

**LEASEHOLD VALUATION TRIBUNAL
OF THE
MIDLAND RENT ASSESSMENT PANEL**

REF: BIR/47UD/OLR/2005/0047

**Decision on applications under Sections 48 and 91 of the Leasehold Reform,
Housing and Urban Development Act 1993 for the determination of the price payable
for the extension of a lease and costs payable under Section 60**

Applicant Leaseholder:	Mr R Day 4 Dingleside West Avenue Redditch Worcestershire B98 7BJ
Respondent Leaseholder:	Southern Land Securities Ltd Stanton House 41 Black Friars Road Manchester M3 7DB
Subject Property:	Flat 4 Dingleside and Garage No 4 West Avenue Redditch Worcestershire B98 7BJ
Date of notice exercising the right to acquire the freehold:	7 February 2005
Hearing:	20 January 2006
Appearances:	Mr E Rutledge FRICS for the applicant Mr L Nesbitt BSc (Hons) FRICS MCI Arb
Members of the Leasehold Valuation Tribunal	Miss T N Jackson, BA Law (Hons) (Chair) Mr D J Satchwell FRICS Mr D Underhill
Date of determination:	

1. Background

- 1.1 This is a decision on an application under section 48 of the Leasehold Reform, Housing and Urban Development Act 1993 for the determination of the price payable in respect of the grant of a 90 year extension of the lease of the subject property and the proposed terms of the new lease. There is also an application under section 91 (2) for the determination of the reasonable costs payable under section 60 of the Act.

- 1.2 The subject property is held under a lease dated **30 July 1965** for a term of 99 years from 24 June 1963 at a ground rent of £22 per annum. The applicant gave notice of tenants claim to extend the lease on 7 February 2005. As at the relevant date, the lease had an unexpired term of 57 ½ years.

2. **Subject Property**

- 2.1 The property is located at the junction of West Avenue and Glover Street to the south of Redditch Town centre. The property is situated within walking distance of the town centre and is served by Redditch station.
- 2.2 The immediate vicinity comprises a mix of houses and flats. Parking restrictions apply in the street with parking bays reserved for resident permit holders. The property is served by all usual residential amenities.
- 2.3 The flat comprises a purpose built self contained unit forming part of a three storey block of flats arranged in two main detached blocks around communal gardens and parking areas. There is a driveway to the left hand side of block one which leads to further parking areas and two blocks of garages. The flats are approached via a communal entrance door and staircase. The blocks appear to have been constructed approximately 40 years ago with cavity bricks/block elevation walls (with tile hung finishing beneath flat asphalt covered roofs). The property comprises a kitchen, living room, two bedrooms, a bathroom and outside, a single garage.

3. **Inspection and Hearing**

- 3.1 The Tribunal inspected the subject property on 20 January 2006 in the presence of the applicant.
- 3.2 The hearing held on the same day was attended by Mr Rutledge representing the applicant leaseholder and Mr Nesbitt representing the respondent freeholder.

4. **Representations of the Parties**

4.1 **Agreed Matters**

- 4.1.1 In addition to the facts outlined above, the following matters are agreed by the parties:-

- The date of valuation for the purposes of determining the premium payable for the extended lease is the 7 February 2005 and the unexpired term of the lease is 57½ years.
- The ground rent reserved under the lease is £22 per annum fixed throughout the term
- No application for compensation is to be made under paragraph 5 of schedule 6 of the Act
- The market value of the flat with an extended lease would be £80,000

4.2 **Matters in Dispute**

The following matters are in dispute:-

- The open market value of the existing lease
- The yield rates to be applied in calculating the diminution in the value of the freeholders interest.
- The proposed terms of the new lease.

5. Evidence and Submissions on Behalf of the Applicant Leaseholder

5.1 Value of existing lease

5.1.1 Mr Rutledge provided written submissions to assist the Tribunal . His starting point for the valuation of the extended lease was market evidence of other flats within Dingleside which had either sold since September 2004 or which were still on the market. On the basis of the limited market evidence, he considered that the justifiable market value with an extended lease should be £80,000, net of tenancy improvement. Mr Nesbitt agreed with this figure.

