UPPER TRIBUNAL (LANDS CHAMBER)

UT Neutral citation number: [2011] UKUT 415 (LC)
LC Case Number: LRA/86/2009

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LEASEHOLD ENFRANCHISEMENT – collective enfranchisement – leases of less than 5 years unexpired – leasehold vacant possession values (relativity) – potential for provision of additional flat(s) on roof – hope value – deferment rate – terms of transfer – appeal allowed in part – enfranchisement price £2,961,613

IN THE MATTER OF AN APPEAL FROM A DECISION OF THE LEASEHOLD VALUATION TRIBUNAL FOR THE LONDON RENT ASSESSMENT PANEL

BETWEEN **TRUSTEES OF THE SLOANE STANLEY ESTATE** **Appellants**

and

CHARLES CAREY-MORGAN (1)
JOHN MATTHEW STEPHENSON (2) **Respondents**

Re: Vale Court, 21 Mallord Street, London SW3 6AL

Before: The President and Paul Francis FRICS

Sitting at: 43-45 Bedford Square, London WC1B 3AS
on 4-6 April 2011

Kenneth Munro, instructed by Pemberton Greenish LLP, solicitors of London SW3, for the appellant landlords
James McDonald for the respondent lessees

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The following cases are referred to in this decision:

Earl Cadogan v Sportelli [2010] 1 AC 226; [2007] EWCA Civ 1042
Cadogan Square Properties Ltd and Others v Earl Cadogan [2010] UKUT 427 (LC)
Cadogan v Erkman [2011] UKUT 90 LC
Cadogan v Cadogan Square Ltd [2011] UKUT 154 (LC)
Culley v Daejan Properties Ltd [2009] UKUT 168 (LC)

The following cases were also referred to in argument:

Arbib v Earl Cadogan [2005] 3 EGLR 139
31 Cadogan Square Ltd v Earl Cadogan [2010] UKUT 321 (LC)
Arrowdell v Coniston Court (North) Hove Ltd [2007] RVR 39
Nailrile Ltd v Earl Cadogan [2009] RVR 95
Phillips v Brewin Dolphin Bell Lawrie Ltd [2001] 1 WLR 143
Dependable Homes Ltd v Mann [2009] UKUT 171 (LC)
Moreau v Howard de Walden Estates (2003) LT Ref: LRA/2/2002 (Unreported)

DECISION

Introduction

1. Mr Charles Carey-Morgan and Mr John Stephenson, acting on behalf of themselves and the other 11 nominee purchasers involved in the collective enfranchisement of Vale Court, 21 Mallord Street, London SW3 6AL, appeal, with permission of this Tribunal, against a decision and supplementary decision of the Leasehold Valuation Tribunal for the London Rent Assessment Panel dated 16 December 2008 and 24 April 2009 respectively. The LVT's initial decision, which followed hearings held over four days between September and November 2008, dealt with five issues that were in dispute. It provisionally determined the premium payable for the freehold pursuant to the provisions of Schedule 6 to the Leasehold Reform, Housing and Urban Development Act 1993 at £2,652,389. No allowance was made for hope value, but in its decision the LVT said that it had had the opportunity to consider the House of Lords' judgment in *Earl Cadogan v Sportelli* [2010] 1 AC 226 which had been published since the hearings, and invited the parties to make further submissions on that issue. Following a further hearing on 5 March 2009 the LVT determined hope value at an additional £14,048, creating a premium of £2,666,407. In its statement of case, the appellant sought an enfranchisement price of £3,568,403.

2. Mr Kenneth Munro of counsel called Mr Damian Greenish, one of the trustees of the Sloane Stanley Estate, as a witness of fact for the appellant. He also called, in connection with the roof development issue, Mr Anthony Hayes, principal of the Michael Barclay Partnership LLP of London WC2, who gave structural engineering evidence, Mr Graham Anthony Oliver BA MA MRTPI, a partner in Gerald Eve, Chartered Surveyors and Property Consultants, who gave planning evidence and Mr Anthony Walker Dip Arch (dist) Grad Dip (cons) AA RIBA AABC of DLG Architects, London E1 who gave evidence in respect of Conservation Area matters. Mr Einar Roberts BSc (Hons) MLE MRICS a partner in Cluttons LLP Chartered Surveyors and Property Consultants of London W1 gave valuation evidence.

3. Mr James McDonald, for the respondent lessees, called Mr Charles Carey-Morgan as a witness of fact, together with Mr Ronald McDonald MRICS, principal of the McDonald Partnership of London SE21, who gave evidence on planning and valuation issues. References in this decision to Mr McDonald are to Mr Ronald McDonald.

Facts

4. Vale Court comprises an L-shaped purpose-built mansion block constructed in the 1920s of brick with multi-pane Georgian style sash windows under flat roofs. It is located on the corner of Mallord Street and The Vale in the Royal Borough of Kensington and Chelsea. It comprises 25 self-contained lateral apartments on basement, raised ground and three upper floors. A small enclosed garden area to the rear is not included within the proposed transfer. The property abuts the Telephone Exchange Building (19 Mallord Street), which is also in the freehold ownership of the appellant landlords, and beyond that is another residential mansion

block – Tryon House (17 Mallord Street). On The Vale elevation Vale Court is adjacent to buildings that front onto Kings Road. These have retail/commercial uses at ground floor. The building is in an otherwise predominantly residential location that forms part of the Chelsea Park Conservation Area.

5. Access to the roofs over Vale Court is available from a staircase leading off the main communal stairwell, and the area contains a number of chimneys, aerial installations and water tank housings.

6. While the appeal relates to the enfranchisement price for the whole block, the issues (see below) relating to relativity and deferment rate are concerned solely with the 6 flats which are subject to leases that have 4.74 years unexpired – flats 6, 9, 12, 13 16 and 20. Flats 3 and 4, also with less than 5 years unexpired, are to be the subject of a lease-back arrangement, and the enfranchisement price therefore excludes any value for those units as terms have been separately agreed. The hope value issue relates to the flats of non-participants that have less than 80 years unexpired, namely flat 1 (70.25 years) and flats 6, 13, 16 and 20 (4.74 years). Terms for the other leasehold interests within the purchase have been agreed as part of the enfranchisement premium. It has also been agreed that the valuation date is 24 September 2007, the capitalisation rate is to be taken at 5.25%, the deferment rate for the leases other than those with less than 5 years unexpired is 5% and the value of the land to the front and side of the property is £5,000.

Issues

7. The issues remaining to be determined are:

(a) The existing leasehold vacant possession values of the flats that have less than 5 years unexpired and which are not subject to lease-back.

(b) Whether there is potential to undertake additional residential development on the roof; if so, whether there is a prospect of obtaining planning consent, and, if so, the value of that potential.

(c) Hope value in respect of the 5 non-participating flats with terms of less than 80 years unexpired.

(d) Deferment rate relating to those flats with less than 5 years unexpired.

(e) Landlord's proposed terms of transfer.

8. We undertook an inspection of the property and the immediate surrounding area on the afternoon of 6 April 2011. Following receipt of counsels' written closing arguments shortly after the hearing, additional submissions were sought as two further decisions where similar issues had been considered had been published: *Cadogan v Erkman* [2011] UKUT 90 LC (consolidated cases LRA/56/2007 and LRA/68/2008) and *Cadogan v Cadogan Square Ltd*

[2011] UKUT 154 (LC) (consolidated cases LRA/128/2007 and LRA/17/2008). We subsequently sought further evidence and submissions relating to the deferment rate issue and these were all received by 13 September 2011**.** We consider the LVT's decisions, the evidence and submissions before us in this appeal, and provide our conclusions below on an issue by issue basis.

Existing leasehold vacant possession values of flats 6, 9, 12, 13, 16 and 20: the parties' cases

9. Before the LVT, Mr Roberts for the applicants (the appellants here) argued for a relativity to unimproved freehold values of 8%, and Mr McDonald, for the respondent nominee purchasers, sought 16.5%. Whilst the LVT stated that it preferred Mr Roberts's "structured approach" to the valuation exercise relating to leasehold vacant possession values, it adopted a relativity of 11.5% ,saying, in paragraph 133:

> "The relativity of flats with less than 5 years was dealt with in paragraph 3.7 of Einar Roberts, and Ronald McDonald's evidence at paragraph 7.5. Mr McDonald says he relied upon his knowledge and experience, however both valuers have considered this issue before at nearby Carlyle House, we consider the approach adopted in that case prudent and accept 11.5%."

10. It was the appellants' case that the LVT's conclusion was not based upon either party's evidence (although in its reasons for refusal of permission to appeal, it said that its conclusion *was* based upon an analysis of both parties' evidence), having used a relativity from another LVT decision without giving the parties an opportunity to comment (contrary to The Lands Tribunal's decision in *Elmbirch Properties PLC's Appeal* (2007) LRA/28/2006 (unreported)). They pointed out that in *Arrowdell Ltd v Coniston Court (North) Hove Ltd* [2007] RVR 39 the Lands Tribunal (the President and NJ Rose FRICS) said this:

> "37. In our judgment leasehold valuation tribunal decisions on relativity are not inadmissible, but the mere percentage figure adopted in a particular case is of no evidential value."

The appellants also relied upon *Nailrile Ltd v Earl Cadogan* [2009] RVR 95 which applied the *Arrowdell* decision in this respect.

11. Although neither party relied upon graphs of relativities, the appellants referred to *Dependable Homes Ltd v Mann* [2009] UKUT 171 (LC), in which the tribunal rejected a graph compiled from LVT decisions and, in the absence of more satisfactory evidence, relied upon the "graph of graphs". Mr Munro pointed to the RICS Research Report: *Leasehold Reform: Graphs of Relativity* published in 2009 in which it said, at 4.6:

> "For leases with very short unexpired terms (say, under 5 – 10 years), the graphs may be found to be unreliable because, in most cases, they simply have a straight line from zero to the five year point. Most practitioners will establish this value by capitalising the rental value over the unexpired term. When valuing a lease with a short unexpired term, consideration needs to be given to any dilapidations obligation."

It was submitted that capitalising the rental value was precisely what Mr Roberts had done, and that his evidence was more satisfactory than that of Mr McDonald, who, in any event, was not contesting the LVT's decision despite having argued for a relativity that was 40% higher than that concluded by the LVT.

12. Mr Roberts is a chartered surveyor with over 14 years experience in the profession and, acting for a number of the Great Estates, has specialised in leasehold reform matters particularly in central London and within the vicinity of the appeal property. He said that he had adopted the approach that his former colleague, Mr Roland Cullum FRICS, had used before the LVT in the case of 9-12 Carlyle House (LON/ENF/1429/05), where one of the four participating flats had a lease with only 6.5 years to run. That approach was to identify an unimproved rental value and capitalise it to the end of the term to arrive at the appropriate relativity. Although in the Carlyle House case there had been no unimproved evidence, such evidence was, he said, available here. Hence, whilst the approach was the same, the resultant relativity would be different.

13. Mr Roberts analysed firstly a surrender of flat 4, Vale Court, a one bedroom unit with a gross internal area (GIA) of 540 sq ft which the Sloane Stanley Estate had taken back in early 2003. It had at the time an assured shorthold tenant (Mr Khan) who remained in occupation until February 2010. The Estate records showed that the flat needed a new bathroom and redecoration. In April 2007, close to the valuation date, the rent was renegotiated to £13,420 pa. Mr Roberts deducted 25% from that figure to give a net rent after the usual management costs of £10,065 pa, and capitalised it over 4.75 years on a dual-rate basis at a gross yield of 3.9%, with a sinking fund at 2.25% and tax at 30%. This produced a short leasehold value of £30,749 – say £31,000. That was a relativity to the agreed freehold unimproved value of £475,802 of less than 7%. Mr Roberts said that the 3.9% was a market rate (per the Savills PCL Index net yield for September 2007) and a proxy for a gross yield on a freehold investment of about 5%. The 25% deduction for costs was his realistic estimate of the estimated rental value on full repairing and insuring terms. The figures he had used, he said, were generous to the purchaser as the Savills PCL Index (which had been produced in evidence by Mr McDonald) showed gross to net ranging from 36% to 41%. He acknowledged that the rent that had been negotiated with the then existing tenant might have been less than could have been achieved in the open market, and it was for this reason, as well as all the other evidence he had relied upon, that he had used a relativity of 8% rather than the 6.5% that this particular analysis created.

14. As a cross-check, Mr Roberts said that he carried out the same exercise on the open market lettings of flats 8 and 17 Vale Court. Allowing for the same £25,000 per unit for modernisation costs that had been adopted by the LVT (and he thought that this could reasonably equate to a dilapidations allowance, which needed to be taken into consideration where the lease was so short) his analysis produced relativities on each of 8%. The costs of modernisation were not, he said, challenged before the LVT, and on his understanding that flats 9 and 20 were in fair/tired condition he had assumed the other short leasehold units were also in need of upgrading. If the allowance was not made, then the relativity, using this approach, would amount to about 13%.

15. Mr Roberts also considered a settlement in respect of the eight flats at 1-8 Carlyle House, which he had agreed with Mr McDonald in summer 2007. There the relativity was 17% on leases that had between 6.90 and 6.96 years unexpired, and this, on a straight line basis, might suggest a relativity of the Vale Court short leaseholds of around 11.5%. He said that he believed it was that valuation that the LVT relied upon in its determination on this case, but that was not the representation of either party and was a component in a wider settlement where there was a *Delaforce* effect in that the parties wished to avoid the costs and risks of tribunal proceedings. Furthermore, there was not sufficient unimproved evidence in that case to rely upon the capitalisation method.

16. Mr Roberts then referred to contemporaneous evidence relating to the open market sale of the unenfranchisable interest in flat 3, Vale Court, an 840 sq ft unit, in October 2007 for £60,000 in, it was believed, 'tired' condition. Whilst that sale was initially on the basis that the property was let, the tenant had left prior to exchange of contracts. This transaction showed a relativity of 8.63%. As to Mr McDonald's criticisms of the use of that sale as a comparable, Mr Roberts said he was happy to rely upon his own evidence, which had been verified in an email from Keith Pankhurst, the selling agent. That email had been before the LVT and Mr McDonald had had over two years in which to check out the information, but he had not done so.

17. The type of purchaser who would be interested in a short leasehold would, Mr Roberts said, be "property cognate" individuals or investors – such as Mr Carey-Morgan – who were in it for short-term profit, buying short-term leases with Act rights that get exercised. Whilst he said that he understood where Mr McDonald was coming from in suggesting that there would be a special purchaser, he did not agree. Although it might on the face of it be an attractive proposition for, for instance, an overseas business person on a short term secondment, in that the purchase price would equate to a forward payment of a fixed rent, the potential for a large dilapidations bill, and possible protracted arguments in relation to it at the lease end would be a severe deterrent.

