



**FIRST-TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)**

- Case Reference** : LON/OOBK/OAF/2013/0059
- Property** : 25 Blomfield Road, London W9 1AA
- Applicant** : The Church Commissioners for England
(landlords)
- Representatives** : Mr A. Radevsky (of counsel) instructed by
Radcliffes LeBrausseau (solicitors) with valuation
evidence from Ms V. Kelsey MA, MRICS
(of Knight Frank, chartered surveyors)
- Respondent** : Etablissement Enterprise Dupont (leaseholder)
- Representatives** : Mr C. Heather (of counsel) instructed by JPC Law
(solicitors) with valuation evidence from
Mr P. Beckett FRICS (of Beckett and Kaye,
chartered surveyors)
- Type of Application** : An application for the determination of the
premium payable in an enfranchisement claim
made under section 1 of the Leasehold Reform Act
1967 ('The Act').
- Tribunal Mem-
bers** : Professor James Driscoll, solicitor (Tribunal
Judge) and Mr Luis Jarero BSc FRICS (Tribunal
Member)
- Dates and venue
of Hearing** : The hearing took place on the 3rd and the 4th June
2014. The tribunal inspected the subject premises
and other properties on the morning of 25 June
2014. It met later on 25 June 2014 to consider the
evidence, the submissions and its decision.
- Date of Decision** : 30 July 2014

DECISION

Summary of the decision

1. The premium payable for the acquisition of the freehold of the premises is the sum of £8,572,004 (Eight million, five hundred and seventy two thousand and four pounds).

Introduction

2. This is an application for the determination of the premium payable for the acquisition of the freehold of the premises which is a house. It is made under the Leasehold Reform Act 1967.
3. It is made by the owners of the freehold who are the landlords under a long lease of the house. That lease is dated 11 November 1958 and it is for a term of 60 years from 29 September 1958. A notice of claim seeking to acquire the freehold under the Act was given on or about 15 July 2013. In a notice in reply dated 2 September 2013, the landlord admitted the right to acquire the freehold and they expressed the view that the house should be valued in accordance with section [9(1C)] of the Act. The landlords are the Church Commissioners for England and the leaseholder is a private company.
4. As the parties could not agree on the premium to be paid, or the terms of the transfer, the landlords applied to the tribunal under section 21 of the Act for a determination of these issues. Directions were given by the tribunal on 3 December 2013.

The hearing

5. A hearing took place on 3 and 4 June 2014 when the parties were represented by counsel and their instructing solicitors. Both parties called expert evidence on valuation. The tribunal carried out an inspection of the house (and other dwellings) on 25 June 2014. At the hearing we were told that the parties had agreed the terms of the transfer but they could not agree on the size of the premium. It was agreed that the valuation date is the 27 July 2013 and that at that date the unexpired term of the lease was 5.17 years.

Evidence and submissions made on behalf of the landlord

7. Before the hearing each counsel produced brief written submissions. After an opening statement the valuers were called to give their evidence. The parties agreed that the capitalisation rate to be applied to in valuing the ground rent should be 7%.; that the freehold value should be reduced by 2.5% to take account of the possibility that the leaseholder will continue in

occupation at the end of the lease; that the freehold value should also be reduced by the costs of leaseholder improvements (£92,000) and by the costs of repairing the property (£250,00).

