UPPER TRIBUNAL (LANDS CHAMBER)

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TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LEASEHOLD ENFRANCHISEMENT – COLLECTIVE ENFRANCHISEMENT – development hope value – s. 24 and paras 2-5, Sch 6, Leasehold Reform, Housing and Urban Development Act 1993 – appeal dismissed

IN THE MATTER OF AN APPEAL AGAINST A DECISION OF THE FIRST TIER TRIBUNAL (PROPERTY CHAMBER)

BETWEEN: **HOUSE OF MAYFAIR LIMITED**

Appellant

and

TIMOTHY FRANK AITCHISON

STEPHANIE WINTERHAGEN

MAURO LELLI

LOUIS JOSEF HERNS

Respondents

Re:22 Underhill Road,

London SE22

Martin Rodger QC, Deputy Chamber President and Mark Higgin FRICS

18 February 2021

By remote video platform

Piers Harrison, instructed by Thirsk Winton LLP for the appellant

Ellodie Gibbons, instructed by Tolhurst Fisher LLP for the respondents

The following cases are referred to in this decision:

Cravecrest Limited v Trustees of the Will of the Second Duke of Westminster [2014] Ch 301

Francia Properties Limited v St James House Freehold Limited [2018] UKUT 79 (LC)

Introduction

1.
In a decision handed down on 30 March 2020 the First-tier Tribunal (FTT) determined that the respondents should pay £22,000 for the freehold of 22 Underhill Road, London SE22, which they

proposed to acquire collectively under section 24 of the Leasehold Reform, Housing and Urban Development Act 1993. That price included £2,000 as the value attributed by the FTT to the small possibility that the building might be capable of development by the addition of a further storey to create either a new self-contained flat or additional accommodation which could be added to the existing top floor flat.

2.
The leaseholder of the top floor flat, Mr Joseph Roberts, is also the sole director of the appellant, House of Mayfair Ltd, which owns the freehold of the building. In this appeal the appellant argues that the FTT failed to take into account the interest Mr Roberts would have in cooperating in the suggested development and says that, when determining the price payable for the freehold, it ought to have attributed a value of £35,000 to the opportunity to develop additional accommodation on the roof.

3.
At the hearing of the appeal the appellant was represented by Mr Piers Harrison and the respondents by Ms Ellodie Gibbons, neither of whom had appeared before the FTT. We are grateful to them both for their helpful submissions.

The facts

4.
22 Underhill Road is a modern detached apartment block of traditional construction built in about 2009 on ground and three upper floors. It comprises five self-contained flats including a two-bedroom flat on the 3rd floor. The building is in a predominantly residential part of south London and has gardens at the front and rear. The flats are reached by a common internal staircase which goes as far as the 3rd floor but not to the flat roof above. The building does not have a lift.

5.
Each of the five flats is held on a lease for a term of 125 years from 1 January 2009. On 30 March 2012 the appellant acquired the freehold of the building, subject to the occupational leases for a purchase price of £14,500.

6.
The lease of flat 5, on the 3rd floor, is owned by Mr Roberts, who is the sole director and shareholder of the appellant.

7.
The respondents are the leaseholders of the remaining four flats. On 1 July 2019 they gave notice to the appellant that they wished to exercise their right to acquire the freehold of the building under the 1993 Act. The appellant did not dispute that entitlement but the parties could not agree a price and on 25 November 2019 the respondents applied to the FTT for a determination of the price and other terms of the acquisition.

8.
The experts instructed by the parties in the FTT were able to agree that the value of the appellant’s interest, disregarding any development value, was £20,000. The only remaining question was whether the price should be increased by an additional sum to reflect the potential, or hope, of further profitable development on the roof of the building.

9.

The respondents' expert, Mr Jeffery Rollings MRICS, did not think anything should be added to the price to reflect development potential. He took account of the fact that the building was only 10 years old, and that no application for further development had been made since it was completed, "despite the present freeholder owning the top floor flat". He also had regard to the advice of a planning consultant, Mr Gunne-Jones, that "the prospects of extending the property upwards and to the rear are extremely low".