18. Mr McDonald postulated an approach that assumed the leasehold value would be increased by what he described as "the prospective shorthold tenant's bid", although he produced no evidence in support. Whereas he had relied upon the "graph of graphs" at the LVT hearing in arguing for a relativity there of 16.5%, in respect of this appeal he undertook valuations of flats 3, 4, 8 and 17 (as Mr Roberts had done) but had not used dual rate tables. On flat 3, he took the gross rental value at £35,490 but only reduced it to a net figure by deducting service charge and insurance – pro-rated from another flat in Vale Court, no. 25. The deduction was thus £1,817 whereas Mr Roberts had deducted 25%. He then used a single rate multiplier of 5% and allowed (as Mr Roberts did) £25,000 for modernisation, but pro-rated it by floor area to give £24,376. A period of 6 weeks was allowed for the works, taking the reversion down to 4.5 years. This resulted in a relativity of 15.96%. Doing the same exercise on the other flats, again using pro-rated modernisation costs, he came to relativities of 16.52%, 14.81% and 17.84% to give an average of 16.28%. He then adopted the "Carlyle House" basis of using dual rate tables but retaining the deduction at £1,817. However, he did not make the 20% allowance for landlord's costs that he had previously done in that case. This produced an average of 11.68% which, he said, was close to the LVT's finding.

19. In Mr McDonald's view, Mr Roberts had failed to allow for the possibility that the existing lease might be sold to a potential shorthold tenant on the basis of the improved security and effectively fixed rent. There was no reason to suppose, therefore, that it would only be investors who would bid. He said that he thought the LVT had been overly conservative in adopting an 11.5% relativity as his evidence supported between 15% and 16%.

20. As to why he had not, in relation to Mr Roberts's evidence on flat 4, considered the email confirmation of the transaction details from Mr Pankhurst, Mr McDonald apologised for not having referred to it, and said, "In reality I failed to pick up the relevance." He said that he had not thought that property was particularly relevant due to the low rent that had been passing before the tenant left, had not realised that it was actually being sold with vacant possession, and had not initially realised that it was an unenfranchisable lease.

Existing leasehold vacant possession values of flats 6, 9, 12, 13, 16 and 20: conclusions

21. We agree with the appellants' submissions regarding the evidential value of past LVT decisions in relation to relativity. The passage from *Arrowdell* that is referred to in paragraph 10 above continues:

> "…The reason for this is that each tribunal decision is dependent on the evidence before it, and thus, in order to determine how much weight should be should be attached to the figure adopted in a decision, it would be necessary to investigate what evidence the leasehold valuation tribunal had before it and how it had treated it. Such a process of investigation is potentially lengthy, and it is inherently undesirable that leasehold valuation tribunal hearings should resolve themselves into re-hearings of earlier determinations.
>
> 38. It is certainly understandable that valuers negotiating the settlement of an enfranchisement claim should have regard to leasehold valuation decisions on relativity, since these might seem to be the best guide of the likely outcome if they were unable to reach agreement, even though…the decisions are disparate and fail to show any established pattern. But the decisions themselves can constitute no useful evidence in subsequent proceedings."

22. The LVT's reliance on the figure adopted in Carlyle House was therefore in our view wrong, as it failed to comply with two of the "three inescapable requirements" referred to at paragraph 23 of the *Arrowdell* decision, where the Tribunal said:

> "… It is entirely appropriate that, as an expert Tribunal, an LVT should use its knowledge and experience to test, and if necessary, to reject evidence that is before it. But there are three inescapable requirements. Firstly, as a tribunal deciding issues between the parties, it must reach its decision on the basis of the evidence that is before it. Secondly, it must not reach a conclusion on the basis of evidence that has not been exposed to the parties for comment. Thirdly, it must give reasons for its decision."

23. Turning to the evidence, it is clear that Mr Roberts's methodology was appropriate and was undertaken in accordance with paragraph 4.6 of the RICS research document referred to above. The methodology adopted by Mr McDonald was on, we must say, a confusing basis and seemed to be designed entirely for the purpose of discrediting Mr Roberts's evidence. Mr Roberts pointed out that Mr McDonald's deduction only for service charge to take the gross rent to net ignored a number of important cost factors. Mr McDonald said in his report that residential units were never let on full repairing and insuring terms, that 25% was too high a reduction to reflect service charges, management and other costs, and that if his figures had been used, the relativity would come out at almost the same 11.5% figure that the LVT had determined. However, he accepted in cross-examination that he did not know whether the Savills PCL Indices included management costs, but thought it conceivable that they did. We prefer Mr Roberts's evidence. It is not, as Mr McDonald said "a swingeing reduction" but in our view fairly represents the level of costs that a purchaser would build in to the equation. Mr McDonald also said that it was inappropriate, in his analysis of the lettings of 8 and 17 Vale Court, for Mr Roberts to use the same £25,000 allowance for renovation costs on flats that were different sizes. Again, we do not concur. It seems to us to have been a fair "ball-park" figure (and one which the LVT accepted), and we do not think that it serves any useful purpose to break it down further.

24. It is apposite to note here that Mr McDonald accepted in cross-examination that, if his method was not adopted, he could not object to Mr Roberts's methodology, and he also acknowledged that the LVT had rejected his earlier evidence. Hence his latest approach, which he also admitted, was "novel". Moreover the respondents have not challenged the LVT's decision, and it is difficult therefore to square his argument for somewhere in the region of 15 to 16.5% relativity with the LVT's adoption of 11.5%.

25. We also note that in his closing submissions, Mr James McDonald said, "None of the evidence produced for the Upper Chamber in anyway changed the situation put to the LVT, and I would invite the Upper Chamber to confirm the LVT decision on this point unchanged at 11.5%." We have already stated that the LVT was, in our judgment, wrong to rely upon information it had apparently taken from another case and, in the light of the evidence before us we are satisfied that Mr Roberts's opinion, formed as it is from a thorough analysis of comparables, is correct. We determine therefore that the relativity should be set at 8%. This conclusion is based upon the evidence before us in this case, and we have reached it on the basis that we have heard nothing to show that Mr Roberts's opinion was wrong. It needs to be said, we think, that the circumstances of this case are very different to those which prevailed in *Cadogan v Cadogan Square Ltd* [2011] UKUT 154 (LC) (which we will refer to as *38 Cadogan Square*), where the issue relating to leasehold values and relativities related to leases of 17.75 years unexpired and where deductions for Act rights had to me made. Reliance was also placed upon graphs, but here, as the RICS working group concluded, that is not appropriate on leases that have such short unexpired terms as those we are dealing with here. We do not think that any comparison can be drawn between the 42% of freehold value applied in *38 Cadogan Square* (after deducting 25% for Act rights) and the 8% found here. It stands to reason that when a reversion becomes as short as 4.75 years, the value of unenfranchisable leases is rapidly approaching the stage where it becomes virtually nil.

Development potential for additional storey: the LVT's decision

26. Before the LVT the Trustees called evidence from Mr Christopher McCue of Paul Davis and Partners, architects, and from Mr Hayes on structural matters, Mr Oliver on planning and Mr Walker on conservation issues. Their case, as it was put in the decision, was that on the basis of this evidence there was potential to develop the roof using various alternatives, including the addition of a penthouse, and that the potential to realise this development value ought properly to be reflected in the price paid by the nominee purchaser. Mr Roberts gave evidence that the highest value scheme, allowing for a planning risk of 50%, would give a development value of £838,125.

27. The nominee purchasers produced to the LVT a letter of 15 July 2008 from Mr Bruce Coey, area planning officer with the council, written in response to a request by an architect instructed by them that he should confirm the opinion he had expressed on the possibility of building an additional storey on Vale House. The letter said:

> "The property is located within the Chelsea Park/ Carlyle Conservation Area, for which the Council published a proposals statement in 1993. The relevant policies towards additional storeys which are set out in the Unitary Development Plan are CD44 and CD45, and those towards development in Conservation areas CD57, CD61 and CD62. The overall requirement for development in Conservation Areas is that it preserves or enhances their character or appearance.
>
> I would advise you that the erection of an additional storey at this property, by rising above the roofline of Mallord Street, and by adding significant bulk to a mansion block of flats, would not comply with Policy CD44. Furthermore, the Conservation Area Proposals statement advises that there is a general presumption against additional storeys throughout the Conservation Area because of the effect that these would have on the townscape of the area. The map on page 55 of the statement examines every property in the Conservation Area that is suitable for any form of roof addition and does not identify Vale House as being an exception to this general policy. I would accordingly advise that an additional storey would not preserve or enhance the character or appearance of the Conservation area and would infringe policies CD57, CD61 and CD62."

28. Following the production of this letter the LVT permitted the trustees to call Mr Greenish to give evidence. His witness statement, dated 27 October 2008, dealt with a question that the tribunal had asked during the early stages of the hearing, namely why the applicant had never submitted a planning application for any of the four schemes that had been produced in evidence. The statement also addressed some of the points made in Mr Carey-Morgan's witness statement. Mr Greenish said that the subject of a roof extension over Vale Court (and over Tryon House, which lies on the other side of the telephone exchange) in conjunction with a residential refurbishment of the exchange had first arisen in 2006 when the Estate's agents had suggested that a case for this could be made. Sketch plans (which were different from those that were before the LVT and this Tribunal) were produced by Paul Davis and Partners, and they, together with representatives of Gerald Eve, attended a meeting with the council's planning department on 30 October 2006 to obtain an initial reaction as to the likelihood of a

planning application being successful. A note of the meeting (which had been prepared by Gerald Eve) was appended to the witness statement.

29. The note of the meeting of 30 October 2006 recorded the following ("GO" is Mr Oliver; "NB" is Mr Nick Booth, described as "Development Control, RBKC"; "AH" is Mr Alec Howard of Paul Davis and Partners; and "AW" is Mr Alan Wito, described as "Conservation, RBKC"):

> " **Introduction**
>
> 1. GO introduced the sketch drawings tabled to RBKC for a roof extension across Vale and Tryon House. Drawings show single storey extension set back from the existing roof line. Sight lines show no visibility from Mallord Street. Internal layout plans show options for 1 and 2 residential units.
>
> **2 Initial comments**
>
> 3 NB explained that within the Chelsea Park/ Carlyle Conservation Area there is a general presumption against all roof top extensions.
>
> 4 In other conservation areas there is an element of flexibility but in this area <u>all</u> buildings are considered to have a roof structure or form of historic interest which should be retained.
>
> 5 Initial comments from NB were that:
>
> - The existing building is already significantly higher than the majority of the buildings on the street;
> - In terms of impact of an extension on the surrounding area consideration will be given to visibility from surrounding buildings as well as ground level;
> - Any extension on these buildings is likely to be visible and considered over dominant;
> - Particular concern in respect of impact of an extension on Vale house and the impact on The Vale;
> - While the provision of two additional residential units would be viewed positively in land uses terms it is unlikely that this alone would be sufficient to override restrictions on roof level extensions.
>
> 6 GO raised the issue of a potential package of environmental improvements measures to off set against the proposals, as identified within the Chelsea Park and Carlyle conservation Area statement.
>
> 7 NB advised that whilst improving the attractiveness of the area as part of a package of improvements provides an argument this is unlikely to outweigh the Councils policy presumption against rooftop extensions.
>
> 8 Based on proposals to date, AW considered that the extension would have an impact on the character of the conservation area and the presumption would be against a roof top extension on these buildings.
>
> 9 Alternative options: Contemporary design approach

10 GO suggested the option of a contemporary high quality design creating a visible extension rather than a design which seeks to reduce visibility and impact.

11 AH identified that such an approach had been taken with a roof extension at Lowndes Square and also at the Duke of York's site where a lightweight glass roof structure was introduced across the extent of the terrace.

12 AW considered that due to the design of the terrace (Telephone Exchange between Vale and Tryon House creating three defined buildings) a contemporary extension each side of the Telephone Exchange would not be in keeping with the whole terrace.

13 AW considered that an extension set back from the existing roofline would appear contrived while a mansard extension to the existing roofline would be over dominant.

14 GO raised the issues of a holistic approach to the roofline to include the Telephone Exchange. This could improve the overall rooftop across the three buildings

15 General concern from AW that an extension across the three buildings would need to including substantial benefits in terms of land use, improvements to the design of the buildings and wider environmental improvements to override restrictions on roof level extensions.

16 Conclusions

17 Initial view of both NB and AW that:

- any extension at roof level would be resisted on the basis of detrimental impact on the character of the conservation area.
- Due to the nature of design of the three buildings unsure that a contemporary design on Vale and Tryon would be suitable.
- Such [proposals would need to be in conjunction with substantial environmental and land use gains.

18 NB concluded that he would carry out a site visit in order to fully understand the potential impact on the surrounding area."

30. In its decision (at paragraphs 81 and 82) the LVT said that an investor, looking at the development potential of the roof, would be concerned about almost certain appeals, delays, cost and an outcome that was said to be 60% certain. The residual valuations that Mr Roberts had given might to an investor seem unreliable, as they were based on final values. The investor would know that the discussions that both applicants and respondents had had with the council suggested that planning permission would be refused, and the tribunal's own inspection and consideration of the planning evidence suggested that there would be considerable local opposition to such proposals. It considered that a "cautious and prudent investor" would reject a residual valuation as too unreliable and would rely on their instinct and knowledge of the market and would allow no more than £10,000 for the prospect.

Development potential for additional storey: the parties' cases

31. The appellants' case was that the LVT must, by implication, have accepted that there was potential for some form of development on the roof of Vale Court in concluding that something would be paid for it; and that it had been wrong to reject all of the evidence that had been called by the appellants and to choose a figure of its own based upon what it thought a "cautious and prudent investor" would pay. Whilst accepting that it was likely that this Tribunal would find that "the hypothetical purchaser is prudent rather than rash" (see *31 Cadogan Square Freehold Ltd v Cadogan* [2010] UKUT 321 (LC)), Mr Munro said that the LVT had adopted the wrong test if it was intended to add anything to "prudent". Although the LVT had said at paragraph 70 of its decision that it adopted the test of an informed purchaser, it had not, in fact, done so. In *Phillips v Brewin Dolphin Bell Lawrie Ltd* [2001] 1 WLR 143, Lord Scott said, at para 30:

> "The value of an asset that is being offered for sale is, prima facie, not less than the amount that a reasonably informed purchaser is prepared, in arms length negotiations, to pay for it."

That, it was submitted, was the appropriate test. The purchaser would have no more, and probably less, material upon which to make a value judgement than had been produced before the LVT (and was reproduced before us), whereas the LVT appeared to have assumed that he would have perfect knowledge and would have access to all the material that a building owner would have obtained by the time he entered into a contract for the proposed works to be undertaken. It was not the Tribunal's function to put itself in the position of a planning committee determining an application, but to consider the approach that a hypothetical purchaser would take in weighing up the difficulties that might be encountered in achieving further development, both in terms of physical and economic factors, and in planning prospects.

