HOUSE OF LORDS SESSION 2008–09
[2008] UKHL 71
on appeal from: [2007] EWCA Civ 1280

OPINIONS
OF THE LORDS OF APPEAL
FOR JUDGMENT IN THE CAUSE

Earl Cadogan (Appellant) *v* Pitts and another (Respondents) and one other action
Earl Cadogan and others (Appellants) *v* Sportelli and another (Respondents) and two other actions

Appellate Committee

Lord Hoffmann
Lord Hope of Craighead
Lord Walker of Gestingthorpe
Lord Mance
Lord Neuberger of Abbotsbury

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Respondents:
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(Pitts and Wang) Andrew PD Walker
(Sportelli and 27/29 Sloane Gardens) Stephen Jourdan
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LORD HOFFMANN

My Lords,

1. For my part, I would have been content to dismiss these appeals for the reasons given by Carnwath LJ in his lucid and convincing judgment. But since your Lordships are minded in one respect to differ from his analysis, I must explain why on this point I regretfully feel obliged to dissent. For this purpose, I gratefully adopt the recital of the facts and statutory provisions in the speech to be delivered by my noble and learned friend Lord Neuberger of Abbotsbury, which I have had the advantage of reading in draft.

2. The Leasehold Reform Act 1967 provided in section 9 that the price payable for the house should be the amount which, on certain specified assumptions, it would be expected to realise if sold on the open market. The open market means everyone who could reasonably be expected to be interested in buying. Among these potential purchasers there will sometimes be one or more to whom the property would be worth more than to others. In *IRC v Clay* [1914] 3 KB 466, 472, Sir Herbert Cozens-Hardy MR gave the example of a small farm in the middle of a wealthy land-owner's estate. Such potential purchasers are sometimes called "special purchasers". It is well established that the additional value to a special purchaser must be taken into account in estimating what the property would fetch in the open market. What effect it will have depends not only upon its estimated value to the special purchaser (often no easy matter) but also upon the likelihood that he would actually buy on the valuation date. However, even if he cannot be assumed to be the actual purchaser on that date, his presence in the

market (if generally known) may cast a shadow because the value of the property to other purchasers ("third parties") may include some prospect of later selling at an enhanced price to the special purchaser. This additional value to purchasers generally is sometimes called "hope value" because it is based upon the hope of a further advantageous transaction. I describe it as a shadow because hope value to a third party is entirely dependent upon the existence of additional value to the special purchaser.

3. When the property to be valued is a freehold subject to a long lease, there is an obvious special purchaser, namely the tenant. The reversion is worth more to him than to others because his lease is a wasting asset, the value of which will inevitably decline to zero unless reinvigorated by extension or merger with the freehold. Thus the value of the lease merged with the reversion is always greater than the sum of the separate values of the two interests. The difference will vary according to the length of the lease: if the unexpired term is very long or very short, so that the reversion or the lease are respectively worth little, the additional value of merger will be low. But when the unexpired term is about to dip below the length which is regarded as adequate security by lenders in the market, it may be considerable. This difference is called the "marriage value".

4. Thus the value of the reversion to the tenant will be greater than to a third party who buys purely for the investment value of the rental stream and the right to possession on the expiry of the term. Furthermore, even if there is some reason (for example, lack of funds) why the particular tenant would not buy at the valuation date, the marriage value to him will be obvious to everyone in the market and it will, as I have said, cast a shadow in the form of hope value to other purchasers who take into account the possibility that sooner or later they may be able to sell to the tenant. It is, of course, impossible for both marriage value and hope value to form part of the same valuation. Marriage value represents the additional value to the tenant which supplies the reason why he would bid a sum higher than the pure investment value. Hope value represents the additional value to a third party who contemplates a future sale to the tenant. Taking into account marriage value assumes that the hypothetical purchaser is the tenant, while taking hope value into account assumes that the hypothetical purchaser is not the tenant. These two hypotheses cannot be entertained simultaneously.

5. There was nothing in the 1967 Act as originally enacted to exclude the assumption that the open market included all potential purchasers, including the tenant himself, and the Lands Tribunal so decided in *Custins v Hearts of Oak Benefit Society* (1969) 209 EG 239. Parliament immediately reversed this decision by section 82 of the Housing Act 1969. The formula which it used was to add an assumption that the tenant (and members of his family living with him) were "not buying or seeking to buy" It seems to me obvious that the purpose of the amendment was to eliminate any consideration of the marriage value, whether to the tenant or in its shadow form of hope value to others. The submission of the appellants was that because the formula excluded the tenant from the market only at the valuation date, it did not prevent him from being a potential purchaser at a later date, so that the marriage value to him could generate hope value in other hypothetical purchasers. As I understand all of your Lordships to be agreed that this is far too literal a reading of the statutory formula, I need not take further time in dealing with it.

