Neutral Citation Number: [2016] UKUT 223 (LC)
Case Nos: LRA 20, 21 & 35/2015

IN THE UPPER TRIBUNAL
(LANDS CHAMBER)

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LEASEHOLD ENFRANCHISEMENT – premium payable in respect of new lease – three separate cases – freehold vacant possession value agreed in one case – decision as to freehold vacant possession values in the other two cases – the value of the existing leases with rights under the Leasehold Reform, Housing and Urban Development Act 1993 - "real world relativity" – the Savills 2002 enfranchisable graph – the value of the existing leases without rights under the 1993 Act – hedonic regression – the Parthenia model rejected – the deduction to be made to reflect the absence of rights under the 1993 Act - other graphs of relativity for leases without rights under the 1993 Act – the resulting values – future cases - Leasehold Reform, Housing and Urban Development Act 1993, sch. 13, Part II

BETWEEN :

THE TRUSTEES OF THE SLOANE STANLEY ESTATE — **Applicants**

- and -

ADRIAN HOWARD MUNDY — **Respondent**

Flat 3, 36 Elm Park Road, London, SW3 6AX

AND BETWEEN :

THE TRUSTEES OF THE SLOANE STANLEY ESTATE — **Applicants**

- and -

ARNAUD LAGESSE — **Respondent**

Flat 11, 26-28 Elm Park Road, London, SW3 6AX

AND BETWEEN :

SOPHIE NATHALIE JEANNE AARON **Applicant**

- and -

WELLCOME TRUST LIMITED

Respondent

Flat 5, 17 Cranley Gardens, London, SW7 3BD

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Mr Anthony Radevsky (instructed by **Pemberton Greenish LLP**) for the **Trustees of the Sloane Stanley Estate**
Mr Stephen Jourdan QC and **Ms Julia Petrenko** (instructed by **CMS Cameron Mc Kenna LLP**) for **Wellcome Trust Limited**
Mr Philip Rainey QC and **Ms Cecily Crampin** (instructed by **Collins Benson Goldhill** LLP) for **Mr Mundy, Mr Lagesse and Ms Aaron**

Hearing dates: 25 – 28 January, 8 – 11 and 15 February 2016

MR JUSTICE MORGAN AND MR ANDREW TROTT FRICS

Rolls Building, Fetter Lane, London, EC4Y 1NL
- -

The following cases are referred to in this Decision:

Arrowdell Limited v Coniston Court (North) Hove Limited [2007] RVR 39
Chelsea Properties Ltd v Earl Cadogan LRA/69/2006, decision dated 16 August 2007, the Lands Tribunal
Earl Cadogan v Sportelli [2007] 1 EGLR 153 (LT) and [2008] 1 WLR 2142 (CA)
Earl Cadogan v Cadogan Square Ltd [2011] 3 EGLR 127

IRC v Clay [1914] 3 KB 466
Kosta v Carnwath (re: 47 Phillimore Gardens) [2014] UKUT 0319 (LC)
Lady Fox's Executors v Commissioners of Inland Revenue [1994] 2 EGLR 185
Lalvani v Earl Cadogan, reported with other cases as Nailrile Ltd v Earl Cadogan [2009] RVR 95
Raja Vyricherla Narayana Gajapatiraju v The Revenue Divisional Officer, Vizagapatam (often referred to as "The Indian Case") [1939] AC 302
Trustees of the Eyre Estate v Saphir [1999] 2 EGLR 123
Xue v Cherry [2015] UKUT 0651 (LC)
82 Portland Place (Freehold) Ltd v Howard de Walden Estates Ltd [2014] UKUT 0133 (LC)

The following additional cases were cited or referred to in skeleton arguments:

Arbib v Cadogan [2005] 3 EGLR 139
Cadogan Estates Ltd v Hows [1989] 2 EGLR 216
Cadogan Holdings Ltd v Pockney LRA/27/2003
Re Coolrace's Appeal [2012] 2 EGLR 69
Daejan Properties Ltd v Weeks [1998] 3 EGLR 12
Dennis & Robinson Ltd v Kiossos Establishment [1987] 1 EGLR 133
Dependable Homes Ltd v Mann [2009] UKUT 171 (LC)
Duke of Westminster v Regis Group (Barclays) Ltd [2007] 3 EGLR 81
Earl Cadogan v Cecil LRA/10/2000
F R Evans (Leeds) Ltd v English Electric Co Ltd (1977) 36 P&CR 185
Grosvenor West End Properties v Harrison 2 January 2006 LON/LVT/1807/2004
Jove Properties (1) Ltd v Kanazeh LON/ooAW/OAF/2013/0060
Langinger v Earl Cadogan LRA/46/2000
Lloyd-Jones v Church Commissioners for England [1982] 1 EGLR 209
Nasser v Grosvenor (West End) Properties LON/OOBK/OLR/2013/0083
Majorstake Ltd v Curtis [2008] AC 787
Metcalfe v Bircham & Co Nominees (No 2) Ltd (LVT) (18 October 2008)
Railtrack plc v Guinness Ltd [2003] 1 EGLR 124
Revenue & Customs Commissioners v Bower [2009] STC 510
Segama NV v Penny Le Roy Ltd [1984] 1 EGLR 109
Sinclair Gardens (Investments) v Ray [2015] EWCA Civ 1247
Sloane Stanley Trustees v Carey-Morgan [2011] UKUT 415 (LC)
Voyvoda v Grosvenor West End Properties GM/LON/OOBK/OLT/2011/0056
Voyazides v Eyre [2013] UKUT 013 (LC)
31 Cadogan Square Freehold v Cadogan [2010] UKUT 321 (LC)

DECISION

CONTENTS **Paragraph no.**

Introduction

1. These three cases are applications under section 48 of the Leasehold Reform, Housing and Urban Development Act 1993 ("the 1993 Act") to determine matters in dispute in respect of applications by lessees to acquire extended leases of their flats under Chapter II of Part I of the 1993 Act. There is now only one matter in dispute in each case and that is the amount of the premium payable by each lessee for his or her extended lease, pursuant to section 56 of, and schedule 13 to, the 1993 Act.

2. The three cases are as follows:

   (1) an application by the Trustees of the Sloane Stanley Estate in respect of an application for an extended lease by the lessee, Mr Mundy, in relation to Flat 3, 36 Elm Park Road, London, SW3 6AX; we will refer to this property as "Flat 3";

   (2) an application by the Trustees of the Sloane Stanley Estate in respect of an application for an extended lease by the lessee, Mr Lagesse, in relation to Flat 11, 26-28 Elm Park Road, London, SW3 6AX; we will refer to this property as "Flat 11";

   (3) an application by Ms Aaron in respect of her application for an extended lease to be granted by her lessor, Wellcome Trust Ltd, in relation to Flat 5, 17 Cranley Gardens, London, SW7 3BD; we will refer to this property as "Flat 5".

3. The applications in relation to Flats 3 and 11 were referred to the Upper Tribunal by the First-tier Tribunal on 16 February 2015. The application in relation to Flat 5 was referred to the Upper Tribunal by the First-tier Tribunal on 27 March 2015. The reason why these three cases have been referred to the Upper Tribunal is that they all involved the same point, namely, the appropriateness of using a particular model (to which we will refer as "the Parthenia model") for the purpose of determining the value of the existing lease of each flat on the assumption that Chapter I and Chapter II of Part I of the 1993 Act conferred no right to acquire any interest in any premises containing the lessee's flat or to acquire any new lease. The use of that model had already been considered by the Leasehold Valuation Tribunal and (on appeal) the Upper Tribunal in Kosta v Carnwath (re: 47 Phillimore Gardens) (the reference to the decision of the Upper Tribunal is [2014] UKUT 0319 (LC)) ("Kosta"). Although the Upper Tribunal did not rely on the Parthenia model in that case, a number of applications, including the present three cases, continued to be made to the First-tier Tribunal for the determination of the premium for an extended lease in which the lessees sought to rely on the Parthenia model. It seemed highly likely that the decisions of the First-tier Tribunal in such cases would be appealed to the Upper Tribunal and so it was considered appropriate to transfer one or more cases to the Upper Tribunal for its decision on the appropriateness of the use of the Parthenia model.

4. These three cases have been case managed and heard together. Mr Radevsky appeared for the Trustees of the Sloane Stanley Estate, Mr Jourdan QC and Ms Petrenko appeared for the Wellcome Trust Ltd and Mr Rainey QC and Ms Crampin appeared for all three lessees. The hearing lasted 9 days. The Upper Tribunal has heard evidence on many matters which have been considered by the Lands Tribunal or the Upper Tribunal on previous occasions but the evidence in this case has been more extensive than the evidence given in any earlier case.

5. We will need to describe the issues raised in these cases in more detail later in this decision but at this stage we will summarise the principal subject matter in dispute which is the method which is generally to be used in order to value an existing lease of the relevant flat on the assumption that Chapter I and Chapter II of Part I of the 1993 Act conferred no right to acquire any interest in any premises containing the lessee's flat or to acquire any new lease. Describing the assumption more succinctly, it is that the existing lease of the relevant flat does not have rights under the 1993 Act. In so far as such a valuation is problematic, that is because, at the present time, the leases of flats which are for sale in the open market in the real world are leases which do have the benefit of rights under the 1993 Act and there is therefore little or no available market evidence involving the sale of existing leases without rights under the 1993 Act.

6. By way of contrast, in the period 1987 to 1991, the leases then existing did not have rights under the 1993 Act, as the 1993 Act did not then exist and it is considered that any anticipation in the market of the future enactment of the 1993 Act did not influence the market during that period. The promoters of the Parthenia model have sought to collect market data for leases in the period 1987 to 1991 with a view to isolating from that data the effect on value of the single variable of the unexpired length of the lease involved in each such case. The statistical method used to isolate the effect on value of that single variable is called "hedonic regression". The promoters of the Parthenia model contend that they have succeeded in isolating the effect of the single variable of lease length for different lengths of leases. They have sought to calculate, in relation to each individual property which is the subject of the data, the relativity of the value of a lease of a certain length of that property as a percentage of what would be the freehold vacant possession ("FHVP") value of the same property. They have sought to plot their findings by drawing an appropriate curve on a graph where the X axis is the length of the lease and the Y axis is the percentage relativity. The promoters of the model contend: (1) that their curve is an accurate depiction of market forces in the period 1987 to 1991; and (2) market forces in this respect would not have altered after the coming into force of the 1993 Act in relation to leases which are assumed not to have rights under the 1993 Act. Accordingly, it is said that if one wants to determine the value of the existing leases (on the assumption that they do not have rights under the 1993 Act) in these three cases with valuation dates in the period February to April 2014, one proceeds by the following two stages. The first stage is to determine the unimproved FHVP of the subject flat. The second stage is to read off the curve, produced by

the Parthenia model, the percentage relativity appropriate for a lease of the length involved in each of these three cases. One then multiplies the unimproved FHVP of the relevant flat by the relevant percentage and the result is the value of the existing lease at the valuation date on the assumption that the existing lease did not have rights under the 1993 Act.

7. We comment at this stage that if we were to find that the Parthenia model were the, or even an, appropriate method for valuing an existing lease, on the assumption that it did not have rights under the 1993 Act, the use of the model would confer a very great benefit on the parties to applications for collective and individual enfranchisement under Chapters I and II of Part I of the 1993 Act, in that it would reduce the number of disputes on the question of the value of the existing lease (without rights under the 1993 Act) which in the past has been a fruitful source of disagreement and has resulted in many cases being fought before the tribunals.

8. We also comment that the reason that the Parthenia model is popular with lessees and the reason that its use is not favoured by lessors is that it throws up a higher relativity for a lease of a particular length as compared with the result of using other possible methods of determining relativity. In a case where the length of the existing lease is 80 years or less, so that the premium payable by the lessee will include a payment in respect of marriage value, the higher relativity will result in a reduction in the amount of the premium payable for an extended lease.

The statutory provisions

9. With that introduction, we now refer to the statutory provisions which deal with the amount of the premium payable for an extended lease under Chapter II of Part I of the 1993 Act. The relevant provisions are in paragraphs 2 to 5 of Part II of schedule 13 to the 1993 Act (introduced by section 56(1) of the 1993 Act). For convenience, we have set out those provisions in full in Appendix A to this decision.

The operation of the statutory provisions

10. Paragraph 2 of schedule 13 provides that the premium payable is made up of, or potentially made up of, three elements, described in sub-paragraphs (a), (b) and (c). In the cases before us, the element in sub-paragraph (c) is not relevant and we need not discuss it.

11. The element in sub-paragraph (a) of paragraph 2 of schedule 13 is elaborated in paragraph 3 of schedule 13. The operation of paragraph 3 of schedule 13 has been discussed in a large number of earlier cases and we do not need to consider it in detail. In the present cases, the parties' valuers agree that what is required is a capitalisation of the ground rent payable under the existing lease and an assessment of the deferred value of the landlord's reversion at the end of the existing lease and also at the end of the extended lease. For this purpose, it is necessary to know, or to determine, the freehold value of the flat with vacant possession. That value has been agreed in relation to Flat 5 but is in dispute in relation to Flats 3

and 11 and we will determine the value of the freehold of those two flats in this decision.

12. It is convenient at this point to state that although the principal relativity which is relevant in these cases is the relativity of the value of the existing lease without rights under the 1993 Act to the FHVP value, there is another relativity which needs to be considered. It arises in this way. For the purpose of determining the FHVP value, valuers will typically use a number of leasehold comparables and some of the comparables may involve comparatively short or medium term leases. It will therefore be necessary to adjust the value revealed by the comparable to reflect the length of the lease and to produce an adjusted value appropriate for a freehold interest. Normally, if not universally, the comparable will involve a lease with rights under the 1993 Act and the relativity of its value to the freehold value is often referred to as "real world relativity". As will be seen, it has become conventional to assess the real world relativity by use of a graph referred to as the Savills 2002 enfranchisable graph. As it happens, there was little controversy before us as to the use of the Savills 2002 enfranchisable graph.

13. We next consider the element of the premium pursuant to sub-paragraph (b) of paragraph 2 of schedule 13. This is elaborated in paragraphs 4, 4A and 4B of schedule 13. This element relates to the payment to the landlord of 50% of the marriage value in the case of existing leases of 80 years or less. The leases in the present cases are for terms which are much shorter than 80 years.

14. For the purpose of the calculation of marriage value, it is necessary to know, or to determine, the value of the interest of the lessee under the existing lease and also the value of the interest of the lessee under the extended lease. The first value is to be arrived at in accordance with paragraph 4A of schedule 13 and the second value is to be arrived at in accordance with paragraph 4B of schedule 13. Both of these paragraphs require one to assess the open market value of the interest. Both of these paragraphs require one to proceed:

> "on the assumption that Chapter I and Chapter II confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease".

15. The quoted assumption refers to a lease without rights under the 1993 Act. This is a significant departure from the position in real life where leases, which were originally long leases, of flats usually, if not universally, have rights under the 1993 Act. In the past, there has been a tendency to refer to the effect of this assumption as requiring one to value the existing lease in a "no Act world". This description is not completely accurate and preferably should be avoided. What the assumption does is to direct a valuation on the basis that the existing lease does not have rights under the 1993 Act. The assumption does not say anything about the leases of flats outside the premises containing the tenant's flat. Therefore, apart from the premises

containing the lessee's flat, one reflects the real position in relation to all other leases of other properties. The 1993 Act will apply in accordance with its terms to other leases of other flats.

16. One has to assess the open market value of the existing lease on the statutory assumptions. The notional sale is to be by a willing seller of the existing lease in the open market. The notional sale is by way of an assignment of the existing lease. The existing lease is assumed to be available on the open market and normally there will be many other properties on the market at the same time and, in so far as the other properties are leasehold flats, the leases of those other properties will typically have the benefit of the 1993 Act whereas the subject property, exceptionally, will not have the benefit of the 1993 Act. It was not in dispute that rights under the 1993 Act are valuable and so the existing lease, without those rights, will have to compete in the open market with other available leases which have those valuable rights.

17. There was discussion before us as to the effect of the statutory assumption that the existing lease has no rights under the 1993 Act on the market in which that lease is notionally available. We consider that the position is clear. The statutory assumption does not change the market in which the existing lease is notionally available. The relevant market is the real market and not a hypothetical market. What is hypothetical is that the existing lease is on the market, that it does not have rights under the 1993 Act and that the existing lease is in fact sold in that market. Of course, the 1993 Act directs further statutory assumptions which must be observed but they do not affect the present point. The position that the market is the real market and not a hypothetical market was well described by Hoffmann LJ in Lady Fox's Executors v Commissioners of Inland Revenue [1994] 2 EGLR 185 at 186 D-F, where he said, referring to the statutory hypothesis required in that case:

> "To this extent, but only to this extent, the express terms of the statute may introduce an element of artificiality into the hypothesis.
>
> In all other respects, the theme which runs through the authorities is that one assumes that the hypothetical vendor and purchaser did whatever reasonable people buying and selling such property would be likely to have done in real life. The hypothetical vendor is an anonymous but reasonable vendor, who goes about the sale as a prudent man of business, negotiating seriously without giving the impression of being either over-anxious or unduly reluctant. The hypothetical buyer is slightly less anonymous. He too is assumed to have behaved reasonably, making proper inquiries about the property and not appearing too eager to buy. But he also reflects reality in that he embodies whatever was actually the demand for that property at the relevant time. It cannot be too strongly emphasised that although the sale is hypothetical, there is

> nothing hypothetical about the open market in which it is supposed to have taken place. The concept of the open market involves assuming that the whole world was free to bid, and then forming a view about what in those circumstances would in real life have been the best price reasonably obtainable."

18. Notwithstanding this statement of principle, Mr Rainey submitted that we should assume a hypothetical market. His suggestion was that the real market dealt in leases with rights under the Act and the hypothetical market would deal in leases without rights under the Act. Even if there was only one lease for sale in the hypothetical market (i.e. the lease to be valued on the statutory assumptions) the hypothetical market should be considered to be different from the real market. Mr Rainey was prepared to accept that the hypothetical market might be a sub-market of the real market. The purpose of this suggestion seemed to be to separate the levels of value in the hypothetical market from levels of value in the real market. It may be that this separation was considered to be helpful to Mr Rainey's submission that it could emerge that the market value of a lease without rights under the Act could conceivably be more than the market value of a lease with rights under the Act, even though he accepted that rights under the Act were beneficial and valuable to a lessee. Whatever the reason for Mr Rainey's attempt to create a hypothetical market, we do not agree with his submission. The statutory assumption does not compel us to assume a hypothetical market. Instead, we are required to assume that a hypothetical asset, a lease without rights under the Act, is available for sale in the real market. In any case, even if we were to assume a hypothetical market for the existing lease without rights under the Act, we do not see how we could disregard the level of values for leases with rights under the Act, even if they were the subject of a different market. If one had regard to such level of values, one would expect that the market value for a lease without rights under the Act would not be more than the market value for an identical lease which did have rights under the Act.

19. The assumption that the relevant lease does not have rights under the 1993 Act applies both to the existing lease and to the extended lease, However, this assumption has not caused any difficulty in these cases in relation to the extended lease. The length of the extended leases in these cases are 113 years (Flat 3), 127.71 years (Flat 11) and 131.32 years (Flat 5). The valuers agreed in each case that the value of these extended leases was 99% of the value of the freeholds of the relevant flats.

20. However, the valuers are far apart on the relativity of the value of the existing leases. The rival positions are as follows:

    (1) Flat 3 (unexpired term of 23 years): lessor's relativity 47.20%; lessee's relativity 59.75%;

    (2) Flat 11 (unexpired term of 37.71 years): lessor's relativity 63.70%; lessee's relativity 77.94%;

(3) Flat 5: (unexpired term of 41.32 years): lessor's relativity 65.46%; lessee's relativity 81.18%.

21. The above figures are before adjusting for the existence of an onerous ground rent in the case of Flats 3 and 11. After adjusting for the onerous ground rent (on an agreed basis), the rival positions as to relativity in relation to these two flats is:

(1) Flat 3: lessor's relativity 45.80%; lessee's relativity 58.35%;

(2) Flat 11: lessor's relativity 61.91%; lessee's relativity 76.15%.

The witnesses

22. Before we consider the detailed valuation evidence which we received in this case, we will comment on the four valuation witnesses who gave evidence before us. For the lessors, these were Mr Roberts (dealing with Flats 3 and 11) and Mr Fielding (dealing with Flat 5). For the lessees, the witnesses were Mr Wyatt (dealing with Flats 3 and 5) and Mr Ingram-Hill (dealing with Flat 11).

23. Mr Einar Roberts BSc, MA, MRICS is a partner in Cluttons LLP with more than 19 years professional experience. He has negotiated a large number of prime central London settlements under the Leasehold Reform Acts, generally in the locality of the appeal properties. Apart from giving expert valuation evidence about relativity and the freehold values of Flats 3 and 11, Mr Roberts also gave evidence about what he identified as four problems with the dataset used by Mr Wyatt and Dr Bracke (to whom we refer below), the differences between the market in 1987-1991 and at the valuation date, and commented on the factual evidence of Mr Shingles and Mr Hollamby.