8. Mr Radevsky called Ms Kelsey MA, MRICS to give evidence. Ms Kelsey works for Knight Frank a firm of chartered surveyors. She spoke to her report which is dated 27 May 2014. She answered questions from Mr Heather for the leaseholder and from the tribunal and she was re-examined by Mr Radevsky.
9. She told us that the subject house has a gross internal area of 5,269 square feet. **She and Mr Beckett agree that it is possible to increase the size of the lower ground floor by 500 square feet.** Ms Kelsey also believes that it is possible to increase the size of the lower ground floor at the rear of the house by 1,500 square feet, but Mr Beckett does not. She considers that both the front and the rear gardens have a potential development value. She also accepts that some of the area should be ignored in calculating the net internal area as it is the result of leaseholder improvements.
10. These factors combined led her to conclude that by making adjustments to reflect the leaseholder's improvements and the development potential that the relevant area is 5,953 square feet.
11. Dealing with the 'freehold value' of the premises she relies on the market evidence provided by five sales of houses sold either freehold or with long leases. She made adjustments to the sale prices to take account of the dates of the sales by comparison to the valuation date, by using the Savills indices. Other adjustments were also made as summarised in the paragraphs following. The first sale she deals with is the sale of 27 Maida Avenue which is the road that runs on the south of the Grand Union Canal and almost opposite the subject property as one looks across the canal. However, she considers that this property is not in such a good location as the subject property and she points to other differences such as the access the leaseholder of the subject property has to communal gardens. Adjusting this sale price to reflect the advantages that the subject property has over this comparable sale produces a freehold figure of £2,100 per square foot. (The table in tab 5 of her report).
12. Her next comparable property is the sale of 33 Blomfield Road which she told us is probably the best comparable sale. Adjusting the sale price to reflect its better condition and its access to off street parking produces a rate of £1,888 per square foot. The next one is the sale of 50 Blomfield Road which does not have access to the communal gardens and in Ms Kelsey's opinion is not in as good a location. Making adjustments to the sale price to reflect these factors produces a rate per square foot of £2,450.
13. The fourth sale is that of 36 Blomfield Road which is a maisonette but in Ms Kelsey's opinion a substantial property close to the subject property making it a useful comparable piece of evidence. Making adjustments to the sale price produces a rate per square foot of £2,004.

14. The final sale is that of 30 Blomfield Road which after various adjustments produces a rate of £2,909 per square foot. Ms Kelsey is of the opinion that this should be regarded as a 'trophy house' which we take to mean that it has such qualities that purchasers will pay over the market price to acquire it. She argued that this is borne out by the fact that it attracts a much higher rate than the other comparables so she decided to exclude it from her analysis and to base her conclusion on the other four sales. This produces a figure of £2,111 and she proposes a figure of £2,000.
15. Ms Kelsey also told us that there should be further adjustments. The parties agree that it would cost £250,000 to bring the subject house up to a standard commensurate with the sales she relies on. A further adjustment of should be made to take account of the 'end allowance' factor given the short unexpired length of the lease. She also agrees with Mr Beckett that there should be a small adjustment to reflect the possibility that a leaseholder might seek to continue to occupy the tenancy under an assured tenancy (that is an assured tenancy under section 186 and schedule 10 of the Local Government and Housing Act 1989).
16. In the next part of her evidence she deals with the value of the existing lease. In her opinion the appropriate way of approaching this aspect of the valuation in this case is by reference to the net rental yield. She justifies this by pointing to the fact that the lease had just over five years left unexpired at the valuation date. In arriving at this view she has been influenced by the decision of the Upper Tribunal in the *Vale Court* case ([2011] UKHT 415), which we consider later in this decision.
17. The difficulty in her view, is that the subject house would require considerable investment to be suitable for letting on a market rent. It is not just the costs of such works that has to be considered, but also the fact that the property would not be available to rent whilst the works were being carried out. It is unlikely, she argues, that an investor would consider it economically viable to invest a large sum of money in renovating the house for what might be a relatively short let.
18. What is more likely in her view, is that the house might be let to a number of individuals paying a far lower rent that it might attract if renovated so that it could be marketed as a letting suitable for a company at a full marked rent. Having regard to rents for comparable properties and to the analysis of yields published by Knight Frank and Savills she arrived at the conclusion that the likely rental yield is 2.13%. This should be rounded up to 2.5% which she proposes as the deferment rate.
19. She told us that she and Mr Beckett agree that the capitalisation rate to be applied to the ground rent is 7%.

Evidence and submissions on behalf of the leaseholder

20. Mr Beckett was called to give his evidence on the premium and he spoke to his report dated 27 May 2014. He was cross-examined and re-examined and he also answered questions from the tribunal.

21. He is of the opinion that to make a valid comparison with house sales, ideally one should carry out an internal as well as an external inspection. His valuation includes the sales relied on by Ms Kelsey and he also makes adjustments to reflect the different dates on which the properties were sold by comparison to the valuation date and by other factors. Of the comparable properties he managed to carry out an internal inspection of 33 Blomfield Road and the house in Maida Avenue.

