are of a type and a magnitude that are commonly used when valuing properties in Cadogan Square and which have been considered in detail by the Tribunal in several appeals in recent years.

Conclusions

157. We value flat 2 at No.38 as a participating tenant as at the relevant date (22 June 2005) - see issue 11 below. As such we are concerned with the unimproved value of the flat.

158. We consider that the best comparables are the first floor flats at Nos. 5 and 9, flat 2 at No.50, flat 3 at No.53, the first floor flat at No.69 (sold twice) and flat 3 at No.74. We summarise our analysis of these comparables in Appendix 2.

159. We do not give these comparables equal weight. Flat 3 at No.74 (weighted 30%) was a sale before the relevant date and requires the smallest number of adjustments. However it was only a 60 year lease and is a significantly smaller flat than flat 2 at No.38. Flat 2 at No.50 and flat 3 at No.53 have the benefit of being long leases (107 years), but they were both sold a long time after the relevant date and in a rapidly rising market. They also require

adjustment for improvements (about the effect of which there is little evidence) and several other factors. The transaction at flat 3 at No.53 was complicated by the sale to a tenant. We weight both of these comparables at 20%. The first floor flats at Nos. 5 and 9 were short leasehold sales and although we admit them as evidence we give them both a reduced weighting of 10%. The first floor flat at No.69 was sold twice in close succession. This flat has the advantage of being very close in size to flat 2 at No.38 but the second sale was nearly two years after the relevant date, when the flat may have been improved (or at least redecorated) to a limited degree and is still a relatively short leasehold with 43 years unexpired (the first sale being of a short leasehold interest of 17 years). We have averaged the adjusted value of these two sales so as not to place too much emphasis on a property that was sold twice in 4 months. We then weight the average figure at 10%. The results of this weighting exercise are summarised in Table 7 below.

TABLE 7

FLAT	VALUE (£/psf)	WEIGHTING (%)	WEIGHTED VALUE (£/psf)
First floor flat at No.5	1,376	10	137.6
Flat 1 at No.9	1,648	10	164.8
Flat 2 at No.50	1,280	20	256.0
Flat 3 at No.53	1,167	20	233.4
First floor flat at No.69 (12/06)	1,503		
First floor flat at No.69 (4/07)	1,581		
First floor flat at No.69 (average)	1,542	10	154.2
Flat 3 at No.74	850	30	255.0
			1,201.0
	Weighted average, say		£1,200

160. Applying these weightings to the six comparables gives a weighted average of £1,200 psf. Using this rate we value the freehold interest in flat 2 at No.38 at £1,468,800 which we round to £1,470,000.

Issue (9): The deferment rate

161. In *Cadogan Square Properties Limited v Earl Cadogan* [2010] UKUT 427 (LC) the Tribunal, The Honourable Mr Justice Morgan and A J Trott FRICS, determined that the appropriate deferment rate to value 38 Cadogan Square in these appeals is 5.25%.

Issue (10): Restrictive Covenants

162. Under Schedule 7 paragraph 5(l)(b) of the 1993 Act the relevant part of the statutory provision as to the inclusion of restrictive covenants is as follows:

> "(1) As regards restrictive covenants, the conveyance shall include….
>
> (b) such provisions (if any) as the freeholder or the nominee purchaser may require to secure the continuance (with suitable adaptations) of restrictions arising by virtue of any such lease or collateral agreement as is mentioned in paragraph (a)(i), being either –
>
> (i) restrictions affecting the relevant premises which are capable of benefiting other property and (if enforceable only by the freeholder) are such as materially to enhance the value of the other property, or
>
> (ii) restrictions affecting other property which are such as materially to enhance the value of the relevant premises; and
>
> (c) such further restrictions as the freeholder may require to restrict the use of the relevant premises in a way which –
>
> (i) will not interfere with the reasonable enjoyment of those premises as they have been enjoyed during the currency of the leases subject to which they are to be acquired, but
>
> (ii) will materially enhance the value of other property in which the freeholder has an interest at the relevant date.
>
> (2) In this paragraph "restrictive covenant" means a covenant or agreement restrictive of the user of any land or building."

