

Spring 2008

2008 promises to be another busy year for us at Pemberton Greenish. The firm is at a pivotal time in terms of expansion, and we are looking forward to another year of growth.

In November 2007 we appointed Ian Gill as our new head of commercial property. His appointment along with others that have been made in the last quarter is a testament to a desire to grow our business in all areas, particularly in commercial property. In September we also welcomed two new trainees to PG.

We are delighted to announce our sponsorship of a small garden at Chelsea Flower Show in May and also of the Chelsea Society's Summer Exhibition in June.

The eagerly anticipated (at least in the world of leasehold enfranchisement) decision of the Court of Appeal in the case of *Earl Cadogan & Others v. Sportelli and Others* [2007] EWCA Civ 1042 was handed down in October. For those expecting something controversial or ground-breaking, it was a disappointment.

We hope that you enjoy this issue, and as ever welcome your feedback, suggestions and ideas.

A handwritten signature in cursive script that reads 'Robert'.

Robert Barham
Managing Partner
Direct Dial: 020 7591 3386
Email: r.barham@pglaw.co.uk

Contents

NEWS - UP TO OUR HIPS	2
CRACKING THE COMMERCIAL PROPERTY CODES	3
PRE-BUDGET ANNOUNCEMENTS: NON-UK DOMICILED INDIVIDUALS	6
CHANGES TO INHERITANCE TAX	8
NEW RULES FOR CAPITAL GAINS TAX	9
MAJOR CHANGES TO COMPANY LAW WITH THE COMING INTO FORCE OF PROVISIONS OF THE COMPANIES ACT 2006	10
SPORTELLI	12
PG PEOPLE	18

Up to our HIPs

Whatever your view, what is clear is that HIPs are here to stay!

Since the Summer of 2007 issue of PG Lore the Government has pressed ahead with its programme of implementing Home Information Packs. From 10 September 2007 all domestic properties with three bedrooms or more being marketed for sale have been required to have a HIP (unless they were already on the market before 1 August 2007).

The requirement to have a HIP was extended to all properties on 14th December 2007. The introduction of the inclusion of three or more bedroom properties has been controversial. The Government argues from its consultation process that HIPs are starting to reduce costs and improve transparency in the housing market, whilst opponents argue that this further implementation has caused a sharp drop in the number of properties being placed on the market.

The Government is due to make a further announcement to set a “drop dead date” which will be the point at which they require a HIP for all properties regardless of the number of bedrooms and when the property was first marketed.

At PG we have organised ourselves so we are able to provide HIPs. The advantage of our HIP is two fold. One, you can be sure it is compliant with current legislation and two, the documents, and the time spent collating them can be used towards the conveyancing process. This may ultimately save time and money – which after all is what they are supposed to achieve.

Also, PG HIPs are not tied to any estate agency, and therefore you can move them around thus allowing you to change estate agents for the purpose of marketing or even allowing you to market your own property without any additional cost.

If you require any further advice or assistance in the preparation of a HIP please contact Jason Eades, a senior solicitor in our residential property team.



Jason Eades
Direct dial: 020 7591 3321
Email: j.eades@pglaw.co.uk

New PG Publications

If you wish to order any of the following publications please either visit our website www.pglaw.co.uk or contact us on law@pglaw.co.uk



PG Corporate Brochure



Residential Conveyancing Factsheet



Probate Brochure



Enfranchisement and Lease Extension Brochure

Cracking the Commercial Property Codes

SERVICE CHARGES IN COMMERCIAL PROPERTY – THE NEW RICS CODE OF PRACTICE

Service charges often represent a significant overhead for commercial tenants and can be unpredictable.

It is perhaps surprising therefore that there is no material legislation governing service charges in business leases - 'what you read is what you get'. The situation is therefore quite different to residential property where a large amount of legislation has been enacted.

This illustrates how important negotiating the terms of a lease can be, as its contents will be the only factor determining how the service charge will be governed.

The new RICS Code of Practice – 'Service Charges in Commercial Property' (the 'Code') was introduced on 1 April 2007 in an attempt to regularise service charges in commercial leases.

The basis of the Code is to promote 'best practice' and to encourage landlords to draft clear and more explicit service charge provisions. The introduction to the Code states that "best practice requires owners and occupiers ensure their advisers" incorporate the code when preparing documentation prior to a new letting and at lease renewal.

Yet the Code is merely advisory. Indeed whether leases were prepared before and after 1 April 2007 there is no obligation to follow its contents. The extent to which it is incorporated into the relevant documentation is a matter for the client's instruction.

Objectives

The Code has five basic objectives.

- 'Best practice on a value for money basis'

- A reduction of conflict
- That service charges are operated on a 'not for profit, not for loss' basis
- That services charges are budgeted and can be a forecastable part of the occupiers overhead and
- That service charge regimes are cash – neutral to the owners income.

'Best Practice Procedures'

These five objectives are incorporated into 'best practice procedures' which are separated into six different areas: Management, Communication, Transparency, Service Standards and Provision; Administration and Additional Shopping Centre Services.

The Code then sets out under each heading its recommendations for the operation of a code complaint service charge regime. For example a clear communication structure should be established and suppliers of all services should be required to perform to written performance standards.

Significantly the Code recommends that any management fee charged should not be linked to a percentage of expenditure but should be fixed for a reasonable period of time and possibly subject to RPI and must be fair and reasonable. The Code does not consider a fee linked to a percentage of expenditure appropriate as it does not provide good 'value for money'.

Limits on Effectiveness

As the Code is only advisory it is somewhat curious that it has been given a date of effect. There is no compulsion to follow its content either before or after 1 April 2007. It will not override existing leases.

- It remains the case that the terms negotiated between each party are binding
- There is no real sanction for non compliance, though it has been speculated that surveyors may be sanctioned by the RICS.

It is nevertheless good practice for all commercial property practitioners to be aware of the Code's content.

There is no statutory requirement for the Code to be taken into account when resolving service charge disputes and no requirement in English law for best practice guidance to be taken into account when interpreting service charge or any other lease terms.