22. On the basis of inspecting 33 Blomfield Road, he notes that (unlike the subject property) it is fully refurbished and reconfigured. Allowances should also be made, he contends, for number 33 having space for parking two cars and a better garden and other advantages it has over the subject property by adjusting the sale price for this comparable house. In this way he arrives at a figure of £1,500 per square foot for the subject property after making all of his adjustments. He describes the sales evidence provided by number 33 as his 'primary comparable' (paragraph 1.215 of his report).

23. Like Ms Kelsey, he believes (though he puts the point rather differently) that the market evidence provided by the sale of number 30 Blomfield Road was a 'special price paid by someone who was determined to have this particular house at all costs..' (paragraph 1.3.9). He rejects this as a comparable sale.

24. As to the sale of number 36 Blomfield Road he considers this property to be in a superior location as it faces not just the canal but the canal basin. Mr Beckett notes that it is in fact a maisonette, not a house, but is in his view a virtual freehold. He adjusts the sales evidence downwards by 504 square feet to the price of 1,500 per square foot.

25. Turning to the sale of number 50 Blomfield Road Mr Beckett expresses surprise that although it is inferior to the subject property it commands a higher per square foot price. He also considers the sales evidence from the two sales of 27 Maida Avenue. His conclusion is that his figure of £1,500 per square foot is 'reasonably reliable' (paragraph 1.4.1).

26. Mr Beckett then dealt with the question of 'relativity'. It is his belief that it is possible to construct a graph of relativity on the principle that what he calls the 'rate of decay' is constant during the term of the lease (paragraph 2.2.6). He calls this the 'principled relativity approach'. By using relativity graphs he concludes that the relativity for a lease with 5.17 years unexpired is 14.32%. He rejects the rental value approach favoured in the *Vale Court* decision.

27. Turning to the deferment rate, he notes that the two UT decisions on valuing short leases do not deal with leases of between 5 and 10 years. He admits that he is not sure about how to deal with this but he starts with the generic

4.75% rate for house leases. In an appendix to his report he puts forward a valuation based on the *Vale Court* approach.

Our inspection

28. The subject property is a large semi-detached corner house built around the mid-19th century which overlooks the Regent's Canal. It has a gross internal floor area of 5269 sq.ft. It is stucco fronted and is arranged over 4 floors (lower ground floor to second floor) with gardens to the front side and rear which have numerous trees which are subject to tree preservation orders. The occupiers have the right to access the ornamental gardens to the rear of the property but the access is not directly from the rear of house.

29. The house is in poor condition needing £250,000 worth of major work (as agreed by the parties) and it is completely unmodernised. The house is not a listed building but comes within the Maida Vale Conservation Area. We also carried out external inspections of the properties the valuers referred to in their reports and we were able to carry out an internal inspection of 33 Blomfield Road. This property, as described by Mr Beckett, had been fully refurbished to a high standard and we found it be in a very good condition.

Our decision

Freehold vacant possession value

32. We met on 25 June 2014 to consider our decision on the premium to be paid. Our reasons for the decision are set out in the following paragraphs.

33. We deal first with the freehold vacant possession value. There are two elements to consider: first, our conclusions on the market evidence provided by the sales data; second, our conclusions on the development value in and around the area of the house.

34. On the first point, both valuers argued that the sale price of 30 Blomfield Road should be excluded from this part of the valuation. Ms Kelsey argued that it is a 'trophy house' (which we take to be a reference to a property whose features are such as to attract 'over' bids) whilst Mr Beckett is of the view that it should be left out of this aspect of the valuation. We have decided that as this sale price is way out of line with the other sales evidence (and there is no proper explanation of why this is, except that it is a "trophy" house in very good condition) it is not truly comparable to the subject property or the other comparables. We have, therefore, excluded it.

35. We have proceeded to take the average of the other adjusted sales evidence which produces a rate per square foot of £2,003. Following Ms Kelsey's reasoning we have made a further reduction of £100 per square foot which produces a figure of £1,900 per square foot. We conclude that Ms Kelsey's analysis of the sales evidence is a more balanced and thorough analysis. She was consistent in her consideration of the market evidence and left out of

account (for good reasons) sales evidence that would have benefited the landlord by producing a higher price. Mr Beckett, in our view, relied too heavily on what he called the sale of 33 Blomfield Road which he described as his primary comparable.

