



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

Case Reference : **BIR/00CT/OAF/2014/0055**

Applicants : **Mr J and Mrs S Grinstead**

Represented by : **Mr. A W Brunt FRICS of Antony Brunt and Co**

Respondent : **JGS Properties Ltd**

Represented by : **Mr K Davis FRICS**

Property : **1 Bowbrook Avenue, Shirley, Solihull, B90 4UY**

Type of Application : **Sections 21(1)(a) of the Leasehold Reform Act 1967 ('The Act') to determine the price payable under section 9(1), in respect of the tenant's acquisition of the freehold, under section 21(1)(ba) of the Act**

Tribunal : **R T Brown FRICS
Judge W J Martin**

Dated : **29 June 2015**

DECISION

Determination

1. The Tribunal determines that, taking account of the evidence adduced, our evaluation of it, using our general knowledge and experience, but not any special knowledge, the price payable by the lessee for the acquisition of the freehold interest in the property in accordance with section 9(1) of the Leasehold Reform Act 1967 as amended is **£7027.75**.

Reasons for Decision

Introduction

2. The right of the Applicants to acquire the Freehold interest in the subject property and that the valuation should be pursuant to section 9(1) of the Leasehold Reform Act 1967 is not disputed.

Inspection

3. The members of the Tribunal inspected the subject property on 27 April 2015 in the presence of Mr Brunt and Mr Grinstead's father.
4. The property which is located some 10 miles south of Birmingham City Centre is a 1980s detached house situated on a corner plot. It has front garden and driveway leading to double in line garage and back garden. The centrally heated double glazed accommodation comprises: On the Ground Floor: Porch, hall, cloakroom (with w/c), living room, extended dining room, kitchen, breakfast and utility. On the First Floor two double (one en-suite) and two single bedrooms and bathroom (full suite).

Lease

5. The lease is for a period of 99 years from 24 June 1982 at an initial ground rent of £75.00 per annum, with a review to £150.00 per annum from 24 June 2016 and from 24 June 2049 £300.00 per annum.

Hearing

6. The hearing was held in Birmingham attended by Mr Brunt and Mr Davis. Mr N Atkinson a director of JGS Properties Ltd was also present.

Matters not in dispute between the Parties

7. Valuation Date: 28 August 2014.
8. Years unexpired at date of Notice: 67.82.
9. Entirety Value: £402,000.00.
10. Site Value Apportionment: 38.00%.
11. The matter of costs payable by the Applicant was agreed and this part of the application withdrawn at the close of proceedings.

12. If the Tribunal determines that *Clarise* (see below) should be applied then the parties are agreed that the appropriate adjustment to the entirety value is 2.50% to reflect the risks posed by Schedule 10 to the Local Government and Housing Act 1989.

Matters in Dispute

13. Capitalisation rate: Mr Brunt 6.50% - Mr Davis 6.00%.
14. Deferment Rate for the reversion: Mr Brunt says 5.50% and Mr Davis 5.25%.
15. *Clarise Adjustment*: The Applicants say there should be no adjustment to reflect the decision in *Clarise Properties Limited [2012] UKUT*.

Applicant's Case

Capitalisation Rate

16. Mr Brunt in support of his conclusion referred the Tribunal to two decisions, which he admitted were not binding on the current Tribunal, namely: *108 Edmond Road Alum Rock* - BIR/00CN/OAFD/2014/0005 and *9 Church Road* - BIR/47UK/2012/0011. In the first case the ground rent was a modern rent of £1,155.00 per annum (and subject to review) and in the case of *9 Church* subject to a commencing rent of £30.00 and fixed reviews to £60.00, £90.00 and £120.00 per annum.

Deferment Rate

17. Mr Brunt contends for a deferment rate of 5.50%.
18. He referred the Tribunal to the history of the *Sportelli* decisions (*Earl Cadogan and Another v Sportelli and Another* [2006] LRA/50/2005), The *Kelton Court* decision (*Zuckerman and Others v Trustees of the Calthorpe Estate* LRA/97/2008) and more recently the decision in *7 Grange Crescent (Sinclair Gardens Investments (Kensington) Ltd* [2014] UKUT 78 (LC). In the last case the subject property was a 2 bedroom maisonette and the rate determined was 5.50%. Mr Brunt said he was not confident in following this decision because of the residual liability for estate management
19. In negotiations with other chartered surveyors in Sutton Coldfield and Solihull he had in a number of cases agreed 5.75% in respect of maisonettes.