Conclusion

The Code provides useful advice to landlords who wish to manage their buildings well and avoid disputes with their tenant. However, unless and until supported by legislation, the Code is toothless. The extent to which practitioners incorporate its proposals into documentation is a matter entirely for the client.

'A managing agent should not follow the Code to the disadvantage of its client, the landlord, without the latter's prior approval. Tenants should not assume a landlord's failure to comply with the Code will give them any rights they would have enjoyed without it'.



Stephen Woolridge
Direct dial: 020 7591 3349
Email: s.woolridge@pglaw.co.uk



CRACKING THE COMMERCIAL LEASE CODE

The Code for Leasing Business Premises in England and Wales 2007 (“the Lease Code”) was launched on 28 March 2007 by Yvette Cooper, the Minister for Housing and Planning. It was published by The Joint Working Group on Commercial Leases comprised of Government, business and legal organisations.

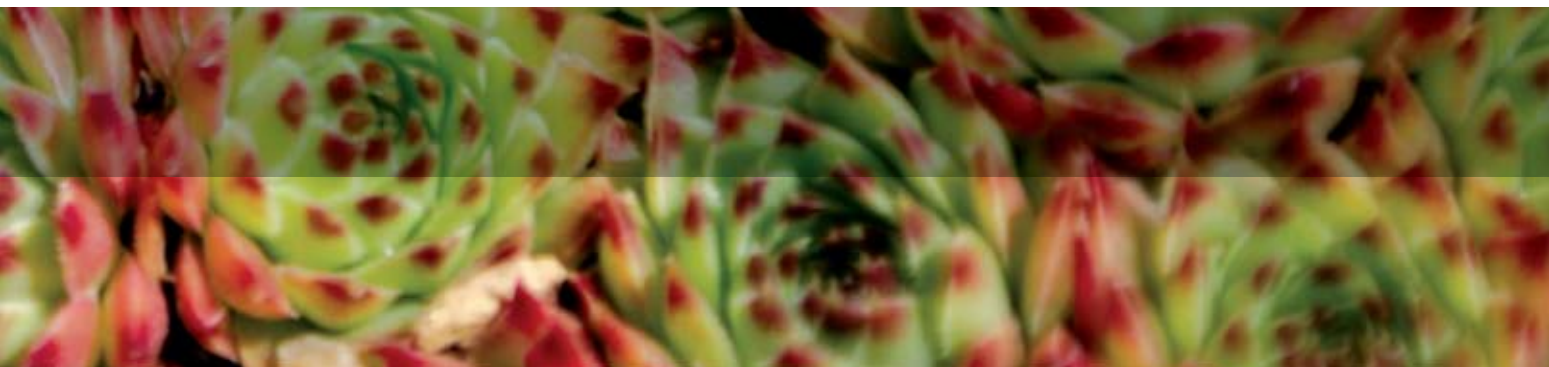
The Lease Code has three elements:

- The Landlord Code
- The Occupier Guide
- Model Heads of Terms

Copies of these documents are available at www.commercialleasecode.co.uk

The Lease Code aims to promote flexible leasing arrangements, efficiency and fairness. It is intended to influence the conduct of landlords and tenants during negotiations and throughout the term of the lease.

The 2007 Lease Code was preceded by the Codes of Practice for Commercial Leases in 1995 and 2002. These Codes of Practice had very little impact. The Government has indicated that it will allow two or three years for the Lease Code to take effect, failing which it will legislate. For now, the Lease Code is voluntary.



Some of the issues covered by the Landlord Code are:

Lease Negotiations

Under the Lease Code landlords are required to make written offers stating the main terms of the lease. They must promote flexibility and if the tenant requests, the landlord must state whether alternative terms are available and propose different rents for different terms. There are some difficulties with the requirement to price different lease terms. The landlord who owns only one or a few properties may not have the expertise to deal with this. Setting a price for a particular lease term could create a precedent which might be used in lease renewals under the Landlord and Tenant Act 1954. This is unlikely to be what either party intends. If landlords are obliged to offer priced alternatives there is a risk that they will simply increase the price of the option which they least prefer.

Rent Review

The Lease Code does not rule out the upwards only rent review. Instead, it requires landlords to offer alternatives if a prospective tenant asks them to do so. Those alternatives might include an upwards/downwards review subject to a minimum equal to the initial rent or a review by reference to indexation. The landlord must state its reasons if it cannot offer alternatives.

Concerns about having upwards/downwards rent reviews imposed on the market will have abated due to the trend towards shorter leases which either review rent by reference to the Retail Prices Index or do not contain a rent review. 65% of leases granted in 2005-2006 were for five years or less. Stamp Duty Land Tax has contributed to this trend given that the duty on leases for terms of 10 years or more is disproportionately expensive.

Repairs

A tenant's obligation to repair should be appropriate to the length of term and the condition of the premises. The Lease

Code provides that unless expressly stated in heads of terms, tenants should only be required to give back the premises in the same condition as existed at the start of the term. This is a significant departure from current practice and is likely to make the use of schedules of condition more common.

Insurance

The Lease Code addresses the issue of damage by uninsured risks. It requires a rent suspension whether the premises are damaged by an insured risk or an uninsured risk. The only exception to this is where the damage is caused by the deliberate act of the tenant. If the lease limits the rent suspension to the period covered by loss of rent insurance either party should be able to terminate the lease if reinstatement has not taken place within that period.

Conclusion

The Lease Code represents best practice and could lead to quicker, cheaper negotiations. All the issues are brought out into the open at the start of a negotiation. This should mean that the parties have realistic expectations of their relationship as landlord and tenant. There are undoubtedly some problems achieving compliance with the Lease Code when dealing with 1954 Act lease renewals or the grant of leases which need to be consistent with other leases of adjoining premises. However, even in those circumstances, observing the spirit of the Lease Code could be helpful.

The Government has indicated that it has already identified the legislation it would put in place if the Lease Code is not put into practice. Legislation could lead to inflexibility which is the very thing that the Lease Code seeks to avoid.



