In for the long term Individual extensions of flat leases under the LRHUDA 1993 (as amended by CLRA 2002) Principles, practice and problems

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Introduction

WHAT?

- Individual right to a new lease, for a term expiring 90 years after the term date of an existing flat lease, at peppercorn rent; on payment of premium to landlord.
- and tenant (T) can repeatedly apply for new leases to extend his term almost indefinitely (s59 of 1993 Act)

- Introduced by Chapter II, Leasehold Reform, Housing and Urban Development Act 1993 ("the 1993 Act"). Originally very much a London-centred problem, and a vote winner amongst flat owners with diminishing terms and big London estate landlords.

- Amendments made by Commonhold and Leasehold Reform Act 2002 ("the 2002 Act") have made it even more attractive, and often preferable to either collective enfranchisement or commonhold. 2002 Act changes came into force in England on 26/7/02, Wales on 1st January 2003.

- If care is taken, and procedure followed, simple and inexpensive way for clients to acquire asset of significant value for a good price.

- L and T cannot 'contract out' of this right: s93 1993 Act makes that void, and also allows court e.g. to set aside and vary agreements to surrender or for new leases made outside the Act procedure

WHO?

- "Qualifying tenant" of "flat": s 5 as qualified by s39

- Big 2002 change was removal of residence/ "only or principal home" condition for former, and removal of "low rent" and longer term requirements

- Now essentially just ownership of "long lease"(s7 1993 Act: essentially term granted for 21 years or more) of flat, for previous 2 years or more

- So can be limited company, same person can be "qualifying tenant" of a number of flats in building [s39(4) 1993 Act; ss. 5(5) and (6) of 1993 don't apply to this Chapter]

- Can be personal representatives of deceased person (if deceased owned for two years prior to death, and right exercised [see below] within two years of grant of probate or administration – s39(3A), s42(4A). They may even have a duty as executors and trustees to maximise estate value by exercising right.

- "Flat" – you know it when you see it, but s101 definition in Act applies – separate set of premises, part of a building, constructed or adapted for use as dwelling, whole or material part of which lies above or below some other part of building.

- extended definition for new lease claims, includes any "garage, outhouse, garden, yard and appurtenances belonging to or usually enjoyed with the flat"

- parking spaces, outdoor "outhouses", but not e.g. storeroom on different floor of same building (*Cadogan v. McGurk* [1996] 4 AER 643)

FROM WHOM?

- the "competent landlord": s40

- must be person with reversion expectant such that they would be able to grant the new +90 years lease

- so either freeholder, or superior leaseholder with term of T's lease +90 years

- so there may well be an immediate, intermediate landlord/reversioner who is not the "competent landlord" : but they will still be relevant for the purposes of notices and payment of the premium [see below]

- qualifying tenant has right to serve notices under s41 to enable him to identify the competent landlord: asking immediate landlord or person receiving rent to state whether he is freeholder, and if not who is; and details of his and all other superior leasehold interests; and similar right to serve notice on freeholder. Recipient has 28 days to respond, in default of which T can serve 14 day default notice then apply to Court for enforcement order under s92

- so need to establish this first.

HOW?

- Notice of Claim, ss. 42 and 43

- No *prescribed* form, but certain essential requirements

- Name and address of tenant, and particulars of flat sufficient to identify premises to which claim extends. Safest to include lease and/or title plan, or additional plan if any particular "appurtenances" not apparent from lease or title plans.

- Particulars of lease sufficient to identify it: date, term and parties. May as well enclose copy of lease with letter serving notice?

- Specify proposed terms of new lease: usually "the terms of the existing lease", but some provision for changes [see below]

- Name of person acting and address for service

- Specify date by which landlord must respond with counter-notice under s45 [see further below], "not less than two months after the giving of the notice"

- Must be signed personally by tenant [s99(5)], signature of solicitor or agent won't do, nor will that of person with power of attorney! (see *Viscount Chelsea v. Hirshorn* [1998] 2 EGLR 90 and *St. Ermins Property v. Tingay* [2002] 2 EGLR 53). What if they can't physically do this?!

- Tenant must "give notice" to competent landlord AND any third party to the tenant's lease e.g. Man Co, surety etc. If THAT isn't done, notice hasn't been "given" at all (*Free Grammar School of John Lyon v. Secchi* [1999] 3 EGLR 49)

- Notice is regarded as "given" to competent landlord if given to any of other landlords instead (Sch. 11, para. 1), BUT tenant must "give a copy" of it to every other person known or believed to be a landlord (para. 2), and the notice must state to whom copies of it are being given [para. 2(3)]!