6. The right to enfranchise under the 1967 Act was confined to houses of low rateable value. The Housing Act 1974 amended the 1967 Act to extend the right to higher value houses, but without the benefit of some of the assumptions which had reduced the price of the freehold. In particular, the valuation provisions for higher value houses under the new section 9(1A) did not include an assumption that the tenant was excluded as a potential purchaser. The marriage value was therefore something to be taken into account.

7. The way in which it was to be taken into account was at first unstated and provided fertile ground for disputes. However, the Leasehold Reform, Housing and Urban Development Act 1993 inserted a new section 9(1C) into the 1967 Act which provided that the tenant's share of the marriage value was to be not more than half and section 145 of the Commonhold and Leasehold Reform Act 2002 simplified the matter still further by providing that it was to be taken to be half. In my opinion the landlord's right to half the marriage value was intended to subsume what might otherwise have been any effect on the valuation of the existence of a marriage value, whether on the assumption that the tenant would be the hypothetical purchaser or on the assumption that there would be hope value to someone else. For the reasons I have given, if marriage value is taken into account, as the statute requires, it is logically impossible for hope value to form part of the same valuation. It requires mutually inconsistent assumptions about the identity of the hypothetical purchaser. Again, I understand that all of your Lordships are agreed on this point.

8. The question on which the House is divided arises in connection with the application of these concepts of marriage value and hope value to a collective purchase of the freehold by tenants of flats pursuant to Chapter I of the 1993 Act. These provisions give half or more of the tenants in the building the right to buy the freehold and have it vested in a nominee purchaser on their behalf. The effect is that the nominee purchaser acquires the freehold of the entire building, including the reversions upon the leases of those tenants who did not participate in the purchase.

9. Schedule 6 to the 1993 Act deals with the price to be paid by the nominee purchaser. Paragraph 2 said that it is to be made up of three elements: the value of the freeholder's interest, the freeholder's share of the marriage value, and certain compensation payments which are not presently relevant. The value of the freeholder's interest is to be calculated in accordance with paragraph 3, which (as originally enacted) contained an assumption that neither the nominee purchaser nor any participating tenant was seeking to buy. The marriage value is defined in paragraph 4(2) as the difference between the sum of the values of the interests acquired and the separate values of those interests, being an increase attributable to the ability of the *participating tenants* to procure that the nominee purchaser grant them long leases without further payment. Thus the only marriage value which enters into the calculation under paragraph 4 is that acquired by the participating tenants.

10. Consistently with this restriction on the calculation of marriage value, paragraph 3 originally excluded from the market on a hypothetical sale of the freehold only the nominee purchaser and the participating tenants. The presence of the non-participating tenants in the market remained to be taken into account. Their presence in the market could be relevant in two ways. First, they could be regarded as potential purchasers of the freehold of the building. As such, they would also gain from a marriage value of their leases and the freehold. But this notional value would have to be heavily discounted, because the disinclination of the non-participating tenants to join in the statutory acquisition demonstrated that they did not want to buy the freehold even in co-operation with the participating tenants, let alone on their own. A more practical possibility was that they might seek an extension of their leases. The hope value derived from the possibility that non-participating tenants might some day show an interest in their marriage values was an element to be taken into account in valuing the freeholder's interest under paragraph 3.

11. The effect of paragraphs 3 and 4 was accurately summed up by Lord Strathclyde in the debate on the 1993 bill in the House of Lords (HL Debates 18 May 1993, col 1679):

> "When valuing the landlord's present interests, any hope value element in the open market value of non-participating tenant's flats is included, as it is only nominee and participating tenants who are assumed not to be in the market."

12. Paragraph 3 was however amended by section 109(3) of the Housing Act 1996, which extended the exclusion to all tenants, whether participating or not. The effect of this amendment is in my opinion clear. By parity of reasoning with the construction of the same exclusion formula in section 9(1) of the 1967 Act, it removed from the valuation any consideration of participating or non-participating tenants as special purchasers, whether as potential purchasers at the valuation date or as creating hope value based on the possibility of purchase at a subsequent date. Lord Strathclyde's reasoning had been entirely dependent upon the non-participating tenants not being excluded from the market. Now that they are, the hope value in respect of their tenancies has disappeared. It would be impossible to reconcile a construction of section 9(1) which excludes hope value, as I think it must, with a construction of paragraph 3 which allows it to be taken into account, whether in respect of participating tenants before 1996 or in respect of all tenants after 1996. Again, I understand that in respect of any hope value attaching to the possibility of selling the freehold to the non-participating tenants, your Lordships are agreed.