32. Mr Munro contended that it was wrong for the LVT to have rejected the planning evidence and opinion that had been provided by Mr Oliver, and the views, on conservation matters, of Mr Walker. There was no possible foundation, it was submitted, for the LVT to find that there would be "considerable local opposition to raising the roof from all sides". In inviting the Tribunal to conclude that on the basis of their evidence, which was based upon potential schemes drawn up by Mr Chris McCue of architects Paul Davis & Partners (PDP), and, in terms of which the detail was not thought to be controversial, there was potential to obtain planning permission for, and to be able physically to construct, a penthouse flat on top of the building. Mr Munro pointed out that no planning evidence had been tendered by the respondents, and that Mr McDonald, who was not a planning expert, had simply concluded that planning consent would not have been forthcoming, and had not suggested any other potential impediment to the proposals. It was submitted that the research that Mr Carey-Morgan had undertaken in getting HUB Architects, at a cost of only about £282, to write to the council and ask for their response to the idea of an additional floor was wholly inadequate, in relation to what a serious prospective purchaser could be expected to do, and the negative answer from the planning office was entirely predictable. Mr Carey-Morgan was wrong when he suggested that there had been an earlier application for rooftop development on the building.

33. On the basis that a prospective purchaser would have sought and obtained the type of advice that had been provided by the appellants' experts, Mr Munro submitted that he would have been confident in offering a price that included the value that Mr Roberts had ascribed to the potential – a figure that reflected an extremely cautious view, as it allowed only 45% for site value and a planning risk deduction of 50%.

34. Four schemes had been prepared by Mr McCue in connection with the LVT application, and upon which the experts based their evidence. In order of value potential they were: (1) a contemporary style penthouse flat of about 1,915 sq ft, having access from the top floor of the adjoining telephone exchange building which was, and is, within the ownership of the appellant, and which it proposed eventually to convert into high class residential apartments, with lift access to all floors; (2) two self contained flats having access from the main staircase of Vale Court (and referred to as "walk-ups); (3) a roof terrace to serve the new telephone exchange flats; and (4) a roof terrace solely for the use of the present flats in Vale Court. At the hearing before us the appellant recognised that the primary focus should be on the penthouse option. It was submitted that the respondents had not challenged the structural engineer's or quantity surveyor's evidence, and that there had been no specific opposition to the details of the schemes. The respondents' only argument had been that planning consent would not be forthcoming.

35. Mr Greenish is senior partner of Pemberton Greenish, the appellants' solicitors, and is a trustee of the Sloane Stanley Estate. He said that the preferred scheme (the penthouse flat) involved creating an access through the telephone exchange which was let to British Telecommunications PLC on a lease expiring on 25 December 2012. There was a real risk, therefore, that if planning permission had been successfully sought when the question of redevelopment with residential units was first mooted, it would have expired by the time vacant possession was obtained. Furthermore, if the lessee of the telephone exchange had got wind of the application (which they undoubtedly would have done), they would have been very likely to exercise their rights either under the Landlord and Tenant Act 1954 or the Telecommunications Acts, if only to negotiate a payment to persuade them to give vacant possession.

36. In any event, Mr Greenish said, even prior to the serving of a section 13 notice it could have been anticipated that the lessees of Vale Court would seek to enfranchise, and in such circumstances any planning consent would be useless to the applicants, and the considerable costs involved in submitting an application (and possibly an appeal) would have been wasted. Although the costs incurred in obtaining the evidence needed to support the applicant's contentions before the LVT (and subsequently this Tribunal) were significant, they were nowhere near the level that would apply in undertaking a full planning exercise. Mr Greenish said that knowing how long it would take to go through the planning process, especially if an appeal was necessary, even if an application had been made as soon as the section 13 notice was served, there would have been no realistic possibility of obtaining a consent before the LVT hearing.

37. Mr Greenish said that seeking planning permission for this development was not one of the Estate's priorities, particularly as it was not known what BT's long-term plans for their occupation of the telephone exchange were. Without vacant possession, and redevelopment of the telephone exchange, the penthouse proposal on Vale Court could not proceed. That was the most valuable option, and it was acknowledged that Mr McCue's other three proposals would provide significantly smaller returns. Mr Greenish said that, since the LVT decision, a new lease had been granted to BT on 9 April 2010, outside the provisions of sections 24-28 of the 1954 Act, and expiring on 28 September 2015. It contained a tenant's break clause that could be exercised at any time after 25 December 2012 upon giving 6 months notice, but it was submitted that this new lease arrangement had no bearing on the issues in this appeal.

38. Mr Hayes is Principal of Michael Barclay Partnership LLP, a central London firm of consulting engineers. He said that his firm had been asked to provide a preliminary structural overview as to the viability of constructing penthouse apartments on the roof of Vale Court. They had carried out an external inspection of the property, and from within the communal areas and upon the roof, but had not undertaken any form of structural survey. He included in his report the caveat that the relationship of any new building work to the existing structure would need to be assessed and the impact of any new loads upon the existing structure evaluated. He gave examples of central London properties that had undergone similar rooftop developments, suggested that a lightweight structural frame (as had been used in a new penthouse constructed on a building in Lowndes Square), would be the most obvious solution, and described the construction and sequencing processes which by judicious use of the framing and load distribution would ensure that occupiers of the existing top-floor units would not need to vacate.

39. Mr Hayes said in cross-examination that he did not think that the difference in levels between the telephone exchange floors and the roof level at Vale Court would create any structural difficulties, but he accepted that he had not considered that aspect in detail or any likely related costs.

40. Mr Oliver is a member of the Royal Town Planning Institute and a partner in Gerald Eve. He advises various London Estates on planning matters generally, has acted for the appellant for over 8 years in respect of properties in the vicinity of Vale Court and has dealt with the Royal Borough of Kensington and Chelsea throughout his professional career. He said he had been asked to advise as to the prospects of obtaining planning permission for any of the four schemes that had been prepared by Mr McCue. He described Vale Court. It was situated in the Chelsea Park Conservation Area but was not a listed building. The immediate surroundings, apart from the adjoining telephone exchange, were predominantly residential and comprised buildings of varying scale, height and mass in a range of architectural styles. The roofscapes in Mallord Street and The Vale were, he said, of varying form, style and building materials, including roofs with gables and pediments, mansard styles with and without dormer windows, pitched and flat roofs. The telephone exchange, being a commercial unit, had floor to ceiling heights significantly greater than the surrounding residential properties, and it had a roofline which rose well above the adjoining units, making it a dominant feature in the streetscape. There were mature London plane trees along the return frontage of Vale Court to The Vale, and the foliage served to restrict views of the building from the street and the Kings

Road. The properties to the rear of Vale Court fronting onto Kings Road tended to be lower in height and had rooftop amenity areas and terraces.

41. At the valuation date, the council, in considering any planning application for residential development, would have had regard to the relevant policies in the London Plan, adopted in 2008, and the "saved policies" of the Royal Borough of Kensington and Chelsea Unitary Development Plan, adopted 25 May 2002 (the UDP). In particular, Policy H2 in the Housing Chapter of the UDP seeks the development of land and buildings for residential use and, within the Conservation and Design Chapter, policy CD27 seeks a high standard of development, sensitive to and compatible with the scale, height, bulk, materials and character of the surroundings; CD28 requires development to be physically and visually integrated into its surroundings; CD33 seeks to resist development that would significantly reduce sunlight/daylight to adjoining buildings and amenity spaces; CD35 requires design to ensure sufficient visual privacy for surrounding residents, and CD36 resists development that will result in a harmful increase to the sense of enclosure to nearby residential property.

42. Of specific relevance to either of the residential alternatives that had been proposed, policy CD44 states:

> "To resist additional storage and roof level alterations on:
>
> a. complete terraces and groups of buildings where the existing roofline is unimpaired by extension, even when a proposal involves adding to the whole terrace or group as a co-ordinated design;
>
> b. buildings or terraces that already have an additional storey or mansard;
>
> c. buildings that include a roof structure or form of historic or architectural interest;
>
> d. buildings which are higher than surrounding neighbours;
>
> e. buildings or terraces where the roofline or party walls are exposed to long views from public spaces, and where they would have an intrusive impact on that view or would impede the view of an important building or open space beyond;
>
> f. buildings which, by the nature of the roof construction and architectural style are unsuitable floor roof additions, e.g. pitched roofs with eaves;
>
> g. mansion blocks of flats where an additional storey would add significantly to the bulk or unbalance the architectural composition;
>
> h. terraces which are already broken only be isolated roof additions."

Policy CD45 states:

> "To permit additional storeys and roof level alterations in the following circumstances:
>
> a. where the character of a terrace or group of properties has been severely compromised by a variety of roof extensions and where anything in between would help to reunite the group; and
>
> b. the alterations are architecturally sympathetic to the age and character of the building and would not harm its appearance."

And in respect of the roof terrace proposals, Policy CD46 states:

> To resist the introduction of roof terraces if:
>
> a. significant overlooking of, or disturbance to neighbouring properties or gardens would result; or
>
> b. any accompanying alterations or roof alterations are not to a satisfactory design, would be visually intrusive or would harm the street scene."

43. Mr Oliver also referred to the Chelsea Park Carlyle Conservation Area Proposal Statement of September 1992 where, at page 38, its guidance said:

> "There is a general presumption against proposals for the additional storeys, roof extensions, roof alterations and attic conversions throughout the conservation area because of the effect these would have on the character of the area. All buildings in the area are identified as including roof structures of architectural interest on which additional storeys will be resisted under the Council's restrictive planning policies."

44. In respect of the appellants' now preferred option (of the four he had originally considered), Mr Oliver said firstly that, in connection with a residential redevelopment of the telephone exchange, the current use of that building was *sui generis* and, furthermore, it was a very small employer with, apparently, only a handful of workers operating in that building. This would not therefore, in his opinion, be an employment use that the council would seek to protect. He had also been involved with the change of use to residential of the former telephone exchange at 21-24 Chesham Place, Belgravia, where the same land use policies apply and there had been no objection to loss of that use. He did not therefore agree with the respondents' assertions that the proposal for a residential unit above Vale Court, with access from the telephone exchange must therefore be doomed to failure. There was also a clear priority in the UDP for additional residential accommodation in the area (Policy H2).

45. Similarly the provision of a new residential unit (or units if the two walk-ups were economically viable) on top of Vale Court would be wholly consistent with this policy. As to design, it was his view that neither of the proposals fell within any of the 8 categories where extensions should be resisted (Policy CD44). Criterion (a) was not relevant as this property did not form part of a complete terrace or group of buildings. The existing building did not already have an additional storey (b), or include any form of interesting or architecturally merited roof structure (c), and the height was lower than the adjacent telephone exchange (d). Mr Walker had assessed the impact the development would have on views as minimal (e), the flat roof was entirely appropriate for an additional storey, being currently cluttered and unattractive in appearance (f), and there would be no significant addition to the bulk or architectural composition of the building (g) as the design was such that the penthouse or flats would be set well back behind the parapet. The building was also not located in a terrace that was already broken by isolated roof additions (h).

46. The proposals accorded, he said, with policy CD45 in that the development would be architecturally sympathetic to the age and character of the building, and would not harm its

appearance. He produced a series of photographs of the building taken from street level at a number of locations, with the outline of the proposed penthouse added. It was evident from these, he said, that particularly in the summer, it would be virtually invisible. He acknowledged that they had not been available to the planning officer at the meeting of 30 October 2006 that he had attended, to which Mr Greenish had referred. He said that he did not think that Mr Nick Booth, the council's development control officer, who had been in attendance at that meeting, had visited the property. Having given some examples of other developments that had been permitted in the area (including particularly 25-39 Thurloe Street), which had been permitted in accordance with the relevant policies, Mr Oliver said he thought this particular roofscape would benefit from tidying up. At present the flat roof contained a variety of utilitarian structures such as chimneys (which would remain), roof access area, water tanks and aerials. Such an extension would achieve that aim, and whilst there was a general presumption against proposals for additional storeys within the conservation area, the benefits that he had outlined would make a strong case for permission being granted in the circumstances.

47. In connection with policy CD46, the development would be virtually invisible from the ground, and in terms of overlooking other properties, the option to provide planters at the back (looking towards the Kings Road properties) and at the edge of the small balcony to the front, would resolve any issues in that regard. He said he did not agree with the LVT's conclusion that either a penthouse or two self-contained flats would overlook other properties or their roof terraces. In his second supplemental report, he said that the only properties that might realistically be overlooked were No 2 The Vale and the roof terraces to 342-346 Kings Road. However, given the close proximity of existing buildings generally, it was necessary to consider whether any additional overlooking from this development would be significant.

48. Although Mr Oliver acknowledged that the indicative elevations of the proposed development were contemporary in design, and thus not precisely in keeping with the existing design and character of the area, he said that they had the benefit of being simple and not visually intrusive. In his view, the indicative drawings that had been provided by PDP (his appendices GO11, GO12 and the identified key views in GO15) would be in accordance with policies which seek high quality design and which reflect the development's context, and would enhance the conservation area. In any event, he said, the precise design was something that would be sorted out through discussions with the planners. In that regard, he accepted in cross-examination that none of these proposals had been put to or discussed with the planners, and the opinions expressed were solely his own. It was possible, therefore, that the reaction of the council's development control officer could well be the same as had been the case at the 30 October 2006 meeting, although in this case there were plans, whereas in the initial meeting there were not.

49. Mr Oliver said in cross-examination that he thought there was, realistically, a 60% to 70% chance of obtaining permission for another storey, and a slightly higher chance of getting consent for a roof terrace or garden. He accepted that it was most likely that, if permission were to be granted, it would be on appeal, and that an initial application would be refused. In response to questions from the Tribunal, Mr Oliver said that, in planning terms, the proposal

for two flats might have a slightly better chance than a single penthouse as there was a greater gain in terms of an additional residential unit.

50. In answer to us Mr Oliver said that the planning permissions he had produced for roof extensions on properties in Thurloe Street and King's Road were the only ones that he was aware of. He had not sought to establish what refusals of permission there had been for such proposals in the area or what decisions there had been on appeal.

51. Mr Walker is a chartered architect and a founding partner of DLG Architects, to which he is now a consultant, and specialises in building conservation, lecturing on the subject at the Architectural Association and universities. He has extensive experience in preparing conservation assessments (including those relating to roof-top developments), is a resident of the Royal Borough and is chairman of the local conservation association. He said that he had been asked to assess the PDP proposals in respect of conservation issues, and the likelihood of obtaining planning consent from the conservation perspective. His report set out in considerable detail the history and background to development in the area and summarised national and local policies. In the local UDP, policies CD44 and CD45 were the most relevant, and he said that it was clear that the main interest was in terraces of buildings where a consistent approach to roof extensions was important in preserving the interest of the group. That was not, he said, the case with Vale Court.