163. The relevant restriction in the present headlease is as follows (Clause X):

> "NOT to use or permit the demised premises or any part thereof to be used otherwise than as follows each unit to be used as a private residence in one family occupation only A self-contained flat on each of the first second third and fourth floors of the demised premises A self-contained maisonette comprising the ground floor and the rear part of the basement A self-contained flat for the Caretaker in the front part of the basement and tenants stores and boiler room in the basement"

164. In its counter-notice Cadogan proposed the inclusion of a restrictive covenant including the following (italics supplied):

> "not to carry on or permit to be carried on at the specified premises or on any part thereof any trade business or profession and not to use nor permit or suffer to be used the specified premises for any auction exhibition meeting or public entertainment or any unlawful illegal or immoral purpose *or otherwise than as either*

> *6 self contained private residential flats each such flat to be used as a private dwelling in the occupation of one family only or as a single private dwelling house to be used in the occupation of one family only*".

165. In its Statement of Case Cadogan altered its position, amending the italicised words in the proposed covenant to read:

> "save that the use of the Property is to be as not more than six self-contained private residential flats each such flat to be used as a private dwelling in the occupation of one family only".

Thus use as a single private dwelling house was omitted but use for fewer than six flats would be permitted.

166. The Nominee Purchaser did not agree this proposal but contended that the concluding words of the covenant should read:

> "Not without the written consent of the Company, such consent not to be unreasonably withheld, to use or permit the Property to be used otherwise than as self contained private residential flats or as a dwelling house and if the Property is used as flats with no more than six flats".

167. The LVT concluded that Cadogan's version of the covenant was the appropriate one. The Nominee Purchaser appealed against this conclusion. On the hearing of the appeal the Nominee Purchaser contended for a variant of the covenant which it had sought before the LVT and submitted that the form of covenant should be:

> "The use of the Property is to be as not more than six self-contained private residential flats each such flat to be used as a private dwelling in the occupation of one family only; or as a single private dwelling house (to be used in the occupation of one family only)."

168. In argument counsel for the Nominee Purchaser accepted that it would be desirable to make clear that a "flat" could extend over one or more floors.

169. On behalf of the Nominee Purchaser it was submitted that Cadogan's proposed covenant was in very different terms to the restrictive covenant which the LVT directed should be included in the transfer, and that covenant could therefore only be justified under paragraph 5(c) and not paragraph 5(b) of Schedule 7, and that therefore the covenant could only be imposed if it would materially enhance the value of other property in which Cadogan had an interest at the relevant date.

170. The Nominee Purchaser accepted that the Lands Tribunal had, in the past, held that the correct approach to "material enhancement" in this sort of provision was to look at the matter broadly and not by reference to money values: see *Moreau v Howard de Walden Estates*

Limited [2003] Lands Tribunal LRA/2/2002 (unreported) at paragraph 185 and *Higgs v Paul* [2005] Lands Tribunal LRA/2/2005 (unreported) at paragraph 60, but submitted that this is incorrect. It was said that paragraph 5(c)(ii) used the language of value, not that of general advantage and a comparison was drawn with the language of section 84(1A) of the Law of Property Act 1925 which refers, in the context of restrictive covenants, to "practical benefits of substantial value or advantage". Accordingly, in the absence of evidence that the proposed covenant materially enhances the value of other property which Cadogan owned in June 2005, it was submitted that the only restrictive covenant which should be included in the transfer was the one that the Nominee Purchaser agreed to.