Abigail Mitchell
Direct dial: 020 7591 3360
Email: a.mitchell@pglaw.co.uk

Pre-Budget Announcements: Non-UK domiciled individuals

One of the major developments in UK taxation in 2007 was the announcement in the Pre-Budget Review on 9 October that the Government is going to introduce new legislation altering the basis on which non-UK domiciled individuals pay tax on their foreign income and capital gains.



For many years the UK has attracted non-domiciled individuals, who are major investors in real estate in London and elsewhere and consumers of services and goods in London, with its relatively benign tax regime for such people.

Historically, resident but non-domiciled individuals have only paid UK tax on foreign income and gains to the extent that they “remit” such income and gains to the UK. There are also additional advantages for non-domiciled individuals who are beneficiaries of non-resident trusts.

The Pre-Budget announcement heralds a sea change in approach.

Pre-Budget Review Note 18 states that:

- The Government will with effect from 6 April 2008 charge non-UK domiciled individuals who have been tax resident for seven years a special tax, initially £30,000 per annum, if they wish to be taxed on foreign income and gains on the “remittance basis”. What is not clear is whether such individuals will be able to opt in and out of the special tax in any particular year after having quantified the benefit or otherwise of using the remittance basis.
- The Government will be consulting on whether non-UK domiciled individuals who have been tax resident for more than 10 years should be taxed on a more draconian basis.
- The remittance basis itself is to be overhauled. Some existing techniques of tax planning, for example “cessation of source” and “alienation” are respectively to be outlawed and severely limited with effect from 6 April 2008.

The press release contains a worrying paragraph which refers to reducing the scope for offshore trusts and companies to be used as a means of “convert[ing] taxable income and gains into non-taxable payments”. We (and others) are

very concerned that this paragraph suggests that there will be a wholesale overhaul of the current, favourable, rules applicable to non-domiciled beneficiaries of offshore trusts.

For those who are regular visitors to the UK, avoiding tax residence is going to become harder. There is to be legislation with effect from 6 April 2008 that days of arrival in and departure from the UK will count towards the day counts currently used to determine tax residence. At the time this article goes to print we await the draft legislation which would carry into effect the announcements.

Lobbying by and on behalf of non-domiciled individuals is going on and we wait to see whether the worst fears of the non-UK domiciled individuals and their advisors will be realised.

Whatever happens, there will be a window between the publication of the draft legislation and 5 April 2008 during which some planning can be carried out by non-domiciled clients. What we do not know is whether 6 April 2008 will mark the start of a dark age for UK resident and non-domiciled individuals and, perhaps in turn, London and the wider UK economy.

We will be providing an update to clients and contacts early in the New Year as soon as we have had a chance to analyse the draft legislation.



John Goodchild
Direct dial: 020 7591 3384
Email: j.goodchild@pglaw.co.uk

Changes to Inheritance Tax

Transferable Nil-Rate Band

The big change to Inheritance Tax this year has been the introduction of the “transferable Nil-Rate Band”. It affects spouses and registered civil partners wishing to leave assets to the survivor on the death of the first.

It used to be best practice on the first death to leave the Inheritance Tax allowance (the Nil-Rate Band) to a Discretionary Trust – a trust for the benefit of the whole family but of which the survivor was treated as the principal beneficiary - or to those who were to benefit on the death of the survivor, typically the children. This ensured that the Nil-Rate Band of the first to die was used and not wasted.

Use now, or use later

It is now possible for a couple to use both Nil-Rate Bands on the death of the survivor even where the first spouse has already died. Instead of Wills containing discretionary trusts of the Nil-Rate Band, the much simpler “all to each other and then equally between the children” is now just as effective Inheritance Tax planning.

Existing arrangements where one spouse has already died

The change will not affect Nil-Rate Band Will provisions which have already been put into effect following the first death. Existing Discretionary Trusts are still effective to avoid Inheritance Tax on the death of the

survivor and they should be left undisturbed. Outright gifts of the Nil-Rate Band will have used up the Nil-Rate Band of the first to die. In both cases the survivor will have just one Nil-Rate Band to use on his or her death, and the assets put into trust or given outright on the first death will not be taxable on the death of the survivor.

Is it necessary to change your Will?

Provided your Will has been properly drafted it will not be necessary to change it. The trust it contains should include a power to distribute capital at any time, and the trustees could use this to distribute the trust assets to the surviving spouse. Provided this is done within two years of the first death, both Nil-Rate Bands will be available to use on the death of the survivor.

Many clients will be happy to leave their Wills unchanged until they next review them – we generally recommend a review every 5 to 10 years. But for those who would like to make the change now, it is a relatively simple and inexpensive exercise.

In Summary

This is a good simplifying measure, which will make Will and estate planning much more straightforward. There will still be instances where a Nil-Rate Band discretionary trust is useful to include in a Will, but it is now unlikely to be for tax reasons.

Example

Mr & Mrs PG’s estates comprise a house worth £800,000 which they hold as joint tenants and chattels, cash and stocks and shares of £500,000, £200,000 in Mr PG’s name and £300,000 is Mrs PG’s name.

Mr PG dies in July 2007 leaving his entire estate to Mrs PG. Mrs PG dies in July 2008.

IHT on Mr PG’s death

Assets: Half share of house	£400,000
Other assets	£200,000
Taxable Estate	£600,000
Spouse exemption:	(£600,000)
Subject to IHT	Nil
IHT on Mr PG’s death	Nil

IHT on Mrs PG’s death

Assets: Full value of house	£800,000
Other assets	£500,000
Taxable Estate	£1,300,000
Mrs PG’s Nil-Rate Band	(£312,000)
Mr PG’s unused NRB	(£312,000)
Subject to IHT	£676,000
IHT on Mrs PG’s death	£270,400

If you have any questions about these changes, please get in contact with us.

A reminder about existing A&M Trusts

With effect from 5th April all existing Accumulation & Maintenance trusts (most commonly grandchildren settlements) will enter a different tax regime: they will be taxed on an ongoing basis at the rate of up to 6% every ten years.