- Landlords also have duty to pass on copies to other landlords of whom they know: para. 3

- If any landlord doesn't receive a notice or copy of notice, and had previously given its details in response to a s41 request, T's notice may cease to have effect at end of period it specified for service of counter-notice (para. 4(1)). If that is not the position, but a person fails to pass on a notice to the competent landlord, he may be liable for losses caused as a result (to T or CL – e.g. if CL is then unable to serve counter-notice in time).

- *Must specify premium which tenant proposes to pay for grant of new lease, and any other amounts payable under Sch. 13 of Act; and must specify separate sums for *each* "landlord" where there is/are intermediate landlord/s being served or notified.

- Premium calculation considered in detail below, but for purposes of notice, it has to be a genuine proposal made in good faith. Can't just rush a notice out with a nominal or 'silly money' figure (see *9 Cornwall Crescent v. Kensington & Chelsea LBC* [2006] 1 WLR 1186: but no longer the position that initial notice figure has to be backed by some valuation basis)

- But best to get some valuation evidence and calculations at outset of process, even if time is short.

- => TRY TO GET IT RIGHT! Don't want to get into arguments, or try to rely on Sch. 12 para. 9 which says notice not invalidated by "inaccuracy in any of the particulars required by s42(3).." (i.e. name, address, particulars of lease); or try to amend notice under Sch. 12 para. 9(2) if property misdescribed. NB Other matters do go to validity i.e. genuine proposal for premium, date for service of counter-notice.

- Once valid notice is served: register it as a unilateral notice on competent landlord's registered title under LRA 2002. If his title is unregistered, register it as land charge against his name.

- Also note that the benefit, rights and obligations arising from a valid notice once given are *assignable* but only with the lease of the flat (if not assigned together, notice is deemed withdrawn under s43(3)).

- Note: circumstances in which qualifying tenant cannot serve a s42 notice, and any notice purported to be served is of no effect (Sch. 12 paras. 1 to 3)

- Include e.g. where tenant obliged to give up possession in pursuance of a court order.
- If proceedings are "pending" to enforce right of forfeiture or re-entry, no s42 notice may be served without the leave of the Court. Post 2002 Act, in relation to forfeiture of residential leases, this will presumably not apply where L has merely applied to LVT for determination of whether T is in breach or not (and so whether he may serve s146 notice then bring forfeiture proceedings?)

- Conversely, L cannot commence forfeiture proceedings without leave of Court if valid s42 notice already served (but leave will be given if T's notice given solely or mainly to avoid consequences of breach of covenant: Sch 12 para. 6)

- And note: *collective* enfranchisement claims take priority over individual lease claims. Section 42 notice and individual lease claims are *suspended* if a CE notice (s13) has been served before it OR if it is served after it (ss. 53 and 54). L required to give T notice of this, but suspension only lifted once CE notice and claim procedure concluded.

WHAT IF YOU GET IT WRONG?

- If an invalid notice is served, or it may be invalid (and L is arguing that it is), what should you do?

- If notice *withdrawn*, or is deemed withdrawn, s42(7) says no new notice until 12 months after date of withdrawal: so in a rising market, your client would lose out (as well as effect of further year of term expiring) if had to wait another year before trying again.

- Better to serve a second notice "without prejudice to contention that first notice is valid". If first one held valid by Court, then second one a nullity, and falls away. OR if you think L is right and first notice was invalid, then state openly that you are treating it as invalid and a nullity, and start again with a second one: see *Sinclair Gardens Investments v. Poets Chase Freehold Limited* [2007] EWHC 1776 (Ch.), Morgan J. (a case on s13 and collective enfranchisement, but same principle must apply here)

WHAT NEXT?

- Over to landlord….

- "Competent landlord" has to give a counter-notice by the date specified in the s42 notice

- If he doesn't, or messes up and serves an invalid notice, then T can simply apply to the Court under s49, within 6 months of the original date specified, for order that a lease be granted in the terms on his notice (including the price); which Court "may" grant if satisfied that T qualified and served a valid notice. If so satisfied, likely position is in fact that Court has little or no discretion and must make order (see *Willingale v. Globalgrange* [2000] 2 EGLR 55)

- L has some ancillary rights as soon as T's notice is served:-

  - right of access to flat for purposes of valuation, on not less than 3 days' notice (s44)
  - right to serve notice requesting payment of deposit by T within 14 days: the greater of £250 or 10% of sum specified in T's notice: LR (CELR) Regs. 1993, Sch. 2 para.2. But non-payment of deposit does not render T notice invalid – L would have to serve default notice and apply for compliance order from court.

    (and right to require T to "deduce title", although this v unlikely to be an issue in most cases).