171. The Nominee Purchaser noted that Cadogan's application to the LVT dated 8 November 2005 applied for the LVT to determine the terms of the freehold transfer of the Property and enclosed a copy of the counter-notice, but made no other mention of the terms that Cadogan sought to have included in the transfer. It was not until Cadogan's Statement of Case for the LVT dated 6 November 2006, almost a year later, that Cadogan contended, for the first time, that the transfer should include a covenant in terms that prevented use of the property as a single dwelling house. The Nominee Purchaser challenged the capacity of the proposed restrictions to benefit other property, and the suitability of the proposed adaptation of the lease restrictions. Its case was that there was no benefit to the Cadogan Estate in being able to prevent the property from being used as a single house. It noted that in the case of both 23 Cadogan Square and 42 Cadogan Square, and also 31 and 37 Cadogan Square, Cadogan sought restrictive covenants that did not prevent the use of the properties as a single dwelling house. It offered no explanation why a covenant preventing 38 Cadogan Square from being used as a single dwelling house should materially enhance the value of its retained Estate, but such a covenant would not have that effect in the case of 42 Cadogan Square, which is one door away, or 23, 31 or 37 Cadogan Square, on the opposite side of Cadogan Square.

172. In answer Cadogan submitted that the Nominee Purchaser was seeking to buy a house converted into flats, at prices derived from and assuming continued use as flats but with the potential to convert to a house without paying for that potential. Cadogan accepted that the statutory power to impose restrictive covenants would not justify imposing a covenant just because the Nominee Purchaser was seeking to obtain a development opportunity without paying for it. The statutory test of material enhancement is not a particularly stringent one. Decisions of the Lands Tribunal such as *Peck v Trustees of Hornsey Parochial Charities* (1971) 22 P & CR 789, *Le Mesurier v Pitt* (1972) P & CR 389 and *Moreau* showed that the maintenance of value of other property would satisfy this test. There is no need for evidence as to effect on value. It was a matter of general impression and not a detailed valuation exercise. There was no evidence and could be no suggestion that the covenant directed by the LVT was unreasonable.

173. Cadogan submitted that the ability to restrict redevelopment as a house was capable of meeting the statutory test. It was suggested first that building works on a major project such as reconverting a house in Cadogan Square could involve disruption for years with a building site, scaffolding and skips affecting adjacent and neighbouring property. Scaffolding is erected not just for external works, it is regularly used to provide access to upper floors so that materials can be taken in and removed externally. Second it was submitted that

satisfying part of the demand for houses in Cadogan Square by creating one at No.38 would reduce the demand elsewhere in Cadogan Square and on the Cadogan Estate.

174. In our judgment the covenant proposed by Cadogan and ordered by the LVT can properly be described as imposing restrictions arising by virtue of the headlease with suitable adaptations. The fact that it permits the user of the property as fewer than six flats is a relaxation of the covenant, but is not (contrary to what was argued by the Nominee Purchaser) in "very different terms" to that covenant. Each covenant requires that the user of the property be as flats. A variation allowing it to be used as fewer flats seems to us no more than a suitable adaptation. In our judgment therefore the question is whether the restrictions are capable of benefiting other property and, since they are enforceable only by the freeholder, are such as materially to enhance the value of the other property.

175. We accept that the statement in *Moreau* at paragraph 185 that "the question of material enhancement can...only realistically be considered in general terms" is correct, as is the statement in *Higgs* at paragraph 60:

> "In my judgment, and following these decisions, the concept of material enhancement includes both an increase in value due to restrictions and the maintenance of value which would otherwise deteriorate. The concept is to be applied as a matter of general impression and not by attempting a detailed valuation exercise."

In our view these statements set out what is now established as a matter of principle and accord with common sense.

176. However we are not persuaded that the imposition of the requirement that prevents the property from being used as a single private dwelling house in the occupation of one family only is either capable of benefiting other property or is such as materially to enhance the value of the other property.

177. The first argument put forward by Cadogan was as to the potential disruption which might be caused by major building works. In our view this is not an objection of any substance. Scaffolding will periodically be erected for decorative and repair work. It may well be erected in connection with internal works. As was accepted in evidence by both Mr Jones and Mr Buchanan the sort of persons likely to purchase flats in No.38 are very likely to engage in major works of internal re-organisation and refurbishment. This may well involve the erection of scaffolding, the placing of skips in the Square and the like, as was apparent from the scaffolding and skips which we observed elsewhere in the Square on our site visit. The covenant will not meet this supposed source of concern.