24. Mr Ed Fielding MRICS is a director of Savills (UK) Limited having qualified in 2008. He joined Savills in 2012 having previously worked for Cluttons LLP. He works in the Prime Estates Team advising landed estates and other landlord clients about asset management and leasehold enfranchisement matters. He estimates that he undertakes 100 enfranchisement claims per annum. Mr Fielding was called as a replacement witness for Mr Alastair Stimson MRICS, a fellow director of Savills (UK) Limited, who was unable to attend the hearing. Mr Fielding adopted and spoke to Mr Stimson's evidence. Such evidence was concerned with the relativity appropriate to the existing lease at Flat 5, the FHVP value having been agreed with Mr Wyatt. In a supplementary report Mr Stimson responded to Mr Wyatt's evidence, explained the differences in the market between 1987-1991 and the valuation date and reviewed the various graphs of relativity. He explained why he considered the Gerald Eve Graph to be the most reliable.

25. Mr James Wyatt BSc, MPhil, FRICS is a director of Parthenia Valuation, Parthenia Research and Parthenia Indices. He was previously an estate agent at Winkworth (1994 to 1997) and Knight Frank (1997 to 2001) before

joining John D Wood & Co in 2003 and becoming their Head of Valuation before leaving in 2014. Mr Wyatt submitted expert reports in two forms. Firstly, for each of the application properties he submitted a detailed report describing the hedonic regression method for obtaining relativity and applying it to derive a relativity for each flat. At the hearing Dr Bracke was cross-examined about this aspect of the tenants' evidence rather than Mr Wyatt. Secondly, Mr Wyatt submitted valuation reports for Flats 3 and 5 in which he calculated the unimproved FHVP value of the flats.

26. Mr Alexander Ingram-Hill MA, MRICS is an Associate Director at John D Wood & Co and the Head of the Valuation and Surveying Department acting on behalf of leaseholders in respect of Leasehold Reform Act valuations and negotiations. Mr Ingram-Hill gave evidence of the unimproved FHVP value of Flat 11 and adopted the relativity derived from the Parthenia model to calculate the value of the existing lease without Act rights.

27. At this stage, we will also identify the witnesses who gave evidence in relation to the subject of hedonic regression and the use of the Parthenia model. The tenants called Dr Philippe Bracke and Mr Wyatt (referred to above). Dr Bracke is an economist at the Bank of England and was the technical author of the Parthenia model. Ms Aaron submitted a report by Professor John Muellbauer but he was not called to give evidence as the result of a prior direction of the Tribunal. He is Professor of Economics at Oxford University and Senior Research Fellow at Nuffield College, Oxford and of the Institute for New Economic Thinking at the Oxford Martin School. The Wellcome Trust Ltd called Professor Colin Lizieri who is the Grosvenor Professor of Real Estate Finance in the Department of Land Economy at Cambridge University and a Fellow of Pembroke College, Cambridge. The Wellcome Trust Ltd also called Mr Chris Buckle who is a Chartered Surveyor and an Associate Director in Savills Residential Research Team. He gave evidence about a new version of the Savills 2002 enfranchisable graph based upon hedonic regression. The Sloane Stanley Estate served a report from Professor Bryan MacGregor who is the MacRobert Professor of Land Economy and a Vice-Principal at the University of Aberdeen. Professor MacGregor was not called to give evidence but other witnesses referred to some of the contents of his report.

Description of the application properties

28. Flat 3 is a third floor walk-up with a GIA of 600 sq ft. It is configured to provide the main reception room and kitchen to the rear of the building, with an internal bathroom and two bedrooms to the front of the building. The building in which Flat 3 is situated is on the south side of Elm Park Road equidistant between The Vale and Beaufort Street.

29. Flat 11 is a lower ground floor flat with a GIA of 438 sq ft. It is configured to provide the main reception room, with semi-partitioned sleeping area, and with a separate kitchen to the front of the building and bathroom to the

rear. The building in which Flat 11 is situated is located on the south side of Elm Park Road on the junction with Beaufort Street.

30. Flat 5 is a split level first floor flat with a GIA of 1,311 sq ft. Flat 5 is configured as a 3 bedroom flat with a main reception room to the rear and two bathrooms, one en-suite. The flat has a balcony to the front and a large roof terrace to the rear. It is situated in a red brick building on the eastern terrace of Cranley Gardens.

The freehold values

31. The parties in relation to Flat 5 have agreed that the FHVP value of Flat 5 at the relevant valuation date (25 February 2014) was £2,750,000.

32. The parties in relation to Flat 3 and Flat 11 are in dispute as to the FHVP value of those flats. The rival positions are as follows:

    (1) Flat 3 (valuation date – 20 March 2014): lessor's value £950,000; lessee's value £876,000;

    (2) Flat 11 (valuation date – 9 April 2014): lessor's value £600,000; lessee's value £545,310.

The freehold value of Flat 11

Evidence

33. For the tenant Mr Ingram-Hill estimated the unimproved FHVP value of Flat 11 to be £545,310 (£1,245 psf), while for the landlord Mr Roberts estimated the value to be £600,000 (£1,370 psf).

34. Between them the valuers relied upon six comparables. Mr Ingram-Hill favoured comparables of lower ground floor flats and, in particular, the two studio flats at 74 Elm Park Gardens ("EPG"). Mr Roberts preferred comparables located in Elm Park Road ("EPR"), even though two such comparables, Flats 7 and 10 at 52 EPR, were on upper floors.

35. Both valuers relied upon Flat 3 at 34 EPR, a significantly larger lower ground floor flat with a private, south facing garden and Flat 7 at 52 EPR, a second floor studio flat of similar size to Flat 11.

36. Mr Roberts relied upon two comparables that were rejected by Mr Ingram-Hill: the third floor Flat 10 at 52 EPR and the sale of Flat 11 itself for £495,000 in April 2014.

37. Mr Ingram-Hill had serious doubts about the reliability of the sale of Flat 10 at 52 EPR because it was acquired by the purchaser without the benefit of an assigned notice to extend the lease. It was a relatively short lease (63 years unexpired) and there was doubt about the accuracy of the stated floor

area. Mr Ingram-Hill said that the sale price of Flat 10 at 52 EPR was an outlier and it should be omitted as a comparable.

38. Mr Ingram-Hill thought that his client, Mr Lagesse, had overpaid for the existing lease of Flat 11. Mr Ingram-Hill advised him at the time of the purchase that the maximum value of a long lease would be £540,000 to £550,000 and that the cost of a lease extension would be between £135,000 and £140,000. Taking the lower pair of figures (for long lease value and cost of a lease extension) gave a value for the existing lease of £405,000. The purchase price of £495,000 indicated a long lease value of £671,369 using the Savills 2002 enfranchisable graph. Deducting the sum of £40,000 to reflect improvements, Mr Ingram-Hill said that the resultant value of £630,000 (£1,438 per sq ft) was inappropriately high when compared with the value of the two lower ground floor studio flats at 74 EPG which he analysed at £1,265 and £1,219 psf.

39. While Mr Roberts accepted during cross-examination that the comparable at Flat 10 at 52 EPR was an outlier in the valuation of Flat 3 at 36 EPR (Mr Mundy's flat), he did not consider it to be an outlier in the context of the valuation of Flat 11 and he continued to rely on it as one of his preferred comparables.

40. Mr Roberts also considered it appropriate to rely on the sale of Flat 11 at the valuation date to Mr Lagesse. Mr Ingram-Hill had explained to Mr Lagesse how the market for existing lease transactions operated and had given his view of the market value of the existing lease. Notwithstanding this advice Mr Lagesse had proceeded to pay the asking price of £495,000 and there was no reason to exclude it from the analysis.

41. Both valuers provided a sense check of their valuation. Mr Ingram-Hill examined the availability of long leasehold studio flats in the area at or around a price of £500,000. He concluded that smaller long leasehold studio flats (with areas of under 300 sf) were available for under £500,000 and showed high rates psf. Larger studios were available on extended leases for more than £600,000 and showed lower rates psf. Mr Ingram-Hill concluded that mid-sized studio flats were fetching from £550,000 to £600,000. Flat 11 was at the lower end of this range due to its proximity to Beaufort Street.

42. Mr Roberts considered how his valuation of Flat 11 at £600,000 compared with similar value property in the area at the valuation date. He identified five such properties and concluded that his valuation was consistent with the evidence in the wider market in this price band. He also noted that of these five transactions, three were sold at slightly under the asking price, one was sold at the asking price and one was sold above the asking price. He did not think there was anything particularly surprising therefore about Flat 11 having sold for the asking price.

43. The key adjustment made by the valuers to their comparables was for location and especially for the differences between EPR and EPG. The

valuers agreed that EPG was in a less sought after postcode district (SW10) than EPR (SW3) and that EPG was less attractive due to the presence of large 1960s blocks of purpose built council flats. 74 EPG, where Mr Ingram-Hill relied upon the sales of Flats A and B, contained council housing.

44. Mr Roberts allowed 20% for the difference in location between EPG and EPR and another 5% for the council housing at No.74. Mr Ingram-Hill allowed 2.5% for each of these factors.

45. In his expert report Mr Roberts assumed that all the comparables in EPR had similar locations and therefore similar values. But under cross-examination Mr Roberts acknowledged that there "could seem to be a modicum of inconsistency between my [20%] adjustment for a prized position in Elm Park Road [Mr Mundy's Flat 3 at 36 EPR] and a less prized position in Elm Park Road [Mr Lagesse's Flat 11]." Mr Roberts said that he might "reduce my location adjustment from 20 to perhaps 17.5 or 15 [%]" in respect of Flat 11.

46. Mr Ingram-Hill considered that all of his comparables were in quieter locations than Flat 11 which was situated at the junction of Beaufort Street and Elm Park Road. Beaufort Street is a busy vehicular thoroughfare and bus route leading from Fulham Road in the north to Chelsea Embankment and Battersea Bridge in the south. Traffic waiting to turn onto or go across Beaufort Street from Elm Park Road queued immediately outside Flat 11. He allowed 7.5% for this factor.

47. The valuers made other adjustments for the matters considered under separate headings in the following paragraphs (a) to (j).

(a) Time

48. Mr Ingram-Hill adjusted for time to the valuation date using the John D Wood & Co Chelsea Index for flats. That index ceased production in May 2014 and the last available index value was for March 2014 which is the value adopted by Mr Ingram-Hill as being appropriate for the valuation date (9 April 2014). Flat 3 at 34 EPR was sold in October 2014, after the John D Wood & Co Index had stopped production. Mr Ingram-Hill made no time adjustment for this comparable because he considered there was no significant market movement between April 2014 and October 2014 that justified indexation.

49. Mr Roberts said he would usually index values for time using the Savills Prime Central London Index but in this case he was "not comfortable that index captures growth over the period reliably." Because his comparables were close to and reasonably spaced around the valuation date he chose not to index them for time.

(b) Lease Length

50. Both valuers adjusted short lease values to freehold values by using the Savills 2002 enfranchisable relativity graph.

(c) Condition

51. Both valuers made an adjustment to allow for the recent refurbishment of Flats A and B at 74 EPG. Mr Ingram-Hill allowed 2.5% while Mr Roberts took a lump sum of £50,000 which he then deducted pro-rata by floor area. This was equivalent to 6.6% for Flat A and 6.3% for Flat B.

52. Mr Ingram-Hill added 2.5% to the value of Flat 7 at 52 EPR to reflect its dated condition. Mr Roberts made no such adjustment.

53. Mr Roberts allowed the sum of £50,000 (£114 psf) for the improvements to Flat 11 which represents an allowance of 7.5% from the fully adjusted FHVP rate.

(d) Vaults

54. Some of the comparables have demised vaults. Mr Ingram-Hill valued the vaults at Flats A and B at 74 EPG and Flat 3 at 34 EPR at one fifth the rate psf of the main floor space. Mr Roberts valued the vaults at Flats A and B at 74 EPG at £50,000 each, which represented approximately one third of the rate psf that he adopted for the main floor space. He adjusted for this in his analysis by making an allowance of 7.5%. Mr Roberts did not make any explicit allowance for the vaults at Flat 3 at 34 EPR although they may be included implicitly in his allowance for "outside space" of 15%.

(e) Floor level

55. Flat 7 and 10 at 52 EPR are on the second and third floors respectively. All the other comparables, including Flat 11, are at lower ground level. Mr Ingram-Hill made an adjustment of 12.5% for the better location of Flat 7 on the second floor. Mr Roberts used a value matrix to calculate the relative value of floor levels in buildings with a lift. He allowed 15% in respect of Flat 10 and 20% in respect of Flat 7.

(f) Outside space/garden

56. Both Mr Ingram-Hill and Mr Roberts adjusted the value of Flat 3 at 34 EPR by 15% for its private rear garden, although it is not clear whether this also included an allowance by Mr Roberts for vaults.

(g) Entrance/access

57. Mr Ingram-Hill made no separate allowance for this factor. Mr Roberts said that the location of Flat 11 at the end of a terrace meant that its access was better than usual for a lower ground floor flat. It had a straight flight of steps to its separate entrance rather than the steep dog-leg steps found at Flats A and B at 74 EPG and at Flat 3 at 34 EPR. He allowed 2.5% for this factor.

(h) Council housing

58. Mr Ingram-Hill allowed 2.5% for the council housing in 74 EPG. Mr Roberts allowed 5%.

(i) Size

59. Mr Ingram-Hill said that smaller studio flats tended to sell for higher rates psf than larger flats. He allowed 7.5% for Flat A at 74 EPG (which was 15.5% larger than Flat 11) and 15% for Flat B (35% larger). But he only allowed 10% for Flat 3 at 34 EPR which is over twice as large as Flat 11. Mr Roberts acknowledged that "studio flats can attract premium rates per sq ft" but he made no specific allowance for this in his analysis.

(j) Other adjustments

60. Mr Ingram-Hill allowed 5% to reflect the potential of Flat 3 at 34 EPR to be converted into a two bedroom flat. Mr Roberts also allowed 5% but this was for the fact that Flat 3 at 34 EPR was larger and better proportioned than Flat 11.

Discussion

61. Of the six comparables relied upon by the valuers, four are lower ground flats, including Flat 11. Flat 3 at 34 EPR can be distinguished from Flat 11 by virtue of its size (at 903 sq ft it is more than twice as large) and its short leasehold interest (21.75 years). It is not a studio flat, but is a one bedroom flat (with potential, says Mr Ingram-Hill, to be converted into a two bedroom flat) occupying the whole of the lower ground floor of 34 EPR and with a conservatory and a south facing garden.

62. The two studio flats at 74 EPG have similar accommodation to the subject property although their kitchen areas form part of the reception rooms. Both studio flats have vaults and 74B has a small utility room. At 506 sq ft (Flat 74A) and 592 sq ft (Flat 74B) the studios are larger than Flat 11 (by 16% and 35% respectively). Both flats had been recently refurbished.

63. The two one-bedroom flats at 52 EPR (Flat 7 on the second floor and Flat 10 on the third floor) are closer in size to Flat 11 (452 sq ft and 430 sq ft respectively). The flats have identical layouts on adjoining floors in the same building and there is no obvious reason why they should have different floor areas. Both flats have a separate bedroom. In each case the kitchen appears to be a partitioned area within the reception room. The lease at Flat 7 had 94 years unexpired and the lease at Flat 10 had 63 years unexpired.

64. The obvious advantage of including the sale of Flat 11 itself is that the only adjustments which are required to obtain the unimproved freehold vacant possession value are adjustments for lease length and condition. Mr Ingram-Hill says that Mr Lagesse overpaid for the property and that the sale price is unreliable evidence as a consequence. But Mr Lagesse did not purchase the property without obtaining professional advice. Mr Ingram-Hill explained to him in some detail in his email correspondence why he thought it was advisable to try to negotiate a reduction to the purchase price. An approach was accordingly made to the vendor's agent but the vendor was not prepared to reduce the price and Mr Lagesse proceeded to purchase at the asking price.

65. We do not accept Mr Ingram-Hill's statement that Mr Lagesse did not act prudently or knowledgably. He had taken and considered professional advice. In our opinion the fact that Mr Lagesse paid the asking price does not make him imprudent. As Mr Roberts pointed out in his sense check some purchasers did pay the asking price or more than the asking price at the valuation date. Indeed we note that Flat 3 at 34 EPR, which sold for £826,105, is shown in the sales particulars with an asking price of £650,000. During cross-examination Mr Ingram-Hill said that "this property was bought by a professional investor, someone who knew what they were doing". There is no suggestion that this investor who, as Mr Ingram-Hill confirmed in answers to the Tribunal, appears to have paid 27% above the asking price, acted imprudently.

66. It was agreed that the existing lease of Flat 11 is subject to an onerous ground rent. In general, one would expect the existence of an onerous ground rent to reduce the value of the lease. Accordingly, in principle, one would expect a valuer using a comparable which involved a lease with an onerous ground rent to adjust for that factor before using the comparable to assess the FHVP. Similarly, when one arrives at the value of the existing lease without rights under the 1993 Act, if the valuer has not already reflected the fact that the existing lease has an onerous ground rent, one would expect the valuer to make an end adjustment to reflect that matter. Indeed, all the valuers in this case agreed that there should be an end adjustment for Flat 11 and, indeed, for Flat 3 and they agreed on the method of making such an adjustment.

67. We are a little concerned that in the case of Flat 11, the sale of which Mr Roberts relies on as a comparable, there was no suggestion by anyone that the price paid by Mr Lagesse should be adjusted to reflect the fact that the

lease was subject to an onerous ground rent. If an adjustment were appropriate on that account when using the comparable for the purpose of assessing the FHVP, any relevant adjustment should have been to increase the resulting value. Mr Roberts did not make such an adjustment. It was not put to him that he should have made such an adjustment. Mr Ingram-Hill did not rely on the sale of Flat 11 as a comparable. In closing submissions, we were not invited to make such an adjustment.

68. We have considered whether we should adjust the price paid for Flat 11 to reflect the onerous ground rent in the lease. In view of the fact that neither Mr Roberts nor Mr Ingram-Hill did so, we do not think that we should. We are encouraged to reach this conclusion by considering the evidence we were given as to the negotiations for the purchase of Flat 11 and as to the advice given to Mr Lagesse in that respect. From the evidence we were given, those negotiations and that advice paid no attention to the fact that the lease contained an onerous ground rent. Accordingly, whatever the valuation logic of an adjustment on this account, it does not seem that the price paid for the lease of Flat 11 was reduced by reason of the onerous ground rent. Nonetheless, the valuers agree that when we later come to assess the value of the existing lease without rights under the 1993 Act and subject to the onerous ground rent we should make an adjustment for that fact. As that matter is agreed, we will give effect to the valuers' agreement. It may be that the fact that Mr Lagesse did not secure a reduction in the price he paid for the lease to reflect the onerous ground rent may show that to some extent he overpaid for the lease.

69. We give weight to all six of the comparables relied upon by the valuers. In our opinion the best evidence, to which we attach the most weight, is the sale of Flat 11 despite Mr Ingram-Hill's reservations. However, we do not rely upon the sale of Flat 11 alone and we will take into account other comparables. We give some, but less, weight to the sales of Flats A and B at 74 EPG; we give equal weight to each of those flats. The sale of Flat 7 at 52 EPR is attributed less weight and the least weight is given to the transactions at Flat 3 at 34 EPR and Flat 10 at 52 EPR.

70. There is a significant difference between the experts about the location of Flat 11 compared with that of the comparables. We accept that the best location is in the mid-terrace section of EPR (Flat 3 at No. 34 and Flats 7 and 10 at No. 52). In our opinion an allowance of 15% is appropriate to reflect all the locational disadvantages of EPG compared to EPR, including the presence of council housing in 74 EPG.

71. Mr Roberts accepted that the location of Flat 11 is not as quiet as that of the other comparables in EPR. We think he was right to make this concession and we allow 5% for this difference.

72. Neither party relied upon Savills Prime Central London Index which is often used to adjust comparables for time. We therefore use the John D Wood Chelsea Flats Index to adjust transactions prior to the valuation date. There is no index available beyond March 2014 and we adopt Mr Ingram-

Hill's approach for the reasons he gave of not indexing values after the valuation date.

73. We adjust for lease length using Savills 2002 enfranchisable relativity graph which was the method adopted by both experts.

74. We allow 5% for Flats A and B at 74 EPG having been recently refurbished. We make no adjustment to the value of Flat 7 at 52 EPR for its "dated" condition. Mr Ingram-Hill estimated the cost of improvements to Flat 11 at £40,000 while Mr Roberts took £50,000. We adopt £45,000 (£103 psf) in the absence of any evidence in favour of either of the experts on this matter.

75. We allow for the vaults at Flats A and B at 74 EPG and Flat 3 at 34 EPR by taking their value at 25% of the main floor space rate. We allow a separate 15% in respect of the private garden of Flat 3 at No. 34. We prefer Mr Roberts' adjustments for floor level which we consider to be reasonable and logically based. We therefore adjust by 20% in respect of Flat 7 at 52 EPR and by 15% for Flat 10.

76. We do not consider that the entrance to Flat 11 is materially better than those to the other lower ground floor flats and we make no allowance for this factor.

77. We accept that small studio flats are likely to command a premium rate psf. In our opinion this is unlikely to exceed 10% and we adjust the rates of the three comparable lower ground floor flats as follows:

Flat A at 74 EPG: 5%

Flat B at 74 EPG: 7.5%

Flat 3 at 34 EPR: 10%

78. Finally we make a single adjustment of 5% from the value of Flat 3 at 34 EPR to allow for any development potential it may have and to reflect its better layout compared with Flat 11.

