



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

Case Reference : LON/00BF/OLR/2022/0904

HMCTS : V: CVPREMOTE

Property : Flat 3, 8 Parkhill, Carshalton, SM5 3RU

Applicant : Vinay Durgadas Mukesh Paw

Representative : Robert Marchant MRICS

Respondent : Raj Properties Limited

Representative : Peter Gunby MRICS

Type of Application : Enfranchisement

Tribunal Members : Judge Robert Latham
Helen Bowers MRICS

Date and venue of Hearing : 18 April 2023 at
10 Alfred Place, London WC1E 7LR

Date of Decision : 24 May 2023

DECISION

The Tribunal determines that the premium payable by the Applicant in respect of the extension of his lease at Flat 3, 8 Parkhill, Carshalton, SM5 3RU is £12,452. The calculation is annexed to this decision.

Covid-19 pandemic: description of hearing

This has been a remote video hearing which has not been objected to by the parties. The form of remote hearing was V: CPVEREMOTE. A face-to-face hearing was not held because all issues could be determined in a remote hearing and no party requested a face to face hearing. The parties have provided a Bundle of Documents for the hearing extending to 1,877 pages.

Introduction

1. This is an application made pursuant to Section 48 of the Leasehold Reform, Housing and Urban Development Act 1993 (“the Act”) for a determination of the premium to be paid and the terms for a new lease.

Background

2. The agreed background facts are as follows:
 - (i) The property: Flat 3, 8 Parkhill, Carshalton, SM5 3RU;
 - (ii) The subject property is a two bedroom flat;
 - (iii) Date of Tenant’s Notice: 31 March 2022;
 - (iv) Valuation Date: 31 March 2022;
 - (v) Date of Application to the Tribunal: 21 November 2022;
 - (vi) Tenant’s leasehold interest:
 - Date of Lease: 29 September 2006;
 - Term of Lease: 99 years 24 June 2006;
 - Ground Rent: £265, doubling at each rent review (every 20 years);
 - (vii) Unexpired Term: 83.23 years;
 - (viii) Deferment Rate: 5%;
 - (ix) Freehold Reversionary Value: £330,000.

The Hearing

3. The hearing of this application took place on 18 April 2023. The Applicant, tenant, was represented by Mr Robert Marchant MRICS. The Respondent landlord was represented by Mr Peter Gunby MRICS. Both experts provided reports and gave evidence. They were cross-examined by the other party. The Tribunal asked a number of questions.
4. The sole issue between the parties is the capitalisation rate that should be adopted:
 - (i) Mr Marchant contends for a figure of 8.82% which would result in a premium of £11,847.
 - (ii) Mr Marchant contends for a figure of 6% which would result in a premium of £17,497.
5. Capitalisation is rarely the issue in dispute in respect of the premium payable for a lease extension. In the current case, the unexpired term is 83.23 years. As a result, there is no element of “marriage value” in the premium. The capitalisation is therefore a critical factor in this case, albeit that the resultant difference in the premium payable is relatively modest, namely £5,650.

The Law

6. In computing the premium payable, the Tribunal is required to determine the capitalised value of the rental income that the landlord can expect to derive from his existing lease. Many valuers have tended to adopt a capitalisation rate at the same percentage as that adopted for the deferment of the landlord's reversionary interest. As George Bartlett QC, the Chamber President, noted in *Nicolson v Goff* LRA/29/2006; [2007] 1 EGLR 84, the factors that are relevant to the determination of the capitalisation rate are so manifestly different from those that are relevant to the deferment rate that there can be no valuation rationale to justify adopting a rate for capitalisation simply because that rate is being taken for deferment. Moreover the application of the factors affecting the capitalisation rate, unlike the application of the factors affecting the deferment rate, is likely to vary in every case. However, he noted that if the ground rent is small and the unexpired term is not long, there will be no significant difference in adopting one particular rate rather than another. In that case, the experts had adopted a figure of 5% as both the deferment and the capitalisation rate. In view of the agreement between the parties, the Upper Tribunal was willing to accept this course.

7. The President identified the following factors as being relevant to the capitalisation rate:
 - (i) the length of the lease term;
 - (ii) the security of recovery;
 - (iii) the size of the ground rent (a larger ground rent being more attractive); and
 - (iv) whether there was provision for review of the ground rent and, if there was such provision, the nature of it.