10.
The appellant's expert, Mr Richard Murphy MRICS, took a much more optimistic view of the prospect of further development at the building. He considered that a hypothetical purchaser of the freehold would make a bid reflecting the possibility of an additional flat being constructed on the roof. He provided an appraisal based on the development of such a self-contained flat at a cost of £350,000, a prospect which he considered would add £45,257 to the value of the freehold. In arriving at that valuation Mr Murphy had regard to the views of Mr Gunne-Jones and to the more bullish assessment of the appellant's planning consultant, Mr Allsop, that there was "a "balanced" chance of securing planning permission" for the development of additional living space on the roof. Mr Murphy also had regard to a shift in national planning policy in favour of upward extensions since the grant of planning permission for the building in 2008.

11.
In constructing his residual valuation Mr Murphy relied heavily on the decision of this Tribunal in Francia Properties Limited v St James House Freehold Limited [2018] UKUT 79 (LC), another collective enfranchisement appeal concerning the value added to a modern building by the prospect of development on the roof. Mr Murphy adopted the same development costs that had been in evidence in Francia (adjusted for time), included an allowance for contingencies "in line with the Francia decision" and a discount for planning and engineering risks "as in the Francia case". At paragraph 36 of Francia the Tribunal had explained why tribunal decisions on factual matters ought not to be relied on in this way:

"36. The assessment of risk is specific to the circumstances of each individual case, and no prospective purchaser would have regard to tribunal decisions in forming its own commercial judgment. For this purpose previous decisions concerning different factual circumstances are of little relevance."

The FTT's decision

12.
The only issue the FTT had to address was what it called "the development hope value" to be added to the premium payable by the applicant for the collective enfranchisement of the property. The only statutory provision it referred to was paragraph 5 of Schedule 6 to the 1993 Act. It will be remembered that, by paragraph 2(1) of Schedule 6, the price payable for the freehold of the premises specified in the leaseholders' notice of claim is to comprise the value of the freeholder's interest in the premises determined in accordance with paragraph 3, the freeholder's share of the marriage value determined in accordance with paragraph 4, and any compensation payable under paragraph 5.

13.
The FTT's reference to paragraph 5 is therefore puzzling. That provision is concerned only with the loss or damage which a freeholder suffers as a result of a diminution in the value of other property belonging to it, rather than with the value of the specified premises which are being acquired. It is true that the example of the kind of loss or damage given in paragraph 5(3) refers to loss of

development value in relation to the specified premises themselves where it is referable to the freeholder's ownership of any interest in other property, but the FTT did not seem to identify what other property it had in mind. We suspect that the FTT was distracted by the definition in paragraph 5(4) of "development value", and focussed on that definition when it gave itself the direction that it was required to assess whether there was any possibility of the freeholder reconstructing or carrying out substantial works of construction on the whole or on a substantial part of the property. It appears to us then to have undertaken that assessment of development value as part of its determination of the value of the freeholder's interest in the block as a whole under paragraph 3, although it is possible that it was confused by the relationship between Mr Roberts and the appellant and treated his interest in the lease of flat 5 as if it was an interest of the freeholder in other property. We will return to that potential confusion shortly.

14.
The FTT then considered the evidence concerning the prospect of development and pointed out that neither of the experts had spoken to the local planning officer about the possibility of permission being granted for an extension.

15.
The appellant's expert, Mr Murphy, had been asked about the fact that the whole of the 3rd floor was demised to the lessee of flat 5 and that there was no independent access to the roof. Mr Murphy had relied on a right of entry for the purpose of development of adjoining premises contained in the lease of flat 5 and appeared to think that would enable the freeholder permanently to take back part of the demise of flat 5 to create the necessary access. The FTT noted his evidence if his understanding of the extent of the right was wrong (which it was):

"… he believed that a deal could be done with the tenant of that flat to surrender a part of its demise at no significant extra cost. At the hearing he suggested that an allowance of £10,000 be made to his net development value of £42,257 to reflect that a deal would have to be struck with the tenant of flat 5. In his submissions he referred to an alternative possibility, that a fifth-floor extension might be incorporated into flat 5."