178. The second argument related to the diminution in value of the remainder of the Cadogan Estate. No evidence was advanced in relation to this submission. This was particularly surprising in the light of Cadogan's apparent preparedness to allow 23, 31, 37 and 42 to be converted to use as single houses, and its initial preparedness to allow 38 to be used as a house in single family occupation. In the light of this, it must be presumed that

Cadogan had formed the view some time between November 2005 and November 2006 that some form of tipping point had been reached at which it became inimical to the Estate's interests to allow more properties to be converted from flats to houses in single family occupation, but no evidence in support of any such argument was advanced.

179. On this state of the evidence we are not satisfied on the balance of probabilities that the proposed covenant against user as a single private dwelling house (to be used in the occupation of one family only) is either capable of benefiting other property or is such as materially to enhance the value of the other property. In these circumstances we direct that the transfer shall contain a covenant in the form sought by the Nominee Purchaser subject only to additional words to make it clear that a flat in this context may extend over more than one floor.

Issue (11): Flat 2 section 42 notice

180. The factual background to this issue is as follows: on 2 July 2004, Sibel Erkman, the then tenant of flat 2, served a notice under section 42 of the 1993 Act on Cadogan, claiming a new lease of flat 2 in the property. On 1 September 2004, Cadogan served a counter notice admitting that on 2 July 2004 she had the right to acquire a new lease of flat 2. She was one of the qualifying tenants who served the initial notice dated 21 June 2005 under section13 of the 1993 Act. Sibel Erkman had to be a participating tenant in order to produce a qualifying majority at the date the notice was served. On 18 September 2006 she executed a transfer of the lease of flat 2 to Amej Properties Limited, a company apparently under the control of her family, and at the same time assigned to Amej the rights and obligations arising from the flat 2 Section 42 notice. Amej was then registered as proprietor of flat 2. On 22 November 2006, the Respondent served notice on Cadogan that flat 2 was assigned by Sibel Erkman to Amej on 18 September 2006 and that Amej had not become a participating tenant in place of Sibel Erkman.

181. Section 14(1) of the 1993 Act defines "participating tenants" as the following persons-

> "(a) in relation to the relevant date, the qualifying tenants by whom the initial notice is given; and
>
> (b) in relation to any time falling after that date, such of those qualifying tenants as for the time being remain qualifying tenants of flats contained in the specified premises."

182. Schedule 6 paragraph 3 of the 1993 Act provides:

> "(1) Subject to the provisions of this paragraph, the value of the freeholder's interest in the specified premises is the amount which at the relevant date that interest might be expected to realise if sold on the open market by a willing seller (with no person who falls within sub-paragraph (1A) buying or seeking to buy) on the following assumptions –

(a) on the assumption that the vendor is selling for an estate in fee simple –

(i) subject to any leases subject to which the freeholder's interest in the premises is to be acquired by the nominee purchaser, but

(ii) subject also to any intermediate or other leasehold interests in the premises which are to be acquired by the nominee purchaser;

(b) on the assumption that this Chapter and Chapter II confer no right to acquire any interest in the specified premises or to acquire any new lease (except that this shall not preclude the taking into account of a notice given under section 42 with respect to a flat contained in the specified premises where it is given by a person other than a participating tenant);

…"

183. Schedule 6 paragraph 4 provides:

"(1) The marriage value is the amount referred to in sub-paragraph (2), and the freeholder's share of the marriage value is 50 per cent of that amount.