Prior to that date, and provided the trust deed allows, the terms of the trust can be changed so as to minimise the effect of this new regime. If you have trusts which have not been reviewed, then it is important to review them now.



Jeremy Curtis
Direct Dial: 020 7591 3324
Email: j.curtis@pglaw.co.uk

New Rules for Capital Gains Tax



As part of its drive to simplify the tax code, the Government announced a number of changes to Capital Gains Tax. As with all changes to taxation there are winners and losers.

Single tax rate of 18%

A single rate of 18% will apply to all disposals made on or after 6th April.

While this may benefit many individuals, particularly those who are higher rate taxpayers disposing of non-business assets, it is by no means good news for others. Basic or lower rate taxpayers disposing of the same asset could be worse off. And for those with assets qualifying for full Business Asset Taper relief and an effective tax rate of 10% the new rate is almost double.

There are other changes which will affect the overall tax bill.

Withdrawal of Indexation Allowance

Indexation, (a measure to compensate for the effect of inflation on gains) is to be withdrawn on 6th April. Gains will be calculated by reference to their 31st March 1982 value or later actual acquisition value, without adjustment for inflation.

Indexation can reduce significantly the taxable gain on assets held long term. In some cases the loss of this relief will result in a higher tax bill despite the new 18% tax rate: the rate might be lower but the gain on which the rate will bite will be bigger.

Identification of shares – Bed & Breakfasting

Abolishing taper relief sees the re-introduction of “pooling” to establish a universal base cost for all the individual shares within a holding. Subject to the application of anti-bed-and-breakfasting “30 day rule” (which stays) the old last-in-first-out rule will cease to apply. Each share within a holding built up over time will have the same base cost as all the others, calculated as an average of the different acquisition costs. Calculating the tax on an actual disposal, or a proposed disposal, will now be much simpler.

Spouse to Spouse

Transfers of assets between spouses will continue to be on a no gain no loss basis: the transfer is not a disposal for the purposes of Capital Gains Tax, and the asset is transferred with its base cost and history.

Is there any hope for those who will be badly hit?

At the time of writing, draft legislation is awaited, and lobbying on behalf of the worst hit seems likely.

“...there is a wider concern in that the serial entrepreneur, those that build businesses, will still

be hit by the proposals to have a higher single rate of 18%. This will damage the entrepreneurial culture in the UK.”

David Frost - Director General of the British Chambers of Commerce

Assuming that the new rules come in to force, what can be done?

The obvious “sell before the 6th April” advice may be sound from a tax perspective, but like all tax advice must be taken in the broader financial or commercial context. It will rarely be appropriate for those hardest hit – owners of private company shares.

However using gifts and, where appropriate, trusts can in certain cases lock in the benefit of the existing regime and minimise the impact of the budget changes.

We will be happy to provide advice specific to your circumstances when full details of the changes are known.



David Vlahos
Direct dial: 020 7591 3322
Email: d.vlahos@pglaw.co.uk

Major changes to company law with the coming into force of provisions of The Companies Act 2006

1 OCTOBER SAW THE INTRODUCTION OF SIGNIFICANT CHANGES TO COMPANIES LEGISLATION AS PARTS OF THE COMPANIES ACT 2006 ("THE ACT") CAME INTO FORCE. THE PROVISIONS OF THE ACT, THE LONGEST ACT TO HAVE BEEN PASSED BY PARLIAMENT, ARE BEING BROUGHT INTO FORCE IN STAGES, WITH ALL OF IT IN EFFECT BY OCTOBER 2009.

The Act introduces reforms which will affect directors, shareholders, auditors and secretaries of private and public companies and will allow companies greater flexibility in choosing how they operate. Particularly, the Government's "Think Small First" approach has resulted in sweeping changes being brought into the running of the private companies.

The key areas of change which private companies in particular will need to be aware of are set out below.

Company Administration

Company decision-making process has been streamlined:

- Private companies are no longer required to hold an annual general meeting. The directors can call a meeting if necessary and shareholders holding at least 10% of the voting rights can still demand a meeting. Shareholders still have the right to receive accounts.
- Unless different arrangements are specified in the articles of association, the notice period for shareholders meetings for private companies has been shortened to 14 days, regardless of whether a special resolution is proposed.
- Other than resolutions to remove a director or auditors, all resolutions of private companies can now be passed in writing. Using written resolutions as an alternative to calling meetings of shareholders is now easier as they no longer need to be signed by all the shareholders. Instead of needing unanimity, written resolutions can be passed by simple majority (for ordinary resolutions) or 75% majority (in case of special resolutions).
- Shareholders now have the right to appoint more than one proxy and proxies have been given the same rights as registered holders to speak, demand a poll and vote both on

a show of hands and on a poll at general meetings.

- The Act makes it easier for companies to use the Internet to communicate with shareholders. The range of information and documentation that can be sent to shareholders electronically has been extended and (provided it is appropriately authorised under its articles of association) the Act allows companies to make certain material available on a website and default shareholders into 'deemed consent' to website communication. Note that the company is still required to notify the shareholders that such material has been placed on the website and where to find it.
- From April 2008 private companies will no longer have to appoint company secretaries unless they choose to do so.

Directors' Duties

The Act introduces a new statutory code of directors' duties to their companies, many of which have until now evolved through case law. Some of the provisions (those dealing with conflicts of interests) will come into force by October 2009.

The general duty is to act in a way that the director considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. The most significant change is a statutory requirement that in doing so the director must have regard, inter alia, to a list of factors including

the likely long term consequences of any decision, the interests of the company's employees, relationships with suppliers, customers and others, the impact on the community and the environment and the need to act fairly as between the members and the company.

Other duties include the duty to act within powers, duty to exercise independent judgement, duty to exercise reasonable care skill and diligence (and note that where a director has specialist knowledge a higher subjective standard must be met), and by October 2009, duty to avoid conflict of interests, duty not to accept benefits from third parties and duty to declare interest in proposed transaction with the company (replace the equitable rule).