36. On the development value (that is the additional space that a hypothetical prospective purchaser would be prepared to pay for without planning permission and diligent enquiries) issue the valuers agree that the front garden could be developed to provide some 500 square feet of basement space. Following the valuers we have treated this by taking site value at 50% which produces a net figure of 250 sq ft. As many of the trees are subject to 'tree preservation orders' and there is a risk that planning permission might not be granted we have taken off 90% for these potential problems which produces a net figure of 25 square feet.

37. As to the rear garden, Ms Kelsey was of the opinion that 1500 sq ft of basement space could be created. Mr Beckett did not think that there was any but if there was it would be very risky. There is a very large tree in the garden and its roots could have a significant effect on any development. We prefer Ms Kelsey's analysis of this issue and we have concluded (having inspected the property) that there is a potential development to which we take site value of 50% and again deduct 9 of the net figure to reflect risks of dealing with the trees and not obtaining planning permission. This produces a figure of additional space of 100 square feet. Thus the total additional space that can be considered in arriving at the internal area is 100 square feet. This coupled with the agreed internal floor area produces 5369 square feet which at £1900 per square foot gives a FHVP value of £10,201,100 (which has to be deferred for the valuation calculation for the remaining term of the lease).

The deferment rate

38. We turn next to the deferment rate. This has been extensively considered by the courts and the UT in recent years. As is well-known, the UT established in *Sportelli v Cadogan* [2007] 1 E.G.L.R. that there should be a generic rate of 4.75% for house lease claims and 5% for flat lease claims, the additional 0.25% to reflect the extra management problems associated with managing blocks of flats. It based these conclusions by considering evidence from the financial markets instead of market evidence of property sales as the latter is difficult to interpret, tainted as it is by the very existence of statutory rights (the 1967 Act in the case of house leases and Part I of the Leasehold Reform, Housing and Urban Development Act 1993).

39. As the UT defined it, the deferment rate is an annual discount of a future receipt, the vacant possession value at term and it incorporates a rate to compensate for the deferment of the enjoyment of that possession (see: *Sportelli*, paragraph 51).

40. In reaching these conclusions the UT adopted the formula $DR = RP + RRF - RGG$. So, the deferment rate (4.75%) equals the risk premium (4.5%) plus the risk-free rate (2.25%) minus real growth rate (2%).

41. Although the evidence in the case was drawn exclusively from properties in prime central London, the UT ruled also that it should apply to all properties regardless of their geographical location.

42. This general approach to determining the deferment rate was endorsed by the Court of Appeal ([2008] 1.W.L.R. 2142) which also upheld the application of the formula to properties outside prime central London (though noting that it is possible that there might in a particular case be evidence on which a tribunal would be justified in departing from the generic rate for properties outside prime central London). The UT also decided that generic rates should apply regardless of the length of the lease though a different approach should be considered for leases with unexpired terms of less than 20 years. In other words, the deferment rate remains constant throughout unexpired terms of 20 years and above.

43. What is the position of leases with unexpired terms less than 20 years? This has been considered by the UT in two cases, *Cadogan Square Properties Limited and others v Cadogan* [2010] UKHT 427 and the later decision of *Trustees of the Sloane Stanley Estate v Carey-Morgan and another* [2011] UKHT 415. For ease of reference we will refer to these decisions as '*Cadogan Square*' and '*Vale Court*' respectively. Both of these decisions were referred to by counsel for the parties.

44. In the *Cadogan Square* case the UT (Mr Justice Morgan and Mr Trott FRICS) was considering appeals from decisions of the LVT on a number of issues including the applicable deferment rate for unexpired leases of 17.5 years, 15.6 years, 16.1 years, 17.8 years and 17.3 years respectively. It decided that in the case of unexpired terms of less than 20 years, regard should be had to the property cycle at the valuation date. In such cases the tribunal should consider whether any of the three components of the *Sportelli* formula should be altered to reflect the position in the property cycle at the valuation date.