(2) Subject to sub-paragraph (2A), the marriage value is any increase in the aggregate value of the freehold and every intermediate leasehold interest in the specified premises, when regarded as being (in consequence of their being acquired by the nominee purchaser) interests under the control of the [persons who are participating tenants immediately before a binding contract is entered into in pursuance of the initial notice], as compared with the aggregate value of those interests when held by the persons from whom they are to be so acquired, being an increase in value –

(a) which is attributable to the potential ability of the [persons who are participating tenants immediately before a binding contract is entered into in pursuance of the initial notice], once those interests have been so acquired, to have new leases granted to them without payment of any premium and without restriction as to length of term, and

(b) which, if those interests were being sold to the nominee purchaser on the open market by willing sellers, the nominee purchaser would have to agree to share with the sellers in order to reach agreement as to price."

184. The words shown in square brackets in Schedule 6 paragraph 4 were introduced by the Commonhold and Leasehold Reform Act 2002 (Commencement No.5 and Saving and Transitional Provision) Order 2004, SI 2004/3056. This states:

"4(1) During the period beginning with 28th February 2005 and ending on the date on which sections 121 to 124 come into force, paragraph 4(2) of Schedule 6 to the Leasehold Reform, Housing and Urban Development Act 1993 shall have effect as if, for "participating tenants", there were substituted "persons

who are participating tenants immediately before a binding contract is entered into in pursuance of the initial notice".

185. Sections 121 to 124 are even now not in force.

186. On behalf of the Nominee Purchaser it was submitted that on this basis, marriage value will only be payable in respect of those flats where the tenants remain participating up to the point that a binding contract is entered into and that Parliament clearly intended that, where a leaseholder ceased to participate, no marriage value should be payable in respect of the relevant flat. There could, it was said, be no possible criticism if a flat ceased to participate. If there was any side deal with the nominee purchaser it had to be disclosed under section 18. It followed that in this case the section 42 notice should not be taken into account.

187. Cadogan disputed this submission and asserted that the series of events was a manipulation by the Nominee Purchaser of the ownership of flat 2 to reduce the marriage value. It was suggested that the construction sought by the Nominee Purchaser could not be right and that it would produce an injustice to the landlord, but no substantive argument was produced to demonstrate why the Nominee Purchaser's argument was incorrect.

188. The LVT accepted the Nominee Purchaser's argument with evident reluctance, saying:

> "The result is that the Tribunal's valuation (see Appendix A) does take into account the s.42 Notice served in respect of flat 1 as indicated above but not that served in respect of flat 2. This seems strictly in accordance with what the statute says (para. 3(l)(b) of Schedule 6). Although, as at the valuation date, both flats were "participating flats" the Tribunal considers that the hypothetical purchaser of the Property must be assumed to be buying on the basis that there is not and will not be any collective enfranchisement or lease extensions (other than in pursuance of a s.42 notice "given by a person other than a participating tenant"). Nevertheless the reality is that the s.42 notice will not proceed re flat 1, because the present tenant is participating in the enfranchisement, whilst theoretically the s.42 notice might proceed re flat 2, because the present tenant is not participating (although here this is unlikely given that the tenant is a connected company). In the light of this, the result to which the Tribunal has been driven by the statutory wording might well not be thought sensible."

189. In our judgment it is an indisputable fact that although Sibel Erkman was a participating tenant at the relevant date, she ceased to be a qualifying (and hence participating) tenant when she transferred the lease of flat 2 to Amej in May 2006 as provided by section 14(1)(b). Amej chose not to elect to participate in the collective enfranchisement and so from the date of the assignment there was no participating tenant in flat 2. The words in Schedule 6 paragraph 4(2) (as amended by the 2004 statutory instrument) permit the taking into account of marriage value only where there are "persons who are participating tenants immediately before a binding contract is entered into in pursuance of the initial notice". Those persons do not include either Sibel Erkman or Amej and so, it appears to us, flat 2 cannot be included within the marriage value calculation even though there was a participating tenant at the

relevant date and the value of the freeholder's interest is calculated on the basis that the leasehold interest is that of a participating tenant. Nor will the Nominee Purchaser pay hope value in respect of flat 2 (which falls to be determined by reference to the status of the leaseholder of flat 2 as a participating tenant at the relevant date).