52. The Chelsea Park Carlyle Conservation Area Proposals Statement from 1992 provided a comprehensive examination of the area, Mr Walker said, and he described the make-up and historical styles of The Vale, Mallord Street and Mulberry Walk. The area was "mixed" and Mallord Street was more "accidental" or random and contained flats that were out of character with the general trend in the area, together with a telephone exchange which was interesting in its own right and "offered opportunities to improve the appearance, specifically in respect of the floorscape in front of the building." Mr Walker said that the statement mentioned clutter on roofs, including aerials and other impedimenta, and that works to roof were dealt with as a specific issue. The problems of arbitrary changes of style, for example from simple eaves to mansard, could have a fundamental impact on appearance. For that reason, the statement considered that all the buildings in the area had a roof structure or form of historic or architectural interest, and there was thus a general presumption against additional storeys. However, Mr Walker said that in spite of this it was acknowledged that there were individual reasons for permitting or even encouraging additional storeys, and the statement set out some examples.

53. Mr Walker said that Vale Court, as acknowledged in the statement, provided a different type of accommodation to that in the rest of the area and was adjacent to one of the tallest buildings (the telephone exchange). He went on to describe its appearance from various vantage points and the impact that he thought the extension as proposed would have. He said that the view along Mallord Street from the east gave a very oblique view of the building and demonstrated its importance in providing a transition between the telephone exchange and the listed buildings on the west side of The Vale. By setting the extension back behind the top of Vale Court's frontage walls this relationship was preserved. Furthermore, it would not

impinge on the view of any of the listed buildings or adversely affect their setting. From the north, in The Vale, the building was extremely well shielded by trees, even in winter. From closer up, the face of the building (which would not be changed) could be seen, but the proposed extension would soften the transition between Vale Court and the telephone exchange, which was currently crude. From Paulton's Square (on the other side of the Kings Road) the existing building, he said, formed a disruptive background to the Kings Road frontages, and the extension would help to provide a more unifying background. The further away from the building that one got, the less the impact of any development.

54. Mr Walker said that the elevational treatment as proposed would ensure that the existing elevations retain their proportion and composition. It would provide a simple, contemporary, form that was part of the managed evolution of conservation areas advocated in PPG15, would continue the tradition which is apparent in this part of the conservation area and would add to the richness of it.

55. Whilst accepting the general presumption against roof extensions in the area, Mr Walker said that as Vale Court did not fall into one of the categories of buildings referred to in Policy CD44, an application for an extension in this location should, and would, be judged on its own merits. Similarly, there was compliance with Policy CD45, as the proposal would not harm the appearance of the building, and would, in fact, enhance the balance of the roofscape. No harm would be occasioned to the setting of the nearby listed buildings, and the development would be of an appropriate scale.

56. In his view there would be a realistic prospect of planning consent being obtained, but in the knowledge that the conservation officer would be likely to object, and the planning officer for the council might place more emphasis on the general presumption against, and rely upon the blanket conservation area statement, an initial refusal could be anticipated. However, in his opinion an inspector on appeal would be more sympathetic. He said that planning permission had been granted on appeal for the construction of two rooftop flats on an existing mansion block, Melbury Court, Kensington High Street. In the light of that success (for the applicant in that case), the council had subsequently granted planning permission for a similar development at Leonard Court, Edwardes Square W8. Mr Walker also referred to the fact that very contemporary rooftop developments had been permitted on 13, 14 and 15 Bedford Square WC1, which were Grade 1 listed buildings. He thought that, in respect of Vale Court, the chances of obtaining permission on appeal were "substantially greater than evens – say 65 to 70%."

57. Asked why he had not referred in his written evidence to an analysis of applications and appeals, and had only referred two these two decisions in his oral evidence, Mr Walker said that as a general principle, each case should be judged on its own merits and he would not usually consider such an analysis helpful. Despite the contrast between the proposed contemporary design of the penthouse and the building upon which it was intended to construct it, he said that he thought that it was an appropriate design and he would support it. A structure that was located further forward than the proposed set-back unit might be difficult to achieve in constructional terms, and might make the corner (of Mallord Street and The Vale)

too strong. He said that he had simply been asked to comment upon the drawings that had been produced, and had no input into the design exercise. Mr Walker said that he was certain such a development would soften and enhance the transition between the building and the extremely dominant telephone exchange. It would also, as he had said, reduce clutter and tidy up the existing roof area. It should be possible to provide a single aerial rather than the plethora that currently exist, but as to the chimneys, he said that if they were still in use, they might have to be extended in height. Asked about the effect that the development would have on views from the upper storeys of properties on the opposite side of both Mallord Street and The Vale, he said that that would be a consideration to be taken into account, and accepted that if the roof garden proposal were to proceed the question of overlooking and invasion of privacy could be an issue.

58. Mr Roberts said, in relation to the penthouse scheme, that when the idea of a rooftop development was first considered, the Estate had received an assurance that the lessees of the telephone exchange had no intention of renewing their lease in 2012. However, since the first part of the LVT's decision was issued in December 2008, which had the effect of "decimating the value of the roofspace", terms had subsequently been agreed for the new lease, outside the provisions of Part II of the 1954 Act, commencing on 29 September 2009 and expiring on 28 September 2015. He said that that action had, in his opinion, no relevance to the valuation exercise he had carried out. At the valuation date, in the no-Act world, the Estate would have had the unfettered opportunity to maximise the development value in December 2012.

59. As to his calculation of development value for the penthouse option, Mr Roberts said that he firstly considered three comparable transactions to establish an open market value for the completed article (which was intended to be a single residential unit of 1,915 sq ft). The fourth and fifth floor of 68 Park Walk, a few hundred metres from Vale Court, was a modern 1,826 sq ft penthouse over 2 floors that sold in May 2007 in excellent condition for £3,500,000 (£1,917 per sq ft). Allowing an adjustment for time based upon Savills PCL SW index, this produced a value per sq ft of £1,937. The other two comparables were from 20 Painters Yard, 10-14 Old Church Street, slightly further away but still in the same part of Chelsea, which was sold twice. Although not strictly a penthouse it provided penthouse style upper floor accommodation of 2,024 sq ft with outside space. The first sale was in March 2007 at £3,850,000 (£1,902 psf) which adjusted to September 2007 became £1,963 psf. It subsequently sold, in the same condition, at £4,250,000 in March 2008 (£2,100 psf). In Mr Roberts's view, the second property supported the first and he concluded that a fair value for the subject property would be £1,950 psf which would give a market value of, say, £3,725,000. He said that he did not agree with the LVT's conclusion that his opinion was "far from realistic." They had not analysed his evidence, which had been based upon the traditional approach and extensive research. They had shrunk from the task and relied upon gut instinct. As to Mr McDonald's view, put to the LVT, that a penthouse in this location would only be worth about £500,000, he thought this was wholly wrong. That was virtually the same as the unchallenged valuation of Flat 7 Vale Court, a small 540 sq ft ground floor unit (£496,490).

60. Mr Roberts then relied, in undertaking a residual valuation, upon the design and build cost estimated by Mr Elliott (who was not called) at £955,000 and applied the usual percentages for fees, finance costs and the like. This produced a site value of £1,800,000 and was 48% of

GDV. Bearing in mind typical ranges of site values to GDV in this type of location were 40 to 60%, he said he took a cautious approach and adopted 45%, £1,676,250, before considering risk.

61. With regard to risk he took account of the opinions of both Mr Oliver and Mr Walker, but as this was quite a complicated development, he said that he took a cautious approach, and adopted 50% of GDV to give £838,125. This would need to be deferred to 2012, which resulted in the claimed amount of £664,746.

62. It was submitted for the appellants that the planning history relating to applications for similar developments in the area was irrelevant and that each should be judged entirely on its own merits. There was evidence submitted that would suggest that a prospective purchaser would seek such information. It could be assumed that the hypothetical purchaser would conduct a similar exercise to that done by the appellants in obtaining advice from an architect, conservation expert and a valuer but would do no more. His bid would be based upon that advice

63. In examination in chief, Mr Roberts said that his evidence showed the market to have been strong and he was aware that the old telephone exchange at 222 Kings Road sold in 2008 for £37.5 million without planning permission. An application on it had been refused. This was indicative of the demand for properties where developers and speculators anticipated potential and were prepared to invest heavily for it.

64. Doing the same exercise for the two walk up units on the basis that access from the telephone exchange would not be available, and taking into account the entirely different market for such a development, Mr Roberts assessed the development value at £220,000. This would not need to be deferred.

65. In his closing submissions for the appellants, Mr Munro said that no prudent or reasonably informed purchaser (and in that respect we accept his arguments about the appropriate test), would not, on the question of a development prospect that could be worth millions of pounds, rely solely upon the sort of advice that the respondents had obtained from HUB Architects. That purchaser would be likely to commission in depth reports and advice of the nature that had been provided by Messrs Oliver and Walker. Similarly, he said, a prudent and reasonably well informed vendor would not be prepared to accept that there was no development value unless he was persuaded by a negative answer that followed such an exercise.

66. Mr McDonald said that he did not hold himself out to be a planning expert but over his many years in practice he had built up a sound working knowledge of planning matters and issues. He had been involved with a number of applications for clients, including a proposal for a complex roof conversion (not penthouses) in Melbury Gardens (which had been successful) and with a property in Edwardes Square. He had undertaken some 12 to 14 planning applications on behalf of clients in the past 5 years. He said that he had been asked by the respondents for his advice in connection with the appellants' somewhat belated stance

on the alleged development potential, and in connection with the response to the enquiry that had been made by HUB Architects on Mr Carey-Morgan's instructions. He said that the letter written to HUB by Mr Bruce Coey of the council on 15 July 2008 was clear and unequivocal. It left absolutely no doubt that any application would be refused on the grounds that it would not comply with the Development Plan Policies CD44 and 45, and those in CD57, 61 and 62. On the strength of that, and his own knowledge, he felt he was able to advise the respondent lessees that this was not something to take forward as there could not possibly be a sustainable claim.

67. To forecast a result, as the appellants had done, that a consent that did not adhere to the UDP would be achieved would, he said, be excessively optimistic. Unless there were special circumstances that warranted deviation from the provisions (and there were none here), a prospective purchaser, having made sufficient enquiries, would conclude that there was no chance of success. The enquiries that had been made by the appellants in 2006, and those made by HUB Architects, had achieved the same result. It was abundantly clear from the council's responses that there was no chance of obtaining planning consent, certainly within the foreseeable future.

68. For these reasons, Mr McDonald said, he would only be able to advise a client that there was a remote possibility of achieving some form of consent in the distant future, and for that reason he concurred with the LVT's view that a purchaser would only be prepared to pay a token amount for that possibility – described by Mr James McDonald in submissions as a "gambling chip." It was clear, Mr James McDonald submitted, that the schemes that had been devised by the appellants, and which had only been made available to the respondents three days before the LVT hearing, had been produced solely to counter the council's letter in 2006, and to attempt to justify development potential.

69. In cross-examination, Mr McDonald said that whilst it was important to consider each planning application on its own merits, he would have (and in the past had) made enquiries of the planning register to gauge the reaction that might be expected if an application were made.

Development potential for additional storey: conclusions

70. This was, in terms of value, by far the largest issue in dispute, with the appellants assessing the value of the development potential (for a penthouse flat) at £664,746, and the respondents, who had argued at the LVT for a nil value, accepting the LVT's decision. The LVT had concluded on the evidence that a "cautious and prudent" investor would reject Mr Roberts's residual valuation as "too unreliable" and that he would rely upon his instinct and knowledge of the market to assess the value of the potential at no more than £10,000.

71. The case for the appellants, as we have said, was that it was likely that planning permission for a roof extension would have been refused by the council but that there was a probability that it would be granted on appeal (Mr Oliver put the overall chances at 60-70%; Mr Walker thought that the would be a 65-70% chance on appeal). The question that we have to decide is

what assessment of the prospects the hypothetical purchaser would have made and whether, in the light of this, the LVT's attribution of a value of £10,000 to such prospect has been shown to be wrong.

72. What we find remarkable is that in all the extensive evidence called on behalf of the appellants there is nowhere any useful factual material as to the pattern of permissions and refusals for rooftop development either by the council or on appeal. A purchaser in our view would undoubtedly wish to be advised about this, rather than basing his bid on the opinions of a planning consultant and a conservation area specialist unsupported by such material. He would know that, due to the very nature of planning, it is often possible to make out a reasonable case that a particular development would accord with planning policy or would be acceptable in planning terms. In support of his evidence that planning permission could be expected Mr Oliver produced ten planning permissions granted by the council for rooftop development. One of these, at 352A King's Road was for the renewal of a 1998 permission for the erection of an additional storey in the form of a mansard roof; another (25-39 Thurloe Square) was for the replacement of existing mansard extensions; and eight (all of them properties in the same terrace on King's Road) were for the replacement of roof access housing. No fuller description of the development and no drawings were produced. These instances are wholly insufficient to suggest that planning permission might be expected for the particular schemes of rooftop development suggested for Vale Court. Moreover Mr Oliver had not sought to establish what planning refusals there had been, so that the picture presented was incomplete and one-sided. We do not think that, in giving the evidence that he did in this respect, Mr Oliver was fulfilling his duty to the Tribunal.

73. We have no doubt that a purchaser, if he had consulted the council on the prospects of planning permission being granted, would have received the strongly negative indications that both the appellants and the respondents in fact received. He would realise that, if permission was to be obtained, he would have to go to appeal. No appeal decisions have been produced to us to suggest that an appeal would probably be successful. Mr Walker referred in his oral evidence to an appeal on Melbury Court, Kensington High Street, that was successful but we have no more information than this.

74. Nor are we persuaded by the evidence of Mr Oliver and Mr Walker that any of the schemes referred to would accord with planning policy or be otherwise acceptable in planning terms. We agree with the view expressed by the planning officer in his response to the HUB Architects letter that the erection of an additional storey at this property, by rising above the roofline of Mallord Street, and by adding significant bulk to a mansion block of flats, would not comply with Policy CD44. We do not consider that any of the proposals would satisfy policy CD 45. We consider that there would be conflict with policy CD46. Mr Oliver admitted that there would be some overlooking of a property in The Vale, and the roof terraces above the Kings Road properties, and Mr Walker admitted in cross-examination that overlooking and potential loss of privacy to other residential units would be a factor to be taken into consideration. Having inspected the property for ourselves, from ground level and from upon the roof, we are in no doubt that each of the schemes would have an adverse effect upon the upper floors of the buildings opposite (particularly in The Vale), and the lower level roof terraces of the Kings Road properties at the rear. We see no reason to disagree with the LVT's

view that there would be serious opposition to the proposals, and in our view it was right to reach the conclusion that it did.

75. The LVT concluded that a purchaser might be prepared to offer a "gambling chip" in the light of the prospect that at some time in the future an application might be treated more sympathetically. The sum of £10,000 was the LVT's opinion of this nominal amount, and the respondents accept this. We therefore include that amount in our valuation.