Conclusions

79. Applying the various adjustments which we have explained above and taking a weighted average of the resultant rates psf gives a figure of £1,327 psf (the arithmetic average is £1,316 psf). Applying this rate to the area of Flat 11 of 438 sq ft gives an unimproved FHVP value for Flat 11 of £581,226 which we round to £581,000.

80. We have explained that we have used the actual sale of the existing lease to Mr Lagesse as one of the comparables, but not the only comparable, for the purpose of arriving at the FHVP of Flat 11. Our conclusion in relation to the FHVP for Flat 11 does indeed suggest that Mr Lagesse overpaid to

some extent for the lease of that flat. However, as we have explained, that did not persuade us to reject the sale price as a comparable. That sale price has not been adjusted upwards, for the purpose of assessing FHVP, to reflect the onerous ground rent. Further, the fact that we have taken the sale price for Flat 11 as one of a basket of comparables has allowed those other comparables to control the influence which the sale price of Flat 11 has had on the FHVP we have arrived at for that flat.

The freehold value of Flat 3

Evidence

81. For the tenant Mr Wyatt estimated the unimproved FHVP of Flat 3 to be £876,000 (£1,460 psf), while for the landlord Mr Roberts estimated the value to be £950,000 (£1,583 psf).

82. Mr Wyatt relied on five comparable sales:

(i) Flat 7 at 52 EPR, a one bedroom flat on the second floor (with a lift).

(ii) Flat 10 at 52 EPR, a one bedroom flat on the third floor (with a lift).

(iii) Flat 9 at 4 EPG, a one bedroom third floor walk-up.

(iv) Flat 7 at 44 EPG, a two bedroom third floor walk-up.

(v) Flat 23 at 93 EPG, a one bedroom first floor flat (with a lift).

83. Mr Roberts considered all of these comparables but only relied upon the sale of Flat 9 at Flat at 4 EPG. He also relied upon another comparable which Mr Wyatt had not considered, the sale of Flat 9 at 118-120 Beaufort Street, a split level two bedroom walk-up on second and third floors.

84. In addition to the direct evidence of his comparables, Mr Roberts referred to settlement evidence which he said showed a rising tone of value that was strongest from the latter part of 2013 to the beginning of 2014. He also undertook a sense check valuation by considering flat sales in the area that were within plus or minus £25,000 of his FHVP valuation of £950,000 and which took place within two months of the valuation date (March 2014). Mr Roberts identified four such sales and concluded that Flat 3 was similar to or better than all of them and that his valuation was therefore well-founded.

85. Mr Roberts rejected both the comparables at 52 EPR as being outliers: No.7 because it was smaller than Flat 3 (452 sq ft compared with 600 sq ft) and No.10 because it produced a rate per sq ft that was considerably higher than that of any other comparable. He rejected Flat 23 at 93 EPG because it was located in a 1960s block of council flats and was of a very different appearance to Flat 3.

86. Mr Roberts did not generally adjust his comparables for time since he was not satisfied that the Savills Prime Central London Capital Value Index accurately reflected the change in values over the relevant period. The exception was Flat 7 at 44 EPG where Mr Roberts used the Savills Central London Flats Index to adjust for time, presumably because this sale was earlier than that of the other comparables (May 2013). Since his two preferred comparables were sold on either side of the valuation date Mr Roberts felt there would be a balanced overall analysis of value. Mr Wyatt adjusted for time using the John D Wood & Co Chelsea Flats Index. This index stopped being maintained in March 2014 so Mr Wyatt consulted three local agents about price movements thereafter and was told that values strengthened until May/June 2014. Mr Wyatt therefore made subjective adjustments to the index after March 2014, increasing it slightly before reducing it again in July 2014.

87. Mr Roberts adjusted for lease length using the Savills 2002 enfranchisable graph. In his original report Mr Wyatt adjusted all his comparables by reference to "Parthenia Research relativity" and then made an adjustment for Act rights. In his supplemental report in November 2015 Mr Wyatt altered his approach to the adjustment for lease length of Flat 10 at 52 EPR. The agents involved in the sale told him that they had used the John D Wood & Co Pure Tribunal Decisions Graph 2011 to set prices for short leases. He therefore adjusted this comparable for lease length using that graph, making a subjective adjustment of "about 2%" for Act rights.

88. The valuers made other adjustments for:

(a) *Location*

Both valuers allowed 20% for the difference in location between Elm Park Gardens and Elm Park Road. Mr Roberts allowed 10% for the location of Flat 9 at 118-120 Beaufort Road on a busy main road. He also allowed 5% for the flats at 52 EPR being in a marginally worse location than Flat 3, since they were close to the junction with The Vale and had a worse outlook.

(b) *Condition*

Flat 7 at 44 EPG was said by both valuers to be in better condition than Flat 3. Mr Wyatt allowed 15% and Mr Roberts £200 psf (approximately 10%). Mr Roberts also allowed £200 psf (11%) for the better comparative condition of Flat 9 at 118-120 Beaufort Road.

(c) *Floor Level*

Mr Wyatt allowed 15% for a lift for flats on the second or third floor. He made no allowance for a lift for the first floor Flat 23 at 93 EPG. Mr Roberts adjusted for a lift by reference to the value matrix that he used to value Flat 11, taking 15% and 10% respectively for Flats 7 and 10 at 52 EPR and 25% for Flat 23 at 93 EPG.

(d) *Outside Space*

Flat 9 at 4 EPG and Flat 23 at 93 EPG both had the use of a communal garden for which Mr Wyatt allowed 5%. Mr Roberts attributed no value to this facility. Flat 9 at 118-120 Beaufort Street had a patio with access from the reception room for which Mr Roberts allowed 10%.

(e) *Council housing*

Mr Wyatt made no explicit allowance for the council housing in Elm Park Gardens. Mr Roberts allowed 5%. In addition Mr Roberts allowed 20% for what he described as the architectural style of Flat 23 at 93 EPG, a purpose-built 1960s council block.

(f) *Layout*

Mr Roberts made a number of adjustments for the differences in layout of the comparables. He considered that Flats 7 and 10 at 52 EPR were disadvantaged by having the kitchen within the reception area, a single aspect and relatively more dead space. He allowed 10% for these factors. He made an adjustment of 5% for Flat 9 at 4 EPG because it could not be configured as a two bedroom unit. He also allowed 5% on Flat 7 at 44 EPG for the second bedroom being accessed directly from the reception room. Mr Wyatt made no separate adjustments for layout.

Discussion

89. We consider that five of the six comparables referred to should be given weight. The exception is Flat 23 at 93 EPG. Unlike the other comparables it is not located in a period building but is part of a purpose-built 1960s council block. It is the only comparable that is on the first, rather than on the second or third, floor. The purchase price has not been verified by reference to the Land Registry. It attracted the valuers' largest adjustment; Mr Wyatt allows combined adjustments of 35% while Mr Roberts makes total adjustments of 70% (albeit the net effect is only 20%). The scale of such adjustments suggests that it is not a reliable comparable.

90. We do not accept that Flat 10 at 52 EPR should be excluded as an outlier. Mr Wyatt included it, as did Mr Roberts when he was valuing the less comparable (except by size) property at Flat 11. It is the only comparable third floor walk-up flat in Elm Park Road and we consider that it should be given weight.

91. We give most weight to the comparables at Flat 9 at 4 EPG and Flat 7 at 44 EPG, both of which are third floor walk-ups. We give equal (but less) weight to the remaining comparables at Flats 7 and 10 at 52 EPR and Flat 9 at 118-120 Beaufort Street. We do not share Mr Roberts' view that the Beaufort Street flat is one of the best two comparables. It is an atypical

split level refurbished flat on a busy main road close to the service road to the rear of the shops in Fulham Road.

92. We make time adjustments for the three transactions which preceded the valuation date using the John D Wood & Co Chelsea Flats Index. We make no adjustment for the two sales after that date since we have no objective evidence upon which to do so and given that the market seems to have stabilised by the early summer of 2014. We do not accept Mr Wyatt's subjective estimates of what that index might have been in May and July 2014 had it continued in existence. Nor do we consider it appropriate to adjust just one of the comparables for time using the Savills Prime Central London Index for flats as Mr Roberts has done in respect of Flat 7 at 44 EPG.

93. We do not find Mr Wyatt's adjustments for lease length to be helpful. He relies upon without Act rights relativities for the most part derived from the Parthenia model. The exception is his analysis of Flat 10 at 52 EPR where he relies instead upon the without Act rights relativity found in John D Wood & Co's Pure Tribunal Decisions Graph 2011. Mr Wyatt does not provide details of these relativities and he adjusts them subjectively for the benefit of the Act. Under cross-examination he said that the adjustment that he had made for Act rights at Flat 10 at 52 EPR was "about 2 percent" but otherwise he provides no information about the adjustments which seem to us to be arbitrary and unexplained other than by a vague reference to an unspecified academic paper that was not included in the trial bundle. We prefer Mr Roberts' use of the Savills 2002 enfranchisable graph which, as Mr Wyatt acknowledged, is the method generally used in the market for adjusting for lease length.

94. We do not accept the valuers' adjustment of 20% for the difference between properties in EPG and EPR. We adopt a figure of 15%, including an allowance for the presence of council housing in EPG, as we did in respect of the valuation of Flat 11. The exception is Flat 9 at 4 EPG where we think that an allowance of 20% is justified because of the additional disadvantage of its proximity to the service road behind the Fulham Road shops. We consider that Mr Roberts' adjustment of 10% for the location of Flat 9 at 118-120 Beaufort Road does not adequately take into account its busy main road position close to the Fulham Road. We allow 15%. We do not accept Mr Roberts' 5% adjustment for a difference in location between Flat 3 and the flats at 52 EPR. The proximity of the latter to The Vale is not, in our opinion, value significant. Mr Roberts' other reason for the adjustment is that Flat 3 has a better view from its northern aspect. In our opinion Mr Roberts' allowance for layout already takes into account any such difference between the properties.

95. We adopt 10% to allow for the better condition of Flat 7 at 44 EPG and Flat 9 at 118-120 Beaufort Street.

96. We think Mr Roberts is correct to distinguish between the benefits of a lift to Flat 7 (second floor) and Flat 10 (third floor) at 52 EPG and we accept his allowance of 15% and 10% respectively.

97. The patio at Flat 9 at 118-120 Beaufort Street adds value and we accept Mr Roberts' adjustment of 10%. We consider that the access to the communal gardens of Flat 9 at 4 EPG is not likely to add significant value to this third floor flat but it is a benefit for which we allow 2.5%.

98. We have allowed for the presence of council housing in EPG in our adjustment of 15% for location.

99. We agree with Mr Roberts that the single aspect of Flats 7 and 10 at 52 EPR and a kitchen which is within the reception area are disadvantages by comparison with Flat 3. But we do not accept that there is a material difference in terms of the proportion of dead space. We allow 5% for the difference in layout. We think there is a marginal advantage in the layout of Flat 3 compared with that of Flat 9 at 4 EPG given the realised possibility in the former of creating two bedrooms and we allow 2.5%. We accept Mr Roberts' adjustment of 5% for the disadvantage at Flat 7 at 44 EPG of the second bedroom having direct access from the reception room.

Conclusions

100. Applying the adjustments that we have described above and taking a weighted average of the resultant rates gives a figure of £1,621 psf (which is also the arithmetic average). Mr Roberts adopts £1,614 psf (the average of his two preferred comparables). Mr Roberts' analysis of the five comparables we favour gives an average value of £1,681 psf. Mr Roberts calculates the FHVP value of Flat 3 as £968,400 (using £1,614 psf) which he then rounds down to £950,000. In our opinion that value is well supported by the comparable evidence and we accept it.

The value of the existing leases with rights under the 1993 Act

101. The statutory provisions in paragraphs 2 to 5 of schedule 13 to the 1993 Act do not refer to the value of the existing lease on the basis of the real circumstance that it has rights under the 1993 Act. Nonetheless, we will now consider the position as to the value of such leases on that basis and then consider whether what emerges in that respect is capable of being helpful in determining the value of the existing leases on the statutory assumption that they do not have rights under the 1993 Act.

102. The parties in relation to Flat 5 have agreed that the value of the existing lease with rights under the 1993 Act at the valuation date of 25 February 2014 was £2,000,000. This agreement is based upon a sale of the existing lease of Flat 5 in the open market which took place on 3 March 2014 for the price of £2,000,000. Although this value has been agreed, it is nonetheless appropriate to record the facts in relation to the sale of the flat shortly after the valuation date.

103. Flat 5 was originally placed on the market in or around June 2013 at an asking price of £2,250,000. The flat was withdrawn from the market in August 2013. The flat was marketed by two agents who gave different information as to the level of interest in the flat. One of the two agents reported that the vendors had received three offers, between £1,950,000 and £1,999,999. Later, the flat was marketed by John D Wood at a guide price of £1,995,000. The vendors received a number of offers and a sale was agreed with the purchaser, Ms Aaron, at the price of £2,000,000. On 25 February 2014, the vendor served on the lessor a notice under section 42 of the 1993 Act seeking an extended lease and the benefit of that notice was assigned to Ms Aaron on completion on 3 March 2014.

104. Mr Wyatt was a partner at John D Wood at the time of the sale of Flat 5. He produced correspondence between the vendors and their agents, John D Wood, as to the likely amount of the premium payable for an extension to the lease of Flat 5 in accordance with the 1993 Act. On 11 October 2013, John D Wood wrote to the vendors offering a service whereby John D Wood would assess the likely amount of the premium payable under the 1993 Act and make that information available to potential purchasers. The vendors agreed that John D Wood could act in that way. On 16 October 2013, John D Wood prepared a letter of advice addressed "To Whom It May Concern" stating their opinion that the premium for an extended lease under the 1993 Act might be between £540,000 and £600,000. Mr Wyatt gave evidence that this letter of advice was provided to Ms Aaron.

105. Having noted this specific evidence about the sale of Flat 5, we make the further comment at this point that there was agreement between the valuers that short or medium term leases which have the benefit of the 1993 Act are sold at a price which reflects the value of an extended lease less the estimated cost of the extension. It may be that the price agreed in the market is not simply the mathematical result of deducting the estimated cost from the estimated value of the extended lease but the estimated price of the extension certainly influences to a significant extent the price agreed for the short or medium term lease. It was also agreed that, for this purpose, in the market the estimated price for the extension is based upon a graph of relativities for leases without rights under the Act and, in particular, a graph which we will later describe and which is usually known as the Gerald Eve graph.

106. The parties in relation to Flat 11 have not agreed the value of the existing lease of Flat 11 with rights under the 1993 Act. We have held that the FHVP value of Flat 11, unimproved, was £581,000. We have also noted that when the valuers adjusted various comparables to reflect the length of the leases of those comparables, they used the Savills 2002 enfranchisable graph to arrive at the FHVP. We consider that it would be potentially helpful to carry out that exercise in reverse to see what figure would be produced for the value of the existing lease with rights under the 1993 Act. Doing that exercise in relation to Flat 11, one arrives at a value for the existing lease, unimproved, with rights under the 1993 Act, and before

adjustment for an onerous ground rent, of £428,371. Later in this Decision, we will comment on the use that might be made of this figure.

107. The parties in relation to Flat 3 have not agreed the value of the existing lease of Flat 3 with rights under the 1993 Act. There was no transaction in relation to Flat 3 at or near the valuation date of 20 March 2014. We have held that the FHVP of Flat 3 was £950,000. If we carry out the same exercise for Flat 3 as we have carried out in the last paragraph in relation to Flat 11, the resulting figure for the existing lease, with rights under the 1993 Act, and before adjustment for an onerous ground rent, is £584,250. Later in this Decision, we will comment on the use that might be made of this figure.

The value of the existing leases without rights under the 1993 Act

108. As explained earlier, the parties in each case are far apart on the value of the existing leases without rights under the 1993 Act. In the case of Flat 5, the sole reason for the difference between them is the difference as to the relativity to be applied to a lease for an unexpired term of 41.32 years. In the case of Flats 3 and 11, the differences were for two reasons; the first reason was the difference as to the relativity to be applied to a lease for an unexpired term of 23 years (Flat 3) and to an unexpired term of 37.71 years (Flat 11); the second reason was the dispute as to the FHVP values of Flats 3 and 11. We have now determined the dispute as to the FHVP values of Flats 3 and 11 so that the remaining issue, which applies to all three flats, is as to the appropriate relativity in relation to the unexpired term in each case.

109. We will begin our discussion of this subject by considering the position in relation to Flat 5. In respect of that flat, the lessor's valuer, Mr Fielding, arrived at the value of the existing lease without rights under the 1993 Act by using a principal method of valuation supported by a number of cross-checks. The principal method of valuation began with the agreed value of the existing lease with rights under the 1993 Act (£2,000,000) and estimated the amount of the deduction (which he considered should be 10%) to reflect the assumption that the existing lease did not have rights under the 1993 Act. In that way the lessor's valuer arrived at a value of £1,800,000.

110. In the case of Flat 5, the lessee's valuer, Mr Wyatt, did not start with the value of the existing lease with rights under the 1993 Act. Instead, he started with the agreed value of the freehold of the flat (£2,750,000). He then took a relativity percentage from the curve generated by the Parthenia model (81.18%) and applied that percentage to the agreed freehold value. The resulting value is £2,232,450.

111. The value of £2,232,450 for the existing lease without rights under the 1993 Act immediately prompts the question: how is that value compatible with the agreed market value of £2,000,000 for the existing lease with rights under the 1993 Act? All the parties in these cases agreed that the rights

under the Act were valuable. Similarly, they all agreed that the value of an existing lease with rights under the Act would be higher than the value of the same lease without rights under the Act, although there was disagreement as to the amount to be deducted from the higher value to arrive at the lower value.

112. In the course of his opening, we asked Mr Rainey to explain his case that the value of the existing lease without rights under the Act was £2,232,450 when the existing lease (with rights under the Act) had been sold for £2,000,000 at around the valuation date. Mr Rainey responded that the sale price of £2,000,000 was, or might be, "an outlier" and for that reason was not a guide to the value of the existing lease without rights under the Act. However, this suggested explanation was contradicted by the lessee's valuer in relation to Flat 5, Mr Wyatt, who fully accepted that the value of the existing lease of Flat 5 with rights under the Act at the valuation date was £2,000,000. Notwithstanding this evidence, Mr Rainey in his closing submissions still invited us to find that the market value of the existing lease with rights under the Act was £2,000,000 and the market value of the existing lease without rights under the Act, at the same valuation date, was £2,232,450.

113. Mr Rainey contended that we would be helped to reach that conclusion by considering the decisions of the Lands Tribunal and of the Court of Appeal in Earl Cadogan v Sportelli [2007] 1 EGLR 153 (LT) and [2008] 1 WLR 2142 (CA) ("Sportelli"). Indeed, Mr Rainey submitted that when we came to consider the evidence as to the value of the existing lease without rights under the Act we should disregard the fact that the existing lease with rights under the Act had sold in the open market for £2,000,000. Mr Rainey appeared to submit that the decision in Sportelli required us, as a matter of law, to disregard that fact.

114. Mr Rainey drew our attention to the parts of the lengthy decision of the Lands Tribunal in Sportelli where the Lands Tribunal considered what conclusions to reach in relation to evidence as to market transactions concerning sales of reversions, subject to leases which had the benefit of rights under the Act, in a case where the Lands Tribunal was seeking to establish the value of reversions subject to leases which did not have the benefit of rights under the Act. In very broad terms, this comparison could be described as being between reversions incumbered by rights under the Act and reversions not so incumbered. If that were the right comparison, it would seem that the reversions which were so incumbered should be worth less than reversions that were not so incumbered.

115. However, Mr Rainey explained the approach of the Lands Tribunal in more detail. He pointed out that the Lands Tribunal in Sportelli wished to value separately two attributes of the reversion. The first attribute was the right to receive the ground rent for the unexpired term. The second attribute was the present value of the reversion falling into possession at the end of the term. This second attribute was therefore being considered as if it were a separate asset which was not income producing until the end of the term and then

had a value. More relevantly, the Lands Tribunal had directed itself that it should leave out of account the value of the hope that the reversioner could grant an extended lease in return for a premium before the term date. This was to be contrasted with the position of a sale of a reversion in the open market in the real world, where the reversioner would have the hope of receiving a premium before the term date, particularly where the reversion was subject to a lease which had the benefit of the Act giving the lessee the right to an extended lease. The argument before the Lands Tribunal was that the value of a reversion unincumbered by the Act but without the benefit of hope value should have been less than the value of the same reversion incumbered by the Act and with the benefit of hope value. We understand the argument as put. That was an argument which it was for the Lands Tribunal in that case to consider. In the result, the Lands Tribunal reached the conclusion that the value of the reversion unincumbered by the Act (even without hope value) was worth more than the value of the reversion incumbered by the Act (even including hope value). At paragraph [78] of its decision, it said that the yield for the unincumbered reversion would be expected to be lower than for the incumbered reversion, i.e. the price for the unincumbered reversion would be higher. When the argument as to the market evidence was considered by the Court of Appeal in Sportelli, it was held that the Lands Tribunal assessment of the evidence and its conclusion did not disclose any error of law and, in particular, was not irrational.