- Counter-notice must:-

  - state that L either admits or does not admit that T had the right to a new lease when notice served
  - if applicable, also state that he intends to redevelop the premises and therefore to apply for an order under s47 declaring that T's right shall not be exercisable

- If T's right admitted, counter-notice must then state which of T's proposals are accepted, and which not; and if not, what L's counter-proposals are. Issue is generally likely to be amount of premium (but see also terms of lease – below). CA held in *9 Cornwall Crescent* case that L can pretty much put any figure in this he likes: no obligation to be 'realistic' or accurate on this, since lease can't be granted in default for this price (unlike position with T's notice).

- If T's right not admitted, then L has 2 months in which to apply to the Court for a declaration on the issue. Strict time limit, and if application not made, T has right as above then to apply under s49 in default. If L's application unsuccessful and Court declares that T has right, must make order requiring L to serve further counter-notice as per an admitting one (s46)

  (But these applications should be pretty rare now that "qualifying tenant" test so simple)

- if L accepts T's right in principle to serve notice, but disputes validity of notice: should serve counter-notice as per an admitted right, but with covering letter saying it is "without prejudice to contention that notice invalid" – then apply to Court under s90 for declaration on issue

- if "intention to redevelop": only in cases where lease has <5 years left to run, L has to apply to Court within 2 months, test is similar to s30(1)(f) LTA 1954

WHEN DOES THE LVT GET INVOLVED?

- If counter-notice admits tenant's right, but any of the "terms of acquisition" remain in dispute 2 months after counter-notice, either party must apply to LVT to have terms of acquisition determined not later than 6 months from date of counter-notice

- So in effect, a 4 month 'application window' – if no application made, then T's notice is deemed to have been withdrawn (s53(2))

- What "terms of acquisition" might be in dispute?

- Almost always money i.e. the amount of the premium to be paid (see below)

- Length of term and rent (peppercorn) fixed by statute

- Parties free to agree new terms if they wish (s57(6)), but default position is terms of existing lease, plus three mandatory statutory terms under s57 (prevention of sub-lessee of tenant of new lease from having his own new lease right; retention of L right to obtain possession on ground of redevelopment in last 12 months of old lease or last 5 years of new lease; plus term saying "this lease is granted under s56 of [the 1993 Act]")

- Unless parties agree, LVT has limited scope to impose any new or different terms

- Main exceptions are:

  - s57(2): insertion of new service charge provisions, if L obliged under new lease to provide services: new lease "shall" include terms that T pay service charge related to cost of these services, and that such obligation be enforceable as if rent obligation
  - s57(4): where necessary to remedy "defect" in lease: not just insertion of new or more convenient term (*Waitt v. Morris* [1994] 2 EGLR 224); or
  - s57(6)(b) where "changes" since date of original lease, either in circumstances or in law, make it unreasonable to retain a particular term.

- Application to LVT is in fairly simple form, in accordance with LVT (Procedure) (England) Regs. 2003 in England; LVT (Procedure) (Wales) Regs. 2004: Regs prescribe what information application must contain and what documents must accompany it.

- Will proceed, via any directions given by LVT, to hearing if not settled.

- LVT: one chair (usually lawyer, sometimes surveyor) plus two wing members (usually one lay and one surveyor). Will hear argument, evidence (including valuation evidence – see below), then give decision in writing shortly afterwards. Appeal lies to Lands Tribunal.

- Once it has done so, if new lease to give effect to the terms of acquisition as determined by the LVT has not been completed within 2 months of that determination, either party must in the 2 months after that apply to the Court for an order for a lease to be granted in such terms as the court orders (reflecting the decision of the LVT) – if this still cannot be agreed, the Court may e.g. refer it to conveyancing counsel to be drafted for execution.

- If no lease executed and no such application made, deemed withdrawal of notice under s53.

- When might this happen? E.g. if price is too high. Obligation to grant lease is dependent upon the premium and sums determined as payable being paid to L, and payment of any rent or costs also due to L. If T gets cold feet and says he won't pay, then will simply not apply for new lease, and accept deemed withdrawal as a consequence.

- On "costs": note this is essentially "section 60 costs" only i.e. L's costs of investigating T title, obtaining valuation, and drafting any lease. NOT costs of arguing or negotiating the claim, and costs before LVT are generally irrecoverable (like CC small claims: costs only awarded in

exceptional cases of frivolous/vexatious/unreasonable behaviour etc. and then only up to maximum of £500!).

HOW MUCH? THE BIG ISSUE

- This is by far the most common contentious issue between L and T, and the principal reason for contested hearings before the LVT.

  Need to obtain expert valuation evidence on this issue at the outset, before any notices are served. While principles not that complex, especially if you have a copy of Parry's Valuation Tables, no point in 'having a go' yourself or giving client a 'rough estimate' or ball park figure. If matter goes further you will need expert valuation evidence in any event.