13. It was however suggested in argument that although the hope value of a possible sale of the freehold to the tenants was excluded, the hope of obtaining a premium on an extension of their leases might not be. Paragraph 3 is said only to exclude them from the market for the freehold. But such a construction would in my opinion defeat the purpose of excluding them from the market. It would be absurd to legislate to exclude from the valuation any consideration that the hypothetical purchaser might hope at some later date to sell them the freehold at a price enhanced by the marriage value, but not to exclude the hope of selling them a lesser reversionary interest (say, a 999 year lease) at a price enhanced by the marriage value. The formula uses the words "not buying or seeking to buy" without saying what they must be taken not to be buying or seeking to buy. That is left to implication. In

my opinion it must mean that the tenants are excluded from the market for any interest in the premises which is reversionary upon their leases.

14. My noble and learned friend Lord Neuberger, in paragraph 104 of his opinion, accepts that the words "buying" and "buy" must cover "seeking a 999-year lease at a peppercorn or any similar interest" because "otherwise they would have no real effect". I agree. But he nevertheless concludes that they do not exclude *non-participating* tenants from the market for some lesser (but unspecified) interest in reversion on their leases. With all respect to my noble and learned friend's expertise in this part of the law, I cannot understand how he is able to distinguish between participating and non-participating tenants when the statutory assumption of exclusion from the market applies to tenants generally or how he is able to distinguish 999-year leases from shorter leases.

15. Reliance is placed upon paragraph 3(1)(b) of the 6th Schedule, which says that the hypothetical sale is to be on the assumption that —

> "this Chapter and Chapter II confer no right to acquire any interest in the specified premises or to acquire any new lease (except that this shall not preclude the taking into account of a notice given under section 42 with respect to a flat contained in the specified premises where it is given by a person other than a participating tenant)."

16. The argument is that if all the tenants were excluded from the market for the freehold or new leases, there would be no need for an assumption that they had no statutory right to acquire such interests. But this argument ignores the structure of the statute and the origins and purpose of the formula in paragraph 3(1)(b).

17. It is normal practice, in all statutes which provide for compulsory acquisition at market value, to insert an assumption that the hypothetical vendor is under no obligation to sell. It has always been what Fletcher Moulton LJ described in *Re Lucas and the Chesterfield Gas and Water Board* [1909] 1 KB 16, 29 as an "absolute rule" that the value of the property is to be estimated "as it stood before the grant of compulsory powers". Thus section 9(1)(a) of the 1967 Act requires it to be assumed that that "this Part of this Act conferred no right to acquire the freehold." The sale is between a hypothetical willing vendor and a hypothetical

willing purchaser and takes place in a market undisturbed by the existence of compulsory powers.

18. The purpose of this assumption is entirely to prevent the value of the property from being *diminished* by an argument that the price offered by the hypothetical buyer would have been affected by his knowledge that, if he bought the property, he would be liable to expropriation under statutory powers – what might be called no-hope negative value. It is not aimed at the exclusion of an assumption that the beneficiary of the statutory powers is using them as a buyer in the hypothetical sale – that would not be easy to reconcile with the assumption that the sale takes place in the open market – but rather at an argument that the price offered by any purchaser would be reduced by reason of the likelihood that he would have to surrender the property at some future date.

19. On the other hand, the beneficiary of the statutory powers is not assumed to be excluded from the market. His interest in purchasing the property in an open market sale is taken into account, including any special reason which he may have for paying more than others in the market. That is why, despite the assumption in section 9(1)(a) of the 1967 Act that the tenant has no right to buy, his interest in the marriage value was taken into account in *Custins v Hearts of Oak Benefit Society* (1969) 209 EG 239.

20. A provision such as section 82 of the Housing Act 1969, which excluded the tenant as a potential purchaser in the hypothetical sale, therefore serves an altogether different purpose from the assumption in section 9(1)(a) of the 1967 Act that the Act conferred no right to buy the freehold. The first is to prevent the price from being enhanced by the tenant's bid and the second is to prevent it from being depressed by the prospect of compulsory purchase. The argument of my noble and learned friends runs the two together. They would presumably argue that once section 82 of the Housing Act 1969 had been passed, the assumption of no right to buy might as well have been repealed. If the tenant was deemed not to be a buyer in the hypothetical sale, it would not matter whether he had a right to buy or not. But I do not think that it would have occurred to anyone to see a link between the two provisions. The primary purpose of the assumption of no right to buy is not to exclude an assumption that the tenant is exercising that right in his capacity as a purchaser in the hypothetical sale (which, as I have said, would be difficult to reconcile with the assumption of an open market) but to prevent an argument (similar in reverse to those which have been

heard in this appeal) that the price offered by a third party would be depressed by the existence, exercisable at any future date, of the tenant's right to buy. The fact that the tenant is assumed not to be a buyer in the hypothetical sale does not touch this argument at all.