In the next issue of PG Lore we will write further on directors' duties and various other aspects of the Act not discussed here.

Do companies need to take action?

The new law is intended to simplify and modernise existing rules and should be welcomed by many of the smaller companies. Some companies will want to change their articles of association to take account of the Act and it would be advisable to ensure that directors are aware of their duties and the implications to the company of the changes made under the Act.



Tally Maor-Mascona
Direct Dial: 020 7591 3375
Email: t.maor-moscona@pglaw.co.uk



SPORTELLI

HAS HOPE YIELDED IN DEFERENCE TO MARRIAGE?

The eagerly anticipated (at least in the world of leasehold enfranchisement) decision of the court of appeal in the case of *Earl Cadogan & Others v. Sportelli and others* [2007] EWCA CIV 1042 was handed down on 25 October 2007. For those expecting something controversial or groundbreaking, it is a disappointment. All the appeals were dismissed and the earlier decision of the lands tribunal (LRA/38&40/2005) stands. However, the issues that the case raised are not easy and the court clearly struggled to deal with them.



Statutory background

Various statutes since 1967 have conferred on owners of long leases of houses or flats rights to “enfranchise” by buying out (individually or collectively with other lessees) the reversionary interests, or simply to extend their leases for defined periods (50 years for houses and 90 years for flats). For ease of reference these rights can be referred to generally as “enfranchisement rights”. The first such statute was the Leasehold Reform Act 1967, which applied to houses. It was followed in 1993 by the Leasehold Reform, Housing and Urban Development Act which applied enfranchisement rights to flats. Over the years, both Acts have been substantially amended, with the intention of reducing the qualifying conditions for the exercise of enfranchisement rights and to make the enfranchisement process simpler. The result is that the legislation is unusually complex, reflecting the draftsman’s attempts to realise Parliament’s not always consistent or indeed understandable objectives within the intricacies of landlord and tenant law. There are now broadly four different rights of enfranchisement.

Under the 1967 Act

1. The right of the tenant of a leasehold house to acquire the freehold
2. the right of a tenant of a leasehold house to acquire an extended lease

Under the 1993 Act

1. The right of the tenant of a leasehold flat to acquire an extended lease
2. the right of the tenants of leasehold flats within a building acting collectively to acquire the freehold of that building.

The Appeals

The Sportelli appeals (and there were four consolidated cases) were concerned with two preliminary issues arising from the rights given to tenants by the 1993 Act, directed by the Lands Tribunal, to determine:

- (i) “the proper deferment rate to be applied to vacant possession value”; and
- (ii) “the proper valuation of any ‘hope value’”.

A further general issue had been raised as to the status of the Tribunal’s decision in relation to future cases in the Leasehold Valuation Tribunal (“LVT”). The LVT has primary jurisdiction to determine valuation disputes in enfranchisement cases with a right of appeal (with leave) to the Lands Tribunal.

The 1967 and 1993 Acts each set out machinery for the assessment of the price at which the freeholder’s interest (or the extended lease) is to be acquired. These are found in section 9 of the 1967 Act and Schedules 6 and 13 of the 1993 Act. In principle

the price is fixed by reference to the market value of the interest, as it would be if unaffected by the existence of the statutory rights (what has become known generally, but not wholly accurately, as “the no-Act world”). This is in practice treated as including 1) the value of the right to receive a rent during the term of the lease and 2) the value of the prospective right to vacant possession at the end of the term. The latter, conventionally, is determined by taking the open market value of the freehold interest with vacant possession at the valuation date, and then discounting that value over the unexpired term of the lease, by application of a “deferment rate”. The deferment rate, in the definition adopted by the Tribunal, is:

“the annual discount applied, on a compound basis, to an anticipated future receipt (assessed at current prices) to arrive at its market value at [the valuation date]”.

That was the subject of the first preliminary issue.

The second preliminary issue derives from the assumption that the market value of the unencumbered freehold in any property will nearly always exceed

WHETHER OR NOT, AS A MATTER OF STATUTORY CONSTRUCTION, THE LEGISLATION ALLOWS “HOPE VALUE” TO FORM PART OF THE STATUTORY VALUATION WAS THE SUBJECT OF THE SECOND PRELIMINARY ISSUE.

the aggregate of the values of the interests of the tenant and reversioner considered separately. That excess is known as “marriage value”. In the real world therefore, a tenant is willing to pay more for the reversionary interest in his property than other potential purchasers – “the tenant’s overbid”. However, it is argued that those other potential purchasers of the reversioner’s interest will pay something more than just the capitalised value of the rent and the value of the right to recover possession at the end of the term because there will be the expectation that, at some point before the end of the lease term, they will be able to sell the freehold or a longer lease to the tenant and thereby release (and share in) the marriage value. That expectation is called “hope value”.

Whether or not, as a matter of statutory construction, the legislation allows “hope value” to form part of the statutory valuation was the subject of the second preliminary issue.

Hope Value

The court considered first the issue of “hope value”. The Tribunal had accepted that in principle “hope value” was identifiable as a separate “element of value” and capable of valuation as such. However, it decided that “hope value” could not, as a matter of statutory construction, be included in the valuation to determine the price to be paid by the tenant for an extended lease under the 1993 Act (the valuation

machinery being set out in Schedule 13 to the Act) or the price to be paid by the tenants collectively for the freehold under the 1993 Act (the valuation machinery being set out in Schedule 6 to the Act). The Tribunal had based its decision broadly on the legislative history of the valuation machinery under the 1967 Act. The Court of Appeal upheld the decision of the Tribunal but for different reasons.

The court stated that hope value and marriage value are directly linked. Hope value represents no more than the anticipation of future marriage value. The scheme of the 1993 Act contains detailed provision for the definition and allocation of marriage value, as a separate element of the price payable to the landlord. The question for the court was whether that left any scope for the separate inclusion of hope value. In the view of the court, it did not.

Schedule 13 1993 Act

Under schedule 13, the price to be paid by the tenant for the extended lease is made up primarily of two elements:

- 1) the value of the landlord’s interest with the tenant excluded from the market
- 2) 50% of the marriage value.