5.1.2 In the absence of evidence of open market sales of the sales of existing leases on the Dingleside development, Mr Rutledge sought to value the existing lease by the application of a percentage uplift from the existing leasehold value to the extended leasehold value. His view, based on a table of negotiated settlements of lease extensions in the West Midlands was that in relation to an unexpired term of 57 $\frac{1}{3}$ years, the evidence suggested a maximum percentage uplift of 10%. Accordingly, Mr Rutledge valued the existing leasehold value at £72,727.

5.2 Yield Rates

5.2.1 Mr Rutledge stated that prior to the Cadogan case, professionals had consistently negotiated a yield rate of 7 $\frac{1}{2}$ % in and around the West Midlands area. He submitted that the Cadogan case required consideration of the quality of location in setting the yield rate. Consideration needed to be given as to what the perception would be in the open market of the landlord's interest in this particular geographical area. The landlord's interest on the ground rent was relatively secure and therefore he submitted that the rate to be applied to the capitalised rental income was 7 $\frac{1}{2}$ %. In relation to the capitalisation of the deferred market value he submitted a summary of Tribunal decisions under the 1993 Act with the yield rates highlighted in which he observed that rates varied from 5.5% to 9% for London locations. Therefore if rates were sensitive to location, the appropriate rate for the subject property should be at the higher end of the range namely 8%. As the landlord's interest in the reversion of the subject property was less secure as its location was not high quality and was less attractive than most other areas of Birmingham, this should be reflected in a yield rate of 8% for the capitalisation of the deferred market value.

5.2.2 On the basis of his submissions, Mr Rutledge submitted the following valuation:-

Ground Rent	£22.00 per annum	
YP 57 $\frac{1}{3}$ years at 7 $\frac{1}{2}$ %	13.122	
		£289.00
Existing Market value	£72,727	
10% uplift to extended leasehold.		
Value	£80,000	
PV in 57 $\frac{1}{3}$ years @ 8%	<u>0.01214</u>	

£971.00
£1260.00

Marriage Value

Extended leasehold value	£80,000
Less	
Existing Leasehold Value	£72,727
Term Reversion (as above)	<u>£1260</u>
	£73,987
Marriage value	£6,013.00
50%	3,007.00
Plus term and reversion	<u>£1260.00</u>
Total	£4,266.00

5.2.3 On cross examination Mr Rutledge accepted that the Cadogan case was due to no market evidence being available and therefore it was necessary to look at other forms of investment. However he did not accept that it was appropriate to just base yield rates on gilts as that would be looking at the matter from a purely financial perspective, whereas his experience showed that the location of a property did affect yield rate. He considered location to be part of a package of factors relating to the value of any investment including the risk of obsolescence, growth rate and volatility, and location had a bearing on these matters.

5.2.4 On cross examination, Mr Rutledge stated he had not considered "hope value" in this particular case as in his view, hope value was taken into account in the choice of the rate of capitalisation of the deferred market value and that to include it in the valuation of the property itself would be double counting.

5.3 Proposed Terms of the New Lease

5.3.1 On pages 4,5 and 6 of his written submission, Mr Rutledge set out the proposed terms of the new lease which, he submitted, were necessary to remedy defects in the existing lease and because it would be unreasonable to include, without modification, the relevant terms in question. He stated that the proposed terms were solely to bring the leases in line with the requirements of the Council of Mortgage Lenders to make the flat saleable and to reflect changes occurring since the date of commencement of the existing lease.

5.3.2 Clause 3(i)(b)

Mr Rutledge stated that this proposal was desirable in order reflect modern practice and there was no reason why the lessees should be paying any tax liability.

5.3.3 Clause 3(i)(d)

This proposal was desirable to reflect modern practice and to enable the lease to work

5.3.4 Clause 3(i)(f)

This proposal was to update fees paid and to reflect modern practice.

