

The search for the holy grail continues

Natasha Rees reviews the decision in Mundy, which saw the Court of Appeal analyse current valuation methods



Natasha Rees is a partner and head of property litigation at Forsters LLP

'The Mundy appeal focused on the method that is used in calculating the marriage value element of the premium of a lease extension, which only applies where the lease has fallen below 80 years.'

The leasehold market has been hitting the headlines recently with the publication of the government's response to the consultation on unfair leasehold practices (*Tackling unfair practices in the leasehold market*) in December 2017, followed closely by the much-anticipated decision of the Court of Appeal in the case of *Mundy v The Trustees of the Sloane Stanley Estate* [2018].

The *Mundy* decision was heralded by the press as a chance for leaseholders to significantly reduce the amount they would have to pay 'rich freeholders' for their lease extensions. The press focused on a new valuation model called the Parthenia model which, when applied, significantly reduced the premium payable in lease extension claims under the Leasehold Reform Housing and Urban Development Act 1993. In fact, the appeal focused on a very narrow point of law concerning the interpretation of the 1993 Act and it was never likely to have the ramifications that leaseholders hoped for, although the Court of Appeal was given an opportunity to either reject or endorse this new valuation model and to provide guidance for future valuations.

The widespread interest in the *Mundy* case has highlighted leaseholders' general dissatisfaction with landlords, which the government tried tackling through its recent consultation. The consultation received 6,000 replies, demonstrating the strength of interest in the issue, and the government's response paper

published on 21 December 2017 was very critical of landlords.

It is clear that the government is going to push through reforms to deal with practices currently adopted by developers, described in the response as 'feudal'. This will include preventing the sale of leasehold houses and tackling the issue of onerous ground rents. For existing leaseholders there will also be wider reforms relating to leasehold ownership that will extend to enfranchisement. The main aim will be to make buying a freehold or extending a lease easier, faster, fairer and cheaper. Although the *Mundy* decision has not produced the result that leaseholders were hoping for, many leaseholders are now waiting to see if there will be a change in the law that will reduce their premium or the cost of their claims.

The Mundy decision

The appeal concerned a lease extension claim relating to a flat in Elm Park Road in London SW3, which was one of three applications originally determined by the Upper Tribunal in 2016. Mr Mundy was given permission to appeal on one ground and the Court of Appeal also considered his application for permission to appeal on two other grounds. The appeal focused

Kosta v Carnwath & ors
[2014] UKUT 0319 (LC)
Mundy v The Trustees of the Sloane Stanley Estate
[2018] EWCA Civ 35

on the method that is used in calculating the marriage value element of the premium of a lease extension, which only applies where the lease has fallen below 80 years. The 'marriage value' is the amount by which the leasehold interest will increase upon the

First, it is used to determine the value of the freehold with vacant possession. A valuer needs to convert the value as derived from actual sales of leases to the value ascribed to the freehold. The relationship between the two, which is expressed as a percentage, is

obviously problematic because leases sold in the open market do not have the benefit of rights under the 1993 Act so there is no direct comparable evidence.

The Court of Appeal acknowledged that the Upper Tribunal (UT) has been grappling with the relativity issue for many years, particularly following the removal of the residence condition. The UT has been presented with varying methods of determining relativity, none of which has proved to be without flaws. The most common or traditional method involves the use of relativity graphs, which plot the relationship between lease length and the freehold value derived from settlement evidence. In 2014 in a case concerning the Leasehold Reform Act 1967, known as *Kosta v Carnwath*, the UT was presented with a new model called the Parthenia model. This was a model proposed by the tenant's valuer, James Wyatt, that relied upon sales data between 1987 and 1991. The UT rejected the Parthenia model. It was also critical of the more traditional methods, recommending the development of a standard graph by the Royal Institute of Chartered Surveyors (RICS). Following this decision, a group from the RICS chaired by Jonathan Gaunt QC tried but failed to produce a definitive graph.

The consultation received 6,000 replies, demonstrating the strength of interest in the issue, and the government's response paper published on 21 December 2017 was very critical of landlords.

grant of the new lease. To assess this increase, the value of the existing leasehold interest must first be established.

Relativity

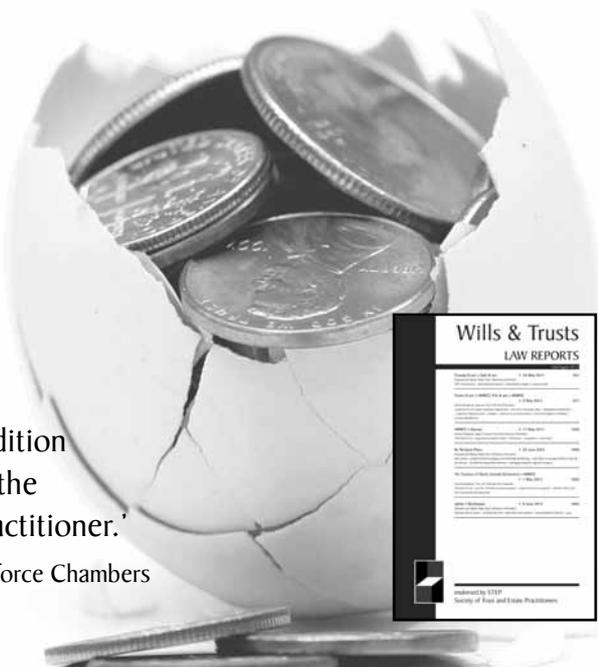
The key issue in the appeal was the method used to determine what is known as 'relativity'. There are two aspects to this concept.