Hope value: the parties' cases

76. The amount in issue under this head (c £61,000) was relatively small as a proportion of the enfranchisement price. Before the LVT, the appellants had argued for 20% of the total marriage value applicable to Vale Court on the basis that, as the issue of hope value was at the time before the House of Lords in the appeal from the Court of Appeal in *Earl Cadogan v Sportelli* [2007] EWCA Civ 1042, it would be appropriate to include it. Mr MacDonald, relying upon the Court of Appeal decision, had not included anything for hope value. As the House of Lords' decision (*Earl Cadogan v Sportelli* [2010] 1 AC 226) was given before the LVT had completed its decision, the LVT in its initial decision of 16 December 2008 gave the parties leave to make further written submissions on the subject by 31 January 2009.

77. The nature of hope value was described as follows by Lord Neuberger of Abbotsbury in the House of Lords (at paragraph 66):

> "66. However, where the landlord is selling his interest when the tenant is not in the market, a potential purchaser may well think that, in addition to its investment value, the freehold interest carries with it the potential benefit of a possible future sale of the freehold to the present tenant or a successor in title (or indeed the acquisition of the leasehold interest), thereby enabling a release of marriage value in the future. In such a case, therefore, it can be said that, even though the tenant is not in the market at the time of the sale, the value of the freehold interest subject to the lease is greater than the aggregate of the capitalised rental stream and the deferred right to possession at the end of the term, and that something should be added for the possibility of a purchaser benefiting from the release of the marriage value. That additional sum is known as 'hope value'."

The conclusion of the House of Lords (Lord Hoffman dissenting) was that hope value can be taken into account under paragraph 3 of Schedule 6, in so far as it is attributable to non-participating tenants wishing to obtain new leases of their flats in the open market (and not pursuant to Schedule 13).

78. The effect of this, in respect of Vale Court, was to render possible the application of hope value on five flats where the lessees were non participators: Flat 1 which had 70.25 years unexpired, and flats 6, 13, 16 and 20, each of which had 4.74 years remaining. In his further submissions to the LVT, Mr Roberts re-calculated his valuation to include hope value at 20% of marriage value on each of those 5 flats, seeking £75,206. Mr McDonald submitted that a

nominal amount of hope value (7.5% of marriage value) might apply to flat 1 but in respect of all those that had only a short unexpired term, and marriage value having substantially diminished, no hope value was appropriate.

79. Following a further hearing, a supplemental decision was produced by the LVT on 24 April 2009 applying hope value in respect of just two of the short-term non-participating flats and nothing for the others. In respect of flat 13 they concluded that, as it was a larger unit than the others that had only 4.74 years remaining, there was some limited expectation that a prudent investor might assume the lessee would come forward before the term expired. They said, at paragraph 32:

> "32. Whilst both valuers before us use a percentage of total marriage value we prefer the more usual expression of the landlord's share which we take as 50% (recognising in the no-Act world that this is not fixed) because this indicates more clearly the risk to the investor."

And determined that on the basis of a total marriage value of £135,553, the landlord's share was £67,776, and that an investor would pay 5% of that – £3,388.

80. In respect of flat 20, where a section 42 notice has been served by the lessee, the LVT acknowledged what Lord Neuberger said at paragraph 107 of *Sportelli*:

> "107. There are two reasons why, in my opinion, the bracketed words in para 3(1)(b) are significant for present purposes. First, all that the service of a section 42 notice does is to give the tenant a right to acquire a new lease: he can pull out at any time – see section 52. Accordingly, para 3(1) permits some hope value attributable to non-participating tenants' flats to be included on any view. Secondly, 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. 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."

81. The LVT said that there was marriage value of £71,068, and the landlord's share at 50% was £35,534. Whilst an investor would have regard to the risk that he sale may not go ahead, he would in their view pay 30% of this: £10,660. The total hope value for the two flats was therefore £14,048. As to flat 1, the unit that had 70.25 years unexpired, the LVT said that with the tenant already having extended his lease less than ten years ago, no reasonable investor would attribute any hope value to that unit.

82. It was the appellants' case before us that the LVT had misunderstood Mr Roberts's valuation approach, had misinterpreted the evidence, and had made a number of erroneous assumptions. In paragraphs 20 and 22 of its supplementary decision, the LVT said:

> "20. We find it difficult to accept this evidence as helpful. If Mr Roberts's advice is correct and the purchaser [of the Anstruther (Thurloe) Estate] paid 50% of total marriage value in the act world where by law marriage value is shared 50/50, where is his profit from the expected early lease extensions? Mr Roberts did not advise the purchaser, did not know who advised him and is not privy to his valuation. In any event, the property we are dealing with is worth some £2 million to an investor and is in a different market.
>
> 22. This Tribunal's understanding of Mr Cullum's evidence [in *Bircham & Co (Nominees) (No2) v Clarke* (2005) LT Ref: LRA/63/2005 (Unreported) relating to 13 South Terrace, SW7)] is that having regard to the actual lease length he envisages that an investor would expect early release of marriage value. The Lands Tribunal, in a paper determination, adopted 20% in an unopposed appeal. There was no other evidence. The lease had 22.58 years unexpired. There is no doubt that the tenant is in the market because he is exercising his right. Thus one could view this hope as a certainty."

83. As a result, it was submitted, the question that the LVT had asked, and sought to answer, in paragraph 23 was predicated on an entirely false basis:

> "23. If 20% of marriage value is right for a certainty, how can the same be right for non-participators? Why should the hypothetical investor use the same percentage for say 5, 22 and 70 year leases? Our understanding is that he is looking to do deals in the near future and that in the no-act world he holds all the cards. This tribunal does not find the percentage used in South Terrace helpful and it is easily distinguished from Vale Court for the reasons given in paragraph 22 above."

That basis assumed an early release of marriage value, but there was no evidence, it was said, to support such an assumption, and nothing that could justify that understanding.

84. It was also the appellants' case that in assuming (as it appeared to have done) that a tenant who has not sought to extend his lease would not change his mind on the basis that there was no good reason why he should, or seek to assign to somebody who might wish to extend the lease, the LVT had wrongly concluded that there would be no hope value attached to flat 1. In asking itself the question: "Why would the prudent investor assume that the remaining three would and could buy a lease?" the LVT repeated the error of assuming certainty if 20% was to be the appropriate percentage to be applied. It was, of course, hope value and not the value of a certainty that was to be ascertained.

85. The appellants said that the LVT's decision also contradicted its apparent conclusion that there was no hope value on the short-term leases when it applied hope value (at 5% of the landlords' share of marriage value) to flat 13 (also 4.74 years unexpired) on the basis that that flat was larger, and there might be some likelihood therefore that an application by the tenant may be made. No evidence had been adduced to support that conclusion and it appeared to be illogical.

86. As to flat 20, the LVT had "massively overstated" the risk of a tenant who has issued a section 42 notice not proceeding to take a lease extension, and there was no evidence upon which that conclusion could be based.

87. Mr Roberts said that he had typically recorded hope value at 20% of marriage value as the median rate in RICS Red Book and Inheritance Tax valuations, and had, in fact never prepared a valuation at a lower rate. When acting for the taxpayer in inheritance tax cases relating to the freeholder's interest in ground rented portfolios in central London, he said he had agreed the inclusion of hope value for treating with the lessees with the Valuation Office, and this was accepted as standard valuation practice.

88. There was only one recent contemporaneous example of the existence and quantum of hope value in the Prime Central London (PCL) market, he said, that being his firm's valuation and analysis of the subsequent sale of the Thurloe (Anstruther) Estate in and around Thurloe Square, South Kensington, in mid-2007. Acting for a prospective purchaser, it had been concluded that the price to be paid should include an element of hope value at around 30% of marriage value, giving a bid price of £38.7 million. Without hope value, the value of the portfolio was calculated at £32.2 million, and at 40% hope value, £40.7 million, with hope value being applied only to leases with less than 80 years unexpired (out of a range 18.32 to 149.83 years, giving an average of 51.83 years unexpired). The potential purchaser was advised that, to be successful in the tender process, the bid would realistically need to include hope value of between 30% and 50% of marriage value, but as it transpired his clients were unsuccessful in the price they actually bid, and the eventual bidder paid a price that, upon Mr Roberts analysis, included hope value at almost 50%.

89. Mr Roberts said that he drew some comfort from that analysis in that there was little reason to suspect that the bid was framed with a sliding scale of hope value according to the unexpired term of the individual reversions. Whilst there was growth inherent in a purchase such as this portfolio, or indeed Vale Court, as the underlying asset wasted towards expiry, it would seem irrational in the normal course of events to pay more than 50% of marriage value. If that were to happen, any overage above 50% might crystallise into an immediate loss if the lessees exercised their statutory rights under the Act directly after the sale. In Mr Roberts's view, whilst the Thurloe sale was acknowledged to have been at the top of the market, and there might have been some exuberance on the part of the eventual purchaser that could not be reflected in a meaningful analysis, his adoption of 20% of [overall] marriage value on the non-participating flats was modest in the extreme.

90. Although the Thurloe sale was the only recent transactional evidence available, Mr Roberts referred to two historic portfolio transactions (in 1995 and 1997 – pre-*Sportelli*) with which his former partner Roland Cullum FRICS had been involved, and where the bids had been formulated on the basis of 20% hope value. He also referred to two post-*Sportelli* (House of Lords) settlements by his firm: 22 Lennox Gardens where hope value was agreed at 20% on non-participating flats with 6.72 years unexpired; and 59 Cadogan Square at 10% where the lease had 70.94 years unexpired. Both those agreements were with Robert Orr-Ewing of Knight Frank.

91. As to the effect that the state of the market at the valuation date would have upon hope value, whilst Mr McDonald had argued before the LVT that the market was aware of the impending economic downturn and was already declining, it was Mr Roberts's view that the economic data available, and predictions published by three major central London agents (Savills, Knight Frank and his own firm, Cluttons) at the time, indicated that the market was, and was expected to remain, at worst, "static." He said that the trend showed that there was a hurdle to be overcome, not that the market was on the cusp of a decline. For instance, Knight Frank said in its report of 30 October 2007:

> "The next 12 months will feel a lot like late 2004 and 2005; a period in which price growth slowed to single digit levels, and more importantly a period when buyers were looking to strike deals were met by over-ambitious vendors."

The LVT had concluded that there was "little or no expectation of growth", which he took to mean the same thing.

92. He said that, although he did not believe this particular point was being challenged, it was clear to him that hope value would be present both with and without the Act, where the market was static or rising, but, purely in the Act world, it might not be present in a declining market. In the no-Act world, hope value would still be present when the market was on a down-swing, but at a diminished level to reflect the fact that a purchaser of the superior interest could veto a sale that did not provide positive marriage value over the acquisition cost but would be likely to have to wait longer for the overage from the bid of the existing or future tenant. The realisation of this value was effectively locked-up until the market hit the corresponding point in the up-swing.

93. Where unexpired terms were very short, whilst marriage value was decreasing as a proportion of the overall enfranchisement price, pressure was increasing for the lessee to seek to extend his lease or buy his share of the freehold. These factors would cancel each other out in a rising or static market, but there might be some diminution in the hope value percentage in a declining market (which was not, as he had said, the case here), where there was no realistic prospect of the market hitting the corresponding up-swing prior to expiry.

94. Mr Roberts said that individual lessees had their own imperatives, but said that in his experience it was often on assignments that rights were exercised. Indeed, that was what happened following the sale of the short lease, with the benefit of a section 42 claim, of flat 20 in a competitive London auction in January 2009 for £70,000. The claim, made in June 2008, had been suspended under section 54 as a result of the section 13 notice of September 2007, and the purchasers' solicitors sent a letter to the Estate's solicitors on confirmation of the assignment expressing a wish to either join in with the collective enfranchisement, or if that was not possible, to extend their lease as "it only has a short time left to run.". It was also a fact, as his firm's records showed, that in 1995 – 2 years after the Act – all of the flats in Vale Court were held under a headlease expiring in 2012. Thus, at that time none had unexpired terms longer than 17 years. Since then, 17 of the flats had treated with the landlord either within or outside the Act so that, at the valuation date 68% of the leases had been extended.

95. There were also other incentives for lessees to seek to exercise their rights at the last minute (protecting their investment where considerable sums might have been spent on refurbishment, or alternatively to avoid a potential dilapidations claim), and it was extremely rare for enfranchisable leases to expire by effluxion of time. Marriage value formed the largest component of the enfranchisement price at around 40 years unexpired, he said. Beyond that time, pressure on the lessee to seek to extend their lease or buy the freehold was reduced, but at shorter terms it increased – all the more significantly when the remaining term got very short. On the basis of this evidence, and particularly that relating to the approach taken by his firm in respect of the devaluation of the Thurloe transaction, Mr Roberts was therefore of the opinion that a constant percentage rate was equally appropriate at 4.74 years and 70.25 years unexpired. He said that the Lands Chamber decision in *Culley v Daejan Properties Ltd* [2009] UKUT 168 (LC) lent support to his conclusion. The Tribunal (the President and P R Francis FRICS) said (at paragraph 63):

> "63. 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. In the present case the unexpired terms of the leases are 65.37 years and 50% of the lessees are non-participators. Taking all matters into account, and bearing in mind the essentially speculative nature of hope value, we conclude that hope value in this case may be expressed as 10% of marriage value…"

In the instant appeal, Mr Roberts said, there were varying unexpired terms – four at 4.74 years and one at 70.25 years. In respect of the whole collective enfranchisement, there were 12 non-participators out of 25 flats and 4 non-participants with leases expiring in 2012, as against 6 leases of the same remaining term not controlled by the appellant. Mr Roberts said that, in his view, the adoption of 20% hope value for all five of the non-participating flats that are before this Tribunal "sits reasonably against the decision in *Culley*."

96. Mr Roberts's assessment of the hope value, at 20% of overall marriage value on each of the relevant flats at September 2007 was:

Flat 1	70.25 years	£ 6,747	
Flat 6	4.74 years	£10,941	
Flat 13	4.74 years	£21,575	
Flat 16	4.74 years	£10,660	
Flat 20	4.74 years	£11,313	(s 42 notice subsequently received)
		£61,236	

97. Mr McDonald produced a report which, whilst acknowledging that, post *Sportelli*, hope value could be applied in respect of non-participating flats, pointed out that there had been no guidance as to precisely how it should be calculated. He accepted that it was appropriate to calculate it as a percentage of marriage value as this was how it had been done in recent cases but, after discussing at length the question of Act and non-Act scenarios, and suggesting (para 5.2) that the calculation "should be equivalent to the basis of a non-qualifying tenant exercising

his rights under section 42", he accepted in cross-examination that his methodology was wrong.