5.3.5 Clause 4 (i)

Mr Rutledge clarified at the hearing that this should have stated "add before the words 'the garage' the words 'the interior of'". This was to clarify the tenants obligation to maintain only the interior of the garage. He did not consider this to be a departure from the lease.

5.3.6 Clause 4 (iii)

The proposed term was to reflect what the respondent did in practice as currently they insured the building and recovered the cost from the lessee in the service charge demands. Such a clause was also required for the Council of Mortgage Lenders. Mr Rutledge stated that the respondent had accepted such a clause in a deed of variation it had agreed for Flat 17 Dingleside.

5.3.7 Clause 5 (c)

The proposed term was reasonable and was to remedy ambiguity.

5.3.8 Clause 5 (g)(i) - (vi)

The proposed term was required to ensure that the landlord insured and maintained insurance for the common parts of the building.

5.3.9 Clause 6

The proposed term had been agreed by the respondent.

5.3.10 Second schedule

Clause 11

The proposed term was required to clarify the lease, as the term reflected what happened in practice.

5.3.11 Fourth Schedule

Clauses 1 and 4

Consequential amendments required if proposed clauses 5(c) and 5(g)(i) to (vi) respectively were accepted.

5.3.12 Mr Rutledge stated that the respondent had already recognised the need for variations because it had agreed and completed a deed of variation relating to 17 Dingleside which dealt with the lessors insuring the common part of the building. He submitted that this showed that the respondent was prepared to deal with amendments on a piece meal basis even though other leases in the block did not at that time contain similar terms.

5.3.13 He also submitted evidence to show the requirements of the Council of Mortgage Lenders in regard to adequate insurance for blocks of flats, failure to comply with which may make the properties unmortgageable. He submitted details of a letter from solicitors relating to the purchase of a flat on the Dingleside development which he stated demonstrated confusion over the insurance clauses in the existing lease as the lease showed the lessee was to pay the insurance, yet in practice, the freeholder paid it and recharged it to the tenants.

5.4 Costs

Mr Rutledge submitted that reasonable fees would be legal costs of £300 plus VAT and a valuation fee of £275 plus VAT.

6 Evidence and Submissions by the Respondent Freeholder

6.1 Value of existing lease

Mr Nesbitt provided a written submission to assist the Tribunal. Mr Nesbitt agreed that the market value of the flat with an extended lease would be £80,000. In the absence of evidence of open market sales of existing leases on the Dingleside development, Mr Nesbitt sought to value the existing leasehold value by the application of a percentage discount from the extended leasehold value. His view, based on a table of settled lease extension cases with approximately 57 years unexpired (the properties for which were located in London) was that the evidence suggested a percentage relativity of 80% to derive the existing lease value. Accordingly Mr Nesbitt valued the existing leasehold value at £64,000. Mr Nesbitt did not consider that the fact that the properties were in north west London affected the value of the short lease. Mr Nesbitt also referred to the decision of the Leasehold Valuation Tribunal in relation to 66 Courtlands Crescent, Banstead, Surrey in which the relativity between the short lease value and the long lease value was determined at 80%. Mr Nesbitt submitted that the existing value of £64,000 reflected the difficulties in the saleability of the flat and reflected the price a cash buyer would expect to pay.

6.2 Yield

6.2.1 Mr Nesbitt submitted that the appropriate yield rate for both the capitalised rental income and the capitalised deferred market value was 7%. He submitted a schedule of comparables of the sale by auction of a number of freehold blocks of converted flats in London which showed an average yield rate of 6.6%. He stated that he did not see that there would be a difference for the price paid for a ground rent investment in London compared to the rest of the country, excluding prime London areas. The type of investment made in the comparables were long leases with modern ground rents therefore providing an income stream for investment. Therefore there was no need to look at the location from which the income stream was derived.

6.2.2 In cross examination, Mr Nesbitt accepted that evidence relating to sales at auctions may have less weight attached to it due to the uncertainty of whether the tenants were bidding. He also acknowledged that his evidence was mainly based on London properties.