16.
The FTT concluded that Mr Murphy had given insufficient thought to how access to any development on the roof would be achieved. It dismissed his reliance on the right of entry reserved in the lease of flat 5, which did not give the landlord the right to remove any part the demised premises, and went on:

"Accordingly, any development potential of a fifth floor would have to be a development undertaken to incorporate it within flat 5. There was no evidence before the Tribunal that a tenant of flat 5 would want to pay for such an extension to its demise."

17.
The FTT did not dismiss the prospect of development entirely. It said this:

"In the circumstances the Tribunal consider that any increase in the value of the freeholder's interest in the premises which is attributable to the possibility of demolishing, reconstructing, or carrying out substantial works of construction on, the whole or a substantial part of the property, by way of a roof extension is very small. But a small possibility of such development in the future should be taken into account and the Tribunal therefore attributes a value of £2,000 to this possibility."

18.
The FTT therefore determined that the premium payable for the collective enfranchisement was £22,000.

The appeal

19.
The appellant sought and was granted permission to appeal on two grounds.

20.
The first ground of appeal suggested that the FTT had been in error in assessing the development value under paragraph 5. The development in question was not development of "other property" such as to fall within paragraph 5(2) of Schedule 6 to the 1993 Act, it was development of the specified premises themselves. The proper question for the FTT was what sum would the hypothetical purchaser of the freehold pay in anticipation of the possibility of developing the subject matter of the acquisition, namely the freehold of the premises themselves.

21.
Secondly, the appellant argued that if the FTT had correctly directed itself it would not have overlooked the relationship between the owners of the freehold and of flat 5. At an early stage in its decision the FTT had stated that the appellant was also the owner of flat 5. That was not strictly accurate since Mr Roberts, the owner of flat 5, was the director and sole shareholder of the appellant. But given that close connection the appellant suggested that the lessee of flat 5 would have been "highly motivated" to cooperate in the suggested development. The FTT ought therefore to have considered what Mr Harrison described in his grounds of appeal as a "hypothetical two-stage process" whereby the prospective purchaser of the freehold would ascertain in advance the likelihood of being able either to acquire part of flat 5 or to sell the roof space to the lessee of flat 5. Such a hypothetical two-stage approach was said to have been approved by the Court of Appeal in Cravecrest Limited v Trustees of the Will of the Second Duke of Westminster [2014] Ch 301 at [31]. The freehold would not have been marketed for sale to a hypothetical purchaser without attention being drawn to the development potential allowing the purchaser to make the necessary enquiries of the lessee of flat 5. The FTT ought therefore to have considered the prospects of a development to incorporate a new 5th floor into flat 5 or a sale by the tenant of flat 5 of part of his flat to enable the creation of an independent access to a new self-contained flat on the roof of the building.

22.
After being granted permission to appeal the appellant also sought permission to rely on new evidence to show that the FTT had been mistaken when it had said that it was also the lessee of flat 5. Permission to adduce additional evidence was refused by the Tribunal on the basis that the inaccuracy was inconsequential and appeared to make no difference to the appellant's argument. The Tribunal directed that it would proceed on the basis of the facts found by the FTT.

23.
In his skeleton argument for the appeal Mr Harrison recast his argument substantially. Rather than criticising the FTT for its reliance on paragraph 5 of Schedule 6, Mr Harrison invited the Tribunal to proceed on the basis that, contrary to reality, the appellant is the owner of flat 5. But that invitation is not based on any specific finding of fact by the FTT and, on Mr Harrison's argument, it makes no difference to the outcome of the appeal.

24.