190. On the face of it these provisions mean that there will be a Catch-22 dilemma whenever the price payable for a collective enfranchisement is referred on appeal to an LVT: the parties will not enter into a binding contract until they know the price the LVT determines is payable for the freehold, but the LVT cannot determine that price until it knows who the participating tenants will be immediately before the binding contract is entered into (and can thus calculate what, if any, marriage value should be included). The only practicable answer to this conundrum appears to us to be that the LVT should assume when making its valuation that the status quo at the time of the hearing before the LVT will be maintained until any binding contract is entered into.

191. In our judgment the LVT was right both in the conclusion which it reached and in the reluctance with which it reached it. The conclusion seems to us inescapable on the words of the section as amended by the statutory instrument, though whether the legislators envisaged the particular effect of the words used may be open to doubt.

Valuation

192. Our conclusions about the issues relevant to the assessment of the price payable for the landlords' interests in the Property may be summarised as follows:

Flat 1: Freehold value: £1,370,000
Existing leasehold value: £552,750 (40%)
Participating tenant for the purposes of Schedule 6 paragraphs 3 and 4.
Section 42 notice served by non-participating tenant but no effect on value as at the relevant date (22 June 2005).

Flat 2: Freehold value: £1,470,000
Participating tenant for the purposes of Schedule 6 paragraph 3 but a non-participating tenant for the purposes of Schedule 6 paragraph 4.
Section 42 notice served by participating tenant and so not taken into account.

Flat 3: Freehold value: £1,070,750 (agreed)
Existing leasehold value: £439,000 (41% - taken as the average of the relativities at flat 1 and flat 5).
Non-participating flat for the purposes of Schedule 6 paragraphs 3 and 4.
No section 42 notice but hope value taken into account at 5% of (total) marriage value.

Flat 4: Freehold value: £772,500 (agreed)
Non-participating tenant with an extended lease with more than 80 years unexpired term.
No hope value.

Flat 5: Freehold value: £595,000 (agreed)
Existing leasehold value: £251,250 (42%)
Participating tenant for the purposes of Schedule 6 paragraphs 3 and 4.
No section 42 notice.
No hope value.

Caretaker's flat: Freehold value: £411,049 (agreed)
Rental value (reflecting 50% reduction due to user restriction): £7,800 pa
Non-participating tenant.

193. The parties' revised valuations produced the following figures for the combined price payable for the freehold and intermediate leasehold interests:

Cadogan: Total price payable £2,614,540 (Mr Jones's valuation CSJ 3 which excludes hope value for the caretaker's flat and takes 22 June 2005 as the valuation date for flat 1)

Nominee Purchaser: Total price payable £1,880,595

LVT: Total price payable £1,888,685.

194. Our valuation, based upon the above conclusions, is shown in Appendix 3. We determine the total price payable at £2,212,179 apportioned £2,181,729 to the freeholder and £30,450 to the intermediate leaseholder.

Dated 21 April 2011

His Honour Judge Robert Reid

A J Trott FRICS

APPENDIX 1

FLAT 1 AT No.38: LANDS CHAMBER ANALYSIS OF PREFERRED COMPARABLES

FLAT	DATE	SALE PRICE (£)	LEASE LENGTH (yrs)	AREA (sf)	PRICE (£/psf)	ADJUSTMENTS						FULLY ADJUSTED FREEHOLD VALUE (£/psf)
						TO VALUATION DATE (6/05) (£)	IMPROVEMENTS (£)	GARDEN/ OUTSIDE SPACE (%)	POSITION ON SQUARE (%)	LAYOUT (%)	RELATIVITY (%)	
1 at No.11	12/05	1,430,000	39	1,861	768	1,410,306	–	–	2.5	–	74.6	1,041
G/LG at No.21 (unimproved)	7/02	2,900,000	111	3,877	748	2,910,906	–	–	–	–	98	766
G/LG at No.21 (improved)	11/04	4,700,000	108	3,931	1,196	4,789,726	300	–	–	–	98	937
E at No.30	11/02	1,129,141[1]	49	1,601	695	1,153,901	–	–	2.5	–	80.2	921
1 at No.44 (improved)	2/03	2,500,000	110	2,098	1,192	2,605,609	300	–	(2.5)	–	98	937
1 at No.58 (unimproved)	4/02	1,825,000	119	2,560	713	1,893,357	–	8.5	(5)	–	98.5	777
10 at No.78	1/07	2,000,000	Share of F/H	1,418	1,410	1,686,872	300	–	–	–	–	890
Notes: [1] Includes Mr Jones's allowance of £16,141 for onerous ground rent.												