21. My noble and learned friend Lord Neuberger bases a further argument upon the exception in paragraph 3(1)(b) which provides that account may be taken of a notice served by a non-participating tenant under section 42 of the 1993 Act, requiring the grant of an extended lease. It should be noted that this is an exception to the rule that the tenants should not be assumed to have the *right* to new leases. It is an exception to an assumption which prevents the price from being *depressed* by an argument that the hypothetical purchaser will be obliged under Chapter II to grant extended leases on the terms there provided. It is therefore hard to see how it can form an exception to a different assumption (in paragraph 3(1)) that the tenants are not in the market and thereby to add hope value to the price. It seems to me that my noble and learned friend's argument again fails to distinguish between the different purposes of the assumption that the tenant has no statutory rights and the assumption that the tenant is not in the market. The two assumptions are quite independent and neither entails the other.

22. The purpose of the exception in paragraph 3(1)(b) seems to me clear enough. If the landlord had actually granted new leases under Chapter II, that would clearly be something which had to be taken into account in a valuation of the freehold. Parliament has decided that once a notice has been served under section 42, the situation is close enough to the grant of a lease to make it unrealistic not to take the imminent grant into account.

23. Even if there were any merit in the argument based on paragraph 3(1)(a), it is hard to see how it enables one to distinguish between the positions of participating and non-participating tenants. Paragraphs 3(1) and 3(1A)(b) exclude *all* tenants from the market and paragraph 3(1)(b) assumes that *no* tenant (with one exception) has a right to buy the freehold or an extended lease. If it is accepted that paragraphs 3(1) and 3(1A)(b) exclude tenants as buyers not merely of the freehold but also of economically equivalent leasehold interests, how can that exclusion be confined to participating tenants? My noble and learned friend Lord Walker acknowledges this difficulty (at paragraph 44) but says that the inclusion of participating tenants would "involve the entirely artificial and indeed false assumption that the participating tenants had not, through the nominee purchaser, already embarked on the process of

acquiring the freehold…". But that argument, as it seems to me, ignores the fact that the valuation process assumes a *hypothetical* sale in the open market. In such a sale, everyone is free to bid, including the buyer in the actual sale proceeding under statutory powers. It could equally well have been said in *Custins v Hearts of Oak Benefit Society* (1969) 209 EG 239 that including the tenant in the open market involved an artificial and false assumption that he had not already embarked on a purchase pursuant to the statute.

24. The other argument relied upon by my noble and learned friend Lord Walker is that the inclusion of hope value generated by the marriage values of participating tenants would involve double counting (because their marriage values are already taken into account) while the inclusion of non-participating tenants would not. But the exclusion of hope value is not based merely upon double counting. It is a consequence of the tenants being treated as excluded from the market. The same language in section 9(1)(a) of the 1967 Act excludes hope value, even though there is no double counting.

25. It is perhaps worth noticing that none of the arguments based on paragraph 3(1)(b) were advanced in the Court of Appeal. Nor did they feature in the printed cases or the argument from the Bar. This alone might incline your Lordships to hesitate before adopting them. It seems to me that your Lordships have formed a view of what construction fairness to landlords requires and have determined to force the language of the statute to yield up such a meaning. I am less confident of what fairness requires. I note that the 1996 amendment, which extended to all tenants the exclusion from the market which had previously applied only to participating tenants, and which undermined the reasoning upon which Lord Strathclyde had three years earlier advised that hope value for non-participating tenants would be taken into account, was not opposed or even debated in its passage through either House. It is hard to believe that its potential consequences had escaped the attention of landlords, who are not without a voice in the counsels of the nation. Not a word of protest appears to have been uttered. Legislation of this kind has usually been the subject of intense negotiation between the interests of landlords and tenants, involving concessions and compromises on both sides. I am therefore not prepared to accept that the apparent mismatch between the inclusion of marriage value (for participating tenants only) and exclusion of hope value (for all tenants) produces such an obvious injustice as to require heroic methods of construction to avoid it. I would dismiss all the appeals.