116. Mr Rainey also drew our attention to a different paragraph, [64], where the Lands Tribunal indicated that it did not find the evidence of market transactions of help in relation to the decision as to the appropriate deferment rate in what it called the "no-Act world" and it stated:

> "The market in the real world is substantially different from the one to be envisaged in the hypothetical no-Act world."

117. We do not consider that the Lands Tribunal in the Sportelli case was laying down a proposition of law which binds us to reach any particular conclusion in the present cases. It is of course important to reflect the fact that there is a difference between the assets which are sold in the open market in the real world and the hypothetical asset. We do not consider that the Lands Tribunal in Sportelli was saying more than that. We do not think that the Lands Tribunal was intending to rule that there was a "no-Act world" in which no lease had rights under the Act and no reversion was incumbered by such rights. The sentence we have quoted does use the phrase "no-Act world" but that usage appears to have been a fairly common practice in the past and did not mean that the market was concerned with assets where no lease had rights under the Act and no reversion was incumbered by such rights. If, contrary to our view, the Lands Tribunal was going further, we do not agree with its comment. Indeed, we did not understand Mr Rainey to submit that we had to assume a world and a market in which no leases had rights under the Act.

118. We conclude that Sportelli does not lay down any proposition of law which binds us in these cases. Further, we do not think that Sportelli contains any persuasive reasoning which guides us in deciding the issues which we have to decide.

119. Mr Rainey made a number of further submissions with which it is convenient to deal at this point. He referred to comments in IRC v Clay [1914] 3 KB 466 at 475 and 478 to the effect that the market value of an asset will not in every case be identical to a price actually paid for an asset; there may be reasons why the price is above or below the market value. We do not see how that comment applies in the case of Flat 5. The valuers have agreed that the price of £2,000,000 paid for the existing lease of Flat 5, with the benefit of rights under the Act, did equate to the market value of that asset.

120. Mr Rainey also analysed the decision of the Privy Council in Raja Vyricherla Narayana Gajapatiraju v The Revenue Divisional Officer, Vizagapatam (often referred to as "The Indian Case") [1939] AC 302. His point seemed to be that where an asset has a value to one group of buyers and a higher value to another group of buyers, an identification of the likely lower value does not help one very much when one is seeking to determine the higher market value. He submitted that the present case was the converse of The Indian Case where a lease with rights under the Act would be likely to have a value different from a lease without rights under the Act. However, we do not think that The Indian Case is of any real help in the present case. The market value of the different asset, the existing lease with rights under the Act, is clear and has been agreed. It is also clear that the existing lease without rights under the Act is a less valuable interest and would not command a value higher than the value of the existing lease with rights under the Act. In that way, the value of the existing lease with rights under the Act provides a ceiling for the value of the existing lease without rights under the Act. There is no reason why the identification of the ceiling should be considered to be irrelevant or otherwise unhelpful when seeking to determine the value of the existing lease without rights under the Act.

121. We return therefore to the question we posed earlier: is it possible to find that the market value of the existing lease of Flat 5 with rights under the Act at the valuation date was £2,000,000 and the market value of the existing lease of Flat 5 without rights under the Act at the same date was £2,232,450? We do not think that it is. If, as has been agreed, the market value of the existing lease of Flat 5 with rights under the Act at the valuation date was £2,000,000 then the market value of the existing lease of Flat 5 without rights under the Act at the same date cannot be greater than £2,000,000. Indeed, it was agreed that the value of a lease without rights under the Act would be less than the value of the same lease with rights under the Act.

The implications for the Parthenia model

122. The figure of £2,232,450 was arrived at by using the curve generated by the Parthenia model. The result produced is impossible. As it was put in the course of argument, the Parthenia model is a clock which strikes 13. It cannot be used as a reliable time piece and we do not consider that we have any alternative to rejecting the use of the Parthenia model. No one suggested that the Parthenia model could be used in a modified form to produce an answer for the existing lease of Flat 5 which was below £2,000,000. No one came up with any suggestion as to how we could repair the broken model in order to make it work. If the Parthenia model is broken and does not work in the case of Flat 5, it seems to us that it cannot be used in any other case to determine the value of an existing lease without rights under the Act. Even if the application of the model produced an answer in another case which was not impossible, that does not mean that the model has been shown to be reliable. If a clock strikes 13, it is broken. It is not a reliable time piece. It cannot be relied upon as a reliable means of telling the time even when it strikes an hour, such as 11 or 12, which are possible times of day.

123. We reach this conclusion as to the Parthenia model without considering the many and elaborate arguments as to the defects which the lessors alleged existed in the Parthenia model. We also do not need to consider whether if the Parthenia model had correctly interpreted market practice in the period 1987 to 1991, that interpretation could be applied without adjustment to the market for leases in central London in 2014. However, as these points were very fully argued, we will record our reaction to them. Because further consideration of the Parthenia model does not help us to decide the cases before us and to avoid obscuring the valuation methods which we prefer for that purpose, we will set out our further findings as to the Parthenia model in Appendix B to this decision.

124. We make one further comment about the Parthenia model. In this case, we are asked to determine how the market would have performed if the existing leases of these three flats had been available in the market on the valuation date relevant to each lease, all three dates being in the period from February to April 2014. Mr Wyatt was asked whether the Parthenia model had influenced the price paid in any market transaction in that period. He told us that the Parthenia model had not influenced the price paid in any market transaction in that period. We conclude that the Parthenia model would not have influenced in any way the market value of the three leases with which we are concerned, if they had been available in the market on the relevant valuation dates. Later in his evidence, Mr Wyatt explained that he was using the Parthenia model to arrive at a "fair and appropriate amount" to pay for the existing leases without rights under the Act. He agreed that "a fair and appropriate amount" was different from the market value of the existing leases without rights under the Act. Instead of doing what Mr Wyatt set out to do, we are required to apply the statutory hypothesis in schedule 13 to the 1993 Act and we are required to arrive at

the market value of the existing leases on the assumptions directed by the 1993 Act.

125. Having rejected the Parthenia model, we now need to consider other possible methods of valuing the existing leases on the assumption that they do not have rights under the Act. We will carry out this exercise separately in relation to the three leases.

The value of the existing lease of Flat 5 without rights under the Act

126. In the case of Flat 5, the lessor's valuer began by assessing the amount of the deduction to be applied to the higher value of £2,000,000 for the existing lease with rights under the Act. We will therefore begin by considering this question. For this purpose, we wish to consider, first, the extent and character of the rights conferred on a lessee by the 1993 Act. We then wish to consider the evidence before us as to the appropriate scale of deduction to be made.

127. In his opening submissions, Mr Jourdan for the lessor of Flat 5 described the benefit of rights under the Act in this way:

> "Act rights are valuable, for a number of reasons. The tenant has the right, at a time of his choosing, to serve a notice claiming a new lease. He can buy the lease of the flat he wants paying, in effect, only part of the price immediately, with a further payment due at a time of his choosing. The price is fixed on a basis which excludes the tenant's overbid whilst guaranteeing him 50% of the marriage value. He has the right to have the price determined by an independent tribunal, and is not at risk as to costs (unless he acts unreasonably). If the claim proceeds, it can take a considerable time before the price is paid, during which period he pays no interest but only the ground rent. If property prices go up, he keeps the increase in the price after the valuation date. If prices go down, he can withdraw the notice and serve another one a year later. The price is determined on a basis which disregards any effect of improvements, so meaning that he can make improvements which might not be economic if he held only an unenfranchiseable lease."

128. We did not understand Mr Rainey to disagree with this description of rights under the Act. We agree that the Act confers these substantial benefits on lessees who qualify under it.

129. We next consider the evidence before us which, it was suggested, could assist us to assess the amount of the appropriate deduction in the case of Flat 5. This evidence related to:

(1) 18 Gerald Road;

(2) 58 Hamilton Terrace;

(3) sales of very short leases;

(4) Mr Ryan's "rule of thumb";

(5) other decisions

130. 18 Gerald Road was a leasehold house where the lease did not have the benefit of the Leasehold Reform Act 1967 as it had been contracted out of the 1967 Act, pursuant to sections 23(4) and (5) of that Act. It was originally marketed on the basis that the lease did have the benefit of the 1967 Act and the vendors agreed that they would serve notice to enfranchise and assign the benefit of the notice to the assignee of the lease. On this basis, the house was marketed at a guide price of £1,950,000, a number of bids were received and a sale was agreed at a substantially higher figure of £2,550,000. Prior to exchange of contracts at that price, it was discovered that the lease did not have the benefit of the 1967 Act. The buyer then withdrew and the house was re-marketed on the basis that the lease did not have the benefit of the 1967 Act. Again, a number of bids were made and the property was sold for £2,205,000. This price was some 13.5% below the price originally agreed. The sale took place in 2007. We were not told the amount of time which passed between the acceptance of the first bid of £2,550,000 and the acceptance of the later bid of £2,205,000. We were told that the market was rising steeply at around the time of this sale. If there had been an appreciable gap between the two agreed bids, then there might have been scope for contending that the discount to reflect the absence of rights under the 1967 Act might have been greater than 13.5%. We were told that the unexpired term of the lease of this property was 43.75 years and we take it this figure is accurate at the time of the sale of the lease without the benefit of the 1967 Act.

131. The facts as to 58 Hamilton Terrace were taken from the decision of the Lands Tribunal (Mr Rose) in Trustees of the Eyre Estate v Saphir [1999] 2 EGLR 123 where it was stated:

> "When discussing the additional value attributable to the right to enfranchise, Mr Briant referred to the history of 58 Hamilton Terrace, where a lease with approximately 53 years unexpired was sold twice in 1995. The first sale was on 31 January 1995, notice having been served 12 days previously. The price achieved was £1.408m. The landlord successfully disputed the validity of the notice, one reason being that the rent payable exceeded the statutory limit. The purchaser resold the property on 17 November 1995 for £1.31m. Prima facie these transactions indicated a difference of approximately 7% between a property with the expectation of a valid notice and one without the right to enfranchise. However, this fall in value took place over a period of nine months, at a time when the evidence shows that confidence was returning to the residential

> property market in St John's Wood. Moreover, the unexpired lease term of 58 Hamilton Terrace was some 40% longer than that of the subject property. It is to be expected that a right to enfranchise will become more attractive as the unexpired term diminishes in length."

132. Mr Fielding supplemented this statement of the facts as to 58 Hamilton Terrace by considering the point made by the Lands Tribunal in Saphir as to the possibility that the market was rising over the period in 1995 which was relevant in that case. He calculated that if one were to increase the earlier sale price of £1.408 million to reflect movement in the market between January and November 1995, using Savills Prime North Houses Index, the increased price would be £1,479,706 so that the later sale price of £1.31 million showed a deduction for rights under the 1967 Act of 11.5%. Mr Fielding also drew attention to the length of lease in that case (53 years) and he stated that the deduction for the absence of rights under the Act would be greater in the case of Flat 5 where the unexpired term was 37.7 years.

133. Mr Fielding introduced evidence of sales of leases of flats with very short unexpired terms of the order of two years or less. Based on this evidence, Mr Fielding stated that, in those cases, very substantial percentages of the purchase price must have been paid for the benefit of the rights under the Act. This evidence is of less direct help to us in relation to the deduction to be made for Act rights in the three cases before us because the unexpired terms in those cases are not comparable to the leases the subject of this evidence. We do accept however that the percentage of the value of a lease with rights under the Act, which is referable to those rights, is liable to increase as the unexpired term gets shorter.

134. The lessor of Flat 5 also relied on certain evidence given by Mr Ryan FRICS, a partner in Carter Jonas. Mr Ryan was called as a witness of fact and not as an expert witness. He had considerable experience as an agent in the residential market in Central London. He referred to a "rule of thumb" which he used to identify the percentage deduction to be made to reflect the absence of rights under the Act. Mr Ryan's percentages varied with the length of the lease in question and varied again by reference to whether a notice to enfranchise had already been served before completion of the purchase. Mr Ryan said that he did not have any evidence to support the accuracy of his rule of thumb although as time went by he noted that his rule of thumb produced results which were close to the position shown on the Gerald Eve graph. We do not consider that we can give much weight to Mr Ryan's evidence for the purpose of assessing the appropriate deduction to make for the absence of rights under the Act. He was not called to give opinion evidence and he volunteered the fact that he did not consider that his rule of thumb was supported by empirical evidence. Further, it was not said that his rule of thumb was accepted more widely in the market as the approach to be adopted. We also note that the Upper Tribunal in 82 Portland Place (Freehold) Ltd v Howard de Walden Estates Ltd [2014] UKUT 0133 (LC) (Mr Rodger QC, Deputy President, and Mr Trott), a case

in which Mr Ryan gave expert evidence, did not feel able to adopt Mr Ryan's approach in this respect: see at [143].

135. We were referred to a number of tribunal decisions on the subject of the amount of the deduction to be made to reflect the absence of rights under the Act. In Trustees of the Eyre Estate v Saphir [1999] 2 EGLR 123, the Lands Tribunal (Mr Rose) accepted a valuer's evidence that the deduction should be 10% where the unexpired term was 37.7 years. In Chelsea Properties Ltd v Earl Cadogan LRA/69/2006, decision dated 16 August 2007, the Lands Tribunal (Judge Huskinson and Mr Rose) accepted a valuer's evidence that the deduction should be 15% where the unexpired term was 18.7 years. In Lalvani v Earl Cadogan, reported with other cases as Nailrile Ltd v Earl Cadogan [2009] RVR 95, the Lands Tribunal (Mr Bartlett QC, President, and Mr Trott) accepted a valuer's evidence that the deduction should be 7.5% where the unexpired term was 44 years. In Earl Cadogan v Cadogan Square Ltd [2011] 3 EGLR 127, the Lands Tribunal (Judge Reid QC and Mr Trott) held that the deduction should be 25% where the unexpired term was 17.8 years. In this last case, the Lands Tribunal carried out at [79] a comparison between the real world relativity, as shown by the Savills 2002 graph, and the relativity for leases without rights under the Act, as shown by the Gerald Eve graph, and pointed out that if the graphs could be relied upon then the difference between the relativities should disclose the appropriate deduction for the absence of rights under the Act for a lease of any particular length. If one were to do that exercise for an unexpired term of 40 years (a figure which is provided in [79] of the decision in that case and which is only a little less than the unexpired term of 41.32 years in the case of Flat 5) the deduction for the absence of rights under the Act would be 12.2%. We will have more to say about the use of the various graphs later in our decision.

136. The four decisions of the Lands Tribunal referred to in 135 above were all before the valuation date in the case of Flat 5. Following that date, the Upper Tribunal has decided 82 Portland Place (Freehold) Ltd v Howard de Walden Estates Ltd [2014] UKUT 0133 (LC) (Mr Rodger QC, Deputy President, and Mr Trott) where it determined a deduction of 20% for an unexpired term of 11.82 years.

137. We heard evidence from only one valuer as to the deduction to be made for the absence of rights under the Act in the case of Flat 5. Mr Fielding ultimately put forward the opinion that the appropriate deduction was 10%, producing a figure of £1,800,000. Mr Wyatt was the other valuer called to give evidence in relation to Flat 5 but he did not attempt to assess the appropriate deduction to reflect the absence of rights under the Act. Instead, Mr Wyatt exclusively used the Parthenia model and expressed the impossible opinion that the value of the existing lease without rights under the Act was £2,232,450. For the sake of completeness, we mention that Mr Wyatt put forward a graph prepared by the College of Estate Management (to which we refer in more detail in Appenix C to this decision) as a suggested fallback if the Parthenia model were not accepted. However, Mr

Rainey did not suggest that we should rely upon this part of Mr Wyatt's evidence.

138. In the course of his closing submissions, Mr Rainey invited us to deduct a nominal amount, say £10,000, from the price paid for the lease with Act rights (£2,000,000) to reflect the absence of rights under the Act but that suggestion was not supported by any evidence from anyone.

139. In assessing the appropriate deduction to be made in the case of Flat 5, we take account of the following:

(1) the evidence in relation to 18 Gerald Road;

(2) the evidence in relation to 58 Hamilton Terrace;

(3) the fact that 18 Gerald Road and 58 Hamilton Terrace were houses and the benefit of the relevant Act may be greater in the case of the right to acquire the freehold of a house as compared with the right to acquire an extended lease of a flat;

(4) the fact that the existing lease without the benefit of rights under the Act will be at a competitive disadvantage in a market where the overwhelming majority of leasehold flats which are available enjoy the benefit of the Act;

(5) the opinion of Mr Fielding;

(6) the absence of any contrary opinion evidence;

(7) the decisions, and the reasoning, in the decisions of the Lands Tribunal and the Upper Tribunal to which we have referred.

140. Having regard to the matters summarised above, we have no hesitation in accepting Mr Fielding's evidence that the deduction for the benefit of the Act in the case of Flat 5, with an unexpired term of 41.32 years is 10%. As the value of the existing lease with rights under the Act was £2,000,000 it follows that the value of that lease on the assumption that it did not have rights under the Act will be £1,800,000.

141. Mr Rainey submitted that we should not attempt to value the existing lease without rights under the Act by making a deduction from the value of the existing lease with rights under the Act. He condemned the attempt as being "subjective" and therefore impermissible. We do not accept this submission. It is a commonplace in valuation that a valuer is asked to determine the amount of an uplift or a deduction to reflect a particular feature of a property. For example, in relation to the value of the freehold of Flats 3 and 11, the valuers have made a number of adjustments to reflect the differences between the comparables and the subject property. In some cases, a valuer will have a great deal to guide him as to the appropriate adjustment to make. In other cases, a valuer may have less to go on but nonetheless it is not impermissible for an experienced valuer to make a

valuation judgment. In this case, Mr Fielding had considered a body of evidence before he decided on his opinion of the appropriate deduction. He was fully entitled to proceed in that way.

142. Mr Rainey also submitted that the lessor's approach in these cases gave rise to circularity of reasoning. He submitted that at the valuation dates, the market value of leases with rights under the Act was arrived at by, or was certainly heavily influenced by, a process of deducting the estimated premium payable under the Act for an extended lease from the estimated value of that extended lease (usually 99% of the estimated FHVP value). We find that the evidence in this case supports that submission. Mr Rainey then submitted that adopting this approach the estimate of the premium required an assessment of the value of the existing lease without rights under the Act and that, in the market at the valuation date, that estimate was often arrived at by using the Gerald Eve graph. Mr Rainey submitted that the estimate should not be based on the Gerald Eve graph and that the market was wrong to use this method. He then submitted that it was circular reasoning to determine the value of the existing lease without rights under the Act by making a deduction from a value for an existing lease with rights under the Act, which value had made an assumption about the matter which was to be determined. Mr Rainey therefore submitted that we should not have regard to the market value of the existing lease with rights under the Act and we should not arrive at the value of the existing lease without rights under the Act by making a deduction from that market value. We agree that there is an element of circularity in the process but we do not accept Mr Rainey's conclusion that we are free to disregard the market value of the existing lease with rights under the Act or that we are prevented from making a deduction from that value to arrive at the market value of the existing lease without rights under the Act. Although Mr Rainey has submitted that the market should not have used the Gerald Eve graph to arrive at the estimate of the premium for an extended lease and therefore should not have used that estimate to arrive at the market value of a lease with rights under the Act, we find that what matters is how the market behaved at the valuation date. The evidence in this case shows that the market did use the Gerald Eve graph in the way described. The Gerald Eve graph was a real market circumstance which influenced market behaviour. The Upper Tribunal is required by statute to determine the market value of an asset in a real market which behaved in that way. It is not the function of the Upper Tribunal to tell the market how it ought to behave in the future and we have certainly no power to replace real market forces at past valuation dates by some other forces which we might consider ought instead to have operated.

143. Mr Rainey submitted that the approach which we favour, as explained in the last paragraph, gives rise to a paradox. He says that if we were to hold that the Gerald Eve graph would in future cases be considered to be unreliable, then the premium assessed by the tribunals in future cases would follow our decision and that, in turn, would produce the result that in the market when a purchaser of an existing lease with rights under the Act was advised on the amount of the estimated premium for an extended lease, he

would be advised in a way different from the way which in the past used the Gerald Eve graph. Accordingly, our decision about the Gerald Eve graph would affect the performance of the market in the future. It was then suggested that it was paradoxical for the Upper Tribunal when it had the power to change market behaviour for the future not to reject market behaviour at past valuation dates. We see nothing paradoxical about our decision. As already stated, our function is to determine the market value at past valuation dates. For that purpose, we need to make findings as to how the market behaved at those dates. It is not part of that function to form a view as to whether the market behaved correctly or logically or anything of that kind. The actual market behaviour is what matters. We must base our findings as to market value at past valuation dates on the then current market behaviour. If market behaviour were to change, and market values were to be affected, that would be recognised in future decisions of the tribunals. However, as stated earlier, it is not the function of the Upper Tribunal to direct the market as to how it should behave in the future, much less to "correct" retrospectively market behaviour in the past.

144. At this point, our reasoning points clearly to a finding that the value of the existing lease of Flat 5 without the benefit of rights under the 1993 Act is £1,800,000. Standing back, we have no real hesitation or doubt about making such a finding. We have reliable market evidence as to the value of the existing lease with rights under the 1993 Act and we have reliable material, including the reliable opinion of an experienced valuer, which allows us to determine that the value of the existing lease without rights under the 1993 Act would stand at a discount of 10%. We do not feel the need to adopt any other method of valuation even as a cross-check of such a finding. However, the Wellcome Trust Ltd submitted that there was a method of cross-checking this finding and that we should adopt that method. This method involved the use of a graph which has become known as the Gerald Eve graph.