98. On his basis, he accepted that in the case of flat 1 (70.25 years) hope value would apply, but it needed to be moderated by the unexpired term. He referred to *Sportelli* at paragraph 63 where Lord Neuberger said:

> "63. The longer the lease, the smaller the investment value of the landlord's interest. The proportion of the total value of the landlord's interest attributable to marriage value increases as the unexpired residue of the lease reduces; it reaches a maximum when the lease has about 35 to 40 years to run, and then the proportion decreases over time. It should also be mentioned that marriage value is released when a tenant under a lease negotiates an extension (or a new long lease) with his landlord. The calculation is a little more complex, but the release of the marriage value is normally a significant feature in the exercise."

Mr McDonald said that although the LVT had not allowed any hope value for this flat, evidence from transactions with which he had been involved, both pre-and post-*Sportelli*, which showed hope values settled at between 5% and 10% of marriage value for terms of between 65 and 76.5 years unexpired, indicated that it would be appropriate to allow "no more than 7.5%". That conclusion was also in line with a post-*Sportelli* LVT decision relating to 61 Eastway, London E9 where they considered an appropriate range was 15-20% of half the marriage value (7.5% -10% of overall marriage value) and in that case they opted for the upper end of the range at 20% because a section 42 notice had been served.

99. In the case of leases such as this with long expiry dates, Mr McDonald said that market conditions would be of little consequence as there was plenty of time for equilibrium to be re-established. That was not the case with the short term reversions. If the market was already falling, or anticipated to fall in the immediate future, a lessee could be reluctant to serve a section 42 notice because even a slight fall in capital values might lead to the lease extension price (with a fixed valuation date at the date of the notice) equalling or exceeding the value at term date especially when costs are taken into account. Thus, it was unlikely that any significant hope value could be anticipated, since the amount of marriage value decreases to virtually zero as the lease end approaches. Having said this, he accepted in cross-examination that lessees would be likely to come forward and hope value could be anticipated if the market was static or rising. He acknowledged that it was rare for leases to run to term and for tenants to hand in their keys – unless they anticipated a major dilapidations claim and might therefore see it as better to negotiate pre-expiry.

100. Mr McDonald produced a series of calculations that indicated the likely return to an investor in such a market, dependent upon deferment rate and relativities adopted, and at hope values of 5% produced figures of between 2.25% and 1%, which were, he said, much less than returns normally sought, and thus confirmed his view that hope value must be virtually nil.

101. As to the LVT's adoption of 30% hope value in respect of the flat upon which a section 42 notice was served after the valuation date, he said: "whilst the total quantum of hope value

that they arrived at seems acceptable, I would have been more convinced by small hope value calculations spread over the non-participating short lease flats." Mr Roberts's blanket 20%, he said, did not seem to take into account the effect market conditions would have on the short term interests.

102. There was little evidence of transactions involving hope value post *Sportelli* and he did not think that the portfolio sales referred to by Mr Roberts were helpful. However, in cross-examination he accepted that Mr Roberts's view that whilst it was unlikely traders would be in the market, estates and other long-term portfolio builders would be, and that the portfolio sales referred to by him did indicate significant hope value. He also said that in his view an investor would be likely to separately analyse hope value percentages for individual flats in circumstances such as those prevailing at Vale Court, particularly because the value of the short leases was a significant part of the overall enfranchisement price.

103. Having set out his views, Mr McDonald concluded by saying that in his view the LVT were right in their assessment of hope value, and that he wholly concurred with their findings.

104. Mr Munro submitted that the quantum of hope value was considered in *Cadogan v Erkman* [2011] UKUT 90 LC, where hope value of 20% of marriage value had been sought on a single flat. In that case, evidence in support of 20% was limited, and the Tribunal analysed the history of section 42 notices, concluding on the facts that there was little to encourage a prospective purchaser that a lessee with 17.33 years unexpired would make an early approach, and included hope value at £8,444 [5.8% of overall marriage value or 11.5% of the landlord's share – if taken at 50%]. However, Mr Munro said, that Tribunal had had before it evidence of the section 42 notices that had been served on the Grosvenor Belgravia and Cadogan Estates which indicated that approximately one third of notices were given when there were unexpired terms of 5.75 years or less. There was nothing, he said, to suggest that the profile at Vale Court, where all but one of the non-participating leases had less than 5 years to run, would be any different.

105. Mr Munro submitted that Mr McDonald appeared to be assuming that that hope value was solely limited to a share of the release of marriage value, whereas there were many other factors by which a tenant might seek a new lease. There was certainly no evidence that the markets were either falling or about to fall so far as to totally wipe out any marriage value, and Mr McDonald had produced no evidence to support his predictions. The forecasts produced by Knight Frank, Savills and Cluttons and which had been relied upon by Mr Roberts, were all predicting continued albeit much slower growth at the relevant time. The respondents' submissions appeared, Mr Munro said, to assume that the purchaser would not pay hope value. Those ignored the vendor's position, whereby unless he shared the purchaser's pessimism about the state of the market, he would not agree a price that did not reflect hope value.

106. The question of hope value had recently been dealt with in *38 Cadogan Square*, where the Tribunal accepted that the correct method of calculating it was by taking a proportion of the marriage value (paragraph 22); rejected an argument that if no section 42 notice had been served prior to the hearing, the tenant had no interest in an extended lease, and the purchaser

would not pay hope value (paragraphs 33 & 34); accepted that where the lease was very short, there was merit in the argument that the landlord would be able to negotiate more than 50% of the marriage value (although that was not being argued in this instance) (paragraph 36); accepted that the tenants seeking lease extensions were not concerned only with the release of marriage value (paragraph 45v); acknowledged that where there was more than one flat with potential hope value, there was the opportunity to spread the risk (paragraph 45vi) and in reaching its conclusions had regard to the evidence before it and to five previous decisions on the issue. In that case, the Tribunal concluded that a figure of 5% of marriage value was appropriate in circumstances where the purchaser would be particularly cautious, there was only one flat where hope value could be applied, there was as an unexpired term of 17.75 years and the evidence had suggested that an application for a lease extension was not imminent.

107. Mr Munro suggested that the Tribunal in *38 Cadogan Square* had been mistaken to assume that the fact that a non-participating tenant had not served a section 42 notice was somehow evidence of what he would do in the no-Act world (if that was in fact what it had done). Hope value, he said, could only arise because the tenant was not participating and the fact that he was not could not be used as evidence to diminish hope value. Further, a section 42 application gives the tenant the right to take a lease extension at any time of his own choosing. If he believed it best suited him, he could make the claim days before the lease expired. In the no-Act world he was in entirely the opposite position. It was submitted that the point Lord Neuberger was making in *Sportelli* was that the service of a section 42 notice would increase the hope value because regard could be had to it under para 3(1A)(b) of Schedule 6. That was a different calculation, and it was not being suggested that the absence of a section 42 notice should decrease hope value.

108. Table 1 in *38 Cadogan Square*, Mr Munro said, showed that Act rights were worth over 35% of the value of a short lease, and that provided further support for the passage in *Hague - Leasehold Enfranchisement* Fifth Edition 2009 at paragraph 1-14:

> "1-14 For practical purposes, these factors […the problems of a wasting asset] render it essential for a leaseholder to negotiate the purchase of the freehold, or the grant of a longer term, from his landlord. Here lies the crux of the matter, for (in the absence of legislation) the landlord holds all the cards in any negotiation. He can refuse to sell or grant a new lease altogether, whether his reasons are good or bad. He can dictate any price and any terms he likes, generous, reasonable or extortionate. He can adopt a 'take-it-or-leave-it' attitude, knowing full well that the tenant has no option except to take it. The landlord is the only person from whom the leaseholder can obtain the freehold or a longer lease, and so has a completely monopolistic and unassailable negotiating position. There are few comparable situations where the bargaining powers are quite so unequal."

Therefore, the shorter the lease, the more desperate the position of the leaseholder became, and, Mr Munro said, there was nothing in *38 Cadogan Square* to undermine the appellants' claim to hope value equivalent to 20% of marriage value on each of the five flats where hope value was in issue.

109. Mr James McDonald summarised the respondents' position in his initial closing remarks, and said it was recognised that in the absence of recent case law and guidance on this subject, the Tribunal should be invited to "deliver clarity on the issue as a matter of precedent". That clarity should, in the respondents' view, produce a result that was broadly in line with that determined in the 61 Eastway case (10% of overall marriage value, or 20% of the landlord's share). That was half the blanket rate applied by the appellants in this case. The appellants' position was not surprising, he said, bearing in mind the nature of the Estate's portfolio. In a second closing submission, Mr McDonald said that it should be clear from the evidence and his submissions that the respondents were satisfied with the LVT's decision, and would be happy for it to be confirmed as correct.

110. However, in a further submission , responding to this Tribunal's invitation to the parties to consider the two recent cases referred to in paragraph 9 above, Mr James McDonald referred to *38 Cadogan Square* and said that the conclusions reached in that case acted to confirm Mr Ronald McDonald's view that on the short reversions of 4.74 years the marriage value would have diminished to a negligible amount due to the worsening market, and that the only hope value that might exist was in respect of the one longer lease (flat1).

Hope value: conclusions

111. We deal briefly with the question of whether the percentage of marriage value (whatever it may be) should be quoted as a figure based upon the overall sum of marriage value, or whether it should be, as the LVT said, a percentage of the landlord's share. Both the valuation experts referred in their various reports and evidence to "a percentage of marriage value" and no clear indication was given by either of them as to precisely what element of marriage value was being referred to. Certainly, as far as Mr Roberts is concerned, we conclude that it must be that his 20% was a percentage of the overall value which, where, as here, it is agreed that the marriage value would be divided 50/50, represents 40% of the landlord's share. His evidence before the LVT was on that basis, and it did not change before us. Mr McDonald said in a note setting out his understanding of the points of difference between the parties (handed in at the hearing and dated 4 April 2011) that, as regards flat 1, although the LVT had declined to apply any hope value, he "believe[d] that a hope value of between 10% and 15% of marriage value would be reasonable – perhaps the lower level is appropriate to make some allowance for market conditions." However, in his report he said, at paragraph 5.12:

> "…it would appear that 5% to 7.5% would be appropriate for a lease of just over 70 years. I am therefore of the opinion that the hope value for flat 1 should be calculated at no more than 7.5% of the marriage value."

That appears to us to support the view we take that in his initial report he was referring to a percentage of overall marriage value, but in the document produced at the hearing, he was referring to a percentage of the landlord's share. Nevertheless, we are, of course, mindful of the fact that despite Mr McDonald's evidence (in this regard relating to flat 1), it was the respondent's case that the LVT's decision should stand – and they said there was no hope value on that flat.

112. In *Culley*, hope value was assessed by us at 10% of the overall marriage value. In *38 Cadogan Square* it was expressed as 5% of overall marriage value and in *Erkman* the Tribunal added an end allowance which was rounded at no specific percentage of marriage value.

113. Particularly in cases where marriage value is agreed to be 50/50, we think it safer and less confusing to express hope value as a percentage of the overall marriage value. We heard no specific evidence that related to a situation where marriage value might be split on a different basis (which we accept, in the circumstances outlined by Mr Roberts in general, it could) and do not therefore need to determine what would be the appropriate way to express and calculate it in such an instance.

114. Looking then at the arguments as to whether there should be a blanket figure for hope value on properties such as this where there are differing unexpired lease lengths, Mr Roberts relied upon his firm's convention, particularly the way in which valuations had been undertaken for investor clients, and analyses of market transactions in opting for 20% of marriage value across each of the non-participating flats. We are unconvinced by this approach as it seems totally to ignore the different circumstances that must apply on the one hand to a lease with over 70 years unexpired, and on the other to leases which are rapidly reaching the end of their term. He said that his figure "sits comfortably" with that determined in *Culley*, but in that case all the leases to which hope value was determined to apply were of the same length, and it was clear from paragraph 63 (see paragraph 95 above), that hope value would be lower the longer the unexpired term. In none of the other cases considered by the parties (*Erkman* and *38 Cadogan Square*), and those transactions used to support Mr Roberts's views, were there differing lease lengths, and so there was no evidence of blanket rates being applied there. We are certainly satisfied by Mr Roberts's arguments as to why there should be hope value in respect of the four short leases (see below) and that the same rate should apply to each of them in this case, but the purchaser's perception of the likelihood of the lessee coming forward when not only was there a significant unexpired term, but also the lessee had already exercised his rights under the Act, and had acquired a lease extension, would be entirely different. It stands to reason, in our judgment, that a purchaser would need to weigh up the circumstances relating to each non-participator, and the percentage of hope value that he would apply would reflect those circumstances. In that respect, therefore, the LVT was, we think, correct in adopting the approach that it did in considering the circumstances that applied to each individual flat.

115. Turning now to the level of hope value that should be applied to each non-participating flat, we accept, as we have said, Mr Roberts's evidence as to the likelihood of lessees coming forward in respect of the four flats with 4.74 years remaining. We agree that the potential imperatives for coming forward prior to lease expiry are many and that each lessee will have his own reasons for doing so. The fact that, with only a short time to go before expiry, the lessee has not served a notice does not mean he will not do so. Despite Mr McDonald's initial arguments that the market was declining at the valuation date, and was anticipated to continue in that vein, it seems to us on the facts that that was not the case. Mr McDonald also accepted in cross-examination that the market was closer to static than the impression he had initially given. Therefore, whilst he mounted a cogent argument as to why in a falling market the

chances of a lessee serving a section 42 notice would be significantly diminished, that was not the situation that existed here.

116. The statistical analysis by Mr Roberts as to the percentages of lessees who had come forward, and the lease lengths that would remain when they did so, adds weight to our conclusion that a purchaser would be justified in anticipating the receipt of such a notice and would build in hope value to reflect that view. For instance, in *Erkman* there was evidence (paragraph 72) that a third of the applications for lease extensions came when there were less than 5.75 years unexpired.

117. We have seen nothing in the evidence to dissuade us from accepting 20% of overall marriage value as appropriate in this case. In *Culley* we determined 10% for a lease length of around 65 years, and we think that this close to the lease end, the likelihood of a lessee coming forward is certainly greater. As to flat 20, where the LVT concluded that the service of a section 42 notice by the lessee in 2009 triggered hope value in that instance, we think they were wrong to take it into account. It was served 18 months after the valuation date, and any post valuation date factual evidence must, of course, be ignored. What that does do, though, is to provide retrospective support for our view that there was a reasonably good chance that an application might be received, not just from flat 20 but from any of the short leasehold units.

118. We also think that the LVT was wrong in its conclusion that, because a flat was bigger, there was more chance of a tenant coming forward. We accept that there was absolutely no evidence to support that conclusion, and we see no basis for it. We therefore conclude that hope value should be applied at 20% of overall marriage value on each of the four flats with 4.74 years remaining.

119. As to flat 1, not only was there over 70 years unexpired but the lessee had already exercised his rights under the Act, and a lease extension had been obtained less than ten years ago. In our view, the chances of a lessee (or an assignee) coming forward again in the near future were slim, but we see no reason why we should differ from the conclusion we came to in *Culley* (where there were 65 years unexpired), and we apply hope value at 10% of overall marriage value. This conclusion is supported by *38 Cadogan Square* where hope value was assessed at 5% for a lease with 17.75 years unexpired, but there were circumstances that would have made the purchaser particularly cautious.