What the court said was that, since the landlord is receiving a share of marriage value under 2), it would be double counting if he also receives “hope value” (determined by reference to anticipated marriage value) under

1). You cannot value hope and the realisation of that hope in the same equation. Furthermore, the words used by the statute to exclude the tenant from the market at the valuation date “the tenant (not) buying or seeking to buy” must be read in a purposive sense, as referring to the acquisition of any interest from the landlord, not only at the valuation date but also at any time in the future. If the tenant is never to be in the market, there can be no expectation of future marriage value and hence no hope value.

This analysis is not without difficulty. Once the court had accepted that marriage value was the additional value to be unlocked only by the tenant, for which he would make his overbid, then the question must arise; additional to what? The answer is the amount to be paid by the third party investor on the assumption that the tenant is not in the market at the valuation date. That third party investor will pay hope value and marriage value is thence the additional amount the tenant will pay above that. It is not double counting but merely moving part of the value from the marriage value (which thereby reduces) to the investment value (which thereby increases). The conclusion that the statutory exclusion of the tenant from the market applies not only at the valuation date but also for all time, requires additional words to be impliedly added in order to give the statute its “purposive” meaning.



Schedule 6 1993 Act

In relation to collective enfranchisement, the court accepted that the position was more complex. Unlike Schedule 13, there is no exact match between the exclusion of the tenants from the assumed market for the value of the landlord's interest and the share of marriage value. All the tenants are excluded from the assumed market, but the landlord's share of marriage value is limited to that arising from the interests of the participating tenants. In relation to non-participating tenants, there is no specific provision for a share of marriage value to be taken into account.

The court pointed out that this was a change from the 1993 Act as originally enacted where only the participating tenants were excluded from the assumed market. Potential bids for lease extensions from non-participating tenants were not excluded from open market value. The court said that the effect of amendments made to Schedule 6 by the Housing Act 1996 seems to have been to leave the position unchanged in respect of participating tenants, but to remove hope value for non-participating tenants. The court took this to be a matter of deliberate legislative policy.

The court accepted (as it clearly had to do) that its decision in relation to collective claims gives rise to anomalies for which it was not able to offer any sensible solutions. First, while the landlord is paid for marriage value in respect of the leases of participating tenants, he receives nothing for the prospective marriage value of the other leases, which the nominee purchaser is left free to exploit without having had to pay for it. Secondly, it is not obviously purposive why a specific exception is made to have regard in the valuation, only to the interests of non-participating tenants who have served a notice under section 42 of the 1993 Act claiming an extended lease. Thirdly, it becomes difficult to explain the purpose of the requirement for the disclosure of agreements under section 18. The court accepted that the requirement to disclose agreements involving non-participating tenants seems to have little purpose if the additional value reflected in such agreements has no effect on the price payable to the landlord. This seems odd given that the whole purpose of section 18 was to provide a landlord with a remedy in those cases where the number of participating tenants is artificially kept to the minimum in order to avoid payment of marriage value.

Section 9(1A) 1967 Act

Although the Tribunal considered the issue of hope value under section 9(1A) of the 1967 Act, this was not part of the appeal. Nevertheless the court expressed a view. In *Sportelli*, the Tribunal had decided that hope value could be part of the statutory valuation under section 9(1A). However, in a subsequent case *Pitts and Wang v Cadogan* (LRA/79/2006, LRA/4/2007), it came to the opposite view and decided that it could not. That case is the subject of a separate appeal to the Court of Appeal. The court nevertheless decided that the Tribunal in *Sportelli* had erred by having regard only to the exclusion of the tenant's overbid under sub-section 9(1A), and ignoring the context of the section as a whole, including the specific provision for allocation of marriage value.

The current position therefore is, save in the specific case of a section 42 notice given by a non-participating tenant in a collective claim under the 1993 Act, hope value plays no part in the statutory valuations under the 1967 Act or the 1993 Act.

Deferment Rate

On the issue of the deferment rate, the Tribunal in *Sportelli* heard evidence from four financial experts and four property valuers, together with extensive legal argument, over a period of 11 days. As the court said "it is difficult to envisage a better qualified panel of experts for the purpose than those called in this case, or of specialist counsel on both sides of the argument". *Sportelli* was heard by a three-member panel of the Tribunal presided over by the President. It followed two earlier cases in the Tribunal on the deferment rate issue: *Cadogan Holdings Ltd v Pockney* (LRA/27/2003, 19 May 2004)

where the Tribunal (N J Rose FRICS) held that a deferment rate of 5.25% in respect of a house in the Prime Central London (PCL) area was not too low and *Arbib v Earl Cadogan* [2005] 3 EGLR 139, where the Tribunal (HH Judge Michael Rich QC and P H Clarke FRICS) considered together five cases and determined a rate for the PCL area of 4.5% for houses and 4.75 % for flats.

The Tribunal had rejected the deferment rate (7%) derived from open market evidence given by one of the property valuers in favour of a deferment rate derived by reference to a formula (familiar to financial analysts); $DR = RFR - RGR + RP$ (deferment rate equals risk-free rate minus real growth rate plus risk premium). Applying that approach they had arrived at the following:

1. Risk free rate: 2.25%; less
2. real growth rate: 2%; plus
3. risk premium: (for houses) 4.5%; (for flats) 4.75%; resulting in
4. deferment rate: (for houses) 4.75%, (for flats) 5%. (The higher rate for flats was intended to reflect "the greater management problems associated with flats")

The appeal was on the basis that the Tribunal had erred in law by irrationally rejecting the market evidence which suggested a higher rate. It was however accepted by the court that the market in the real world and the hypothetical market that the Act required for the purpose of the statutory valuation, were substantially different and it could not therefore be irrational for the Tribunal to reject evidence that came from a market which was so different from the market that the Act assumes. The appeal therefore failed.

Effect of Lands Tribunal decisions.