145. Although the Gerald Eve graph was put forward in relation to Flat 5 only as a method of cross-checking the result arrived at by a different method, that graph was heavily relied upon by the Trustees of the Sloane Stanley Estate. Indeed, reliance on the Gerald Eve graph led to very extensive evidence being called to explain the origin and the continued use of the Gerald Eve graph and further evidence was then assembled and presented in relation to a large number of other graphs which have been prepared over the years. In the end, we heard a substantial amount of evidence in relation to these various graphs and we have decided that it would be helpful to summarise the effect of that evidence and our reaction to it. This we do in Appendix C to this decision. In Appendix C we comment in detail on the Gerald Eve graph. We also record that over the years, the Gerald Eve graph has been extensively used both for the purpose of settling and arguing claims to enfranchisement but it is also used in the market place. Of course, existing leases without rights under the 1993 Act are not typically for sale in the market place but when parties are negotiating for the sale and purchase of an existing lease with rights under the 1993 Act, one or both parties to the negotiation will have regard to the relativity shown by the Gerald Eve

graph when calculating the premium which would be expected to be payable for an extended lease and the amount of that premium will then influence the price paid for the existing lease. Accordingly, the Gerald Eve graph has not been simply a valuation tool used in relation to disputed claims to enfranchise, but it has also influenced the performance of the market in relation to the sales of existing leases with rights under the 1993 Act.

146. Because we have been invited to do so, we will consider using the Gerald Eve graph to cross-check the valuation in relation to Flat 5, arrived at in a different way. The existing lease of Flat 5 has an unexpired term of 41.32 years. The Gerald Eve graph gives a relativity of 67.06% for an unexpired term of that length. Applying this to the agreed FHVP value of £2.75m gives a value for the existing lease without rights under the 1993 Act of £1,844,150. Compared with the established market value for the same lease of Flat 5 with rights under that 1993 Act (£2 million), that value shows a deduction of 7.8% for the benefit of the Act.

147. We will now reach our conclusion in relation to Flat 5. The valuation justified by an appropriate valuation method in which we have confidence is £1.8 million. The suggested cross-check figure throws up a figure of £1,844,150. Our reaction to those facts is that we should adopt the figure of £1.8 million as our valuation. The cross-check provides a broad measure of support for that figure. Because the cross-check is only a cross-check, and because of the degree of confidence which we have in the figure of £1.8 million, we do not think it would be right to average the two figures. That would be to allow a figure in which we have less confidence to have an effect on a figure in which we otherwise can have confidence.

148. For the reasons set out above, we conclude that the value of the existing lease of Flat 5 at the valuation date on the statutory assumptions is £1.8 million.

The value of the existing lease of Flat 11 without rights under the Act

149. We have already made a number of findings in relation to the value of Flat 11 on the valuation date, on various bases. We have held that the FHVP value of Flat 11 at that date was £581,000. We have also referred to the sale price of the existing lease, with the benefit of rights under the 1993 Act, at around the same date and we expressed the view that the purchaser had overpaid to some extent for that existing lease.

150. We now need to consider the value of the existing lease of Flat 11 at the valuation date on the assumption that that lease did not have the benefit of rights under the 1993 Act. On the basis of the evidence in this case, it seems to us that it would be possible to approach that question using two methods. The first method is to use the Gerald Eve graph to ascertain what it suggests as the value of the existing lease for an unexpired term of 37.71 years as compared with a FHVP value of £581,000. The second method is to use a graph of real world relativity to arrive at a value for the existing

lease with rights under the 1993 Act and then to make a deduction from that value to reflect the absence of rights under the 1993 Act (on the statutory assumption).

151. The first method produces the following result: the Gerald Eve graph shows a relativity of 63.71% giving a value of £370,155.

152. The second method produces the following result: the Savills 2002 enfranchisable graph for real world relativity produces a relativity of 73.73% giving a value of £428,371. We did not have specific evidence from the valuers dealing with Flat 11 as to the amount of the deduction which would be appropriate. However, the length of the unexpired term in the case of Flat 11 was 37.71 years which is not very different from the length of the unexpired term in the case of Flat 5, on which we had very considerable valuation evidence. These three cases were heard together and the evidence given in relation to one particular property is admissible in relation to all three properties. If a deduction of 10% was right for Flat 5, and we think that it was, then a similar deduction would be appropriate for Flat 11. Making that deduction, the resulting value for Flat 11 would be £385,534.

153. In Appendix C we discuss in detail the Gerald Eve graph and the Savills 2002 graph. We are not able to give an unqualified endorsement to the use of either of these graphs for the reasons set out in Appendix C. In particular, there is reason to think the relevant market forces at the valuation dates in 2014 would have been different from the relevant market forces at the times at which these two graphs were prepared; we refer to paragraphs 28 to 32 of Appendix B in this respect, the significance of which as regards the graphs is further explained in Appendix C. In this way, there is reason to believe that the relativities shown by these two graphs are higher than appropriate for the market which existed at the valuation dates.

154. Our reaction to these considerations is as follows. The two methods throw up different figures. Each method is subject to some doubt and qualification. The doubts tend to suggest that the resulting figures are too high rather than too low. The figure suggested by the first method is lower than the figure suggested by the second method. In these circumstances, we consider that the least unreliable answer is the lower of the two answers. As it happens, that is a figure arrived at by directly using the Gerald Eve graph which is the method urged on us by the landlords of Flat 11. However, we wish to stress that although we are prepared to adopt that figure, it should not be regarded as an unqualified endorsement of that method but only because it is probably the least unreliable figure of those available to us on the evidence in this case.

155. We now need to reflect the fact that the existing lease of Flat 11 has an onerous ground rent. On the basis that the FHVP is £581,000, applying the agreed method of calculation in relation to the onerous ground rent in the lease of Flat 11, the deduction on that account is £10,424. Making that

deduction from £370,155, the resulting value for the existing lease, unimproved, with an onerous ground rent and without rights under the 1993 Act is £359,731 which we would round to £360,000.

The value of the existing lease of Flat 3 without rights under the Act

156. We have already held that the FHVP value of Flat 3 on the valuation date was £950,000. We now need to consider the value of the existing lease of Flat 3 at the valuation date on the assumption that that lease did not have the benefit of rights under the 1993 Act. As in the case of Flat 11, which we considered above, on the basis of the evidence in this case, it seems to us that it would be possible to approach that question using two methods. The first method is to use the Gerald Eve graph to ascertain what it suggests as the value of the existing lease for an unexpired term of 23 years as compared with a FHVP value of £950,000. The second method is to use a graph of real world relativity to arrive at a value for the existing lease with rights under the 1993 Act and then to make a deduction from that value to reflect the absence of rights under the 1993 Act (on the statutory assumption).

157. The first method produces the following result: the Gerald Eve graph shows a relativity of 47.2% giving a value of £448,400.

158. The second method produces the following result: the Savills 2002 enfranchisable graph for real world relativity produces a relativity of 61.5% giving a value of £584,250. We did not have specific evidence from the valuers dealing with Flat 3 as to the amount of the deduction which would be appropriate. The length of the unexpired term in the case of Flat 3 was 23 years. We had very considerable valuation evidence in relation to Flat 5 where the length of the unexpired term was 41.32 years. These three cases were heard together and the evidence given in relation to one particular property is admissible in relation to all three properties. We also have the findings as to the appropriate deductions which were made in earlier decisions of the tribunals, which we summarised above when we considered the position in relation to Flat 5. We consider that the deduction in the case of Flat 3 must be much greater than 10% to reflect the shorter term. We would have preferred to have heard the opinions of experienced valuers on this question but in the absence of that evidence we will do the best we can on the material before us. On that material, we consider that the appropriate deduction in the case of Flat 3 should be 20%. Making that deduction, the resulting value for Flat 3 would be £467,400.

159. In the case of Flat 3, having considered these two possible methods of assessing the value of the existing lease without rights under the 1993 Act, we are faced with a similar situation to that which we discussed in relation to Flat 11. We will adopt the same approach in the case of Flat 3 as we adopted in the case of Flat 11. We will therefore take the lower of the two figures as the least unreliable figure on the basis of the evidence before us.

160. We now need to reflect the fact that the existing lease of Flat 3 has an onerous ground rent. On the basis that the FHVP is £950,000, applying the agreed method of calculation in relation to the onerous ground rent in the lease of Flat 3, the deduction on that account is £13,302. Making that deduction the resulting value for the existing lease with an onerous ground rent and without rights under the 1993 Act is £435,098 which we would round to £435,000.

The result in these cases

161. We have now decided the dispute as to the FHVP values for Flats 3 and 11. In order to do so, we have used the Savills 2002 enfranchisable graph to assist with the analysis of comparables. We did so because that was the method generally used by the valuers who gave evidence before us. We have also determined the value of the existing leases, without rights under the 1993 Act, in relation to Flats 3, 5 and 11. In the case of Flat 5, we did not rely upon any of the graphs to which we were referred, including the Gerald Eve graph. In the case of Flats 3 and 11, we identified methods of valuation which used the Gerald Eve graph and the Savills 2002 enfranchisable graph although we are not able to say that those graphs are wholly reliable. Nonetheless, we had to reach conclusions based on the available material and on the evidence before us. We were able to conclude that the values we arrived at for the existing leases of Flats 3 and 11 were the least unreliable values based on that material. We understand that the matters we have now determined were the matters in dispute in these cases so that the parties will be able to use those figures to complete the calculation of the premium payable under schedule 13 to the 1993 Act in each of these cases.

162. We will expressly grant permission to the parties to apply if there is any disagreement as to the calculation of the premium using the values which we have determined.

Future cases

163. In these cases, the Tribunal has heard extensive evidence about hedonic regression and about the various graphs which have been used. We have also heard elaborate arguments as to the appropriate way to arrive at the value of an existing lease on the statutory assumption that it does not have rights under the 1993 Act. In these circumstances, we have considered whether our decision in these three cases will be useful in future cases and whether our decision will help parties settle future cases without having to incur the expense of a hearing before a tribunal.

164. We would have liked to have arrived at a method of valuation which would be clear and simple and predictable as to its future application to determine the relativities for leases without rights under the 1993 Act. If we had been able to support the use of the Parthenia model that might have been the result. Further, if we had been able to give unqualified approval to the Gerald Eve graph, that too would have simplified matters. However, in the

event, it is clear to us that we cannot support the use of the Parthenia model and we have reservations about the use of the Gerald Eve graph. Nonetheless, we will try to describe those matters which might be of use in future cases.

165. First, this case was brought to provide a test of the Parthenia model. It is clear to us that the Parthenia model has failed that test. It should not be put forward in a future case as a method of arriving at the value of an existing lease without rights under the 1993 Act.

166. Secondly, the valuations required under schedule 13 to the 1993 Act relate to market value on the statutory hypotheses. When the parties attempt to negotiate the amount of a premium in accordance with schedule 13 and when the tribunal comes to determine a dispute as to the amount of such a premium, the relevant valuation date will generally be a date in the past. The parties and the tribunal must focus on the state of the market at that date. What matters is how the market performed at that date. If the market, for example, for leases with rights under the 1993 Act at that date was influenced by certain matters, then that influence must be taken into account. For example, if the market at a date in the past was influenced by a particular graph of relativity then that influence is a market circumstance which is to be taken into account. It is not open to a party when discussing the market at a date in the past to suggest that the market was badly informed or operating illogically or inappropriately in order to invite the tribunal to replace actual market forces with what are suggested to have been more logical or appropriate considerations.

167. Thirdly, it is possible that the market might perform differently in the future from the way it has performed in the past. It is possible that in the future less weight will be given in the market to a particular graph or a new graph might emerge. If those new developments affect market behaviour then they must be taken into account when assessing market forces. It is conceivable that decisions of the tribunals might also influence valuers and in turn influence parties in the market. If that were to occur, then the changed market circumstances before a relevant valuation date must be taken into account when considering market value at that date.

168. Fourthly, in some (perhaps many) cases in the future, it is likely that there will have been a market transaction at around the valuation date in respect of the existing lease with rights under the 1993 Act. If the price paid for that market transaction was a true reflection of market value for that interest, then that market value will be a very useful starting point for determining the value of the existing lease without rights under the 1993 Act. It will normally be possible for an experienced valuer to express an independent opinion as to the amount of the deduction which would be appropriate to reflect the statutory hypothesis that the existing lease does not have rights under the 1993 Act.

169. Fifthly, the more difficult cases in the future are likely to be those where there was no reliable market transaction concerning the existing lease with

rights under the 1993 Act, at or near the valuation date. In such a case, valuers will need to consider adopting more than one approach. One possible method is to use the most reliable graph for determining the relative value of an existing lease without rights under the 1993 Act. Another method is to use a graph to determine the relative value of an existing lease with rights under the 1993 Act and then to make a deduction from that value to reflect the absence of those rights on the statutory hypothesis. When those methods throw up different figures, it will then be for the good sense of the experienced valuer to determine what figure best reflects the strengths and weaknesses of the two methods which have been used.

170. In the past, valuers have used the Savills 2002 enfranchisable graph when analysing comparables, involving leases with rights under the 1993 Act, for the purpose of arriving at the FHVP value. The authority of the Savills 2002 enfranchisable graph has been to some extent eroded by the emerging Savills 2015 enfranchisable graph. The 2015 graph is still subject to some possible technical criticisms but it is likely to be beneficial if those technical criticisms could be addressed and removed. If there were to emerge a version of that graph, not subject to those technical criticisms, based on transactions rather than opinions, it may be that valuers would adopt that revised graph in place of the Savills 2002 graph. If that were to happen, valuers and the tribunals might have more confidence in a method of valuation for an existing lease without rights under the 1993 Act which proceeds by two stages. Stage 1 would be to adjust the FHVP for the property to the value of the existing lease with rights under the 1993 Act by using the new graph which has emerged. Stage 2 would be to make a deduction from that value to reflect the absence of rights under the 1993 Act on the statutory hypothesis.

APPENDIX A

The Statutory Provisions

The relevant statutory provisions are contained in Part II of Schedule 13 to the 1993 Act. They are as follows:

"Part II PREMIUM PAYABLE IN RESPECT OF GRANT OF NEW LEASE

Premium payable by tenant

2. The premium payable by the tenant in respect of the grant of the new lease shall be the aggregate of—

(a) the diminution in value of the landlord's interest in the tenant's flat as determined in accordance with paragraph 3,

(b) the landlord's share of the marriage value as determined in accordance with paragraph 4, and

(c) any amount of compensation payable to the landlord under paragraph 5.

Diminution in value of landlord's interest

3.—(1) The diminution in value of the landlord's interest is the difference between—

(a) the value of the landlord's interest in the tenant's flat prior to the grant of the new lease; and

(b) the value of his interest in the flat once the new lease is granted.

(2) Subject to the provisions of this paragraph, the value of any such interest of the landlord as is mentioned in sub-paragraph (1)(a) or (b) is the amount which at the relevant date that interest might be expected to realise if sold on the open market by a willing seller (with neither the tenant nor any owner of an intermediate leasehold interest buying or seeking to buy) on the following assumptions—

(a) on the assumption that the vendor is selling for an estate in fee simple or (as the case may be) such other interest as is held by the landlord, subject to the relevant lease and any intermediate leasehold interests;

(b) on the assumption that Chapter I and this Chapter confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease;

(c) on the assumption that any increase in the value of the flat which is attributable to an improvement carried out at his own expense by the tenant or by any predecessor in title is to be disregarded; and

(d) on the assumption that (subject to paragraph (b)) the vendor is selling with and subject to the rights and burdens with and subject to which the relevant lease has effect or (as the case may be) is to be granted.

(3) In sub-paragraph (2) *"the relevant lease"* means either the tenant's existing lease or the new lease, depending on whether the valuation is for the purposes of paragraph (a) or paragraph (b) of sub-paragraph (1).

(4) It is hereby declared that the fact that sub-paragraph (2) requires assumptions to be made as to the matters specified in paragraphs (a) to (d) of that sub-paragraph does not preclude the making of assumptions as to other matters where those assumptions are appropriate for determining the amount which at the relevant date any such interest of the landlord as is mentioned in sub-paragraph (1)(a) or (b) might be expected to realise if sold as mentioned in sub-paragraph (2).

(5) In determining any such amount there shall be made such deduction (if any) in respect of any defect in title as on a sale of that interest on the open market might be expected to be allowed between a willing seller and a willing buyer.

(6) The value of any such interest of the landlord as is mentioned in sub-paragraph (1)(a) or (b) shall not be increased by reason of—

(a) any transaction which—

(i) is entered into on or after the date of the passing of this Act (otherwise than in pursuance of a contract entered into before that date), and

(ii) involves the creation or transfer of an interest superior to (whether or not preceding) any interest held by the tenant; or

(b) any alteration on or after that date of the terms on which any such superior interest is held.

Landlord's share of marriage value

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

(2) Subject to sub-paragraph (2A), the marriage value is the difference between the following amounts, namely—

(a) the aggregate of—

(i) the value of the interest of the tenant under his existing lease,

(ii) the value of the landlord's interest in the tenant's flat prior to the grant of the new lease, and

(iii) the values prior to the grant of that lease of all intermediate leasehold interests (if any); and

(b) the aggregate of—

(i) the value of the interest to be held by the tenant under the new lease,

(ii) the value of the landlord's interest in the tenant's flat once the new lease is granted, and

(iii) the values of all intermediate leasehold interests (if any) once that lease is granted.

(2A) Where at the relevant date the unexpired term of the tenant's existing lease exceeds eighty years, the marriage value shall be taken to be nil.

(3) For the purposes of sub-paragraph (2)—

(a) the value of the interest of the tenant under his existing lease shall be determined in accordance with paragraph 4A;

(aa) the value of the interest to be held by the tenant under the new lease shall be determined in accordance with paragraph 4B;

(b) the value of any such interest of the landlord as is mentioned in paragraph (a) or paragraph (b) of sub-paragraph (2)

is the amount determined for the purposes of paragraph 3(1)(a) or paragraph 3(1)(b) (as the case may be); and

(c) the value of any intermediate leasehold interest shall be determined in accordance with paragraph 8 , and shall be so determined as at the relevant date

4A.— (1) Subject to the provisions of this paragraph, the value of the interest of the tenant under the existing lease is the amount which at the relevant date that interest might be expected to realise if sold on the open market by a willing seller (with neither the landlord nor any owner of an intermediate leasehold interest buying or seeking to buy) on the following assumptions—

(a) on the assumption that the vendor is selling such interest as is held by the tenant subject to any interest inferior to the interest of the tenant;

(b) on the assumption that Chapter I and this Chapter confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease;

(c) on the assumption that any increase in the value of the flat which is attributable to an improvement carried out at his own expense by the tenant or by any predecessor in title is to be disregarded; and

(d) on the assumption that (subject to paragraph (b)) the vendor is selling with and subject to the rights and burdens with and subject to which any interest inferior to the existing lease of the tenant has effect.

(2) It is hereby declared that the fact that sub-paragraph (1) requires assumptions to be made in relation to particular matters does not preclude the making of assumptions as to other matters where those assumptions are appropriate for determining the amount which at the relevant date the interest of the tenant under his existing lease might be expected to realise if sold as mentioned in that sub-paragraph.

(3) In determining any such amount there shall be made such deduction (if any) in respect of any defect in title as on a sale of that interest on the open market might be expected to be allowed between a willing seller and a willing buyer.

(4) Subject to sub-paragraph (5), the value of the interest of the tenant under his existing lease shall not be increased by reason of—

(a) any transaction which—

(i) is entered into after 19th January 1996, and

(ii) involves the creation or transfer of an interest inferior to the tenant's existing lease; or

(b) any alteration after that date of the terms on which any such inferior interest is held.

(5) Sub-paragraph (4) shall not apply to any transaction which falls within paragraph (a) of that sub-paragraph if—

(a) the transaction is entered into in pursuance of a contract entered into on or before the date mentioned in that paragraph; and

(b) the amount of the premium payable by the tenant in respect of the grant of the new lease was determined on or before that date either by agreement or by the appropriate tribunal under this Chapter.

4B.—(1) Subject to the provisions of this paragraph, the value of the interest to be held by the tenant under the new lease is the amount which at the relevant date that interest (assuming it to have been granted to him at that date) might be expected to realise if sold on the open market by a willing seller (with the owner of any interest superior to the interest of the tenant not buying or seeking to buy) on the following assumptions—

(a) on the assumption that the vendor is selling such interest as is to be held by the tenant under the new lease subject to the inferior interests to which the tenant's existing lease is subject at the relevant date;

(b) on the assumption that Chapter I and this Chapter confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease;

(c) on the assumption that there is to be disregarded any increase in the value of the flat which would fall to be disregarded under paragraph (c) of sub-paragraph (1) of paragraph 4A in valuing in accordance with that sub-paragraph the interest of the tenant under his existing lease; and

(d) on the assumption that (subject to paragraph (b)) the vendor is selling with and subject to the rights and burdens with and subject to which any interest inferior to the tenant's existing lease at the relevant date then has effect.