APPENDIX 2

FLAT 2 AT No.38: LANDS CHAMBER ANALYSIS OF PREFERRED COMPARABLES

FLAT	DATE	SALE PRICE (£)	LEASE LENGTH (yrs)	AREA (sf)	PRICE (£/psf)	ADJUSTMENTS						FULLY ADJUSTED FREEHOLD VALUE (£/psf)
						TO VALUATION DATE (6/05) (£/psf)[1]	LEASE LENGTH[2] (£/psf)	POSITION ON SQUARE	IMPROVEMENTS	BALCONY	TENANTED	
1st floor at No.5	9/06	995,000	16	1,282	776	688	1,311	5%	–	–	–	1,376
1 at No.9	6/06	1,100,000	16	1,228	896	824	1,570	5%	–	–	–	1,648
2 at No.50	1/07	3,350,000	107	1,578	2,123	1,791	1,828	(5%)	(20%)	(5%)	–	1,280
3 at No.53	11/06	3,053,777	107	1,778	1,718	1,489	1,519	(5%)	(£200 psf)	–	(5%)	1,167
1st floor at No.69	12/06	1,165,000	17	1,169	997	854	1,582	(5%)	–	–	–	1,503
1st floor at No.69	4/07	1,970,000	43	1,169	1,685	1,362	1,769	(5%)	(£100 psf)	–	–	1,581
3 at No.74	8/03	585,000	60	878	666	724	850	–	–	–	–	850

Notes: [1] Adjusted to valuation date using Savills PCL Index
[2]Adjusted by Savills enfranchisable (2002) graph source data (trial bundle, p.305)

APPENDIX 3

38 CADOGAN SQUARE: LANDS CHAMBER VALUATION

	Valuation date: 22 June 2005				
		£	£	£	£
1.	**VALUE OF FREEHOLDER'S INTEREST**				
(i)	*Participating flats (Flats 1, 2 and 5)*				
	(a) Apportioned head rent		493		
	x YP 17.75 years @ 6%		10.742		
				5,296	
	(b) Reversion to FHVP value				
	Flat 1		1,370,000		
	Flat 2		1,470,000		
	Flat 5		595,000		
			3,435,000		
	x PV of £1 in 17.75 years @ 5.25%		0.403		
				1,384,305	
	Value of freeholder's interest in participating flats				1,389,601
(ii)	*Non-participating flats (Flats 3, 4 and caretaker)*				
	(a) Apportioned head rent		282		
	x YP 17.75 years @ 6%		10.742		
				3,029	
	(b) Reversion to FHVP value				
	Flat 3	1,070,750			
	Caretaker's flat	411,049			
		1,481,799			
	x PV of £1 in 17.75 years @ 5.25%	0.403			
			597,165		
	Flat 4	772,500			
	x PV of £1 in 107.75 years @ 5%	0.005			
			3,862		
				601,027	
	(c) Hope value re Flat 3				
	FHVP value		1,070,750		
	Less				
	(i) Freeholder's present interest				
	Term rent receivable (apportioned)	141			
	x YP 17.75 yrs @ 6%	10.742			
			(1,515)		
	Reversion to FHVP value	1,070,750			
	x PV of £1 in 17.75 yrs @ 5.25%	0.403			
			(431,512)		
	(ii) Intermediate leaseholder's present interest				
	Rent receivable	318			
	Less apportioned rent payable	141			
	Profit rent	177			
	x YP 17.75 yrs @ 6%, 3%, 30p tax	8.189			
			(1,449)		
	(iii) Existing leasehold interest at 41% relativity		(439,007)		