- Schedule 13 of 1993 Act: premium to be paid to landlord is aggregate of:

  - diminution in value of L's interest in flat
  - L's share of "marriage value" (<u>but</u> if unexpired term exceeds 80 years, this is deemed to be nil)
  - any additional compensation payable to L under para. 5 if grant of new lease adversely affects value of other property of L (e.g. thwarts some development plans he might have for rest of building)

- Note valuation assumptions under Sch. 13 para. 3 for L's interest

- = OMV but with no tenant seeking to buy it (so no 'special purchaser' factor), subject to existing lease, and assuming there was no 1993 Act right to acquire a new lease.

- And disregard of T's improvements to flat (of both T and predecessors)

- Diminution in value of L's interest: 2 elements =

  i) sum to compensate L for loss of ground rent for remaining years of lease (since new lease will be at a peppercorn rent). This will therefore be a capitalised value for that rent, arrived at by selecting a capitalisation or 'yield' rate, then consulting Parry's Tables to see what multiplier is arrived at for the ground rent for x number of 'years purchase' ("YP") @ the yield rate chosen: usually expressed as e.g. "YP 57 years @ 7% = 13.9837" or similar.

     If the ground rent is small, this may not be a very large sum in the end.

  ii) the value of L's reversion now. Despite use of the word "diminution", the value of L's interest after the grant of the new lease is usually regarded as virtually nil, so LVTs and valuers will usually just take the value of L's interest now as their figure.

     The basic idea of reversion valuation is to take the present vacant possession value of L's interest, then apply a 'deferment' multiplier to it to reflect the fact that such vacant possession is several years away (i.e. the unexpired term of the lease). The multiplier is arrived at by using the Present Value of One Pound Table ("PV£1") in conjunction with a % deferment rate

     So you might see it expressed by a valuer as e.g. "PV £1 deferred 57 years@ 5% = 0.06197"

     It is that by that last decimal fraction that the present vacant possession value is multiplied to arrive at the figure for the value of L's interest . So obviously, the fewer years there are left, the bigger that decimal fraction multiplier will be.

Marriage value

- remember, only applicable in new lease cases if >80 years to run

- it is, essentially, the difference between (on the one hand) the aggregate value of the interests of T, L and any intermediate leasehold interests before the new lease; and (on the other) that aggregate value after grant of the new lease. The two important figures in this calculation will be the rise in value of T's interest (from getting a nice longer lease) and the loss in value of L's interest (the figure calculated above)

  Additional compensation (para. 5)

- this is fairly rare: there are few reported cases in which such compensation has been ordered. Hague on Leasehold Enfranchisement makes the point that if L complains of loss of development potential, T may point to L's reserved s61 right to terminate for redevelopment and argue that he suffers no loss. One LT case cited by Hague resulted in an award to L of £288,000 for the additional loss caused by a new lease of a flat in a building in Belgravia preventing the building being converted back into a more valuable single house.

- since the 2002 Act, L's share of marriage value is always 50%

  Intermediate leases

- just to complicate matters, in a case where there are intermediate leasehold interests, T must also pay them the diminution in value of *their* interest as a result of the new lease, plus any additional compensation under para. 5 if applicable. However, the marriage value is split between the freeholder and those intermediate landlords in proportion to the diminution in value of their respective interests. T pays the marriage value sum to the competent L, and it is then his duty to pay his fellow Ls' shares of it (Sch. 13 para. 10)

- Valuation of intermediate leasehold interests: detailed LT guidance in *Nailrile v. Cadogan* and others (LT, 22/12/08)

***Big recent and current issues in valuation and premium calculation**

- What % rates to apply?

- i) to capitalisation of ground rent

- see *Nicholson v. Goff* [2007] 1 EGLR 83 (LT)

- Para. 9 of judgment: various factors, including length of term, amount of ground rent, and whether any provision for review of it.

- Recent economic effects may now have some influence on yield calculations

- LT says: don't always assume that this % rate will be same as deferment rate (below), although very often valuers have traditionally used same rate for both.

- ii) to deferment of L's interest

- *Cadogan v. Sportelli* [2007] EWCA 1042

- CA refused to disturb LT's conclusion, on all the (very complex) expert evidence, of a generic deferment rate for the Prime Central London area of 5% for flats. Outside that area, while 5% would be the starting point, local risk and investment factors might be capable of affecting it: this would be a matter for evidence in future cases.

- HL in *Sportelli* [2008] UKHL 71: appeal only on question of whether 'hope value' in purchase of freehold reversion (i.e. prospect of early realisation of marriage value if T exercises right) could be taken into account in valuation of L's interest: HL said no in relation to Sch. 13/individual flat leases

- All sounds complex? It is, but see worked example…

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