Finally, the court chose to comment on the Tribunal's guidance on the future effect of its decision as a precedent for LVTs. This was not strictly an issue in the appeal, since it did not affect the result but the observations made by the Tribunal on this point in its decision had been the subject of criticism. What the Tribunal did was to invite LVTs to adopt the deferment rates determined by them as the generic rates for the country as a whole, in the absence of compelling evidence to the contrary. As the Tribunal put it:

"This is justified because, as we have explained above, the deferment rate is unlikely to vary according to factors particular to the individual case. Some factors, including in particular the prospect of long-term growth, will not vary from case to case, while other factors, such as location and obsolescence, will already be reflected in the vacant possession value."

The Tribunal had gone on to say that the deferment rate could be treated as stable over time and it would require a trend movement in the risk-free rate, an established change in the long-term prospects for growth in residential property or some other compelling reason for the rate to be different. It was accepted that each case needed to be considered on its own facts but LVT's would need to be satisfied that there

were factors not reflected in the vacant possession value or in the rate itself that would justify a departure from the guidance rates.

The court agreed with the Tribunal that an important part of its role is to promote consistent practice in land valuation matters. It was therefore appropriate for the Tribunal to offer guidance and to expect LVT's generally to follow it. However, the court did think that, having heard evidence solely in relation to properties within the PCL area, there must be an implicit distinction to be made between PCL and other areas. As the court put it:

"That must leave the way open to the possibility of further evidence being called by other parties in other cases directly concerned with different areas. The deferment rate adopted by the Tribunal will no doubt be the starting point; and their conclusions on the methodology, including the limitations of market evidence, are likely to remain valid. However, it is possible to envisage other evidence being called, for example, on issues relevant to the risk premium for residential property in different areas."

This may appear to open a door that had been firmly closed by the Tribunal. However, that may not be easy to achieve. The court has endorsed the Tribunal's general approach to and the methodology used to calculate the deferment rate, and has indicated that the generic rate determined by the Tribunal is to be the starting point. The example given of what might be relevant evidence is the risk premium. The component parts of that, according to the Tribunal, are volatility, illiquidity, deterioration and obsolescence. What evidence is likely to be available of long-term regional variations in these factors? Market evidence, settlement evidence and previous decisions of tribunals on matters of fact and valuation evidence are all discredited as useful evidence and unlikely therefore to be of benefit. It is difficult to think of what evidence might usefully be called.

Is this the end of this particular battle? Maybe, although it is quite likely that one or more of the parties will seek leave to appeal to House of Lords, particular on the issue of hope value. In the meantime the regional valuers will no doubt be trying to find some evidence which can help them wedge open the door that the Court of Appeal has at least unlocked.



Damian Greenish
Direct dial: 020 7591 3350
Email: d.greenish@pglaw.co.uk

Congratulations to Karen Albany for 35 years at PG

KAREN ALBANY, ONE OF OUR LEGAL EXECUTIVES AT PG, RECENTLY CELEBRATED HER 35TH ANNIVERSARY OF WORKING AT THE FIRM.

What are you most proud of achieving at PG?

One of our old partners once told me that he went into the law to help people as opposed to a purely business outlook to make money. So I am proud to receive letters thanking me for my help from my clients tenants and the tenants buyers as well as my clients as I know my work benefits everyone involved.

gesture. On a lighter note, I remember Damian playing cricket in the corridors using a ruler and balls of paper...

Best night out at PG?

The very first Office Christmas Party at the Bung Hole Wine Bar in Chancery Lane. Everyone let their hair down a little too much and there were anecdotes from the party which were discussed for years afterwards. One of which was a solicitor who found himself at the bottom of some roadworks and had to be rescued.

Has PG changed much in the past 35 years?

Yes, then the height of technology was a Telex machine which punched holes in a tape which could then be fed through to another Telex machine elsewhere - the prototype e-mail! Documents were also sewn up with ribbon which was actually very relaxing - a bit like getting your knitting out.



Karen (on the right) outside the old PG offices, 11 South Square, Gray's Inn, in 1973

Fondest memory?

It was very early in my career when we received cash pay packets. I had only been working a couple of months when my paypacket was stolen from my bag by a pickpocket in the street. The next morning I found an envelope on my typewriter with some money inside from an anonymous benefactor - I never discovered who it was but it was such a kind

Ian Gill joins Pemberton Greenish

Ian's philosophy towards clients is really quite simple. It is always to try and exceed their expectations whether in terms of the quality of legal advice given or in the speed and efficiency of its delivery.

"What attracted me to PG was its evident commitment to excellence. This is something that is essential to any law firm hoping to expand the quality of its client base and particularly is true of commercial property work."

Ian lives just 8 minutes walk from the office so has no excuse for being late for work. He is married with 3 children, one of whom is at Sandhurst, one in Shanghai learning Mandarin and one in her last year at Durham University.

He is a keen golfer and tennis player and regularly struggles to understand the meaning of plays at the Royal Court Theatre.

Ian Gill
Direct dial: 020 7591 3363
Email: i.gill@pglaw.co.uk

PG Estates Shoot

In September PG was delighted to hold its inaugural Estates Clay Pigeon Shoot down in the wilds of Sussex. Six estate teams competed for a range of prizes including best and worst shot of the day, and the Best Team award of the PG Cup! The Grosvenor team, led by Giles Clarke were the ultimate winners. So congratulations to them and the other participants of the day.

The winner of the individual cup was Richard Grant, finance director of the Cadogan Estate. The shoot was held at Northall Clay Pigeon Club run by the Dan and Jan Kerwood, the parents of Charlotte Kerwood. Charlotte is an Olympic hopeful who we have been sponsoring for the last two years.

We are very much hoping that Charlotte will be selected to represent the United Kingdom in the ladies event at the Beijing Olympics next summer.