		£	£	£	£
	Total (potential) marriage value		197,267		
	Landlord's hope value at 5% of total marriage value		0.05		
			9,863		
	Freeholder's share				
	£433,027 =		0.997		
	£433,027 + £1,449				
				9,833	
	Value of freeholder's interest in non-participating flats				613,889
	Total value of freeholder's interest				2,003,490
2.	**VALUE OF INTERMEDIATE LEASEHOLDER'S INTEREST**				
(i)	*Participating flats (flats 1, 2 and 5)*				
	Rent receivable (until rent review on flat 5)	940			
	Less rent payable	493			
	Profit rent	447			
	x YP 5.75 yrs @ 6%, 3%, 30p tax	3.432			
			1,534		
	Reversion to rent receivable	1,140			
	Less rent payable	493			
	Profit rent	647			
	x YP 12 yrs @ 6%, 3%, 30p tax	6.224			
	x PV of £1 in 5.75 yrs @ 6%	0.715			
			2,879		
	Intermediate leaseholder's interest in participating flats			4,413	
(ii)	*Non-participating flats (flats 3 and 4)*				
	Rent receivable	318			
	Less rent payable	282			
	Profit rent	36			
	x YP 17.75 yrs @ 6%, 3%, 30p tax	8.189			
	Intermediate leaseholder's interest in non-participating flats			295	
(iii)	*Caretaker's flat*				
	Rental value reflecting user restriction				
	(50% deduction)	7,800			
	Recoverable rent at 4/11^{ths}	2,836			
	x YP 17.75 up @ 6%, 3%, 30p tax	8.189			
				23,224	
(iv)	*Hope value re Flat 3*				
	Apportioned share			30	
	Total value of intermediate leaseholder's interest				27,962

		£	£	£	£
3.	**MARRIAGE VALUE**				
	Participating flats with less than 80 years unexpired (Flats 1 and 5)				
	FHVP value			1,965,000	
	Less				
	(i) Freeholder's present interest				
	(a) Term rent receivable	352			
	x YP 17.75 yrs @ 6%	10.742			
			(3,781)		
	(b) Reversion to FHVP	1,965,000			
	X PV of £1 in 17.75 yrs @ 5.25%	0.403			
			(791,895)		
	(ii) Intermediate leaseholder's present interest				
	(a) Term rent receivable	730			
	Rent payable	352			
	Profit rent	378			
	x YP 5.75 yrs @ 6%, 3%, 30p tax	3.432			
			(1,297)		
	(b) Reversionary rent receivable	930			
	Rent payable	352			
	Profit rent	578			
	x YP 12 yrs @ 6%, 3%, 30p tax	6.224			
	x PV of £1 in 5.75 yrs @ 6%	0.715			
			(2,572)		
	(iii) Lessee's present interest				
	(a) Flat 1		(552,750)		
	(b) Flat 5		(251,250)		
				(£1,603,545)	
	Marriage value			361,455	
	Landlords' share at 50%				180,727
	Total value of landlords' interests				2,212,179
4.	**APPORTIONMENT OF MARRIAGE VALUE AND PREMIUM PAYABLE**				
	(i) Freeholder				
	(a) Value of freeholder's interest		2,003,490		
	(including hope value at flat 3)				
	(b) share of marriage value				
	£2,003,490 x £180,727		178,239		
	£2,031,452				
				2,181,729	
	(ii) Intermediate leaseholder				
	(a) Value of intermediate leaseholder's interest (including hope value at flat 3)		27,962		
	(b) Share of marriage value				
	£27,962 x £180,727		2,488		
	£2,031,452				
				30,450	
	Total premium payable				**2,212,179**