120. Hope value for the five relevant flats will, therefore, be expressed thus:

Flat 1	70.25 years	10%	£ 3,374
Flat 6	4.74 years	20%	£ 8,972
Flat 13	4.74 years	20%	£17,669
Flat 16	4.74 years	20%	£ 8,730
Flat 20	4.74 years	20%	£ 9,265
			£48,010

Deferment rate: the parties' cases

121. The issue of the deferment rate arises in relation to the six flats which are subject to leases that have 4.74 years unexpired. In terms of the overall difference between the parties, the amount at issue under this head is relatively small (about £75,000). Before the LVT the deferment rate used by Mr Roberts was 5%, and Mr McDonald contended for 9.5%. The LVT dealt with the issue very shortly. It said:

> "Having regard to the short leases and to the property market at the time of valuation, although not accepting that the '*credit crunch'* would have an impact on the figures, we consider that there was at the time little or no expectation of growth. Given this the Tribunal have concluded that the deferment rate should be adjusted to 7% in the short term."

122. In their evidence before us both valuers addressed what they had to say by reference to the Tribunal decisions on the deferment rate in *Sportelli* (upheld by the Court of Appeal) and in *Cadogan Square Properties*. *Sportelli* was concerned with leases with unexpired terms of 21, 41, 23, 71 and 57 years respectively (see at paragraph 51), and it laid down guidance on the deferment rate for leases with more than 20 years unexpired, its conclusion being that the deferment rate was constant beyond 20 years. *Cadogan Square Properties* concerned leases of flats with between 15.6 and 17.8 years unexpired and established the approach to be followed for reversions of between 10 and 20 years.

123. The decision in *Cadogan Square Properties* was given on 3 December 2010, after the valuers' reports in the present case had been filed. Both Mr Roberts and Mr McDonald filed supplemental reports, in which they expressed further opinions in the light of *Cadogan Square Properties*. During the hearing we asked both valuers to set out what factors affecting the deferment rate were, in their view different, as between leases with 15 years unexpired and those with less than 5 years unexpired, and we were provided with notes that did this. Following the hearing, after we had formed provisional views on the appropriate approach to valuation, we invited observations on them, and we received a further report from Mr Roberts and submissions from Mr Munro and Mr James McDonald.

124. The deferment rate is an annual discount of a future receipt, the vacant possession value of the house or flat at term, and it incorporates a rate to compensate for the deferment of the enjoyment of that possession: see *Sportelli* at paragraph 51. *Sportelli* followed *Arbib* in establishing a deferment rate (DR) composed of three components – a risk-free rate (RFR) derived from index-linked gilts; a real growth rate (RGR) reflecting the long-term growth in house prices; and a risk premium (RP) reflecting the individual components of the risks of investment in long reversions (volatility, illiquidity, deterioration and obsolescence). These are combined in the formula DR=RFR+RP-RGR. The Tribunal took for the RFR 2.25%, for the RP 4.5% and for the RGR 2%, giving a deferment rate of 4.75%. It added 0.25% for flats to reflect the problems of management.

125. One matter that was considered in *Sportelli* was whether any adjustment to the deferment rate might need to be made if at the date of valuation house prices were above or below the level that would have resulted from a projection of past average growth rates. The Tribunal concluded (see paragraph 73) that it was likely that the optimism of a buoyant market would feed through to purchasers of the sort of long-term reversions under consideration, and that the same would be true when the market was low and pessimistic; so that it could be expected that this would be reflected in a reduction or increase, as the case might be, in the risk premium. The view was taken that it was a reasonable working assumption that there would be an effective counterbalancing, so that the deferment rate would not need to change according to whether prices were above or below trend. But the Tribunal said (paragraph 85) that for reversions of less than 20 years the rate would need to have regard to the property cycle at the time of valuation.

126. In *Cadogan Square Properties* the evidence showed that at one of the valuation dates, June 2005, it was reasonable to assume that values were 15% above trend (see paragraphs 172-174) and that by August 2007, the other valuation date, prices had risen further. The Tribunal concluded that it was appropriate to adjust the RGR to reflect this and to ask what reduction in the RGR the parties in negotiation would agree. Very short reversions (less than 5 years remaining) had yet to be tested. It thought (see paragraph 185) that in June 2005 the parties would have settled on a real growth rate of 1.75%, giving a deferment rate of 5.25%, and that in August 2007 (see paragraph 186) they would have agreed on 1.5%, giving a deferment rate, therefore, of 5.5%.

127. Among the further observations, which it added at paragraph 189, the Tribunal said, referring to the approach that it had adopted and to the evidence of Professor Lizieri, who had been called on behalf of the tenants:

> "(vii) The approach is suitable for use with lease lengths of 10 to 20 years. Below 10 years Professor Lizieri said, and we accept, that different considerations arise, in particular as to whether the risk free rate adopted in *Sportelli* would remain appropriate and whether a forecasting model should be used. Such considerations were not explored at the hearing. We also accept that for very short unexpired lease terms the possibility of using net rental yields as a guide to the deferment rate should be examined more closely."

128. In his original report Mr Roberts said that, pending the Tribunal's expected decision in *Cadogan Square Properties* he followed the guidance in *Sportelli*. As far as the components of the deferment rate were concerned, he said that he adopted the *Sportelli* risk free rate of 2.25%; that he was "below trend as to real growth in the short term in line with the LVT determination"; and that he was "below trend as to the risk premium as the proximity of the reversion affects volatility and deterioration and obsolescence". He said that he was comfortable, therefore, to maintain 5% as the appropriate deferment rate.

129. Following *Cadogan Square Properties*, Mr Roberts produced a further report on the deferment rate. Much of this was directed to criticism of the evidence that Professor Lizieri had given in that case, and we do not need to address this. To the extent that such evidence

was accepted it is embodied in the decision; and to the extent that it was not accepted it does not require further consideration here. The fundamental point that Mr Roberts made, independently of the matters considered in *Sportelli* and *Cadogan Square Properties* was that the asset to be valued, the vacant property on reversion, had a worth that was not limited to a sale at the term date. The owner could sell at the term date or in the alternative he could hold the property vacant or rent it out or occupy it himself. A typical investor was unlikely to have an investment horizon for Vale Court anywhere near as short as 4.74 years. Implicit in the freehold vacant possession values, which were agreed, were expectations for future house prices or cyclical movement and the ability to "trade out" at such time as might be expedient to the home-buyer or investor. Risk and growth were viewed beyond the term of the reversion and the growth and risk profile identified in *Sportelli* did not work at these very short terms. In a market above trend the ability of the owner to hold and trade ameliorated the necessary adjustment; while at 4.74 years unexpired there was a downward pressure on yield from competition from the rack rented market. All in all, Mr Roberts said, he would expect downward pressure from the influence of the rack rented market to outweigh the upward pressure from the limited influence of short run future growth. He believed that the deferment rate to be applied to the relevant flats would be between 4% and 5%, and out of caution he maintained the 5% that he had supported before the LVT.

130. Mr McDonald, in his original report, made a single adjustment to the *Sportelli* 5% to reflect the expectation of investors at the valuation date that the market was going to fall substantially. In the short term, if the market was going to fall, it was necessary to substitute for real growth the appropriate level of real decline. It was reasonable to allow a decline of 10%, over and above the discount in his comparables analysis, over the succeeding period of five years, or approximately 2.5% per annum. This required, therefore, an adjustment to the *Sportelli* 5% of 4.5%, producing a deferment rate of 9.5%.

131. In his further report following the decision in *Cadogan Square Properties* Mr McDonald said that the considerations that led the Tribunal to increase the deferment rates to reflect the extent to which price levels were above trend would apply to shorter term reversions also, but the effect would be increased because of the much shorter period over which prices might fall. He did not think that net rental yields were of any assistance because of the inverse relationship of capital values and rental yields. Rental levels had been much less volatile than capital values and if they were used they would tend to balance out any divergence from equilibrium in capital values. His conclusion was that the "valuer's instinct" was the only real method for assessing how far the deferment rate should differ from the *Sportelli* 5%. He thought that a fall of 20% in capital values would have seemed very likely at the valuation date, with a possible recovery of 5% during the unexpired term. He would have advised, therefore that the deferment rate should be adjusted so as to allow for a fall of 15%, or 3.25% per annum compound. This would imply an adjustment of the real growth rate from 2% to -3.25%, giving a deferment rate of 10.25%. Such a figure would not, however, be acceptable to the seller, and he would expect agreement to be reached halfway, at 7.625%. The same end result, Mr McDonald said, would be reached by applying to the expected value at term (15% below the valuation date value) the cost of holding the asset without income for the term. Taking a holding cost of 4%, which he considered conservative, the net value of the reversion would be the same as if a deferment rate of 7.62765% had been applied to the freehold vacant possession

value at the valuation date. Accordingly he believed that a deferment rate of 7.625% was appropriate.

132. For the purpose of relating the process of determining the deferment rate for short leases to that carried out in *Cadogan Square Properties* we asked the parties in the course of the hearing to identify the factors that were different as between a 5-year reversion and a 15-year reversion. The appellants referred to five matters: the prospect of obtaining possession was more immediate at 5 years; the effect of illiquidity might be felt more; rental returns were more likely to influence the deferment rate; the market was less likely to pass through a cycle than over 15 years; and predicting the future might seem more reliable over the shorter period. The respondents said that market forecasts were more likely to be correct over 5 years; that any lack of equilibrium in the market was more likely to be ironed out over 15 years; that predicting the future might be more reliable over 15 years than 5 years because there was longer for any lack of equilibrium to be ironed out; and that any adjustment of the deferment rate to take account of disequilibrium would need to be greater for a 5-year reversion.

Deferment rate: conclusions

133. For our part we do not consider that the *Sportelli* formula is properly to be applied to the valuation of very short-term reversions. The formula was devised to deal with the valuation of hypothetical long-term reversions for which there was no relevant market evidence. Such interests were hypothetical in that they lacked two elements of real world interests – the entitlement to ground rent and the opportunity to bargain with the tenant. Lacking not only these elements but also the prospect (because of their long-term) of the purchaser enjoying possession, they were in the nature of financial interests, and they fell to be valued as such. Because they were long-term interests the foundation of the method of valuation was a long-term risk-free rate derived from Government securities.

134. The very short-term reversions that we now have to value are significantly different from the reversions under consideration in *Sportelli* and *Cadogan Square Properties*. While they are hypothetical in lacking the same two elements as the longer term reversions with which those cases were concerned, their key characteristic is that they contain the guarantee of the early enjoyment of possession. They are not interests that would be bought only as financial interests. The purchaser can look forward to being able, within a short period of time, to let, occupy, keep vacant or redevelop (as he chooses) the property in which the interests are held.

135. Since possession is deferred for only a short time, such short-term reversions are much more akin to freehold interests in possession, and the correct approach in valuing them appears to us to be to start with the value of the freehold interest and to make explicit adjustments to reflect the fact that the right to possession is deferred. We do not consider that a proper approach to their valuation could properly be based on the long-term yields on Government securities.

136. The potential elements of the adjustment that would need to be made appear to us to be three. The first is the value of possession that is lost during the currency of the lease. This can, it seems to us, be allowed for by discounting (applying Present Value) at what Mr Roberts referred to as the net rental yield.

137. The second potential element is the lack of control that the owner of an interest giving the right to future possession has as compared with the owner of an interest in possession. He is reliant on the covenants in the lease and can do nothing with the property until the lease falls in. We can see that considerations of this sort might affect the comparative value and thus call for some additional allowance. This could be in the form of an end allowance or as an adjustment to the yield.

138. The third potential element is real growth. This fell to be included in the *Sportelli* formula because of the observed historic real growth in residential values of about 2% per annum in the long run. While the current value of a freehold in possession will be underpinned by the market faith of such growth continuing in the long term, it is not, ex hypothesi, allowed for within the current price. An explicit allowance for it would, therefore, need to be made in valuing a long-term reversion. Different considerations clearly arise in relation to a short-term reversion. The time horizon of a purchaser of a short-term reversion is unlikely to be the period of the reversion. He will look beyond this, with the expectation of retaining the freehold, possibly for a long time after the reversion has fallen in. To the extent that he does this his outlook will be the same as the purchaser of the interest in possession. Freehold vacant possession prices will always reflect market sentiment about short-term future price levels. Annual variations in growth, positive and negative, vary greatly from the long-run average. An expectation that prices are about to rise will cause them to do so, and the equivalent applies if the expectation is that prices will fall. In the absence of evidence to suggest otherwise we do not think that the purchaser of a short-term reversion would, in regard to growth and future price movements, take any different a view from that of the purchaser of the freehold in possession or that he would make any allowance for possible movements during the period of the reversion.

139. Following the hearing, having set out in a note the thinking that we have just expounded, we invited the parties' views, asking them to address the three elements that we identified, including their quantification. Both parties expressed opinions, but only the appellants provided further evidence related to the questions we had raised. In his additional report Mr Roberts agreed that the value of possession that is lost during the currency of the lease can be allowed for by present valuing the net rental yield. He sought to quantify it by examining the published sources, analysis of the evidence available for the property itself and through his own knowledge of the local market. The figures published by Savills and IPD showed a net rental yield of 2.60%, and the records of his firm, Cluttons implied a net yield of 1.87%. The letting of flat 8 in May 2008 showed a net rental yield of 3.04% after allowing for its condition compared with the subject flats and allowing a gross to net reduction of one-third. Flat 17, let in January 2008, showed a net rental yield of 3.58%. Balancing this slightly disparate evidence, Mr Roberts said, and relying on his own knowledge of yields in the area, he thought a net rental yield for flats at Vale Court would not be higher than 2.75%.

140. Mr Roberts considered that an adjustment of not more than 5% would be appropriate for the fact that the owner would be, as he put it, "locked out" until his reversion fell in. It was a valuation custom in prime central London to allow a modest reduction of 5% to reflect the existence of a shorthold or contractual tenancy. Taking into account the letting practices of the major estates, Mr Roberts thought that a purchaser of Vale Court would probably be content to buy subject to shorthold or contractual tenancies with rights for the tenants to occupy for up to three years. This suggested that an adjustment of up to 5% might be appropriate to allow for being locked out for up to three years and for the usual risks of non-payment of rent and disrepair. The allowance could either be made as an end allowance or by adjustment of the net rental yield. So adjusted, the 2.75% net rental yield would become 3.87%.

141. As far as growth and future price movements were concerned, Mr Roberts said that there was no evidence of which he was aware to suggest that the purchaser of a short-term reversion would take any different view from the purchaser of the freehold in possession or that he would make any allowance for possible price movements during the period of the reversion. The result, therefore, was a deferment rate of 3.87%. Following the guidance in *Sportelli* that the rate should not be defined to an accuracy of less than 0.25%, this became 4%, which was within the range identified in his earlier evidence.