8. In support of his argument that the Tribunal should have regard to market transactions where these are available, Mr Marchant refers us to the decisions of the Upper Tribunal in *Trustees of the Sloane Stanley Estate v Mundy* [2016] UKUT 223 (LC); [2016] L&TR 32, *Deritend Investments (Birkdale) Ltd v Treskonova* [2020] UKUT 164 (LC), and *Sportelli* [2007] 1 EGLR 153, where HHJ Michael Rich QC, the then President, stated (at [8]):

"We were not concerned with the other element in the value of the reversion, the ground rent and how this should be capitalised. Nothing that is said in this decision has any direct application to capitalisation rates. Market evidence should be more readily available for those, and in any event such rates, applying as they do to an element of static value, are determined by different criteria from those that are relevant to the deferment rate."

9. We have been referred to the small number of First-tier Tribunal decisions in which market evidence has been used to compute capitalisation.

However, these decisions are based on the market evidence adduced in these cases. The FTT decisions to which we were referred were:

(i) *St Emmanuel House (Freehold) Limited and Others v Berkeley Seventy-Six Limited* (CHI/21UC/OCE/2017/0025; 0026; 0029) [2017] – a figure of **3.35%** was adopted. It should be noted that the evidence from the lessees' side was limited;

(ii) *3 and 4 Observatory Way and other properties* (CHI/21UC/OCE/2019/0013; 0004; 0008; 0009; 0010; 0011 and 0012) – a figure of **6.15%** was adopted which was the average of only two reliable comparables (6.3% and 5.9%) and

(iii) *Lawrence Wharf Ltd v The Trustees of the Matliwala Family Charitable Trust* (LON/00BE/OCE/2020/0025/ 0028; 0029; 0039; 0031 and 0109) in which a figure of **6.35%** was adopted.

The Submissions of the Parties

10. Mr Marchant, for the tenant, contends for a capitalisation rate of 8.82% based on an analysis of open market transactions of similar ground rent transactions. The ground rent of the subject Flat is currently £265 per annum. This doubles to £530 in 2026 and thereafter doubles every 20 years.
11. In considering his market evidence comparables, Mr Marchant has regard to the factors identified in *Nicholson v Goff*:
 - (i) the length of the lease term – longer leases provide a more valuable ground rent asset;
 - (ii) the security of recovery – he identifies the following sub-factors: (a) size of block – a larger block is a lower risk because the income stream is better diversified; (b) age/quality/maintenance of block – a newer/higher-quality/better maintained block will present a lower risk; (c) consistency of leases – a block let with modern and consistent leases will reduce risks associated with management;
 - (iii) the size of the ground rent (a larger ground rent being more attractive); and
 - (iv) whether there is provision for review of the ground rent and, if there was such provision, the nature of it. For example, a more frequent increase (e.g., over 15 years is more attractive than every 25 years).
12. Mr Gunby ~~rather~~ prefers to rely on the rates that have traditionally been adopted for capitalisation, which he suggests have been between 6 – 7%. His starting point is *Nicholson v Goff* in which the ground rent was a

relatively nominal £50 per annum for the 25 years unexpired term. The experts had agreed that the deferment rate of 5% should also be adopted as the capitalisation rate. The President had noted that had a capitalisation rate of 7% been taken, rather than 5%, the premium of £47,023 would have been reduced by £60!

13. Mr Gunby recognises that under the subject lease, the ground rent doubles every 20 years. It will increase to £530 pa after 4 years. He accepts that the ground rent is much more desirable than in *Nicholson v Goff*. He therefore suggests a figure of 6%. He accepts that his figure is based on those conventionally used for capitalisation. It is not linked to market evidence comparables.