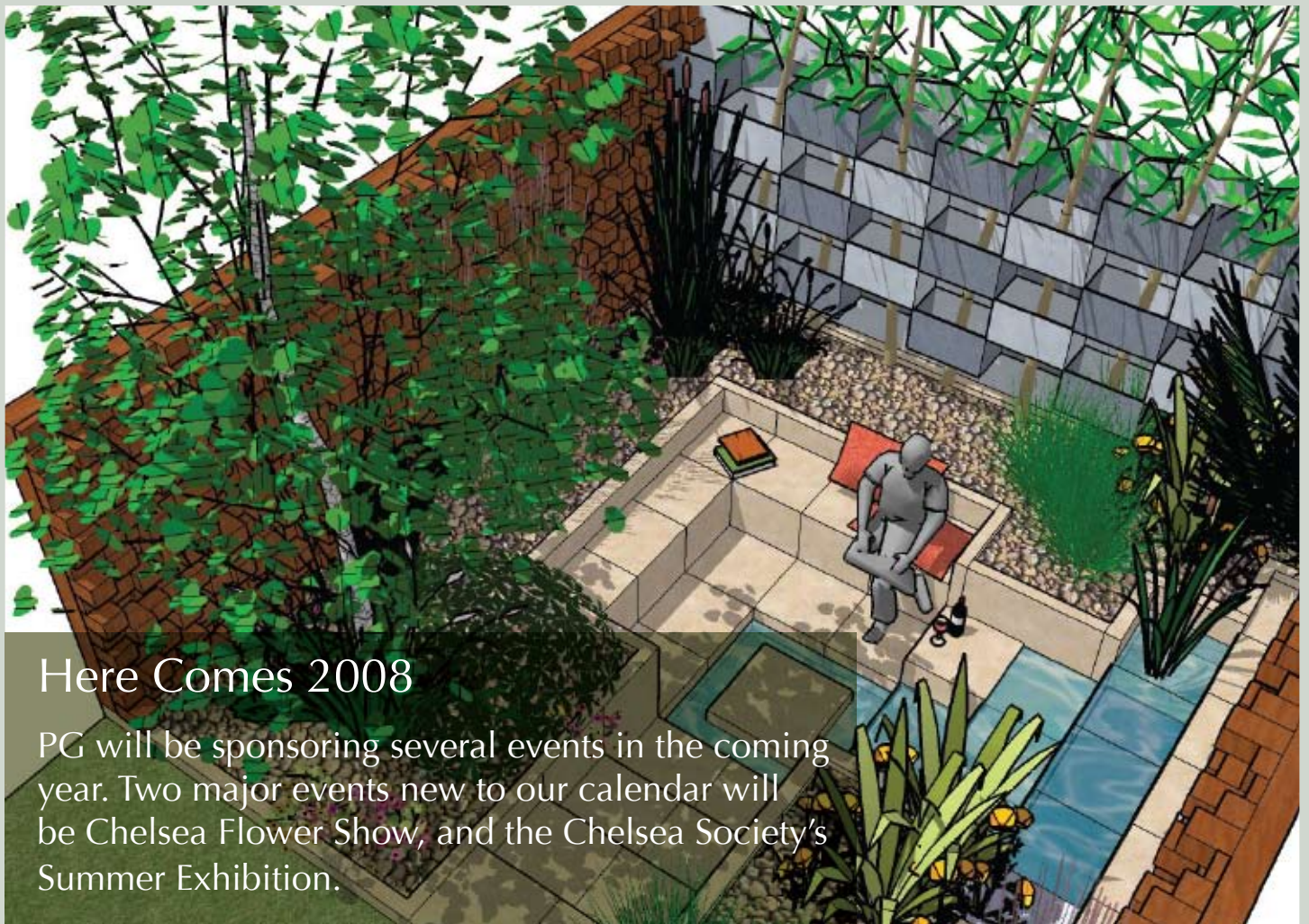
Robert Barham and Damian Greenish with Olympic hopeful, Charlotte Kerwood, and one of the winners, Richard Grant of the Cadogan Estate.



Sponsorship

Surrey Cricket

We have continued with our sponsorship of the Youth Academy at Surrey Cricket Club. The PG Scholarship Fund, a fund aimed at giving financial assistance to an Academy graduate, was presented to Stuart Meaker at an Awards Ceremony in September.



Here Comes 2008

PG will be sponsoring several events in the coming year. Two major events new to our calendar will be Chelsea Flower Show, and the Chelsea Society's Summer Exhibition.

This will be the first time we have sponsored a garden at Chelsea Flower Show. The Show, is to be held this year on 20 – 24th May at the Royal Hospital, Chelsea, London.

We are working with garden designer Paul Hensey of Elysium Designs to create an urban garden design suitable for a house in Chelsea which will be entered in the small gardens category. Paul has previously designed gardens for the Royal Horticultural Society's Tatton and Hampton Court garden shows, where he has won Best in Show, Gold and Silver-Gilt medals. This is the first time he has exhibited at Chelsea.

We are very excited by his design (see above) and are looking forward to seeing it at the show.

www.rhs.org.co.uk/chelsea

Disclaimer: The articles in this publication are intended as a general guide only. Readers are advised to take specific advice before relying on anything stated herein.

In addition to the Flower Show we will also be sponsoring The Chelsea Society's summer exhibition, **Actors & Musicians of Chelsea** which will be held at Chelsea Old Town Hall at the same time as the 2008 Chelsea Festival, 20th – 29th June.

This free exhibition will be largely pictorial and possibly less academic than some previous Chelsea Society exhibitions. Record numbers of visitors are expected to attend.

The popular theme for the show will embrace talents as diverse as Mozart and Mick Jagger of the Rolling Stones. Technically, Mozart did actually reside in Pimlico - but Mick Jagger is moving

back to Cheyne Walk imminently, following his famous sojourn there in the 1960s. The exhibition will also showcase actors such as Sir John Gielgud, Noel Coward, Christopher Lee, Dirk Bogarde, Felicity Kendall, and musicians such as Neil Tennant and Julian Lloyd Webber.

The period covered will commence with 18th century Ranelagh Gardens and later Cremorne entertainments, right up to the present day.

www.chelseasociety.org.uk

Pemberton Greenish
45 Pont Street
London SW1X 0BX
T: 020 7591 3333
F: 020 7591 3300
E: law@pglaw.co.uk
www.pglaw.co.uk