LORD HOPE OF CRAIGHEAD

My Lords,

26. There are three distinct elements in the valuation of the freehold interest of premises which are subject to a long lease: the right to receive the ground rent, the right to vacant possession at the term of the lease and the option, or at least the potential, to deal early with the tenant and thus release the marriage value which will be realised at the term before the term arrives. It is the third element which is known colloquially as the hope value. This analysis is the product of valuation practice, not a rule of law. As the landlords point out, it is not set in stone. In practice the first two elements will always require to be valued, subject to any statutory direction to the contrary. Hope value, on the other hand, is a more elusive concept. As the valuations that were referred to in argument have shown, sometimes it is there. Sometimes it is not. Where it does appear, the methods of valuation differ from case to case. In all cases where it does appear, the value that is attached to it is relatively small in the overall valuation context.

27. It was the elusive, will o'the wisp character of hope value that, for me, created a difficulty at the outset in accepting the respondents' argument that the effect of the legislation is that it must be disregarded. None of the statutory provisions that are in issue in this case refers to hope value. I found it hard to accept that a tool of valuation to which Parliament does not appear to have addressed its mind at all had been entirely eliminated. The respondents submitted that the phrase "with the tenant and members of this family not buying or seeking to buy" in section 9(1) of the Leasehold Reform Act 1967, as amended, had this effect. This was said to be the natural meaning of those words. But they are directed to the state of affairs at the valuation date, and to one aspect only of the hypothetical transaction. The fact that any special, or enhanced, value that would otherwise be attributed to the fact that the tenant is the actual purchaser is to be disregarded does not seem to me to require the valuer to disregard any of the other elements that would normally be taken into account in a transaction with a third party purchaser.

28. One can, of course, point to the apparent absurdity of disregarding the tenant's bid on the valuation date but not the prospect of his making the same bid only one day later: see Carnwath LJ's comment about the effect of para 3(2) of Schedule 13 to the Leasehold

Reform, Housing and Urban Development Act 1993 where the same words appear, as they do also in para 3(1) of Schedule 6 to that Act: [2008] 1 WLR 2142, para 49. But that assumes a degree of precision in this part of the valuation exercise which it does not possess. The elusive character of hope value contradicts that assumption. It looks in an entirely general way into the future and to a transaction which may or may not occur to which persons who cannot yet be identified may be parties. The valuer could, I think, say with some justification that the absurdity that is being pointed to in this example distorts the way that, in practice, a value is attached to this element in the overall analysis.

29. On the other hand there is much to be said for giving a purposive construction to these words. As my noble and learned friend Lord Neuberger of Abbotsbury points out in para 83 of his opinion, it seems likely that the valuation exercise that section 9(1) of the 1967 contemplated was intended to be relatively simple. The inclusion of a discussion about hope value in the case of relatively low value houses would risk defeating that exercise. My noble and learned friend Lord Walker makes the same point in para 37 of his opinion, and I have found the way he puts the argument equally persuasive. I appreciate too the force of the point that the Tribunal made in para 20 of its judgment in *Pitts and Wang* on the issue as to whether the appellant was prevented as a matter of law from contending for hope value that, by providing in section 9(1D) of the 1967 Act that the marriage value must be divided equally, the statute envisaged a marriage value without regard to hope value. In effect, Parliament was substituting for the judgmental approach a system of valuation by formula. This indicates an intention to simplify the whole exercise. It leads to the conclusion that, as in the interests of simplicity the valuer's judgment as to the split of marriage value was to be disregarded, any addition for hope value was to be disregarded too.

30. In the end, therefore, I have come to be of the opinion that we are indeed dealing here with words that were intended to simplify the valuation exercise, and that the meaning that must be given to them to achieve that result where they appear in section 9 of the 1967 Act must be applied to them in the same way where they appear in Schedules 6 and 13 of the 1993 Act.

31. I would therefore dismiss the appeals in *Pitts and Wang*, *Atlantic Telecasters* and *Sportelli*. But on the issue on which your Lordships are divided, I agree with Lord Walker and Lord Neuberger, for the reasons they give, that para 3 of Schedule 6 to the 1993 Act permits hope value to be taken into account in the valuation in so far as it is attributable to

the possibility of non-participating tenants seeking new leases of their own flats. I would therefore allow the appeal in the *Grandeden* and *27/29 Sloane Gardens* cases to the extent indicated by Lord Neuberger and make the orders that he proposes.

LORD WALKER OF GESTINGTHORPE

My Lords,

Some preliminary observations

32. The legislation which your Lordships have to construe is set out or summarised in the opinion of my noble and learned friend Lord Neuberger of Abbotsbury, and I gratefully adopt his account of it. The legislation is complicated and has been amended a good deal over the years. The legislative purpose of some of these amendments is far from obvious. That is particularly true of the amendment of Schedule 6, para 3 of the Leasehold Reform, Housing and Urban Development Act 1993 ("the 1993 Act") by section 109 of the Housing Act 1996 ("the 1996 Act") as described in para 12 of the opinion of my noble and learned friend Lord Hoffmann.