Clarise Adjustment

20. Mr Brunt agrees that in certain cases the *Clarise* adjustment should be used but not in this case.
21. In his opinion, valuing a reversion some 50 years after the term date looks precarious and further some suggest that if the adjustment is less than 5.00% it should be ignored.
22. Mr Brunt says that he cannot accurately prescribe a value to the adjustment as a 'stand alone' item. The reason for this is that these statutory valuations are so far away from reality, that another addition which further dissects the Freeholders constituent parts making up the freeholder's compensation is to be accepted and even made welcome.

23. The more remote an element of value the less it can be relied upon as providing a sound contributory factor to the end result. A lot of things could change over the next 118 years.

Respondent's Case

Capitalisation Rate

24. Mr Davis contends for a rate of 6.00%.
25. Mr Davis bases his conclusions on the contested case of *25 Inchford Road* BIR/000CT/OAF/2007/0098 where the Applicant sought 6.50% but the Tribunal determined 6.00% (on appeal to the then Lands Tribunal the appeal was rejected). Further in the contested case of *6 Trajan Hill* BIR/44UB/OAF/2014/0029 (where Mr Brunt represented the lessee) 6.00% was determined.

Deferment Rate

26. After consideration of the *Sportelli* decision (above) Mr Davis contends for 5.25%.
27. The rate determined in *Sportelli* (above) was 4.75%. The current rate adopted by the Birmingham FtT is 5.50% after applying an additional 0.75% to reflect poorer growth outside the PCL (*Kelton Court* above).
28. Currently the same deferment rate applies to Flats, Maisonettes and Houses and this cannot be right.
29. In reaching 5.25% Mr Davis puts forward the following arguments:
30. Property values on this estate have increased substantially since 2004, whereas values in *Kelton Court* have shown little or no movement. Examination of the Land Registry data for 2004 to 2015 shows house prices in Solihull increasing at approximately 16.78% per annum whereas flats in Birmingham only show an increase of 5.5% per annum.
31. Mr Davis said in his personal experience there is a clear difference in responsibilities between the management of houses, maisonettes and flats.
32. In *Mansal Securities Ltd* LRA/185/2007 Mr Rose said at paragraph 22:

'the final component of the deferment rate was the risk premium, or the additional return required by investors to compensate for the risk of not receiving a guaranteed return. The Tribunal concluded that in forming an overall assessment of the premium, which would be required by investors and the type of asset it was considering, it was necessary to have regard to the individual components of the risks of investment in long reversions. These were volatility, illiquidity, deterioration and obsolescence. Of these components, the Tribunal concluded that the physical deterioration and obsolescence were factors that were required to be reflected in the generic deferment rate to the extent that the risk related to them was common to all residential property viewed in the long term'.

33. Volatility: Mr Davis said that that whilst there were up and downs in the market it was his experience that investors are keen to acquire freehold ground rents, lock them away and let them accumulate value.
34. Liquidity: The freehold of a house can be sold immediately compared to a maisonette/flat which is subject to Section 5 of the Landlord and Tenant Act 1987 Notice which can delay a sale between 2 and 4 months. In Mr Davis's experience there is a great demand for ground rents on houses and flats.
35. Deterioration: In paragraph 23 of *Mansal* Mr Rose said:

'Mr Davis's view that there was an argument for a lower deferment rate under Section 9(1), because a site was not subject to obsolescence in the way that a house was and less likely to deteriorate than a house. I think Mr Davis is right on this point'.
36. Obsolescence: This is a piece of land which is unlikely to be affected by flooding or coastal erosion and unlike a house or a flat it will not deteriorate.
37. Mr Davis referred the Tribunal to the Welsh case of *22 Mervyn Way Pencoed, Bridgend CF35 6JH LVT/0031/10/1422*. The Tribunal in that case adopted a deferment rate of 5.00% and a 3 stage calculation.