There was no issue before the FTT about ownership of other interests in the building. Although the FTT referred in passing to the freeholder as “also the tenant of flat 5” the material before it showed that Mr Roberts was the lessee of flat 5. Mr Rollings on behalf of the respondents, had pointed out in his evidence that no attempt had been made to develop the roof of the property “despite the present freeholder owning the top floor flat” and Mr Murphy had described himself as “instructed by … House of Mayfair Limited (flat 5)”. The language of the experts was imprecise but understandable given that the appellant was a company controlled by Mr Roberts. There is no reason to think that the FTT’s equally loose language discloses some misunderstanding of the true facts. In any event, Mr Harrison himself argued that whether the suggested loss of development value is to be accounted for under paragraph 3 as part of the value of the premises being acquired, or under paragraph 5(2) as referable in part to the ownership of an interest in other property, or by a combination of the two, ought not to make any difference to the outcome. If the relationship between the owner of flat 5 and the owner of the freehold (whether they be taken to be one and the same, or so closely connected as to make no practical difference) the price payable by the respondent purchasers ought, he submitted, to reflect the loss caused to the appellant by, as Mr Harrison put it, divorcing the marriage of the two interests. That being Mr Harrison’s position, there is no need for the Tribunal to make any assumption contrary to the facts when determining the appeal.

25.
Mr Harrison next submitted that the FTT had reached the wrong decision because it had viewed the lack of access through flat 5 to the roof of the building as the main obstacle to development, but had overlooked the relationship between the lessee of flat 5 and the owner of the freehold. It should have valued the freehold on the basis of Mr Murphy’s assessment of the development value and should have adopted his deduction of £10,000 to reflect the fact that providing access would diminish the value of flat 5. That part of Mr Murphy’s evidence had not been contradicted and should have been accepted by the FTT.

26.
Mr Harrison relied on the decision of the Court of Appeal in Cravecrest as providing guidance applicable to the valuation in this case.

27.
The facts of Cravecrest are far removed from this case. It concerned the simultaneous acquisition of the freehold of a substantial house which had been converted into three flats and of two intermediate leases. Each of the flats was let on a separate underlease which was due to expire two days after the valuation date. The intermediate leases which sat between the leases of the flats and the freehold were to be acquired by the participating lessees. It was agreed that there was potential to convert the building back into a single house and that its value would then be far greater (by £5m) than the aggregate value of the individual flats. The Tribunal had valued on the assumption that the hypothetical purchaser of the freehold would be willing to pay a price which reflected the prospect of being able to realise the development value by acquiring the intermediate interests. In fact, as the Court of Appeal recorded at [56] no discussions had yet taken place at the valuation date between the owners of the intermediate interests and the acquiring leaseholders. Nevertheless, the Court of Appeal agreed that the statute did not prohibit valuation on the assumption that the owners of the intermediate interests would be willing to sell their interests. The Court also held, at [79], that the Tribunal had been entitled to posit a two-stage sale of the various interests. It had been entitled:

“to postulate what enquiries the reasonably prudent buyer would have made of whatever of them would be the potential second seller and what the reaction would have been. What enquiries the

purchaser would have made and what answers would have been received are partly matters of fact and partly expert evidence. What would have been the valuation consequences of those matters is a matter for expert evidence. None of those issues raises an issue of law".

28.
As this passage demonstrates, Cravecrest does not establish any valuation principle of general application. Whether additional value can be attributed to the prospect of a development based on the acquisition of the freehold and another interest is a question of fact. The fact that the two interests currently belong to, or are controlled by, the same person may make the achievement of any development more likely, but it does not mean that the existence of an attractive development opportunity can be assumed. It all depends on the facts. The building in this case is not ripe for redevelopment, with the occupational leases on the point of falling in and a substantial uplift in value in prospect, as in Cravecrest. Even on the most optimistic assessment there is no substantial development value to be realised. After making a very significant discount for risks, Mr Murphy put the net development value at only £35,000. There was no evidence that Mr Roberts was interested in realising additional value by carving up or extending his flat. He appears to have taken no steps in the ten years of his ownership of flat 5 and the seven years of his ownership of the freehold of the building as a whole to progress any such scheme.