6.2.3 On the basis of his submissions, Mr Nesbitt submitted the following valuation:

Term	Loss of rent x YP	57.33 years @	7.00%	£22.00 13.9904	£308
Reversion	FHVP x PV	57.33 years @	7.00%	£80,000 0.21	£1654
					£1962
Less Value of Freeholders proposed interest	x PV	147.33 years @	7.00%	£80,000 0.000	£3.75
	(Existing term plus 90 years)				
				Lessor's Interest	£1958

Calculation of Marriage Value

	Tenant's Extended Lease Value	£80,000	
	Landlords' Extended Lease Value	£4	
	Sum of Proposed Extended Lease Interests		£80,004
Less	Landlord's Present Interests	£1962	
	Lessee's Present Interest	£64,000	£65,962
			£14,042
Marriage Value	Take	50% Marriage Value	£7,021

Premium Payable to Freeholder

	Total of Diminution in Freehold Interest	£1958	
Plus	Freeholders Share of Marriage Values	£7021	
	Total		£8,979
		Say	£9,000

6.3 Proposed Terms of the New Lease

Mr Nesbitt submitted that under Section 57 of the Act new terms may only be included to amend any defect in the existing lease. He also submitted advice obtained from solicitors on whether the proposed new terms fell within the provisions of the Act.

6.4 Clauses 3(1)(b) and 3(1)(d)

Mr Nesbitt submitted that Mr Rutledge has described these proposals as desirable and therefore this was not a defect within the terms of Section 57 of the Act

6.5 Clause 3(i)(f)

Mr Nesbitt accepted this proposal subject to the sum of £20 being replaced by the sum of £50.

6.6 Clause 4(i)

Mr Nesbitt stated that it had always been the arrangement that the tenant repaired the garages both internally and externally. This was not a defect in the lease but the intended repairing obligation and if the lease were to be modified in this respect there would be inconsistency with the other lessees.

6.7 Clause 4(iii)

Mr Nesbitt stated that this was not a defect but rather to make the clause more desirable.

6.8 Clause 5(c)

The alterations proposed did not remedy a defect and the inclusion of the words may render the lessor liable to incur costs recoverable from some tenants but not others.

6.9 Clause 5(g)(i) to (vi)

The leases had been structured on the basis that the tenants insure and it was not reasonable for a lease variation to be sanctioned which arbitrarily exposed the landlord to expenditure of costs which may not be recoverable from other lessees in the building.

6.10 Clause 6

Mr Nesbitt accepted this proposal.

Second Schedule

6.11 Clause 11

The inclusion of this clause did not remedy a defect but rather made the lease more desirable to the lessee by granting additional rights.

6.12 Fourth Schedule

Clauses 1 and 4

These variations would be consequential amendments which would only be necessary if the variations to clauses 4 and 5 were made.

6.13 In cross examination Mr Nesbitt initially did not accept that there was a conflict between paragraph 8 of the Fourth schedule and clause 4(i). However, he subsequently accepted that the "defect" was in paragraph 8 of the Fourth schedule

but any modification should not result in an extra burden being placed on the landlord. He stated that he would have no objection to paragraph 8 of the Fourth schedule being removed.

6.14 In relation to the insurance clauses, Mr Nesbitt accepted that there was a difference regarding what was happening and what was stated in the lease. However, he did not accept that the proposed terms fell within the definition of section 57 of the Act. He accepted that the lessee had executed a deed of variation in relation to a similar property on the development though he stated that the variation was done on a commercial basis and for consideration which recompensed the lessor for assuming the risk factor in covenanting with only certain individual lessees to insure the building as a whole. Mr Nesbitt advised that the landlord had of his own volition placed the whole block under an insurance policy and was claiming a proportion of that back from the lessees.

6.15 Costs

Mr Nesbitt submitted that reasonable fees would be legal costs of £400 + VAT and it had been agreed that £315 + VAT would be reasonable fees for valuation.

7. Determination

The Tribunal gave full consideration to the evidence and submissions of the parties.