Clarise adjustment

38. Mr Davis's made reference in his witness statement to the move away from a 2 stage valuation to a 3 stage valuation following the decision in *Clarise*. Since that decision he had adopted the 3 stage approach in all valuations regardless of the term unexpired and this had not been challenged by opposition valuers.

The Tribunal's Deliberations

39. The Tribunal considered all the oral and written evidence submitted by the parties and summarised above.

Capitalisation Rate

40. The Tribunal noted the cases referred to and reminds the parties that it is not bound by its own previous decisions and that of the Welsh leasehold Valuation Tribunal. The decision reached in *108 Alum Rock Road* was made without the benefit of expert evidence. The decision in *Church Road* was reached in the light of the significant site difficulties.
41. The Tribunal is not persuaded on the evidence before it that the rate should be increased and accordingly determines the Capitalisation Rate at 6.00%.

Deferment Rate

42. In *Earl Cadogan and Another v Sportelli and Another (2006) LRA/50/2005* and related cases valuers have defined the deferment rate as the "annual discount applied, on a compound basis, to an anticipated future receipt (assessed at current prices) to arrive at its market value at an earlier date" (Sportelli paragraph 2).

43. For many years the Midland LVT used, by convention, 7% for houses being valued under section 9(1) and 9(1A) of the Act. However in *Arbib v Earl Cadogan (2005) LRA/62/2004* the Lands Tribunal, in making its decision reminded LVTs those rates should not be established by convention.
44. In *Sportelli* the Lands Tribunal determined what they referred to as a generic deferment rate of 4.75%. This was endorsed by the Court of Appeal in *Cadogan and Another v Sportelli and Another (2007) EWCA Civ 1042*.
45. The Lands Tribunal in *Mansal* concluded that the correct deferment rate for section 9(1) was 5.00%. In considering the elements of that rate, the risk free element and the growth rate are the same under section 9(1) as 9(1A) of the Act but the risk premium is increased by 0.25% to 4.75% (and so the deferment rate rises to 5.00%) because the reversion under Section 9(1) is to a ground rent only which increases volatility and illiquidity.
46. In *Zuckerman* (above) the Lands Tribunal adopted 6%. Additions for the management of flats and obsolescence are not appropriate in this case but in view of the perceived increase in the risk of not reaching the growth assumed in *Sportelli* (above) the Midland Region has adopted, on a number of subsequent occasions, a rate of 5.50%. In *Zuckerman* the Lands Tribunal concluded that the growth rate in the West Midlands region was slower than in London and that as a result 2% real growth was less likely to be achieved.
47. In *7 Grange Crescent* (above) the Upper Tribunal concluded that the correct rate for maisonettes was 5.50%. Whilst Mr Brunt does not feel confident in following this decision at present (because of the differing input with regard to estate management on this type of estate) he believes that there is no justification for changing the current rate of 5.50% for houses.
48. Mr Davis's position is essentially that 'it cannot be right' for the rate in respect of house and flats to be the same at 5.50%. He supports this contention by reference to the Land Registry indices with evidence of differing growth rates in the value of flats in Edgbaston and houses in Solihull over the period 2004 to 2105.
49. The Tribunal acknowledges the point Mr Davis makes about the difference in risk between house and flats but is not persuaded to move away from the established rate of 5.50% for the following reasons:
 - a) *7 Grange Crescent* (above) considered the risk in respect of maisonettes not houses and is not therefore persuasive evidence of risk in respect of houses.
 - b) The statistical evidence of the movement of values in houses and flats is over a relatively short period of time (approximately 10 years) compared to the analysis produced in respect of *Kelton Court* (above) where the trend of values was considered over a substantially longer period. In *Kelton Court* (paragraph 49) Mr N J Rose FRICS acknowledged that evidence over such a long period (referring to *Hildron Finance Ltd v Greenhill (Hampstead) Ltd [2008] 1ELGR 179*) where it was suggested that evidence over a 50 year period would be required was simply not available but concluded that in that part of Edgbaston (B15) there was a real

prospect that growth would be lower than in the PCL). This Tribunal is not persuaded that evidence over 10 years is a sufficient period over which to predict the future growth rate.