Decision of the Tribunal

14. The Tribunal is satisfied that we should prefer the approach adopted by Mr Marchant based on market evidence, rather than the "conventional figures" suggested by Mr Gunby.
15. Mr Marchant's team at Homehold have analysed all auction sales of ground rent assets by Allsop Residential Auctions since September 2019, up to and including the February 2023 auction. There were 706 in total. He considers that this is the best source of open market transactions of ground rent assets conducted at an arms-length. Ground rent assets, particularly smaller interests like the subject, are commonly sold at auction.
16. Mr Marchant selected sales at Allsop Residential Auctions as his source for several reasons: (i) they auction a sufficiently large number of ground rent assets to provide a diversified and reliable dataset; (ii) the auction particulars are detailed and accurate, which ensures the bidders are fully informed; (iii) as a large and reputable auction house, Allsop have a sufficient number of bidders to ensure each asset realises a fair value; and (iv) transactions from Allsop have been considered to be of assistance in other tribunal hearings.
17. Mr Marchant has excluded transactions that cannot be analysed. He notes that a potential purchaser may assign a value to different constituent parts of the asset. For example, if a freehold asset sells with two leases with 70 years unexpired and fixed ground rents of £100, a potential purchaser may assign a value to (a) the income stream associated with the ground rent payments, (b) the reversionary value and (c) the hope value of the tenants paying marriage value having exercised their enfranchisement rights. A valuer can only accurately derive a capitalisation rate from the sale transaction of a ground rent asset if it is possible to separate the value which will have been assigned to the income stream provided by the ground rent from the other constituent parts.
18. For this reason, many sales of ground rent assets are not of assistance. The

Homehold Team screened each of the transactions and excluded those where one or more of the following constituent parts could be identified: (i) Hope value associated with tenants exercising their right to enfranchise (defined as assets with leases <110 years unexpired); (ii) a high reversionary value (defined as assets with leases <110 years unexpired); (iii) Development value and/or significant undemised property; (iv) Mixed ground rent schedules (e.g., some flats sold with RPI-linked ground rents, some flats with doubling ground rents); and (v) commercial properties, houses and garages let separately to flats. He has also excluded any transactions that are not listed as “Sold” at the auction, i.e. those that may have been sold before or after. He has also excluded transactions where the tenants have exercised their rights of pre-emption. Where a potential bidder knows that the tenants have exercised their pre-emptive rights, this is likely to reduce the sale price and by doing so increase the capitalisation rate. Mr Marchant notes that excluding these transactions is to the benefit of the landlord. This sifting has excluded **587** transactions, leaving **119** for further analysis.

19. Whilst, Mr Marchant has sought to exclude all transactions where there is a commercial element or potential to develop the property, there may be asset management opportunities in some of the properties he has screened to which he has not attributed any value (e.g. the value of managing the property or hope value for further development in the future). He has not attempted to consider whether such value exists, or to quantify it. Again, he suggests that this is to the benefit of the landlord. Had he attributed value to such opportunities, this would reduce the value attributed to ground rent and therefore increase the capitalisation rate (rather than reduce it).
20. Mr Marchant has then applied a number of criteria to identify the **29** best comparables to the subject property:
 - (i) Length of lease: The unexpired term of the subject flat is 83.23 years. Comparable Criteria: Any transactions not excluded by the initial screening process outlined above by definition will be assets with flats let on longer leases than the subject property.
 - (ii) Security of Recovery: (a) Size: The subject flat is set in a block of three other flats; Comparable Criteria: Seven or fewer units; (b) Age/quality/ maintenance: The subject asset is a converted period (c. 1900s) semi-detached property. It is presumed to have been converted into four non-identical flats in the mid-1970s when the original lease for Flat 2 was granted. This is likely to pose a higher-risk than more modern period-conversion properties or purpose-built blocks. Comparable Criteria: Both purpose-built and period-conversion properties (regardless of conversion age); (c) Consistency/ Quality of Leases: The leases within the subject asset were all granted with different commencement dates. Flats 1 and 4 are held on 99 year leases from June 2007 and June 2010 respectively. Flat 2 had a statutory lease extension in 2008 and is

now held for a term of 189 years from December 1975. Comparable Criteria: Any transactions not excluded by the initial screening process outlined above by definition will have flats held on more consistent leases than the subject property.

(iii) Size of Ground rent: The ground rent on the subject flat is currently £265 pa, which represents a valuable income stream to the landlord, but is not what he considers to be an onerous ground rent. Comparable Criteria: Passing Ground rent of no less than £100

(iv) Ground Rent Reviews: The ground rent for the subject flat is currently £265 pa, and doubles to £530, £1,060, £2,120 and £4,240. These reviews counteract the effect of inflation over time but are considerably less onerous than one that doubles every 10 or 15 years. Comparable Criteria: Ground rent which increases by pre-defined amounts (whether doubling or not) at intervals of 20-25 years.