45. Depending on the evidence, it may be appropriate to depart from the 2% real growth rate. Where a tribunal concludes on the evidence that (as in *Cadogan Square*) the current growth rates are above the long-term trends of a 2% rate, it may be appropriate to increase the deferment rate. In this case, for the first, fourth and fifth leases which had valuation dates in 2005, there was evidence that values were then considerably above the expected trends. As a result the parties could have been expected to agree that the real growth rate was 1.55 with the result that the deferment rate is therefore 5.25% for those three cases. But by 2007, the valuation dates for the other two leases, the market had increased dramatically in such a way that the purchaser would have been in a stronger position to argue that future growth in capital prices would be less than the 1.75% figure that applied two years earlier. The parties would, the UT concluded, have settled on a real growth rate of 1.5% which produces a deferment rate of 5.5%.

46. Turning to the *Vale Court* case, here the UT (The then President and Mr Francis FRICS) was considering a claim collectively to enfranchise where 6 of the participating leaseholders had leases with just 4.74 years unexpired at the

valuation date. The UT was considering an appeal which raised several issues including the deferment rate for leases with less than five years unexpired. It decided that for such short unexpired terms a different approach needs to be taken. The *Sportelli* formula was adopted, it reasoned, to deal with the valuation of hypothetical long-term reversions for which there is no relevant market evidence. As such reversionary interests are long-term interests the valuation methodology is based on the long-term risk-free rate derived from Government securities. But in the case of very short reversions the hypothetical purchaser, the UT reasoned, can expect within a short space of time, to either occupy the premises, keep it them vacant, let them, or develop them.

47. As possession is deferred for only a short time, such short-term reversions 'are much more akin to a freehold interest in possession, and the correct approach valuing them is 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.' To this the UT added 'We do not consider that a proper approach to their valuation could properly be based on the long-term yields on Government Securities' (paragraph 135).

48. Adopting this approach the UT stated that one has to value the possession that is lost during the period of the unexpired term. This should be based on a discounted 'net rental yield'. One must also make an allowance to reflect the lack of control the owner has until the end of the term. An additional allowance in the form of either an 'end allowance' or an adjustment to the yield should be made. Another element is real growth but the UT concluded that the purchaser of a short-term reversion would not make any allowances for possible movements during such a short period of the reversion.

49. In the *Vale Court* case the UT concluded the deferment rate for reversions less than five years should be the net rental yield based on the evidence available. In addition there should be an end allowance 'which in the absence of evidence establishing some other percentage should be 5%' (paragraph 143).

50. On the basis of the evidence in this case the UT decided that that the deferment rate should be 3.25% based on the evidence of yields. It deducted 5% from the freehold vacant possession value of the 6 short leases and applied a deferment rate of 3.25% to this figure. How should we apply the principles in these two cases to this application?

51. Mr Radevsky submitted that we should follow the reasoning in the *Vale Court* decision whilst Mr Heather urged us to follow the reasoning in the *Cadogan Square* case. Ms Kelsey supported Mr Radevsky's view. Mr Beckett was of the opinion that the *Cadogan Square* case approach should be followed.

52. Mr Radevsky and Ms Kelsey made the point that the unexpired term in this case is not much longer than those in the *Vale Court* case, that is to say 5.17 years as opposed to 4.74 years. That much is obvious, but so is the UT decision in that case which at paragraph 143 concluded that 'for future guid-

ance we conclude that the deferment rate for reversions of less than five years should be the net rental income...'. As we pointed out during the hearing there will always be cases that on the face of it look anomalous. Does the *Sportelli* generic rate apply where a lease has 20 years and one day unexpired at the valuation date? How should one approach a lease with an unexpired term of 19 years, or a lease with an unexpired term of 10 years?

53. On balance though, we consider that the reasoning in the *Vale Court* decision should be applied to this case. Mr Beckett did not adduce any evidence that at the valuation date there were trends in prices that would justify an increase in the deferment rate (as there was in the *Cadogan Square* case). We reject his suggestion that the starting point should be the generic 4.75% for house leases as the UT stated in *Sportelli* that the generic rates apply to leases with unexpired terms of 20 years or over.