33. I shall come back to that particular riddle (which is the crux of the difference of opinion between your Lordships). Approaching the matter more generally for the moment, I think that there are two particular reasons, beyond the general intractability of this lengthy and much-amended legislation, that have led to the problems which your Lordships have to resolve.

34. The first is that Parliament has, in this legislation, departed a long way from a simple statutory rule of open market value (calling for expert evidence from valuers). But at the same time it has not entirely displaced open market value by some clear (though arbitrary) statutory rule, such as taking the annual value of a house to be its value as shown in the official rating list, however out of date that list is. Parliament's usual technique, when assets have to be valued for some statutory purpose, is to start with a simple test of market value, but to supplement that test by spelling out the assumptions which are to be made for the purposes of the hypothetical open market sale which the test postulates.

Parliament may direct, for instance, that no reduction is to be made because under the hypothetical sale the whole property is to be put on the market at once; or that a hypothetical purchaser of unquoted shares is to be assumed to have all the information which a prudent purchaser might reasonably require (see for instance Inheritance Tax Act 1984, sections 160 and 168; Taxation of Chargeable Gains Act 1992, sections 272(1) and (2) and 273(3)).

35. In the Leasehold Reform Act 1967 ("the 1967 Act"), in both its original and its amended forms, Parliament has adopted a statutory test of open market value, subject to modifications. But in the 1993 Act, in both its original and its amended forms, Parliament has to my mind adopted a hybrid technique, combining a mandatory formula (in Schedule 6, para 2 and Schedule 13, para 2) followed by provisions which take open market value as a starting-point, but subject it to some far-reaching statutory assumptions (and the puzzling possibility of further unspecified but "appropriate" assumptions under Schedule 6, para 3(2) or Schedule 13, para 3(4)). It is not surprising that valuers and lawyers have found these provisions difficult. The issue of whether "hope value" should be taken into account in the deferment rate which valuers customarily use (and indeed whether this is a question of law, or a matter within a valuer's professional judgment) can be seen as symptomatic of the confusion.

36. The second particular matter giving rise to difficulty is the parliamentary draftsman's understandable inclination, in framing the detailed provisions of Schedule 6 and Schedule 13 to the 1993 Act, to follow a similar pattern. But Schedule 6 (introduced by section 32, in Part I, Chapter I of the 1993 Act) is typically concerned with the price to be paid by a single purchaser ("the nominee purchaser") for the freehold of an entire block of flats, whether or not all the tenants are joining in this exercise in collective enfranchisement (in other words, are participating tenants rather than non-participating tenants). By contrast Schedule 13 (introduced by section 56 in Part I, Chapter II) is typically concerned with the premium to be paid by a single non-participating tenant for the grant of a new lease of a single flat in a block of flats. That is the exercise of an individual right, and it is something that may happen to coincide with collective enfranchisement by and on behalf of a group of participating tenants, a possibility noted and provided for in Schedule 6, para 3(1)(b). Because Schedule 6 and Schedule 13 are directed at such different operations, the superficial similarity between their provisions is a little deceptive.

Section 9 of the 1967 Act

37. Here the argument turns on the meaning and effect of the words "(with the tenant and members of his family not buying or seeking to buy)" in section 9(1) as amended. I agree with all your Lordships that these words must be given a purposive construction. Parliament's plain intention was to remedy the mischief perceived to have been caused by the decision in *Custins v Hearts of Oak Benefit Society* (1969) 209 EG 239, and it would frustrate the statutory purpose (and lead to strange mental contortions) if the statutory assumption were somehow to be restricted to the "relevant date" (the date of the tenant's notice claiming the freehold) to the exclusion of what might happen afterwards. Any potential marriage value or hope value in the house in question is therefore excluded.

Schedule 13 of the 1993 Act

38. As between the two relevant Schedules of the 1993 Act I take Schedule 13 first, because it is more straightforward. This Schedule is concerned with quantifying the premium to be paid for a new extended lease of a flat. In the simple case where there is no intermediate interest (that is, no head lease interposed between the freeholder and the tenant seeking a new lease) there are only two parties interested in the transaction, the freeholder and the tenant. The other tenants in the block of flats are not concerned. In this respect it is closer to a transaction under the 1967 Act (enfranchisement or grant of an extended lease of a house) where (again, on the assumption of no intermediate interest) only two parties are involved.

39. Schedule 13, para 2 sets out a formula in three parts, that is the aggregate of

> "(a) the diminution in value of the landlord's interest in the tenant's flat as determined in accordance with paragraph 3,
>
> (b) the landlord's share of the marriage value as determined in accordance with paragraph 4, and
>
> (c) any amount of compensation payable to the landlord under paragraph 5."