21. Applying these criteria, Mr Marchant reduced his basket of comparables from **119** to **29**. In his experience, the Allsop particulars are generally reliable. However, to ensure accuracy for the 29 comparables, he has (i) Validated that the lease start date and term was correct, by reviewing one or more sample leases.; (ii) Validated the schedule of leases, using the freehold title; (iii) Validated the sale value of the transactions, preferably using the freehold title but where this is not available (i.e. where the asset has sold again since the auction), he has relied on the price published by the auction house; (iv) Validated the passing ground rent/ground rent reviews in the auction particulars, by reviewing one or more sample leases; (v) Recorded the basis that any reversionary value was calculated.
22. Mr Marchant has annexed to his report, the Auction Particulars, Freehold Title Register and Sample Leases in respect of his 29 comparables (at p.102-1494). His analysis of the capitalisation rates is at p.100. This is summarised at [7.2.42] of his report. The tribunal focused on his analysis of one of his comparables, 16 Albion Way, which is at p.102. We could not identify any flaw in his methodology. We also considered his analysis for his other comparables.
23. Mr Marchant's analysis of his **29** comparables suggest a range for the capitalisation rate of between 6.8% and 15.01%. He decided to exclude the three highest and lowest as "outliers". The remaining **23** comparables suggest a range of 7.25% and 10.92%. The simple average of these is 8.88%, whilst the median is 8.82%. He has decided to take the median figure of 8.82% which favours the landlord.
24. Mr Gunby noted that some of the sales dated back to March 2019, namely three years before the valuation date. However, the older comparable, 16 Albion Way, was the one that most favoured the landlord. The table does

not suggest any discernible change in the capitalisation rate over the past three years.

25. The is one relevant issue which we raised. In each of the 29 comparables, the rent doubled every 25 years. In the current case, it doubles every 20 years. Mr Marchant accepted that this was a relevant factor and that a reduction of 0.5% should be made for this. We therefore adopt a capitalisation rate of 8.32%.
26. In his closing submissions, Mr Gunby highlighted the capitalisation rates which had been adopted in other case, namely the Upper Tribunal Cases of (i) *Arrowdell* (LRA/72/2005): 7%; (ii) *Deritend* [2020] UKUT 164 (LC): 6.5%; (iii) *Nicholson v Goff*: 5%; and the First-tier Tribunal decisions in (i) *Lawrence Wharf*: (ii) 6.35%; *Observatory Way*: 6.15%; (iii) *Mansfield Road* (BIR/00FY/OAF/2021/0011): 5.25%; and (iv) *St Emmanuel House*: 3.35%. In none of the Upper Tribunal were the capitalisation rates based on market evidence. The experts rather adopted conventional figures, including the rate adopted for deferment. Where the FTTs have determined the capitalisation rate, this has been based on the market evidence adduced before the tribunal.
27. The Tribunal recognises that this rate for capitalisation is at the higher level of the scale. However, the Upper Tribunal has urged First-tier Tribunals to favour market evidence. Mr Marchant has produced an impressive range of market comparables. Mr Gunby was unable to identify flaws in the analysis. We are satisfied that we should have regard to market evidence, rather than conventional figures adopted in other cases. It is only Mr Marchant who has adduced market evidence. His methodology has not been undermined by cross-examination. We have made a reduction of 0.5%. Mr Marchant readily conceded that such a reduction should be made, when we pointed out that the rent for the subject property doubles every.

Judge Robert Latham
24 May 2023

RIGHTS OF APPEAL

1. If a party wishes to appeal this decision to the Upper Tribunal (Lands Chamber) then a written application for permission must be made to the First-tier Tribunal at the Regional office which has been dealing with the case.
2. The application for permission to appeal must arrive at the Regional office within 28 s after the Tribunal sends written reasons for the decision to the person making the application.

3. If the application is not made within the 28 day time limit, such application must include a request for an extension of time and the reason for not complying with the 28 day time limit; the Tribunal will then look at such reason(s) and decide whether to allow the application for permission to appeal to proceed despite not being within the time limit.
4. The application for permission to appeal must identify the decision of the Tribunal to which it relates (i.e. give the date, the property and the case number), state the grounds of appeal, and state the result the party making the application is seeking.