50. The Tribunal therefore determines the Deferment rate at 5.50%.

Clarise Adjustment

51. The Tribunal is guided by the decision of the Upper Tribunal in *Clarise* (above) particularly paragraph 36:

'We consider the time has now come to move away from the two-stage approach as the standard practice in section 9(1) valuations and to apply instead the three stage approach. As a matter of good valuation practice, where a price has to be determined, every element of value should in general be separately assessed unless there is some reason not to do so. There is now a much greater likelihood that the ultimate reversion will have a significant value than there was when the two stage approach became standard practice 40 years or more ago. There are two reasons for this. The first is that house prices, including the prices of houses that would fall to be valued under section 9(1), have increased substantially in real terms; and the second is the lower deferment rates that are now applied in the light of Sportelli. There is, we think, a real danger that applying the two stage approach as standard will in some cases lead to the exclusion of an element of value that ought to be included in the price. This is particularly so if valuers and LVT's test as the criterion for the application of a Haresign addition whether the house is 'substantial' and thus exclude any element of value in the ultimate reversion (other than that included in the capitalisation of the section 15 rent in perpetuity) where the house does not meet this ill-defined criterion. The only relevant question is whether the ultimate reversion does have a significant value. In future, therefore, we consider that the appropriate approach will be to capitalise the section 15 rent to the end of the 50-year extension and to assess the value (if any) of the ultimate reversion'.

52. The Tribunal is not persuaded by Mr Brunt's evidence that it should move away from this position. Whilst acknowledging that *'the more remote an element of value the less it can be relied upon as a contributory factor to the end result'* does not in the Tribunal's view lead to the inevitable conclusion that it should be ignored altogether. Mr Brunt's suggestions that there should be a cut of point where the 3rd stage should be ignored or that if the 3rd stage adds less than 5.00% to the end value it could be ignored are unsupported.

53. In this case the property is a substantial property on a good estate and as Mr Davis points out on a piece of land which is unlikely to be affected by flooding or coastal erosion.

54. The Tribunal is not persuaded that there is any reason to differentiate this case from *Clarise* and accordingly determines that the 3 stage valuation approach should be applied with a 2.5% (as agreed by the parties) adjustment to the entirety value to reflect the possible effect of Schedule 10 to the Local Government and Housing Act 1989.

Conclusion

55. Applying those findings to the determination, the Tribunal calculates the price payable for the Freehold as follows:

Stage 1	Term			
	Current Ground Rent		£75.00	
	YP 1.83 years @ 6.0%		<u>1.6857</u>	126.43
	Ground Rent from 24/06/2016		£150.00	
	YP 33 years @ 6.0%	14.2302		
	PV £1 in 1.83 years @ 6.0%	<u>0.8988</u>	<u>12.79</u>	1,918.52
	Ground Rent from 24/06/2049		£300.00	
	YP 33 years @ 6.0%	14.2302		
	PV £1 in 34.83 years @ 6.0%	<u>0.1314</u>	<u>1.8698</u>	560.95
Stage 2	1st Reversion			
	Entirety Value	£402,000		
	Site apportionment 38.00%	£152,760		
	Section 15 Modern Ground Rent 5.5%	£8,401.80		
	YP 50 years @ 5.5%	<u>16.9315</u>		
		£142,255.08		
	PV £1 in 67.83 years @ 5.5%	<u>0.0264</u>		3,755.53
Stage 3	2nd Reversion			
	Standing House Value	402,000.00		
	Schedule 10 @2.5%	391,950.00		
	PV £1 in 118.83 years at 5.5%	<u>0.0017</u>		<u>666.32</u>
				£7,027.75

Appeal Provisions

56. If either party is dissatisfied with this decision they may apply to this Tribunal for permission to appeal to the Upper tribunal (Lands Chamber). Any such application must be received within 28 days after these written reasons have been sent to the parties (rule 52 of The Tribunal Procedure (First-tier Tribunal) (Property Chamber) Rules 2013).

Robert T Brown FRICS
Chairman