It is common ground that your Lordships need not be concerned with head (c). Nor does any serious difficulty arise on head (b) (which incorporates Schedule 13, para 4) though it is to be noted that that paragraph is concerned only with the so-called marriage value in the particular flat in respect of which the new lease is to be granted. There is no question of marriage value in respect of the block of flats as a whole. Moreover the "marriage value" in respect of the particular flat is something of a misnomer, since there is not to be any merger of the freehold and leasehold interests in the flat. The expression is used as a label to describe the effect of a leasehold interest with (say) twenty years unexpired being extended to a total term of 110 years (an interest the value of which is not far short of that of a freehold, the value of the freeholder's interest in the flat being dramatically reduced by the new lease). In most cases in which a tenant finds it expedient to seek a new lease the aggregate value of the two interests identified in para 4(2)(a)(i) and (ii) is significantly lower than the aggregate value of the two interests identified in para 4(2)(b)(i) and (ii). In some cases, however (especially when the interest at para 4(2)(a)(i) is a long unexpired term) the difference in the two sets of aggregate values is much less significant, and para 4(2A) covers these *de minimis* cases.

40. The only real difficulty is on Schedule 13, para 3, and in particular the words "(with neither the tenant nor any owner of an intermediate leasehold interest buying or seeking to buy)" in para 3(2) as amended by section 110 of the 1996 Act. In my opinion these words must be construed in just the same way as s.9(1) of the 1967 Act, on which they are obviously modelled. Any potential marriage value or hope value in the flat in question is excluded under para 3. It comes in exclusively under para 4.

Schedule 6 of the 1993 Act

41. Why then does not the same symmetrical pattern apply under Schedule 6? In the opinion of my noble and learned friend Lord Hoffmann it does, and I hesitate to differ from the closely-reasoned analysis in his opinion. Nevertheless I do respectfully differ from him, basically because (as I have indicated in my preliminary remarks) the apparent symmetry between Schedule 13 and Schedule 6 is deceptive. Schedule 13, like the 1967 Act, is dealing (typically, that is where there is no intermediate interest) with a bilateral transaction, and the only marriage value to be considered (whether it is true marriage value on the enfranchisement of a house, or so-called marriage value on the grant of a new lease of a single flat) is in respect of a single unit of

accommodation in which only the freeholder and the tenant are interested.

42. Schedule 6, by contrast, is typically dealing with a tripartite transaction in respect of a complex of units—a block of flats which starts off in the ownership of the freeholder, and ends up owned, through the nominee purchaser, by some of the tenants (the participating tenants), subject to the continuing rights of the other tenants (the non-participating tenants). Marriage value as between the freeholder and the participating tenants, so far as attributable to their control of the freehold and their ability to grant themselves advantageous leases (see Schedule 6, para 4(2) and especially para 4(2)(a)) is dealt with exclusively by para 4, as under Schedule 13. But there is to my mind no good reason why any hope value in respect of future deals that may possibly be negotiated between the freehold owner and non-participating tenants (other than those who have actually served section 42 notices before the valuation date) should be disregarded. The possibility of gain (whether large or small) from such negotiated deals will pass from the original freeholder to the nominee purchaser. It is not dealt with in para 4. So I approach Schedule 6, para 3 (and the amendments made to it by the 1996 Act) without any strong expectation of finding a close parallel with Schedule 13, para 3.

43. Schedule 6, para 3 is concerned with head (a) of the para 2 formula—"the value of the freeholder's interest in the specified premises" (in the typical case, the whole of a block of flats—see section 13(12) of the 1993 Act). Where the "specified premises" consist of a large block of flats, the prospect of a single tenant being in the market for the freehold of the whole block may be remote—the tenant would often have to pay a very high price to realise a modest marriage value on a single flat. In other cases (such as a large house converted into a small number of flats, with more than one leasehold interest owned by a single person or members of his family) the prospect might be much greater. But whatever the likelihood, that is the transaction to which para 3 is, by its terms, directed: a purchase of the freehold interest in the whole building. If the hope value arising from the possibility of a future negotiated deal with one or more non-participating tenants is to be excluded, then "buying or seeking to buy" the freeholder's interest in the specified premises must be extended, as a process of construction, in two respects: that is so as to include the grant of a new lease, at a premium, of one or more flats belonging to non-participating tenants. Such a double extension might be fairly easy to make if it accorded with an obvious statutory purpose, but for the reasons which I have tried to explain, I am not satisfied that that is part of the statutory purpose.