7.1 Value of the Existing Lease

The Tribunal notes that the parties are agreed that the open market value of the extended lease is £80,000 net of any tenancy improvement. In the absence of evidence of open market sales of existing leases, the Tribunal accepts that the value of the existing lease must be determined by the application of a percentage discount to the value of the extended lease. Mr Rutledge submitted that the uplift from the existing lease should be 10% whereas Mr Nesbitt submitted that the discount from the extended lease should be 20%. The Tribunal attached more weight to the evidence submitted by Mr Rutledge regarding negotiated settlements for lease extensions on properties in the locality rather than Mr Nesbitt's evidence which was based on properties in London and the regions. The Tribunal considers that the appropriate uplift is 10%. Accordingly, the Tribunal determines the value of the existing lease of the subject property at the date of valuation at £72,727.

7.2 Yield Rates

Mr Rutledge submitted that the rate for the capitalisation of the deferred market value should be 8% with the lower rate of 7.5% for capitalisation of the ground rent. However, Mr Nesbitt had valued both yield rates at 7%. The Tribunal considered that as the subject property had an unexpired of 57 1/3 years, then there should be a differential between the relevant yield rates. Mr Rutledge submitted evidence showing negotiated settlements with yield rates ranging from 7-7.5%. Mr Nesbitt submitted evidence in relation to yield rates arising from sales at auction. The Tribunal attached little weight to Mr Nesbitt's evidence as it related to properties in London and also related to auction sales of ground rents which must be treated with extreme caution. The Tribunal determines that the rate to be applied to the

capitalised rental income is 7% and that the rate to be applied to the interest in the reversion is 7.5%.

- 7.3 On the basis of those figures for the open market value of the existing lease (£72,727) and of the yield rates of 7% and 7.5% and the agreed figures detailed in paragraph 4 above, the Tribunal calculates the premium payable as follows:

Valuation

Ground Rent		£22	
YP 57.33 years @ 7%		<u>13.9903</u>	£308
Existing market value		£72,727	
10% uplift to extended leasehold Value		£80,000	
PV £1 57.33 years @7.5		<u>0.0158307</u>	<u>£1,266</u>
			<u>£1,574</u>
 Marriage Value			
Extended leasehold value		£80,000	
Less			
Existing leasehold value	£72,727		
Term and reversion	<u>£1,574</u>		
		<u>£74,301</u>	
Marriage Value		£5,699	
	50%	£2,850	
Add term and reversion		<u>£1,574</u>	<u>£4,424</u>

7.4 Proposed Terms of the New Lease

Section 57(6) of the 1993 Act states that:

"either of them may require that for purposes of the new lease any term of the existing lease shall be excluded or modified insofar as

- (a) it is necessary to do so in order to remedy a defect in the existing lease; or
- (b) it would be unreasonable in the circumstances to include, or include without modification, the term in question in view of changes occurring since the date of commencement of the existing lease which affect the suitability on the relevant date of the provisions of that lease"

- 7.5 The word "necessary" has been construed strictly and is not equivalent to "convenient". The word "defect" is not defined but as the paragraph requires it to be "necessary" to make the change requested, the Tribunal's view is that this suggests a restrictive interpretation. Further, section 57(6)(b) is directed at excluding or modifying existing provisions in the lease and not at including wholly new but suitable terms.

Clauses 3(i)(b) and (d)

- 7.6 On the basis of the arguments put forward the Tribunal does not accept that the proposed terms in relation to clauses 3(i)(b) and (d) fall within the terms of the legislation.

Clause 3(i)(f)

- 7.7 The Tribunal notes the respondent's agreement to that clause subject to the sum of £20 being replaced by the sum of £50.