(2) It is hereby declared that the fact that sub-paragraph (1) requires assumptions to be made in relation to particular matters does not preclude the making of assumptions as to other matters where those assumptions are appropriate for determining the amount which at the relevant date the interest

to be held by the tenant under the new lease might be expected to realise if sold as mentioned in that sub-paragraph.

(3) In determining any such amount there shall be made such deduction (if any) in respect of any defect in title as on a sale of that interest on the open market might be expected to be allowed between a willing seller and a willing buyer.

(4) Subject to sub-paragraph (5), the value of the interest to be held by the tenant under the new lease shall not be decreased by reason of—

(a) any transaction which—

(i) is entered into after 19th January 1996, and

(ii) involves the creation or transfer of an interest inferior to the tenant's existing lease; or

(b) any alteration after that date of the terms on which any such inferior interest is held.

(5) Sub-paragraph (4) shall not apply to any transaction which falls within paragraph (a) of that sub-paragraph if—

(a) the transaction is entered into in pursuance of a contract entered into on or before the date mentioned in that paragraph; and

(b) the amount of the premium payable by the tenant in respect of the grant of the new lease was determined on or before that date either by agreement or by the appropriate tribunal under this Chapter.

Compensation for loss arising out of grant of new lease

5.—(1) Where the landlord will suffer any loss or damage to which this paragraph applies, there shall be payable to him such amount as is reasonable to compensate him for that loss or damage.

(2) This paragraph applies to—

(a) any diminution in value of any interest of the landlord in any property other than the tenant's flat which results from the grant to the tenant of the new lease; and

(b) any other loss or damage which results therefrom to the extent that it is referable to the landlord's ownership of any such interest.

(3) Without prejudice to the generality of paragraph (b) of sub-paragraph (2), the kinds of loss falling within that paragraph

include loss of development value in relation to the tenant's flat to the extent that it is referable as mentioned in that paragraph.

(4) In sub-paragraph (3) *"development value"*, in relation to the tenant's flat, means any increase in the value of the landlord's interest in the flat which is attributable to the possibility of demolishing, reconstructing, or carrying out substantial works of construction affecting, the flat (whether together with any other premises or otherwise)."

APPENDIX B

The Parthenia Model of Relativity

Introduction

1. The claimed purpose of the Parthenia model is to enable one to determine, by reference to a graph, the value of a lease of any given length without rights under the 1993 Act, relative to its FHVP value.

2. The model is based upon a statistical technique known as hedonic regression, the underlying concept of which is that the price of a good (in this case a flat) is the aggregation of the prices of the individual attributes of that good. These attributes can be physical (e.g. size, number of rooms, layout, amenities, condition), locational (e.g. accessibility, distance from key destinations, view, quality of the environment) and contractual (e.g. the length of the lease, the existence of an onerous ground rent).

3. These attributes of a property are not individually priced in the market but are sold as a bundled package. The Parthenia model looks at a sample of property transactions in prime central London where both the price and the relevant attributes of each property are known and by using statistical procedures tries to isolate the unobserved contribution to price of each attribute, including lease length. A regression is essentially a way to decompose a variable (the price of a property) into a part which is explained (by property attributes) and a part which is not (known as the residual).

4. The unexpired lease length is the hedonic attribute of interest with the other attributes representing control variables. The model uses the mathematical procedure of regression analysis to derive the "best fit" relationship among the variables and to produce an estimate of the reduction required in the price of a freehold property to obtain the price of an otherwise identical property held on a lease of a given unexpired term.

5. The key to a hedonic model that produces results which reflect the underlying market pricing process is to identify a sample of properties which is representative of the whole market and to specify a functional form for the statistical procedures which accurately predicts the way in which the attributes combine into an overall price. The experts agree that a well specified hedonic model is one appropriate approach to the determination of relativities in a particular time period.

The Construction of the Parthenia Model

(*i) The data sample*

6. In order to obtain leasehold relativities without the benefit of Act rights the sample of market transactions cannot be taken from a period when the Act was either in force or anticipated. The Parthenia model therefore uses a data sample based upon flat and house sales that took place in the period 1987-1991. The source of these transactions was two-fold: the internal archives of John D Wood & Co and the Lonres.com tabular archive. The raw data was cleansed and merged into a final data set of 7,969 transactions (72% of which were leasehold and 28% freehold or a share of the freehold). In the case of 2,583 of these transactions, the purchase price was verified.

(ii) The hedonic attributes

7. Parthenia classify the property attributes used in their model into three groups: primary, additional and extracted. Primary attributes are said to be the most important determinant of price and comprise: whether the property is a house or a flat; the number of bedrooms (which also acts as a proxy for size); the sale quarter and the street (which captures all time-invariant localised factors). Additional attributes are those, like the primary attributes, that are immediately available from the source data and include floor level, type of accommodation (e.g. maisonette, purpose-built flat), onerous ground rent etc. Extracted attributes are extracted from the "notes" column of the John D Wood & Co data or from the pdf records of Lonres data. These include whether a property is detached, has two or more bathrooms, a garden, balcony etc.

8. The attributes are measured by numerical and categorical variables. Numerical variables can be either continuous (e.g. price) or discrete (e.g. number of bedrooms). Categorical variables are used extensively in the Parthenia model in the form of "dummy" variables to indicate the presence (value "1") or absence (value "0") of a particular attribute.

(iii) Functional Form

9. The mathematical relationship between the dependent (price) and independent (hedonic attribute) variables is known as the functional form of the model. The choice of functional form is important because an incorrect choice can result in inconsistent estimates. The relationship between the dependent and independent variables is not necessarily (or usually) linear and so other logarithmic functional forms can be used such as semi-log (also known as "log linear") and log-log forms. The Parthenia model assumes a semi-log functional form which is recognised as a standard (but not the only) approach in house price modelling.

10. The experts agree that the theory of hedonic pricing offers limited assistance in the selection of the correct functional form so that the researcher must make choices and the results may be sensitive to those choices.

(iv) Modelling relativity

11. The Parthenia model derives relativity in two stages. Firstly, a linear equation of standard form is applied to each member of the data set and the results collectively subjected to a least squares regression analysis to determine the coefficients (the size of the contribution to value) of each of the hedonic attributes. The attribute of interest is the length of lease and the model produces coefficients which are the logarithms of the average relativities for each of the integer leasehold terms from 1 to 99 years. These coefficients are exponentiated to give the estimated relativities. The model requires an intercept term which represents a baseline category against which every other property is compared. In the Parthenia model the baseline is a one bedroom, first floor, freehold flat.

12. Least squares regression analysis is a standard statistical tool which is used to minimise the error (the sum of the squares of the errors) between the prices predicted by the model and the observed prices that are used to construct the model.

13. In the second stage of the model a curve is fitted to the relativity point estimates from which the relativity for any lease length can be found. The Parthenia model uses a weighted local polynomial regression to fit the curve. (A weighted regression is used to take into account the fact that some lease terms – e.g. around 60 years – have more data points than others).

14. The results obtained from the model depend upon the data sample which is used and whether that sample is a true reflection of reality. The results would not be the same if a different sample was used and it is important to establish a measure of confidence that the results would not radically change if such another sample was chosen. A common way of calculating a confidence interval is to use a measure known as the standard error. It is not possible to generate formal standard errors and confidence limits in this case due to the two-stage approach adopted and the ad hoc "theory free" procedure which is taken to fitting the relativity curve. Instead the Parthenia model uses a procedure known as "bootstrapping" to estimate confidence bands. This procedure involves running the regression repeatedly using random data points taken from the dataset (with replacements). On each occasion therefore data may be chosen once, more than once or not at all. The result of the procedure gives the 95% confidence band around the original estimate. So if the confidence band was 10% around the point estimate relativity of, say, 60% then one can be 95% confident that the range 55%-65% contains the true value.

15. The results of the Parthenia analysis were presented in three forms:

(a) *Model 1* uses all the data points (7,969) and relies only upon the primary attributes, i.e. those that were already present in the original raw data and not extracted later.

(b) *Model 2* uses the data points (7,327) for which the additional attributes could be extracted from the John D Wood & Co dataset and the Lonres dataset for which a pdf was available.

(c) *Model 3* uses only those data points (2,583) where the purchase price had been verified.

16. Table 1 below shows the results of the Parthenia analysis for each of the three models adopted by Mr Wyatt (before adjustment for onerous ground rents).

TABLE 1

PARTHENIA MODEL: RESULTS

Property/unexpired lease term	RELATIVITY:CONFIDENCE BAND			
	MODEL 1	MODEL 2	MODEL 3	ADOPTED RELATIVITY
FLAT 3/23 years	60.1%: 6.22%	59.54%: 7.03%	63.87%:19.79 %	59.75%
FLAT 5/41.32 years	82.43%: 6.52%	79.92%:7.69 %	84.72%: 22.43%	81.18%
FLAT 11/37.71 years	79.04%: 6.46%	76.84%: 7.47%	81.7%: 22.02%	77.94%

Diagnostic Tests

17. There are a number of standard statistical diagnostic tests that can be applied to the Parthenia model. Such tests can be grouped according to their purpose:

(i) Normality of residuals (SKtest, Shapiro-Francia, Shapiro-Wilk and Kolmogorov-Smirnov tests)

The null hypothesis in these tests is that the distribution of residuals is normal, i.e. random. Models 1, 2 and 3 fail these tests.

(ii) Homoscedasticity (Breusch-Pagan/Cook-Weisberg test)

The null hypothesis is that of homoscedasticity of the residuals (constant variance) i.e. a situation where the error term (residual) is the same across all values of the independent variable. Models 1 and 2 fail this test. Model 3 passes this test.

(iii) Omitted variables (Ramsey RESET test)

The null hypothesis is that the relationship between independent and dependent variables is linear. If a non-linear relationship can be shown to exist then the model is mis-specified. Models 1, 2 and 3 fail this test.

(iv) Appropriate functional form (Box-Cox tests)

The Box-Cox transformation can be used to test for the correct functional form i.e. the mathematical relationship between price and the explanatory variables. Models 1, 2 and 3 fail this test for linear, semi-log (the preferred form) and log specifications.

(v) The regression model (R^2 and adjusted R^2)

The Parthenia model uses a set of attributes to explain the variation in price by variations in these attributes. Part of the price of each property (the deterministic part) can be explained by the model but part of it will be unexplained (the residual). The residual of any observation is the difference between the actual price and that predicted by the model. The regression procedure seeks the model which minimises the sum of the squared residuals (R^2). Generally it is better to look at adjusted R^2 which corrects for sample size and the number of coefficients that are estimated. R^2 will always increase when a new attribute is added to the model but adjusted R^2 will only increase if the new attribute improves the model by more than is expected by chance.

Other things being equal the higher the R^2 the better the goodness of fit of the model. An R^2 value of 0 means that knowing the value of the independent variable will not help you predict the value of the dependent variable and an R^2 value of 1 means that if the value of the independent variable is known then it is possible to predict the value of the dependent variable perfectly.

The R^2 values for models 1, 2 and 3 were 0.838, 0.858 and 0.887 respectively.

(vi) Multicollinearity (Variance Inflation Factor (VIF))

> Multicollinearity occurs where the regression model includes multiple variables (attributes) that are moderately or highly correlated not just to the dependent variable (price) but to each other. Severe multicollinearity is a problem because it will increase the variance of the regression coefficients making them difficult to interpret. It is a problem where, as here, the purpose of the regression model is to establish the effect of an individual attribute (lease length) on price. Multicollinearity reduces the effective amount of information available to assess the unique effect of the lease length on price.

The VIF quantifies by how much the variance of the estimated coefficients is inflated. A VIF of above 5 indicates a problem with the model and a value above 10 indicates a serious problem. The Parthenia model has VIF values for the house/flat dummy variable for models 1 to 3 of 5.4, 12.0 and 27.7 respectively.

Summary of the main criticisms of the Parthenia model

18. Criticisms of the Parthenia model can be categorised into three types: (1) technical criticisms of the construction of the model; (2) criticisms of its application in the changed economic environment that prevailed at the valuation dates; and (3) consideration of the constraints that exist when modelling relativity.

1. Technical criticisms

19. Professor Lizieri identified a number of problems and issues with the Parthenia model which gave him concern about the robustness and reliability of the relativities produced by the model. These were considered in the context of the results of the diagnostic tests outlined above.

(i) Not all the relevant priced variables were included in the model

20. A hedonic model that omitted variables that influenced the subject variable (price) would be mis-specified and produce biased coefficients. Examples of omitted variables in the Parthenia model included the presence or absence of a lift, the age of a building, construction type and neighbourhood characteristics.

(ii) Some interaction effects were not accounted for in the model

21. If the variables included in the model interacted with each other and such interaction was not incorporated in the model then it would be mis-specified. Professor Lizieri gave the example of the categorical variable "two or more bathrooms" which was treated in the Parthenia model as a dummy variable independent of the number of bedrooms. But these variables were unlikely to be independent of each other since the absence of a second bathroom in a two bedroom flat was likely to be less significant than its absence in a five bedroom house.

(iii) Important spatial effects were related to unexpired lease length

22. There were potential interactions between street address and property characteristics and between street address and lease lengths, in both cases because of the particular historic ownership and management policies of estate owners such as the Grosvenor and Cadogan Estates. Properties in particular streets would often share characteristics and attributes which were price sensitive.

23. Professor Lizieri correlated street dummy coefficients from Model 2 with unexpired lease length. The results showed that streets with lower than average lease lengths tended to have higher than average street coefficients (i.e. the property in that street was more valuable). This suggested a relationship between the price of properties in particular streets and typical lease terms that raised doubts about the model's estimated relativities. Mr Roberts gave a detailed analysis of the transactions used in the Parthenia model which showed that short leaseholds – less than 50 years – were predominantly to be found "in the most prime and valuable areas". Exclusion of such price sensitive characteristics of properties from the model could create spatial errors which made the coefficients unreliable. The inclusion of such characteristics alongside the dummy street variables used in the Parthenia model could lead to problems of multicollinearity.

(iv) There were likely to be differences in the characteristics of long leasehold and freehold properties when compared to shorter leases.

24. The Parthenia model combined freehold properties and leaseholds with an unexpired term over 99 years into a single category (Model 1) or placed such leaseholds into a single category called "long lease" (Models 2 and 3). If lower quality properties were being sold on 125 year leases then these transactions would contribute to the hypothetical freehold value and bias the relativity curve upwards. Mr Shingles gave evidence that before the 1993 Act it was the policy of two of the major prime central London landed estates, the Cadogan and Grosvenor Estates, to grant lease extensions of no more than 65 or 75 years respectively. Such policies would have a direct impact on the estimation of relativities in the pre-Act period by increasing the coefficients of such shorter leases relative to long leases and freeholds. Furthermore it was not until the 1993 Act that the most valuable houses could be enfranchised. So in the dataset period of 1987-1991 many lower and medium value houses had been enfranchised but the most valuable houses were held leasehold. This would cause the model to overstate relativities.

(v) There were very large error margins for individual year estimates of relativity that were not accounted for in the curve fitting process.

25. The Parthenia model relied upon a two-stage approach. The first stage derived coefficients which were point estimates for the relativity of unexpired (integer) terms from 1 to 99 years (with terms of 100 years or more being included with freeholds as a single reference category). In the second stage a smooth curve was fitted to these individual points using a second order weighted polynomial format. The point estimates of

relativity were volatile and subject to large confidence intervals. Some results were implausible, e.g. in Model 1 the relativity of a 75 year lease was 107% which was 7% higher than the value of the equivalent freehold. The relativities for Model 3 (using the smaller sample of verified data) were more volatile and the confidence limits much greater. The second stage curve fitting disguised this volatility in the point estimates. The bootstrapping procedure used in the Parthenia model treated the point estimates of relativity as being certain and took no account of the uncertainty and wide confidence intervals about these coefficients, especially in Model 3. Each bootstrap relied upon the same dataset and so any specification and/or data sampling problems were reproduced every time the procedure was run.

26. Professor MacGregor echoed these criticisms in his expert report and he shared many of Professor Lizieri's concerns about the structure of the Parthenia model. Instead of combining the leases with unexpired terms over 99 years either with freeholds (model 1) or into the single category "long lease" (models 2 and 3) Professor MacGregor re-estimated the Parthenia models by using all the unexpired lease terms. He noted that if the model was valid for unexpired terms up to 99 years it should also be valid for longer terms, particularly in the period 110-125 years where there was a large number of observations. He described the results of this exercise as:

"Striking and severely undermining relativities that are derived from the models. The fitted curves are flat from around 65 years to around 105 years and then rise slowly towards 125 years but only as a result of the weighting applied to individual years."

27. Professor MacGregor noted that 89% of the freeholds in the dataset were houses and 92% of the leaseholds were flats. Essentially the models were comparing leasehold flats to freehold houses. This gave rise to problems of collinearity as evidenced by the VIF results for the house/flat dummy variable (see paragraph 17(vi) above). Professor MacGregor concluded that houses and flats should not be in the same model because the house variable was strongly correlated positively with other variables, such as 5, 6 and 7 bedrooms, more than one bathroom, garden and verified sales and negatively correlated for 3 bedrooms. Mr Wyatt used a single dummy variable (the price of an "otherwise identical" house) to make a proportional adjustment between flat and house prices. For Models 1 to 3 the respective prices of an otherwise identical house were 61%, 33% and 40% higher than that of a flat. These adjustments were critical when determining relativities. Professor MacGregor then considered a houses only model which showed that the estimated relativity curve for houses, especially with unexpired terms between 50 and 99 years, gave values of over 100%, suggesting that the relativity was too high in that range.

2. Application of the Parthenia model at the valuation date

28. Professors Lizieri and MacGregor both rejected the application of the Parthenia model, based upon a historic data set (1987-1991), to the market at the valuation date. The experts considered that there had been substantial changes in the market and the economic environment over the intervening period leading to changes in relativity. These included:

(i) Substantial and structural changes to the level of interest rates and discount rates

29. The 2009 RICS Report "Leasehold Reform: Graphs of Relativity" noted that "changes in economic conditions may impact on freehold or leasehold values to a greater or lesser extent, thereby affecting relativity." Professor Lizieri said that the 10 year nominal zero coupon yield was 10.1% at the beginning of 1987 and 9.4% at the end of 1991. At the end of February 2014 it was 2.9%. Even allowing for reduced inflation in 2014 compared with 1987-1991, the real yield fell by over 4.2% since the dataset transactions. Put simply, if discount rates went down the value of the future enjoyment of the leasehold property (whether expressed as the right to occupy or to rent out) would increase and therefore longer leases became worth relatively more than shorter leases.

(ii) Changes in the nature of the market

30. Purchasers at the valuation date might have had very different preferences and time horizons from those purchasing in 1987. Since that time there had been an influx of foreign purchasers. Mr Fielding gave evidence that between 1986 and 1992 32% of purchasers in prime central London were from overseas. For the period 2006 to June 2015 that figure had risen to 54%. Such overseas buyers sought safe havens for capital, making assumptions about future capital growth, and were less interested in shorter leases. Such a change in the structure of the market, with a preference among the majority purchasing group for longer leases, would affect (lower) the relativity of short leases. Professor MacGregor said that there would also be changing preferences for the attributes of a property based on need or fashion which would be reflected in the relative prices of the hedonic attributes.

(iii) Changes in the institutional and legal structure of the residential market

31. The structure of the market had changed since 1987-1991, not least because of the operation of the Act and the growth of leasehold enfranchisement. There were fewer short leaseholds on the market at the valuation date than during 1987-1991. This change in the market structure and in the preference for long leases would not lead to a premium price being paid for relatively scarce short leaseholds. The prime central London estates could no longer enforce a policy restricting the length of lease granted to 65-75 years. Mr Buckle produced evidence to show that whereas in 1987-1991 33% of flats in prime central London had unexpired terms of 60 years or less, by 2010-2014 that figure had more than halved to 15%. In 1987-1991 only 25.3% of leases had unexpired terms over 100 years; by 2010-2014 that figure had more than doubled to 56.6%. That

meant that the value of short and medium length leases would have gone down relative to long leases.

32. In 1987-1991 the value of short leases was supported by the right of a tenant in occupation to a statutory tenancy upon the expiry of the lease at a fair rent. That support was phased out over the period 1989-1999 pursuant to Schedule 10 of the Local Government and Housing Act 1989 and replaced by the less favourable (to the tenant) right to an assured tenancy at a market rent.

3. Constraints

33. The two stage approach adopted in the Parthenia model is one which is not constrained to comply with known market features, in particular with the need for relativity to fall within the range 0-100% and for relativity to increase strictly with the unexpired lease length. A single-stage modelling approach could have incorporated such constraints and would have made the unexpired term a continuous variable rather than including each year of term as a separate dummy variable. That would have avoided the need for the unexpired term to be rounded to the nearest integer value.

34. The results of the model must not only satisfy statistical and econometric criteria but should also satisfy economic and market logic. The Parthenia model did not do this, e.g. it failed to distinguish between the relativities of longer leases and produced results that were so out of line with the evidence of Act world transactions and market practice that it raised doubts about the validity of the supporting research, technically sophisticated as it might appear.

The suggested responses to the criticisms

35. Both Dr Bracke and Mr Wyatt rejected concerns about the Parthenia model's failure to pass a number of standard diagnostic tests as being irrelevant and not reflecting current empirical research practice. They contended that the criticisms did not reflect the intention of the research and in many cases were not applicable to the methods that had been used. We will summarise their contentions.