29.
A further fundamental difficulty with Mr Harrison's argument is that it criticises the FTT for failing to adopt an analysis which formed no part of Mr Murphy's evidence until he voiced it, on the hoof, in response to questions from the FTT. The FTT was quite right that Mr Murphy had given little thought to the practical and legal difficulties of creating an access to the new self-contained flat which he assumed could be created on the roof. It was only when questioned by the FTT itself that he suggested £10,000 would secure the cooperation of the lessee of flat 5. By that time Mr Rollings had already given his evidence. There is no suggestion that he was asked about the price of purchasing the cooperation of the leaseholder of flat 5, nor was there any reason why he should have been, as Mr Murphy's case was that there was no need to pay because "the leases … allow the freeholder to carry out this work without compensation" (paragraph 6.1 of Mr Murphy's report). The "two-stage approach" which Mr Harrison argued the FTT should have adopted, depends on there being evidence of what a prospective purchaser of the freehold would anticipate having to pay the owner of the other interest to enable the development to progress. There was no evidence about the price the lessee of flat 5 might require to surrender a sufficiently large portion of his flat to enable independent access to the roof of the building, apart from Mr Murphy's ex tempore suggestion of £10,000, which had not formed part of his considered written evidence and on which Mr Rawlings had had no opportunity to comment.

30.
Given the way Mr Murphy's evidence about purchasing the cooperation of the leaseholder emerged, we reject Mr Harrison's contention that the FTT was obliged to adopt his assessment of the allowance required and that this Tribunal should do the same. Mr Harrison suggested that the FTT must itself be taken to have accepted Mr Murphy's assessment because it said nothing to contradict it. We disagree. In paragraph 19 of its decision the FTT rejected the suggestion that the roof of the building could be developed as a self-contained flat. The premise of Mr Murphy's assessment that £10,000 would be enough to purchase the necessary surrender of part of flat 5 was necessarily rejected by the FTT when it found that any development would have to be incorporated as an extension to the existing flat.

31.

Mr Murphy provided no assessment of the difference such a development, or the hope of such a development, would make to the price the freehold of the building would fetch in the open market. Quite apart from his reliance on the costs of the Francia scheme (a different building in a different location which already had access to the roof) Mr Murphy's gross development value assumed the creation of a new one-bedroom self-contained flat with a balcony, rather than an enlargement of flat 5 to form a three or four-bedroom maisonette. Even accepting Mr Murphy's approach to development costs, it is impossible to know whether such a development would have yielded a positive value, taking account of the loss of the separate value of flat 5.

32.
The FTT assessed the prospect of a development of the roof as being "very small". Mr Harrison suggested that it was obvious that a person in Mr Roberts' position would want to realise the development value but we can see no reason for making that assumption on the facts of this case. Even if we are wrong about that, we do not accept Mr Harrison's submission that the FTT's modest assessment depended entirely on the absence of evidence that the lessee of flat 5 would have been prepared to pay for an extension to its demise. In paragraph 20 of its decision, the FTT stated that "in the circumstances" it considered the value of the prospect of development to be very small. The difficulty of access was one of the circumstances Mr Rollings had identified as obstacles to the development, and the FTT clearly agreed with him on that point. But there is no reason to think that it discounted the other difficulties he identified, including the view of Mr Gunne-Jones that planning policy would not have supported it. The FTT's assessment of the prospects of achieving a development as very small indicates that it was not persuaded that all the uncertainties and problems could be solved by a payment of £10,000 to one leaseholder.

33.
In our judgment the FTT was entitled on the evidence to determine the premium payable for the collective enfranchisement to be £22,000.

Martin Rodger QC, Mark Higgin FRICS

Deputy Chamber President Member

23 March 2021