Clause 4(i), 5(c) and Fourth Schedule Clause 1

- 7.8 Mr Nesbitt accepted that there appeared to be a conflict between clause 4(i) and paragraph 8 of the Fourth schedule in the existing terms of the lease. The Tribunal notes the respondent's concern that they would be put in a difficult position if they were specifically bound to assume responsibility for structural repairs to some garages but not others as this would cause problems with apportionment of service charges between all the tenants. However, the Tribunal does not consider that that point outweighs the need to remedy the defect in the lease. As the Fourth schedule explicitly and expressly includes the garages then the Tribunal's view is that clause 4(i) should be modified to reflect that the lessee covenants to keep the interior of the garage in good and tenable repair. This would also require the consequential modification of clause 5(c) and Fourth schedule Clause 1. The Tribunal therefore determines that the applicant's proposed clause 4 (i) 5(c) and Fourth Schedule Clause 1 should be included.

Clause 4(iii) and Clause 5(g)(i) to (vi), Fourth Schedule Clause 4

- 7.9 Clause 4 (iii) contains the existing covenant by the lessee to insure and keep insured the flat and garage against loss or damage by fire and to produce to the lessors the insurance policy and the receipt for the last premium whenever required. It is proposed by the applicant to replace that clause with a new clause 5(g)(i) to (vi) which in the Tribunal's experience, sets out standard clauses requiring the lessor to covenant with the lessee to insure the buildings and garages and common parts from a variety of risks and sets out the consequences following any such risk occurring. The intention is for the lessor to insure the property and recover the costs from the tenant. Mr Rutledge has submitted that this is already happening in practice and Mr Nesbitt has acknowledged that the respondent of its own volition has insured the properties and has then recovered the costs from the tenants through service charge demands. The Tribunal is aware that to amend the lease in this respect may render the lessor liable to incur costs recoverable from some tenants but not others. The Tribunal does not consider the proposed term is necessary to remedy a defect in the existing lease but considers on the basis of the evidence submitted, that changes have occurred since the date of the commencement of the lease which affect the suitability on the relevant date of the provisions of that lease within the provisions of section 57(6)(b) of the Act. The Tribunal therefore determines that clause 4(iii) be deleted and clauses 5(g)(i) to (vi) and Fourth Schedule Clause 4 in the terms set out by the applicant be included in the new lease.

Clause 6

7.10 The Tribunal notes that the respondent has agreed to the proposed new term.

Second Schedule

Clause 11

7.11 The applicant proposes to add a new clause 11 to the second schedule which sets out the easements, rights and privileges included in the lease. It is proposed to include "the right to use and enjoyment of the garden and grounds Dingleside". It had been pointed out that paragraph 2 of the Fourth schedule requires the lessee to contribute to the lessors costs, expenses and outgoings in relation to "all rates, taxes and outgoings (if any) payable in respect of the forecourt, garden way and other parts of Dingleside shown on the plan annex year 2 and thereon hatched and edged". The Tribunal does not consider that this comprises a defect in the lease. The addition of a new clause which is not seeking to modify or exclude a term of the existing lease does not fall within the Tribunal's jurisdiction under the provisions of section 57(6) of the Act. The Tribunal therefore determines that the proposed new clause 11 is not within the Tribunal's jurisdiction.

8. Costs

During the hearing it was agreed between the parties that costs in relation to a valuation fee of £315 + VAT and costs in relation to legal fees of £400 + VAT were reasonable.

Summary

The decision of the Tribunal may be summarised as follows:

- Premium payable by the lessee - £4,424
- The terms of the existing lease to be excluded or modified as follows
- Clause 3(i)(f) by the deletion of the words "a fee of two guineas" and the insertion of the words "a reasonable fee not exceeding £50"
- Clause 4(i) be modified to include before the words "the garage" the words "the interior of"
- Clause 5(c) to be modified by the addition after the words "the main structure" the words "including the exterior of the demised premises and the garage"
- The modification of clause 5 by the insertion of new clauses 5(g)(i) to (vi) as set out in the applicant's submission
- The modification of Clause 6(i) by the deletion of the words in "where the formula demanded or not" and the addition of the word "any" before the word "covenant"
- The modification of Fourth schedule clause 1 in the terms set out in the applicant's submission

N. Jackson
Chair
15 MAY 2006