36. The purpose of the research was to estimate the effect of the unexpired lease term on price. The model was not intended to be a complete representation of the process of property price determination capturing all variables affecting house/flat prices. This being so the exact specification of the control function comprising the property attributes and their location was not crucial and measures of model fit such as R^2 and the other diagnostic tests were largely irrelevant.

37. The Ramsay RESET test examined whether untried combinations of the control variables in the regressions explained prices. Parthenia had run a large number of robustness checks using different combinations of control variables. These had very little effect upon the estimated relativities and therefore the results of the Ramsay RESET test were not of concern.

38. Street coefficients were used as a control variable for difficult to measure locational factors and were not intended to assist in the estimation of the true premium of each street.

39. The technique of bootstrapping used in the Parthenia model did not require reliance upon standard errors from the first stage regressions and meant that multicollinearity and heteroscedasticity were already taken into account in the models. Tests for multicollinearity (VIF) and for heteroscedasticity could safely be ignored. Similarly given the large number of observations in the dataset the diagnostic tests for the normality of distribution were irrelevant since ordinary least squares regression coefficients were asymptotically distributed regardless of the distribution of the underlying data.

40. Professor MacGregor's concern that it was inappropriate to include houses and flats in the same model was addressed by running a flats only model based on Model 2 and an unexpired term of 41.32 years. This regression had 5,400 observations and produced a relativity of 79.88% compared to 79.92% in the model which included house data. Dr Bracke said that there were too few houses to estimate a relativity curve for houses only and that Parthenia had never produced such a curve.

41. Dr Bracke answered Professor Lizieri's criticism that not all relevant priced variables had been included in the Parthenia model by noting that Model 2 had incorporated as many variables as possible while Model 1 had very few such variables. The results of both models were similar (see Table 1 above). Dr Lizieri's other criticisms (see paragraphs 19-25 above) were mainly addressed by further iterations of the Parthenia model using what Dr Bracke described as a variety of techniques, data samples and sets of controlled variables. Dr Bracke concluded that:

> "The overall insight is that when one adequately controls for location and has a large enough sample, relativities estimated from the historic dataset are remarkably insensitive to all other modelling choices."

42. Parthenia had shared its code and data with a number of other experts so that they could run their own regressions and tests on the data. Those experts had been able to replicate Parthenia's results. Professor Muellbauer had used a "one stage" approach using a different software package and had produced results that were statistically very close to those of Parthenia.

43. Apart from the "flats only" regression referred to in paragraph 40 above Parthenia ran alternative specifications with onerous ground rents excluded or dropped as a variable, using complete postcodes rather than streets, using council tax bands and a combination of all these factors. For an unexpired lease of 41.32 years the results varied from 78.14% to 80.39% compared with the original Model 2 result of 79.92%. Dr Bracke concluded that the results were robust to significant changes in the model.

44. The Parthenia model was criticised because it relied on data from the period 1987-1991 which was then applied to the market at the valuation dates in 2014. Although Mr Wyatt accepted that relativity may have altered over time there was no solid evidence to support the hypothesis that it had so changed. Indeed the RICS 2009 Report recorded Gerald Eve, whose graph was relied upon by the landlords, as saying "It is considered that there is no reason for relativity to have changed over time". Any problem with the data period would equally be a problem for all of the graphs in the 2009 Report.

45. Market and economic change affected all capital values but it was only necessary to consider whether such changes affected the relative value of short leases and FHVP values.

46. The data period was not tainted by the prospect of the Act since it was only in July 1991 that a proposal for collective enfranchisement appeared.

47. There was no evidence that a change in the mix over time of long and short leases affected relativity. Indeed any reduction in the number of short leases would logically increase their price due to their relative scarcity.

48. The increase in overseas purchasers was only relevant in the context of Mr Fielding's view that such purchasers did not like short leases. That view was anecdotal and unsupported by evidence or by Mr Wyatt's experience. In this case two of the three tenants (Ms Aaron and Mr Lagesse) were overseas buyers of short leases.

49. The valuation assumption was that the existing leasehold interest had to be valued without Act rights in a market where Act rights otherwise applied. But it was not accepted that this meant that leases without Act rights necessarily became worth less. That would imply a drop in their intrinsic value for which there was no evidence. Even if such evidence existed such an argument would subvert the purpose of the statutory disregard which was to preserve the landlord's value rather than diminish the tenant's value.

50. The rights of tenants to remain at a fair rent after the expiry of a lease term may have uplifted the values of short leases but there was no evidence that it affected other values or that there was any tenant's hope value arising from the prospect of a landlord granting a new lease. Any such hope value should have been excluded from the valuation anyway following Sportelli.

51. The fact that deferment rates were higher in 1987-1991 than they were in 2014 was not relevant because the subject valuations were concerned with unenfranchiseable leases. The value of the landlord's reversion was irrelevant to establishing how much a purchaser would pay for the unexpired term.

52. Professor Muellbauer was the only expert to consider the effect of changing interest rates on the model by comparing high interest rate years

with low interest rate years in the period 1987-1991. That showed that changes in interest rates had little effect on relativity. Professors Lizieri and MacGregor considered the point by equating the purchase of a leasehold with that of a freehold and foregoing all the benefits of ownership and occupation for the term of the lease. But that was effectively deferring the reversion and not applying a yield over a term of years.

Discussion

53. The econometric experts agree that a well-specified hedonic model is one approach to the determination of relativities in a particular time period. Model estimation, model evaluation and model selection are agreed to be an iterative process until a preferred model has been derived. This is based on theory, statistical tests and the judgment of the researcher. The output of a regression model is conditional on the data used and on the model specification.

54. Hedonic modelling is therefore characterised by the need for the researcher to make choices, such as the dataset to use, the functional form of the model and the choice of hedonic attributes (which may be constrained by the limitations of the data set) to explain the variable of interest. The dispute between the experts focussed on these choices and on whether the results of the models were robust and reliable in the light of them.

55. We find the use of a substantial number of actual transactions which were unaffected by the Act is a potentially attractive feature of the Parthenia model but we do not accept that the model can fairly be described as an objective analysis of those transactions given the significant exercise of subjective judgment that the model requires.

56. In the evidence before us, the examination of the choices that were made in the construction of the Parthenia model was rigorous and informed and we acknowledge the considerable time and effort that the econometric experts took to explain hedonic regression and its application to the issues before us.

57. The Wellcome Trust have themselves relied on a hedonic regression model in Mr Buckle's revised Savills enfranchiseable graph which uses up to 10,887 prime central London transactions between 2010 and June 2015. There are five versions of the Savills model, the first three of which echo the Parthenia approach (but the transactions in question related to leases which had the benefit of the 1993 Act) while Savills Models 4 and 5 make what Mr Buckle describes as "better use of the current data".

58. Mr Buckle's preferred model is Model 5 which analyses 5,904 sales of leasehold flats and uses a curve form which is constrained in particular by the fact that a longer lease is always worth more than a shorter lease of the

same property and, however long the lease, cannot be worth more than the freehold.

59. The relativity of a lease with an unexpired term of 41.32 years, with rights under the 1993 Act is shown by Model 5 to be 71.9%. The relativity for this length of lease, without rights under the 1993 Act, is shown by the Parthenia model as the higher figure of 81.18%. One, or both, of these results must be wrong for the current or recent market. This pair of results conflicts with the overriding constraint that a lease which has the benefit of the 1993 Act cannot be worth less than the same lease without rights under the 1993 Act. The conflict in this case could be due to the Parthenia and/or the Savills enfranchisable hedonic regression model being technically deficient or to a change in (lowering of) relativities over time.

60. In the main part of our decision we drew attention to the fact that the result produced by the Parthenia model was incompatible with the market evidence in relation to the market transaction represented by the sale of the existing lease of Flat 5, with rights under the 1993 Act. It was thereby demonstrated that the Parthenia model produced an impossible result. In Xue v Cherry [2015] UKUT 0651 (LC), the Upper Tribunal (Judge Huskinson and Mr Trott) said at paragraph 61(1) that:

"If a valuer conjectures a theoretical solution to the problem of determining relativity, its predictions must be tested against market transactions to see whether the model gives results that are observed in practice."

Accordingly, the Parthenia model fails this fundamental test.

61. In the main part of our decision, we reached the conclusion that the Parthenia model was not suitable to be used to determine relativity in respect of leases without rights under the 1993 Act. We also held that the Parthenia model was not capable of being revised or modified so that its use might become appropriate. Strictly speaking, we do not have to diagnose why this is so. However, we think it is highly likely that some at least of the technical criticisms of the model are justified and contribute to this failure. We can be reasonably confident that the criticism in paragraph 23 of this Appendix is fully justified and has a substantial adverse effect on the reliability of the Parthenia model. In addition, we consider it is probably the case that the economic and market changes since 1987-1991 have indeed lowered relativities. In particular there have been significant changes in the pattern of property ownership in prime central London, in the ratio of short to long leases and in the level of interest rates. (Professor Muellbauer's analysis of the effect of changes in interest rates was limited to the relatively small changes between 1987 and 1991.)

APPENDIX C

The Graphs of Relativity

1. John D Wood & Co (1996) and Gerald Eve Graph, also known as the Gerald Eve ("GE") Graph.

1. Evidence about this graph was given by Mr Ian Macpherson MA, FRICS (formerly a partner in Messrs Gerald Eve), Mr George Pope FRICS (formerly a partner in John D Wood & Co), Mr Julian Clark BSc, MRICS (a partner in Gerald Eve LLP), Mr Kevin Ryan FRICS (a partner in Carter Jonas LLP), Mr Guy Hollamby MRICS (currently a director of Symington Elvery but between 1999 and 2005 the Head of Professional Valuation Services at John D Wood & Co) and Mr Justin Shingles (who set up his own company, Justin Shingles Limited, in 2000 having previously been a partner in Strutt & Parker).

2. Mr Macpherson explained that both Gerald Eve and John D Wood & Co were instructed by the Grosvenor Estate during the mid 1970s to advise on leasehold reform valuations arising from the Leasehold Reform Act 1967 ("the 1967 Act"), as amended by the Housing Act 1969 and the Housing Act 1974. John D Wood & Co was an estate agency with a large share of instructions in the prime central London housing market and they were instructed to advise on values with vacant possession. Gerald Eve were instructed to advise on the statutory valuations. This work subsequently extended to valuations for higher value houses and flats. Mr Macpherson took over responsibility for all Gerald Eve's advice to the Grosvenor Estate on leasehold reform valuations from 1978 until he retired in 2007.

3. Mr Macpherson began keeping a schedule by the end of 1975 of the settlements Gerald Eve had negotiated, including details of relativity. He explained the process of negotiation and the reporting procedure for the approval of settlements by the Grosvenor Estate. Grosvenor relied upon John D Wood & Co's advice about the acceptability of vacant possession values and upon Gerald Eve's advice about the other component parts of the statutory valuation. Sometimes the make-up of the final valuation was agreed explicitly with the leaseholder (although not usually in writing), but in most cases the component parts of the valuation were apparent from explicit agreements reached earlier in the valuation. In some cases, nothing was agreed other than the settlement price.

4. The same procedure also applied to instructions from the Cadogan Estate where Gerald Eve were responsible for the entire valuation until in 1985 WA Ellis were instructed to undertake a similar role to that which John D Wood & Co fulfilled for the Grosvenor Estate.

5. The schedule comprised settlements reached by both the Grosvenor and Cadogan Estates. It was shared with John D Wood & Co and also the

valuers acting on behalf of leaseholders. All the Grosvenor cases were settled by negotiation until 1995 when a dispute over a collective enfranchisement price was heard by the Leasehold Valuation Tribunal. Grosvenor were disappointed by the LVT's decision on relativity and they decided to publicise more widely the relativities (without Act rights) that they would generally expect to see in enfranchisement price settlements. Mr Pope of John D Wood & Co was asked to produce relativities at five year intervals of unexpired lease term which could be defended before the LVT or the Lands Tribunal. Mr Pope's relativities were generally a little higher than those contained in the schedule of settlements. Mr Pope discussed a table of such relativities with Mr Macpherson and it was agreed that the relativities for unexpired terms of between 20 to 35 years were too low and should be increased.

6. Mr Macpherson said that he and Mr Pope eventually produced a table of relativities at 5 year intervals which was converted into a graph by the Gerald Eve drawing office and became the John D Wood & Co (1996) and Gerald Eve Graph. The Grosvenor Estate made the graph available to anyone asking for it from October 1996 onwards. When Mr Pope left John D Wood & Co in 2000 that company wrote to the Grosvenor Estate and asked to be dissociated from the graph.

7. The settlement schedule has been maintained and enlarged over subsequent years. Mr Macpherson said that the more recent settlements reached by Gerald Eve generally supported the pattern shown by the original 1996 graph and although the graph has been constantly reviewed it has not been changed.

8. Mr Pope agreed with Mr Macpherson's account of the preparation of the graph in 1996. He reiterated that the graph showed higher relativities than were recorded in the schedule of settlements. He thought that the Grosvenor Estate had achieved relatively favourable settlements and the Estate said it wanted a graph that was realistic and not avaricious. Mr Pope's view about the graph had not changed over the years and he still considered it to show the appropriate relativities.

9. Mr Clark gave further details of Gerald Eve's clientele and about the construction and use of the Gerald Eve graph. He said that the firm's principal leasehold enfranchisement work was for the major central London estates, including Grosvenor's Belgravia and Mayfair Estates (since 1973), the Cadogan Estate (since 1976) and the Howard de Walden Estate (since 1982). Until recently it had also acted for the Ilchester (Holland Park) Estate (1992-2014).

10. Mr Clark first dealt with leasehold reform claims in 1994 and from the start it had been his firm's practice to record details of the settlements. He explained that the responsible valuer would keep a detailed copy of his valuation on a dedicated estate file and record the main elements of the valuation in a settlement schedule for that estate. Separate schedules were kept for house claims under the 1967 Act depending upon whether the

basis of valuation was section 9(1) or 9(1A). After the Leasehold Reform, Housing and Urban Development Act 1993 ("the 1993 Act") settlements of house claims under section 9(1C) were recorded on the same schedule as section 9(1A) settlements. New schedules were produced for lease extensions of flats under Schedule 13 of the 1993 Act and for the collective enfranchisement of blocks of flats under Schedule 6. For the past 10 years settlements had been recorded when the transaction was completed rather than when the settlement was agreed. Mr Clark described the settlement schedules as "working documents, to which additions are made as new claims settle."

11. As at July 2015 the schedules comprised records of 3,404 settlements of house enfranchisements (1,249) and lease extensions (2,155) and 170 records of the collective enfranchisement of blocks of flats. These records included determinations by the LVT/First-tier Tribunal and the Lands Tribunal/Lands Chamber where valuers from Gerald Eve had given expert evidence. The settlements only included data where Gerald Eve had been directly involved. Mr Clark adduced copies of all of the settlement schedules (including the collective enfranchisement data). Every settlement shown in the schedule was supported by a hard copy of the corresponding detailed Gerald Eve valuation.

12. In 2007, following a request from the Lands Tribunal in Arrowdell Limited v Coniston Court (North) Hove Limited [2007] RVR 39, the RICS established a working party to consider whether standard graphs of relativity could be produced. Gerald Eve was invited to participate and Mr Clark provided details of the Gerald Eve graph to the RICS. In a letter to the RICS dated 7 December 2007, Mr Clark said that the data on which the graph was based included:

    (a) settlements between 1974 and 1996 of prices for enfranchisements and lease extensions under the 1967 Act and the 1993 Act;

    (b) prices realised on the sale of leases without rights, that were used as comparables during negotiations concerning the claims in (a) above;

    (c) prices realised on the sale of freeholds with vacant possession, that were used as comparables during negotiations concerning the claims in (a) above and

    (d) opinion.

13. Mr Clark provided further details in autumn 2008 at the request of the RICS by way of a pro-forma response sheet which was then incorporated into the RICS Report "Leasehold Reform: Graphs of Relativity" published in October 2009. In the further response, Mr Clark said that the graph had been reviewed in the light of continuous challenges during negotiations and before the LVT and Lands Tribunal. It had not been amended "because it is believed that the evidence that was available then is stronger than that which has emerged since 1996." He went on to say that "it is

considered that there is no reason for relativity to have changed over time."

14. Mr Clark explained that there were 246 pre-1996 claims which formed the basis of the 1996 graph. He had traced files in respect of 109 of these claims with dates ranging from 1974 to 1994. An examination of the files showed that parts of the valuations were agreed between the parties in 46 cases. In 38 of those cases the relativity was below that predicted by the Gerald Eve Graph; in two cases the relativity was the same or virtually the same as the graph; and in the remaining six cases the relativity was above the graph.

15. In a written response to questions from counsel about the 246 settlements Mr Clark said that 35% of the settlements were for unexpired terms of 20 years or less, 11.4% were for unexpired terms of 60 years or more and none of them were for unexpired terms greater than 80 years. Mr Clark further explained that the relativities produced by Mr Macpherson and Mr Pope were taken at five yearly intervals and that the Gerald Eve graph simply joined up the relativity points.

16. Mr Ryan said that after the 1993 Act he had "worked to a rough guide" as to the uplift in value attributable to the benefit of the Act. He found that the application of this rough guide gave results that were closer to the Gerald Eve Graph than to any other graph then in use. They were sufficiently close for Mr Ryan to adopt the Gerald Eve Graph for the purpose of calculating the without Act rights relativity in most cases.

17. Mr Hollamby said that at the time the Gerald Eve Graph was produced he could not find any evidence to support it and he thought that the relativities that it produced were too low and were skewed in favour of the freeholder. He said this was particularly pronounced in leases where the unexpired term was for 50 years or less. Because of this Mr Hollamby said that he did not rely upon the Gerald Eve Graph, even when acting for landlords.

18. In 1999 Mr Hollamby joined John D Wood & Co and acted almost exclusively for leaseholders. He was unable to find the relevant John D Wood files to support the Gerald Eve Graph and was unsuccessful in his requests for the same to Mr Pope and Mr Macpherson. On 9 March 2000 Mr Hollamby wrote to the Grosvenor Estate and told them that the 1996 graph no longer had the support of his firm and he requested that their name be removed from it. At that time he prepared his own relativity graph ("the JDW Graph") and wrote to other valuers acting within prime central London seeking details of their settlements. He used the data that he received together with John D Wood & Co's own data, that of his previous firm, Chestertons, and evidence from LVT decisions to produce a spreadsheet of 650 analysed cases. That became the JDW Graph which had a relativity line that closely followed the line of LVT decisions.

19. Mr Shingles gave evidence of negotiations he had undertaken in 1991 with the Cadogan Estate for lease extensions of flats at Tedworth House,

Tedworth Square, London SW3, one of which (Flat 2) he owned. He compared the results of these negotiations for the extension of leases that had unexpired terms of 11.75 years (averaging a relativity of 50.77%) with the Gerald Eve Graph for the same unexpired term (28.5%) and other graphs (average of RICS graphs 32.29%). He concluded that the Tedworth Square transaction showed that freeholders adopted a much higher rate of relativity pre-1993 than was suggested by "whatever data was used to compile the Gerald Eve Graph." Mr Shingles said that the Gerald Eve graph had had the effect of anchoring relativity values.

2. Knight Frank ("KF") Graph

20. Mr Jeremy Dharmasena MRICS, a partner and Head of the Leasehold Reform Department in Knight Frank LLP, gave evidence about this graph.

21. Mr Dharmasena explained that there were two versions of the KF Graph. The original graph was prepared in 2009 as part of the RICS working party deliberations and a revised version was published in June 2011. The graphs were based on schedules of enfranchisement and lease extension settlements (from 2002 onwards) agreed between Knight Frank and the valuers acting for the other party. The 2009 graph also included analyses of LVT and Lands Tribunal decisions involving Knight Frank. The settlement schedules recorded details of the individual elements that made up the price/premium calculated in accordance with either the 1967 Act or the 1993 Act. The relativities were therefore those applicable without Act rights. The graphs were drawn before making adjustments for onerous ground rents.

22. Settlements of more than 200 flats and houses formed the basis of a table of relativity percentages between 0 and 100 years set out in five yearly intervals together with a corresponding graph (the 2009 KF graph) that was submitted to the RICS in September 2008. The schedule was updated subsequently and a revised version of the graph, based on 350 settlements, was published in June 2011.

23. Mr Dharmasena explained that the 2011 KF graph excluded LVT (but not Lands Tribunal) decisions and included data from "a major landlord estate client" who instructed Knight Frank on 1 January 2010. The revised graph also included data from older settlements where the information had not been retrieved in time for the RICS research in 2009. The revised graph had been made publicly available since June 2011.

24. Mr Dharmasena said the most significant difference between the two graphs was that the table of relativities in the 2011 version was derived from a graph which was automatically created by the best fit Excel polynomial formula.

3. The WA Ellis Graph

25. Evidence about this graph was given by Mr James Wilson MRICS, FCIArb, a director of Jones Lang LaSalle since its merger with WA Ellis

in October 2014. Mr Wilson previously worked for WA Ellis for 19 years, for the last 11 of which he was a partner. Mr Andrew McGillivray, formerly a partner at WA Ellis and a co-author of the WA Ellis index of relativities, was also called to give evidence.