known as 'the real world relativity'. Secondly, the concept is used to describe the relationship between the value of the leasehold interest in the real world and the same interest where the tenant has no statutory right to acquire a new lease. This is because the statutory valuation requires that these rights be disregarded. This is

The specialist set of law reports for the specialist practitioner

Wills & Trusts LAW REPORTS

Endorsed by:



'An essential addition to the library of the private client practitioner.'

Mr M Studer, Wilberforce Chambers

The Parthenia model

In *Mundy*, the Parthenia model was in the spotlight again. The Parthenia model is based on a statistical technique known as hedonic regression analysis. This method of analysis seeks to isolate particular characteristics and attribute a value to them. The Parthenia model was applied to sales transactions which took place between 1987 and 1991 before the coming into force of the 1993 Act, which neatly eliminated the effect of the Act on relativity as required by the statutory valuation method.

Upper Tribunal decision

The UT in its original decision had considered a number of relativity graphs but didn't specifically endorse any of them. After hearing evidence for nine days, it reached a determination that relied on a

Special subscription rate for STEP members – save £100
For subscription enquiries call 020 7396 9313

combination of the Savills 2002 enfranchiseable graph and the Gerald Eve Graph. It rejected the Parthenia model both as a model for determining the freehold vacant possession value and for determining the value of the lease on the assumption that it did not attract 1993 Act rights.

It is generally accepted that a lease with 1993 Act rights is worth more than one without such rights. The main problem that the UT had with the Parthenia model was that when applied to agreed values it produced a figure for a lease without rights under the Act which was higher than the same lease with rights under the Act. This was an impossible result. In reaching this conclusion, the UT had referred to the Parthenia model as 'the Clock which strikes 13'. The UT also criticised the fact that it was a model that relied on sales data from the period 1987-91 and it was generally accepted that relativities had changed significantly since that period due to changes in the market. The model therefore failed to produce results that were observed in practice.

Ground of appeal

Mr Mundy's ground of appeal concerned the statutory assumption that the lease has to be valued with no statutory rights. The question was whether it was possible to compare the value of the lease in the real world with the value of the lease without such rights as shown by the Parthenia model. The Court of Appeal dismissed the appeal, deciding there was no legal justification for ignoring real market transactions. It made the following points:

- It decided that the issue was not a point of law and that the acceptance or rejection of the Parthenia model was a question of fact that had been properly determined by the UT after considering detailed evidence.
- It considered that any property valuation proceeds by way of comparison with appropriate adjustments and that the

comparison between no-Act and subject-to-Act valuations is a matter of valuation judgement.

- The assumption is that the sale takes place in the open market. The principle of reality must be applied, which among other

relativity and thus a lower premium, in some cases resulting in a 30% reduction in the price. It seems that valuers will have to continue to rely on their valuation judgement and their ability to make the necessary adjustments to comparable evidence in determining the premium payable.

The Parthenia model is based on a statistical technique known as hedonic regression analysis. This method of analysis seeks to isolate particular characteristics and attribute a value to them.

things means that although the sale is hypothetical there is nothing hypothetical about the market in which it takes place. The valuer is not precluded from considering transactions in the real world.

Conclusion

The Court of Appeal ruled that the UT had reached its verdict that the Parthenia model should be rejected based on ample evidence. It also considered that the UT was entitled to rule out the future use of the Parthenia model in its current form in order to provide definitive guidance to tribunals on valuation matters going forward.

The wholesale rejection of the Parthenia model has caused upset to leaseholders, because this model generally produces a higher

The time limit for appealing the decision has now expired and Mr Mundy has not sought permission to appeal this decision to the Supreme Court. For the time being, the traditional methods for valuing relativity will continue to be applied.

There is, however, some light at the end of the tunnel for leaseholders. Following the government's paper on unfair leasehold practices, the Law Commission is considering how to simplify valuations under the 1993 Act. The government also seems keen to tackle the issue of statutory costs with a view to making the whole process a lot cheaper. So, it seems that leaseholders will have to continue to wait and hope. As Lewison LJ, who gave the leading judgment, concluded, 'it may be, that the Holy Grail will one day be found'. ■

The 'no rights' assumption

The Court of Appeal also refused permission to appeal on two further grounds that related to the 'no rights' assumption.

Schedule 13 of the 1993 Act states:

... on the assumption that Chapter 1 and this Chapter confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease...

Mr Mundy sought to argue that there was a 'no Act world' rather than a 'no Act building', ie that no one in the country had 1993 Act rights.

The Court of Appeal felt that this was not the natural meaning of the words of the 1993 Act and since the argument had already been conceded at the UT hearing, it could not be relied on now.