54. The factors that led the UT to take a different approach to the deferment rate in the *Vale Court* case have a resonance in this case. We are considering an unexpired term of just over 5 years (and just a few months longer than the unexpired terms in *Vale Court*) and not a long-term investment where the right to possession is deferred for a long period. In a cases such as this, with a very short unexpired term, we consider that a net rental yield should be applied. Ms Kelsey concludes that in the case of the subject property the available evidence show a net yield is the figure 2.13% which should be adjusted to the nearest 0.25%. The deferment rate in this case is, therefore, on her analysis 2.25%. **Mr Beckett adopts this yield in his alternative valuation based on the *Vale Court* approach.**

Relativity

55. Ms Kelsey has looked at the graphs produced by her firm, Knight Frank, and they show a relativity of 14.44%. If applied to her estimated capital value of £10,763,000 (rounded up) this produces a value for the existing lease of £1,554,177 which equates to a weekly rent in the region of £8,800. She does not believe that this figure is achievable.

56. Mr Beckett's theory of their being a 'constant rate of decay' is interesting but we are not convinced that it is mathematically sound. His conclusion that the appropriate relativity in this case is 14.32% which is very close to Ms Kelsey's figure obtained from her firm's graph. She did, however, explain that in view of the *Vale Court* decision Knight Frank were revising their graph but that at the present time it had not been published. We have also adopted Ms Kelsey's analysis of valuing the existing lease. She estimates that the subject property could command a rental income (net of costs) of £52,000 per annum and that the appropriate yield to apply is 2.13%. This she obtained by averaging the figures from the tables of rental yields produced by Knight Frank and Savills.

Summary and conclusion

57. Our valuation is appended to this decision.

58. In conclusion, and by way of a summary, we find that the freehold vacant possession value is the sum of £10,201,000 from which (following *Vale Court*) an end allowance of 5% needs to be deducted (£510,000), less the agreed percentage representing the risk that the leaseholder could continue in occupation at the end of the lease (2.5%), less the agreed value of the leaseholder's improvements (£92,000) and also deducting the agreed figure for the costs of repairing the subject property (£250,000). This produces an adjusted freehold value of £9,094,017.

59. The ground rent lost is capitalised for the unexpired term by applying the agreed rate of 7%. The adjusted freehold figure is deferred for 5.17 years at 2.25%. The value of the existing lease is found by calculating the estimated net annual income if let applying the figure 2.13% yield for the unexpired term which produces the figure £176,424. This enables one to calculate the marriage value 50% of which is payable to the freeholder. In this way we arrive at our conclusion that the premium payable is the sum of £8,572,004.

Professor James Driscoll, solicitor (Tribunal Judge) and Mr Luis Jarero BSc FRICS (Tribunal Member)

First Tier Tribunal Chamber (Residential Property)

Appendix A

Ref: TW/LON/00BK/OAF/2013/0059

Valuation of 25, Blomfield Road, London W9 1AA

Valuation Date	27 July 2013	
Lease expiring 29 September 2018		
Ground rent	£80 pa	
Unexpired term	5.17 years	
Capitalisation rate	7.0%	
Deferment rate	2.25%	
Value of freehold		£10,201,100
Less 5% end allowance	£510,055	
less 2.5% for security of tenure	£255,028	
less agreed value of improvements	£92,000	
less agreed figure for disrepair	£250,000	
Total deductions		<u>£1,107,083</u>
Adjusted freehold value		£9,094,017

Valuation of Freeholder's current interest

Ground rent	£80		
YP 5.17 years @ 7%	4.21668	£337	
Reversion to freehold value	£9,094,017		
Deferred 5.17 yrs @ 2.25%	0.89133	<u>£8,105,770</u>	
			£8,106,107

Value of existing lease.

Annual rental	£52,000		
less voids etc @ 30%	<u>£15,600</u>		
Net rent	£36,400		
YP 5.17 yrs @ 2.13%	4.8468	£176,424	

Marriage Value

Value after enfranchisement			
Freeholders interest	£0		
Tenant's interest	£9,094,017		
Value before enfranchisement			
Freeholders interest from above	£8,106,107		
Tenant's interest	<u>£176,424</u>		
Marriage value	£811,486		
Divide equally between parties			<u>£465,897</u>
Premium payable to freeholder			£8,572,004