26. Mr Wilson said that WA Ellis prepared an index comprising a schedule of relativities as at January 2001 for unexpired lease terms in five yearly intervals from five to 100 years. Mr Wilson explained that the index was derived from the opinion of three partners at WA Ellis: Mr McGillivray, Mr Michael Duncan and, to a lesser degree, Mr Graeme Scott-Dalgleish. The index did not summarise or plot a series of settlement or transaction points. The partners' opinions about vacant possession values were based on transactions said to be "uncorrupted by actual or potential rights" under the 1967 Act and the 1993 Act.

27. The schedule of relativities was based on transactions of approximately 200 houses, equally divided between freehold and unenfranchiseable leasehold sales. The relativities were calculated by reference to matched pairs of sales in a similar location, one freehold and one leasehold. The data was collected between the mid-1980s to January 2001.

28. WA Ellis did not produce the graph which appears in the RICS Research Report. The data was converted into a graph by the RICS. Mr Wilson said, and Mr McGillivray agreed, that there was an atypical shift in the graph between 10 to 15 years which he attributed to the analysis of the data from the Trevor Estate where for a time the only interests granted by the freeholder were for 20 year terms.

4. The Cluttons Graph

29. Mr Einar Roberts, a partner in Cluttons LLP, gave evidence about the construction of this graph with which he was personally involved.

30. Cluttons only recorded settlements for properties in St John's Wood where they acted in particular for the Eyre Estate and John Lyon's Charity. They produced separate graphs for flats and houses because they considered St John's Wood to be more prime for houses than for flats. Mr Roberts explained that in tribunal cases Cluttons would provide the data as a series of points without fitting a curve to them. They would usually seek a determination by reference to an average of the settlements plus or minus one to three years either side of the unexpired term of interest. Insofar as Mr Roberts had ever ascribed a curve to the data points he had done so using a polynomial curve function available in Excel.

31. The individual data points were shown as a scatter graph in Mr Roberts' evidence and were supported by detailed schedules of settlements. Mr Roberts emphasised that the relativities shown were the result of Cluttons' own analysis and were not necessarily agreed by the counter-party valuers. The data as provided to the RICS excluded any settlements involving onerous ground rents. The curve lines shown in the RICS Research Report were apparently not produced by reference to a regression analysis.

5. John D Wood & Co Graph

32. Mr Hollamby explained that John D Wood & Co dissociated itself from the John D Wood & Co (1996) and Gerald Eve Graph in 2000. It then produced its own graph although this was not submitted in evidence by Mr Hollamby. He explained that it was based upon "a spreadsheet consisting of 650 or so of analysed PCL cases".

33. In his response to Mr Hollamby's evidence Mr Roberts produced a letter dated 2 June 2004 from Mr Hollamby to Mr Damian Greenish of Pemberton Greenish enclosing a copy of John D Wood & Co's (then) latest graph and providing details of its construction. The graph was said to have been compiled from a combination of open market transactions, settlements and tribunal decisions. The earliest valuation date was 1978 and the graph was said to be continually updated. It included both flats and houses. The data set comprised 642 cases. Mr Hollamby did not include "the hundreds" of Gerald Eve settlements because he thought that would distort the graph. Of the 642 cases, 298 were settlements reported by agents who usually represented leaseholders, 202 were settlements reported by agents who usually represented freeholders and the remaining 145 cases were tribunal decisions. (The total came to 645, but some cases were reported by two parties; the actual total was 642 different cases, details of which were contained in a spreadsheet.) Each of these three types of case was plotted as a separate line on a graph together with a composite curve.

34. In his letter Mr Hollamby said that he had adjusted for onerous ground rents "by adding the value of the landlord's rental income onto the value of the tenants' existing interest". During cross-examination he was referred to a number of entries on his spreadsheet where he had used improved values rather than unimproved values when calculating relativity. He acknowledged that he might have made a mistake but considered it likely that this was how the settlements had been reported to him.

35. The version of the John D Wood graph that appears in the RICS Research Report is an updated version of the 2004 Report. By this time (2008) there were over 930 cases in the database although the time spread of the data had apparently not changed (1978 to 2004). The data comprised settlements (75% acting for the tenant) and tribunal decisions.

36. Mr Wyatt referred to a further update of the John D Wood & Co graph which first appeared in a working paper on relativity graphs published in June 2011. It was later published by John D Wood & Co in September 2011 as "The Pure Tribunal Graph" and was based on 601 LVT and Lands Tribunal decisions from "the London Region". It was described as forming "an important consensus between the more subjective graphs available" and was presented as "a natural and pragmatic solution to dealing with the issue of relativity." The Pure Tribunal Graph produced lower relativities than the 2008 graph for the lease term range 0 to 70

years, higher relativities from 70 to 95 years and equal relativities thereafter.

6. Charles Boston Graph

37. Mr Stimson gave evidence (through Mr Fielding) about this graph. Mr Stimson wrote to Mr Charles Boston FRICS in May 2015 asking for details of how the Charles Boston graph was compiled. Mr Boston agreed to provide this information.

38. The graph is based upon negotiated settlements undertaken personally by Mr Boston and not by his other partners. Mr Boston gave details of 269 settlements that he had reached between August 1986 and March 2015 (the corresponding number as at October 2009 was stated in the RICS Research Report to be 120). The unexpired lease terms ranged from 0.5 years to 123 years,. The settlements were mainly in respect of prime central London properties. The line of the graph was plotted using a sixth order polynomial.

7. College of Estate Management ("CEM") Graph

39. Mr Wyatt was asked how he would determine relativity if the Parthenia model was not accepted by the Tribunal. He rejected the use of the prime central London graphs contained in the RICS Research Report since "by reason and logic" if the Tribunal were to reject the Parthenia model it would have to reject those graphs also. He thought that "there may be a slight premium for a property to have the option to extend the lease or buy the freehold when compared to a property without the right." But he did not believe that it was appropriate to make a deduction from the price paid for a lease with Act rights to reflect the benefit of the Act because that price was itself determined by reference to existing graphs of relativity and therefore the analysis would be circular.

40. Mr Wyatt turned instead to "the theoretical approach" of the College of Estate Management in their report "Relative Values: Valuation for Lease Extension and Enfranchisement" published in August 2000. The Report was commissioned by the then Department of the Environment, Transport and the Regions and aimed to explore the scope for prescribing key valuation factors such as relativity.

41. The Report concluded that market data showed that "relativity patterns are difficult to pick out clearly" but said that two relativity indices could be constructed from LVT decisions: one for Inner London and one for the rest of England and Wales.

42. These indices were derived from a statistical analysis of LVT decisions and were indexed to base 100 at 90 years which CEM said was "the de

minimis cut-off point for marriage value." Appendix J of the CEM Report gave the full relativity indices together with a table of relativities where the results are not based to 100 at 90 years but are continued to 999 years. Thus the relativity for an unexpired term of 41 years for Inner London LVT cases is 76.34% whereas the Inner London index figure for the same unexpired term (i.e. based to 100% at 90 years) is 79.71%.

43. CEM said the following about the LVT evidence at page VII of its executive summary:

"Given an imperfect market, and the fact that there is no alternative, available data, our conclusions on relativity rest on the assumption that LVTs have been accurate in reflecting available market evidence within their relativity figures. However this must be set against the fact that the LVT process has been questioned and concerns expressed over whether the LVT decisions always produce a correct valuation."

44. Mr Wyatt described the CEM research as having "used an objective, but hypothetical approach which is far superior to the fundamentally flawed analysis of the opinion-based relativity curves or trying to make arbitrary adjustments with post-Act sales."

45. Mr Wyatt said that the relativity of Flat 5, using the relativity in the CEM Report, was 80.09%.

8. The Savills Enfranchiseable (2002) Graph

46. In Spring 2003 Savills published a research report entitled "The Impact of Leasehold Reform on the Prime Central London Residential Market". It included the results of research undertaken in 2002 into the values of leasehold property in central London. The key element of the project was obtaining open-market valuations for 240 leasehold properties of varying lease length in prime central London (broken down into 10 sub-market areas). For each of the properties in the sample Savills collected sufficient data to enable a desk-top valuation to be made. They then invited a number of valuers (from 12 firms as well as from Savills) to provide three different valuations for a sample of 10 properties each under a standard set of requirements:

(i) the open market value at the stated lease length assuming an enfranchiseable lease;

(ii) the open market value at the stated lease length assuming a non-enfranchiseable lease; and

(iii) the freehold value.

47. The results were collated and a regression analysis undertaken to produce a table and graph showing relativities with Act rights (i.e. for enfranchiseable leases).

9. The Savill's enfranchiseable (2015) Graph

48. Mr Christopher Buckle MSc, MPhil, MA, MRICS, an associate director in Savills Residential Research Team gave evidence about this graph which appeared in a Savills research report entitled "Leasehold Relativity: Analysis of The Real World" dated 11 September 2015.

49. Mr Buckle explained that the research was an analysis of current market transactions, using hedonic regression, to give an estimate of the relativity of leases with Act rights. The data was obtained from LonRes and comprised 10,887 transactions between 2010 and 2015. Five hedonic models were produced, the first three of which followed Mr Wyatt's approach when constructing the Parthenia model. Mr Buckle's preferred model was Model 5 which analysed 5,904 leasehold flat sales.

50. The functional form of the graph curve (relativity = $1 - a^x$, where a is a constant and x is the unexpired term) was such that it could only show increasing relativity for higher lease lengths and had an asymptote at 100%. (Mr Buckle also identified an alternative functional form which had an intercept term, i.e. the relativity for a lease with zero years unexpired may not be zero.)

51. The starting point for the research was the approach taken in the Parthenia model and in his evidence Mr Buckle described the hedonic variables that he had used compared with those adopted by Parthenia. The results of the first four of Savill's models highlighted potential multi-collinearity problems, with the most significant being attributed to the fact that the majority of freehold properties were houses and almost all the flats were leasehold. The purpose of the fifth model was to look at flat sales only and thereby avoid this multi-collinearity problem. Model 5 also excluded the variable for onerous ground rent.

52. A comparison of Savills Model 5 with the Parthenia model showed that all of the Model 5 point estimates were lower than the Parthenia point estimates for leases with unexpired terms under 65 years. The curve fitted to the Model 5 point estimates (for leases with rights under the 1993 Act) followed the shape of the Gerald Eve curve (for leases without rights under the 1993 Act) very closely between 10 and 80 years unexpired term, albeit at a slightly higher level.

53. The Savills 2002 graph had a logarithmic functional form and so a direct comparison between that graph and the 2015 hedonic regression version was not appropriate. The relativity point estimates for Model 5 (based on transactions) were similar to those of the 2002 model (based on opinions) at longer lease lengths but were lower at shorter lease lengths.

Discussion

54. The only one of the nine graphs considered above that is directly based upon transactions is the Savills Enfranchisable (2015) Graph ("Savills

2015 graph") which was produced specifically to be part of the Wellcome Trust's evidence in relation to Flat 5.

55. We will first discuss the Savills 2002 graph and the Savills 2015 graph, both of which concern leases with rights under the 1993 Act. We will then discuss the other graphs and, in particular, the GE graph, which concern leases without rights under the Act.

56. Like the Parthenia model, the Savills 2015 graph is based upon hedonic regression and like that model it was the subject of technical criticism which led Mr Buckle to submit a supplementary report in which he acknowledged that all five of his models failed both the Box-Cox test and the Ramsey RESET test. The Savills 2015 graph was also based upon transactions that reflected the benefit of the Act and so could not be used to estimate leasehold relativity on the statutory basis without further adjustment. But what the Savills 2015 graph shows is that almost all of its (with Act rights) point estimates are lower than the (without Act rights) point estimates in the Parthenia model for unexpired lease terms less than 65 years. If the Savills 2015 graph were reliable, this would provide further support to our conclusion that the Parthenia model cannot be used to estimate relativities for leases without Act rights at the valuation dates, all of which fell within the latter part of Savills' data collection period between 2010 and June 2015.

57. Mr Rainey submitted that the Savills 2015 graph was unreliable because the transactions (concerning leases with rights under the 1993 Act) upon which it was based reflected the embedded use of graphs, and in particular the GE graph, in the market. It was agreed by the valuation experts that the price payable for an existing lease was influenced by the amount arrived at by deducting the estimated cost of the lease extension from the long lease value. The estimated cost of the lease extension requires as an input the value of the existing lease without rights under the 1993 Act (in order to calculate marriage value); so it is necessary to assume, by the use of graphs, that which it is desired to estimate. The process is circular. We also note that the figure which is arrived at, simply by deducting the premium from the value of the extended lease, assumes that the vendor of the existing lease will receive all of the lessee's 50% share of marriage value. We are not satisfied that this will always be the case. The process would be no less circular if one were to use the relativity derived from the Parthenia model when estimating the cost of the lease extension rather than the relativity found from the GE graph.

58. If market transactions involving leases with rights under the 1993 Act relied exclusively on the relativities shown by the GE graph, then there would be no reason for relativities for leases with rights under the 1993 Act to have changed between 2002 and 2015 (the dates of the two Savills enfranchisable graphs) since the GE graph has not changed over that period. Nonetheless, a comparison of the Savills 2002 graph and the Savills 2015 graphs does suggest that there has been a change in relativities for leases with rights under the 1993 Act. This may be due to

either the difference in the methodology of construction of the Savills 2002 and 2015 graphs, or a real change in relativity in the market. Any such market change is not reflected in the GE graph; this would suggest that the GE graph is not relied upon by the market to quite the extent which has been suggested (although we do accept that the market has been influenced by the GE graph).

59. At the valuation dates, the Savills 2002 graph was in common use by valuers to determine the FHVP value of a property from transactions concerning leases with rights under the 1993 Act, being the only one of the graphs then current that showed relativities for such leases. That graph relies upon neither transactions nor settlements but is based solely upon the subjective opinions of a panel of valuers. We consider the Savills 2015 graph to be a significant improvement on its 2002 equivalent, being based upon recent market transactions which have been objectively analysed, albeit subject to technical criticism. But the Savills 2015 graph was not available at the valuation dates and could not have affected the market's approach to the assessment of relativity at that time.

60. When we discussed the criticisms which have been made of the Parthenia model, we discussed the evidence that the market forces at the relevant valuation dates in 2014 were different from the market forces in the period (1987–1991) which was used to provide the data for the Parthenia model. That evidence is summarised at paragraphs 28 to 32 of Appendix B. That evidence would suggest that the relativities for leases with rights under the 1993 Act might well have changed in the period from 2002 to 2014 or 2015; in particular, the suggestion would be that relativities have moved downwards during that period. Indeed, a comparison of the Savills 2002 graph and the Savills 2015 graph tends to support that suggestion.

61. We will now consider the other graphs, all of which concern leases without rights under the 1993 Act.

62. We are satisfied that the GE graph was the graph which was in most common use at the valuation dates for leases without rights under the 1993 Act. It was certainly used by valuers for the purpose of negotiating the relativities for leases without rights under the 1993 Act. Further, as already explained, it did influence the market for leases with rights under the 1993 Act to the extent that the parties to transactions for such leases wanted to calculate the likely amount of the premium payable for an extended lease.

63. To all intents and purposes the GE graph was the industry standard. Parties may have referred to other graphs but they were unlikely to have ignored the GE graph. The graph was first produced in 1996 and was based on 246 settlements in respect of leases without rights under the Act, which were then adjusted subjectively by Messrs Macpherson and Pope. Since that time Gerald Eve have continued to maintain schedules of settlements (by July 2015 there were 3,404 such records excluding collective enfranchisements) but they have not altered the original 1996 relativities. In their submissions to the RICS working party in October

2008 Gerald Eve said that there was "no reason for relativity to have changed over time". But in an earlier letter to the RICS dated 7 December 2007 Gerald Eve (and from the reference presumably Mr Clark) said that the exclusion of hope value following the Court of Appeal decision in Sportelli and the reduction of the deferment rate to 5% were factors that meant that "the relativities shown by the [GE graph] may be said to be overstated". Since that time a further material factor has been a sustained climate of low interest rates. We have seen no convincing reason why the relativity of leasehold to freehold value should be considered immutable.

64. The evidence discussed in paragraphs 28 to 32 of Appendix B and the Savills 2015 graph suggest that the GE graph may indeed now overstate relativities for leases without rights under the 1993 Act, as Mr Clark had previously anticipated. The relativities shown in the Savills 2002 graph (to the extent that they are reliable) are all higher than their equivalents in the Savills 2015 graph which means the gap between the with Act rights relativities in the latter graph and the without Act rights relativities in the GE graph has narrowed. (Beyond 75 years unexpired term the Savills 2015 graph gives lower relativities than the GE graph which is anomalous.) However, we have seen no evidence to suggest that there has been a reduction in the benefit of the Act rights which might explain the narrower differential between the graphs.

65. The GE graph is based upon a limited number of 246 settlements, details of 109 of which are still available. The relativities were expressed in five yearly intervals and were not all directly based on those settlements but were adjusted upwards subjectively by Messrs Macpherson and Pope. The relativities were only indirectly based on transactions (which would have informed the settlements). There was no evidence of any settlements of leases with unexpired terms of over 80 years and over a third of the settlements were of leases with unexpired terms of 20 years or less. Onerous ground rents were not excluded. The line of the graph was produced by Gerald Eve's drawing office on an unspecified basis. In our view the graph was to a large degree based upon subjective, albeit informed, opinion directed to the particular requirement of the Grosvenor Estate to espouse what it considered to be "defensible" relativities. Its predominant use in the market does not seem to us to depend upon the robustness of its methodology or its pre-eminence as a graph; rather it is due to its being the first of its kind and the most familiar to practitioners.

66. Mr Rainey submitted that the adoption of the GE graph amounted to significant "anchoring bias" and "confirmation bias". We understand those terms to have been used colloquially rather than in any formal psychological sense. We accept that the GE graph has had a very significant effect on settlements. Mr Buckle produced supplementary evidence containing graphs of the settlements provided in the appendices to Mr Clark's witness statement. These plotted each settlement point's percentage variation from the GE graph (taken as 0%) on the vertical axis against the year of settlement along the horizontal axis. Before 2000 there is considerable variation around the GE graph, but thereafter the variation

reduces noticeably, an effect which is particularly pronounced in the Schedule 13 flats settlements graphs. This suggests to us that there is a real effect at work and that valuers have indeed come to rely upon the GE graph as Mr Rainey submitted. We also consider that the GE graph has influenced (but not to the same degree) market transactions involving leases with rights under the Act.

67. Of the remaining six graphs that were considered at the hearing we gained no assistance from the CEM graph which Mr Wyatt adopted as his alternative to the Parthenia model. There was no evidence that either he or any other valuer had used this graph in negotiations. It was ultimately based solely upon LVT decisions which the researchers acknowledged may not always produce a correct valuation. We do not accept Mr Wyatt's description of this research as being objective and far superior to the other graphs.

68. There have been several versions of the John D Wood & Co graph over the years including the latest in 2011 known as the Pure Tribunal Graph and which Mr Wyatt said he used while Head of Valuations at that company. That graph is heavily dependent upon LVT decisions and, as with the similar CEM graph, we do not gain assistance from it. The 2004 version of the John D Wood graph, which Mr Ingram-Hill said "was supported up to 2008", was criticised for its treatment of onerous ground rents and for using improved rather than unimproved values. That graph is apparently no longer shown on the John D Wood & Co website and seems to have been superseded by the Pure Tribunal Graph.

69. The WA Ellis graph was produced by the RICS from an index of relativities at five yearly intervals which represented the opinion of three of that firm's partners about matched pairs of transactions. It is not known how the RICS fitted the curve of the graph to the adopted relativities. The index of relativities was not a summary of without Act rights settlements or transactions but reflected the partners' subjective views. Unlike other graphs the WA Ellis graph does not appear to have been updated subsequently. It also has a shape that is inconsistent with that of other graphs at unexpired terms of 10 to 20 years. We do not find this graph to be useful.

70. We did not hear direct evidence from the author of the Charles Boston graph but from Mr Fielding's evidence we understand that it was the result of settlements reached by Mr Boston himself and by nobody else. Both the KF graph and the Cluttons graph were also settlement based and like all such graphs it was not clear to what extent, if at all, the relativities had been agreed by the other party. The graphs were all based on small sample sizes and each had particular problems, e.g. the Charles Boston graph was based upon the settlements of a single surveyor and would reflect any personal bias that he may have; the Cluttons relativities were based around a form of moving average rather than being depicted by a best fit curve; and the KF graph had varied over time to exclude LVT (but not Lands

Tribunal/Lands Chamber) decisions, to include data from a major landed estate and was under review again at the date of the hearing.

71. In *Kosta* the Tribunal held that a prospective purchaser of an existing leasehold interest, acting prudently, would have taken an average of the relevant graphs contained in the RICS 2009 report when assessing relativity. We have had the benefit of hearing detailed evidence about the construction and use of those graphs. From such evidence we are satisfied that at the valuation dates a prospective purchaser would not have taken an average relativity from those graphs. It is most likely that they would have referred to the GE graph first and foremost. The evidence was that the market had only started to adopt an average relativity from the graphs following the decision in *Kosta*.

72. We will take the comments in this Appendix into account when we reach our conclusions as to the value of the existing leases of Flats 3, 5 and 11 and when we express our views as to the approach to be adopted in future cases.

Dated: 10 May 2016

Mr Justice Morgan

A J Trott FRICS