142. In the light of Mr Roberts's evidence we conclude that the best evidence of net rental yield is to be found in the two Vale Court lettings. As analysed by Mr Roberts these showed yields of 3.04% and 3.58%, and we adopt the mean of these two, 3.31%. We are not persuaded that the lower yields derived from more generalised material justifies reducing this property-specific figure. We accept the appropriateness of a 5% adjustment to reflect the owner's lack of control during the period of the reversion. There is no evidence to suggest that the purchaser of a short-term reversion would approach possible future price movements in any way differently from the purchaser of the freehold with vacant possession, and no allowance falls to be made, therefore, in this respect. We consider that the parties to the hypothetical transaction would have reached agreement on this basis, and we take as the deferment rate, therefore, the 3.31% established by the evidence (or more correctly the rounded value of 3.25%), and we make a 5% end allowance for lack of control. (We note that, included as an adjustment of the 3.25%, this would have resulted in a deferment rate of 4.37%).

143. Accordingly for future guidance we conclude that the deferment rate for reversions of less than 5 years should be the net rental yield that the evidence shows to be appropriate for the property in question; and that in addition there should be an end allowance, which, in the absence of evidence establishing some other percentage, should be 5%.

Terms of Transfer: the issue

144. The following clauses of the proposed deed of transfer were in dispute:

> "3. The Transferee covenants with the Transferor for the benefit of the Estate:

3.1 Not without the previous consent in writing of the Transferor (such consent not to be unreasonably withheld or delayed) to alter or permit or suffer to be altered any building now or hereafter on the Property nor to erect or permit or suffer to be erected on the Property any new building;"

and

"4. It is hereby agreed and declared that the Property shall not enjoy any rights of light or air over the Estate which will inhibit or prevent the free use of the Estate for building or other purposes."

145. The LVT accepted the nominee purchasers' contention that these terms were inappropriate. It said:

"151. At paragraph 50 of the Applicant's closing argument Mr Munro cites the fact that clause 3.1 and 4 of the draft terms of transfer are within the existing terms of the lease. He cites two cases and states that maintenance of the value of other properties would satisfy that test. Mr Munro did not explain why in his view the freeholder needed a restrictive covenant that required the consent for internal changes, we consider this inappropriate.

152. The tribunal having considered the terms of the transfer are of the view that the covenant's proposed are inappropriate, the subject premises has been valued with the existing space light and air, any further development would impact on the existing value of the flats. Neither valuer addressed how if these rights were exercised it would affect the value, which it potentially would (considering the impact of light and air on basement flats) The Tribunal consider that it would be wrong to impose these terms on the purchaser. The Tribunal accept the submissions of the Respondent on these issues."

146. The statutory provisions relied on by the appellants for the inclusion of these clauses are contained in paragraphs 3 and 5 of Schedule 7 to the 1993 Act:

"Rights of support, passage of water etc

3(1) This paragraph applies to rights of any of the following descriptions, namely –

(a) rights of support for a building or part of a building;

(b) rights to the access of light and air to a building or part of a building;

(c) rights to the passage of water or of gas…

(d)rights to the use or maintenance of cables…

and the provisions required to be included in the conveyance by virtue of sub-paragraph (2) are accordingly provisions relating to such rights.

(2) The conveyance shall include provisions having the effect of:

(b) making the relevant premises subject to the following easements and rights of way (so far as they are capable of existing in law), namely-

(i) all easements and rights for the benefit of other property to which the relevant premises are subject immediately before the appropriate time, and

(ii) such further easements and rights (if any) as are necessary for the reasonable enjoyment of other property, being property in which the freeholder has an interest at the relevant date…

Restrictive covenants

5(1) As regards restrictive covenants, the conveyance shall include –

(a) such provisions (if any) as the freeholder may require to secure that the nominee purchaser is bound by, or to indemnify the freeholder against breaches of, restrictive covenants which –

(i) affect the relevant premises otherwise than by virtue of any lease subject to which the relevant premises are to be acquired or any agreement collateral to any such lease, and

(ii) are immediately before the appropriate time enforceable for the benefit of the property: and

(b) such provisions (if any) as the freeholder or 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."

147. The case for the appellants consisted of submissions on the part of Mr Munro. No evidence was called. Mr Munro submitted that both paragraph 3(2)(b) and paragraph 5(1)(b) of Schedule 7 were mandatory, and neither allowed for any discretion or provided for a test on equitable principles or necessity as was being argued by the respondents. Specimen leases of flats in Vale Court were produced, and these contained provisions to the same effect as clauses 3.1 and 4 of the draft transfer. What was sought, therefore, Mr Munro said, was the continuance of existing restrictions that fell within paragraph 3(2)(b)(i).

148. Pausing there, neither of the disputed clauses could in our view fall within paragraph 3(2). That provision is concerned with rights of the specified descriptions (light etc). Clause 3(1) does not relate to such rights. As for clause 4, paragraph 3(2) provides for the inclusion of rights of (for instance) light for the benefit of other property. Clause 4 does not make such provision. What it does is to restrict the rights of Vale Court in relation to light and air.

149. If the clauses are to be justified, therefore, this can only be by reference to paragraph 5(1)(b)(i) or (c). Mr Munro relied in the alternative on each of these provisions. Since, however, the proposed clauses are in effectively the same terms as provisions in the leases it is, in our view, (b)(i) that is relevant. Mr Munro said that the LVT had been wrong to say that the freeholders had not explained why they needed the restrictive covenant. Both during the hearing and in written closing submissions they gave an example of the benefit of being able to control alterations – that it would prevent the building being sub-divided or used for other than residential flats. Planning controls were insufficient protection. Vale Court formed part of a block owned by the appellants, comprising Vale Court, the Telephone Exchange and Tryon House. It was the value of the Telephone Exchange and Tryon House that was most immediately in issue. The test of material enhancement, Mr Munro said, was not a particularly stringent one.

150. Under paragraph 5(1)(b)(i) the question that arises is whether the restrictions contained in the clauses are such as to materially enhance the value of other property of the appellants. The approach to be adopted to the question of material enhancement has been the subject of recent consideration by this Tribunal (in *Cadogan v Erkman* [2011] UKUT 90 (LC)) and earlier consideration by the Lands Tribunal in a number of cases. In *Moreau v Howard de Walden Estates Ltd* (LRA/69/2002) the Member (P H Clarke FRICS) said this (at paragraph 185):

> "…I heard evidence and submissions on material enhancement, including attempts to evaluate precisely in monetary terms the effect of the restrictions on the adjoining property. In my judgment, this is an impossible valuation exercise. The question of material enhancement can, in my view, only realistically be considered in general terms. I give no weight to this particular evidence nor to the alleged admission…that there would be only a slight diminution in value in the absence of the respondents' restrictions. We are not concerned with diminution in value but with the *material enhancement in value* in consequence of the restrictions. In my judgment, material enhancement is a matter of general impression."

151. This passage was accepted and adopted by the Tribunal (HH Judge Huskinson and A J Trott FRICS) in *Erkman* (at paragraph 105), and the Tribunal went on to say:

> "We do not accept [counsel for the nominee purchaser's] argument that, having regard to the comparison of language between Schedule 7 paragraph 5 of the 1993 Act and section 84(1A) of the Law of Property Act 1925 as amended it is a prerequisite of a finding under subparagraph 5(1)(c)(ii) (ie a finding that a restriction will materially enhance the value of other property) that there must be valuation evidence which quantifies in money terms the effect on value of other property owned by the Freeholder. We conclude that it

is not necessary for there to be quantified valuation evidence to show that the inclusion of a restriction will uplift the value of other relevant property by £x or will prevent the diminution in value of other relevant property by £y (where £x and £y are quantified sums). However there must be evidence to satisfy the Tribunal, albeit as a matter of general impression, that there will be some monetary uplift in value (albeit unquantified) or the prevention of some monetary diminution in value (albeit unquantified). If all that was proved was that the landlord lost some advantage, being an advantage which could have no effect one way or the other on monetary values of other relevant property, then this would not be sufficient. In the present case we conclude that adequate control over the nature of occupation of No. 42 or the various units within it is a matter of importance for the Freeholder. A restriction which sufficiently controls the nature of this occupation is a restriction which in our judgment will materially enhance the value of other property owned by the Freeholder in Cadogan Square. We reach this conclusion despite there being only broad evidence on the topic from Miss Joyce rather than a fully worked valuation."

152. For our part we adopt the observations in both the passages we have quoted. Of particular importance is the indication in the *Erkman* decision that evidence is required to establish that the restriction will materially enhance the value of other property of the freeholder, although quantification of such enhancement in value is not needed. That must, in our view, be the case, and mere assertions by counsel on behalf of the freeholder are not evidence and are not sufficient. In the present case we have no evidence on behalf of the appellants, only the assertions of counsel. It may be that there would be advantage to the appellants in having the restrictions imposed (and indeed the fact that they want the restrictions suggests that there would be) but that does not establish that the restrictions or either of them would materially enhance the value of other property that they own. The appellants have failed to establish their case.

153. This determines the substantive issues that were before us, and the appeal is allowed in part. The Tribunal's composite valuation is at Appendix 1, together with the individual calculations relating to flats 1, 6, 12, 13, 16 and 20, and we determine the price in the sum of £2,961,613.

Dated 10 October 2011

George Bartlett QC, President

Paul Francis FRICS

Flat 1 – Vale Court

LRA/86/2009

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		25/12/98		
Lease to expire:		24/12/77		
Unexpired Term:		70.25		
Ground rent (pa):		£100		
Ground rent on review (pa)		£200	25/12/19	
		£400	25/12/40	
		£800	25/12/61	
FHVP Value		£389,521		
Extended LHVP Value	99%	£385,625		
LHVP Value		£339,467	87.15%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£100		
YP 12.25 years @	5.25%	£ 8.8716		
			£887	
Term 2:				
Ground Rent:		£200		
YP 21 years @	5.25%	12.5444		
PV 12.25 years @	5.25%	0.5342		
			£1,340	
Term 3:				
Ground Rent:		£400		
YP 21 years @	5.25%	12.5435		
PV 33.25 years @	5.25%	0.1824		
			£915	
Term 4:				
Ground Rent:		£800		
YP 16.00 years @	5.25%	10.6463		
PV 54.25 years @	5.25%	0.0623	£530	
Reversion:				
Unimproved FHVP		£389,521		
PV £1 70.25@	5.00%	0.0325		
			£12,647	
				£16,320
HOPE VALUE:				
FHVP:		£389,521		
Less				
Landlords interest:		£ 16,320		
Leasehold interest:		£339,467		
Total marriage value:			£33,734	
Take 10% Qualifying Non-Participant				£3,374
Freeholders interest:				£19,694

Flat 6 – Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£15		
FHVP Value		432,773		
Extended LHVP Value	99%	£428,446		
LHVP Value		£ 34,622	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£15		
YP 4.74 years @	5.25%	£4,1037		
			£62	
Reversion:				
Unimproved FHVP		£432,773		
Less 5% end allowance		£411,135		
PV £1 4.74@	3.25%	0.8593	£353,288	
				£353,350
HOPE VALUE:				
FHVP:		£432,773		
Less				
Landlords interest:		£353,350		
Leasehold interest:		£ 34,622		
Total marriage value:			£ 44,801	
Take 20% Qualifying:				£ 8,960
Non-Participant				
Freeholders interest:				£362,310

Flat 9– Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£15		
FHVP Value		£528,669		
Extended LHVP Value	99%	£523,383		
LHVP Value		£ 42,294	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£15		
YP 4.74 years @	5.25%	4,1037		
			£62	
Reversion:				
Unimproved FHVP		£528,669		
Less 5% end allowance		£502,236		
PV £1 4.74@	3.25%	0.8593	£431,571	£431,633
MARRIAGE VALUE				
FHVP:		£528,669		
Less				
Landlords Interest:		£431,633		
Leasehold Interest:		£ 42,294		
Total Marriage Value:				
Take 50% Participant			£54,742	£27,371
Freeholders interest:				£459,004

Flat 12 – Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£15		
FHVP Value		£509,220		
Extended LHVP Value	99%	£504,128		
LHVP Value		£ 40,738	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£15		
YP 4.74 years @	5.25%	4,1037		
			£62	
Reversion:				
Unimproved FHVP		£509,220		
Less 5% end allowance		£483,759		
PV £1 4.74@	3.25%	0.8593	£415,694	£415,756
MARRIAGE VALUE:				
FHVP:		£509,220		
Less				
Landlords interest:		£415,756		
Leasehold interest:		£ 40,738		
Total marriage value:			£52,726	
Take 50% Participant				£26,363
Freeholders interest:				£442,119

Flat 13– Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£30		
FHVP Value		£853,415		
Extended LHVP Value	99%	£844,881		
LHVP Value		£ 68,273	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£30		
YP 4.74 years @	5.25%	4,1037		
			£123	
Reversion:				
Unimproved FHVP		£853,415		
Less 5% end allowance		£810,744		
PV £1 4.74@	3.25%	0.8593	£696,672	
				£696,795
HOPE VALUE:				
FHVP:		£853,415		
Less				
Landlords interest:		£696,795		
Leasehold interest:		£ 68,273		
Total marriage value:			£88,347	
Take 20% Qualifying Non-Participant				£17,669
Freeholders interest:				£714,464

Flat 16– Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£15		
FHVP Value		£421,677		
Extended LHVP Value	99%	£417,460		
LHVP Value		£ 33,734	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£15		
YP 4.74 years @	5.25%	4,1037		
			£62	
Reversion:				
Unimproved FHVP		£421,677		
Less 5% end allowance		£400,593		
PV £1 4.74@	3.25%	0.8593	£344,230	
				£344,292
HOPE VALUE:				
FHVP:		£421,677		
Less				
Landlords interest:		£344,292		
Leasehold interest:		£ 33,734		
Total marriage value:			£43,651	
Take 20% Qualifying Non-Participant				£8,730
Freeholders interest:				£353,022

Flat 20 – Vale Court

Valuation Date: 24/09/07

LEASE TERMS				
Lease commenced:		24/06/13		
Lease to expire:		21/06/12		
Unexpired Term:		4.74		
Ground rent (pa):		£15		
FHVP Value		£447,477		
Extended LHVP Value	99%	£443,002		
LHVP Value		£35,798	8.00%	
LANDLORDS INTEREST:				
Term 1:				
Ground Rent:		£15		
YP 4.74 years @	5.25%	4.1037		
			£62	
Reversion:				
Unimproved FHVP		£447,477		
Less 5% end allowance		£425,103		
PV £1 4.74@	3.25%	0.8593	£365,291	
				£365,353
HOPE VALUE:				
FHVP:		£447,477		
Less				
Landlords interest:		£365,353		
Leasehold interest:		£ 35,798		
Total marriage value:			£46,326	
Take 20% Qualifying Non-Participant				£9,265
Freeholders interest:				£374,618