44. It may be said that this argument proves too much, because it would (in the hypothetical world postulated by para 3) apply to possible negotiated deals with participating tenants also. But that would involve the entirely artificial and indeed false assumption that the participating tenants had not, through the nominee purchaser, already embarked on the process of acquiring the freehold in the whole block of flats, giving them freedom to grant new leases to themselves as described in para 4(2)(a). It would also involve an obvious case of double counting.

45. I would therefore, in agreement with my noble and learned friends other than Lord Hoffmann, hold that para 3 permits the inclusion of hope value, such as it is, in respect of new leases of the flats of non-participating tenants. But that is, I must stress, hope value in respect of deals which might be freely negotiated, rather than leases granted under any statutory right. Para 3(1)(b) excludes statutory rights (except where section 42 notices have already been served) but not the possibility of negotiated contracts. Para 3(1)(b), if read with an emphasis on "right", is not therefore inconsistent with this construction.

46. If that is the correct construction of Schedule 6, para 3, it helps to explain why the amendment made to it by section 109 of the 1996 Act was regarded (as it seems to have been regarded) as technical and uncontroversial. The amendment recognized that if any tenants were to be excluded from the market as prospective purchases of the freehold of the entire block of flats, for the purposes of the para 3 valuation, then all the tenants (participating and non-participating) should be excluded. But in the average case that was unlikely to make a significant difference to the valuation exercise.

Human Rights Act 1998

47. I can, without disrespect to the appellants' submissions, deal quite shortly with the points raised on the Human Rights Act 1998 and Article 1 of the First Protocol to the Convention. This issue was not raised at all below. Before your Lordships the appellants' position was that they placed most reliance on section 3 of the Human Rights Act, if it was necessary to do so, in relation to Schedule 6 of the 1993 Act. A majority of the House holds that the appellants succeed on the Schedule 6 point on ordinary principles of statutory construction, and without the need to invoke section 3.

48. In relation to section 9 of the 1967 Act and Schedule 13 of the 1993 Act the appellants' reliance on section 3, in their oral submissions, was less than whole-hearted, and for good reason. The decision of the Strasbourg court in *James v United Kingdom* (1986) 8 EHRR 123 presents them with an insuperable obstacle. It is for Parliament as the national legislature to decide on policies to remedy social injustice, with a wide margin of appreciation. Parliament's conclusions on social policy will be accepted by the Strasbourg court unless manifestly unreasonable. It is true that the scope of leasehold enfranchisement and associated rights has increased greatly since the 1967 Act, especially with the removal of the requirement for occupation by the tenant. But Parliament concluded that that requirement created difficulties in the enfranchisement of large blocks of flats where there was a rapid turnover of some of the flats. Against that the landlord does under section 9(1D) of the 1967 Act and Schedule 13 of the 1993 Act receive half of the marriage value, a provision which cannot be attacked as lacking a reasonable relationship of proportionality (see paras 49 to 54 of the judgment in *James*).

Conclusion

49. For these reasons, and for the fuller reasons set out in the opinion of Lord Neuberger, I would dismiss the appeals in *Pitts and Wang, Atlantic Telecasters* and *Sportelli* and allow the appeals in *Grandeden* and *27/29 Sloane Gardens* to the extent indicated by Lord Neuberger.

LORD MANCE

My Lords,

50. I have had the benefit of reading in draft the speeches of my noble and learned friends, Lord Hoffmann, Lord Walker of Gestingthorpe and Lord Neuberger of Abbotsbury. For the reasons given in the speeches of Lord Walker of Gestingthorpe and Lord Neuberger of Abbotsbury, with which I am in full agreement, I consider that the landlords' appeals in the cases of *Sportelli, Pitts and Wang* and *Atlantic Telecasters* should be dismissed, and that the landlords' appeal in the cases of *Grandeden* and *27/29 Sloane Gardens* should be allowed to the extent that my noble and learned friends indicate.

LORD NEUBERGER OF ABBOTSBURY

My Lords,

51. These five appeals arise out of legislation enabling residential tenants to acquire new leases or to buy their freeholds. The specific issue raised on each appeal is whether the price payable for the new lease or the freehold, as the case may be, should include what is called "hope value". The Court of Appeal agreed with the tenants (Mr and Mrs Sportelli, 27/29 Sloane Gardens Ltd, Grandeden Property Management Ltd, Mr Pitts and Ms Wang, and Atlantic Telecasters Ltd,) in each case that it should not – see *Earl Cadogan v Sportelli* [2007] EWCA Civ 1042, [2008] 1 WLR 2142, and *Earl Cadogan v Pitts and Wang* [2007] EWCA Civ 1280. The landlords (Earl Cadogan in all five cases, together with Cadogan Estates Ltd in three of them) now appeal to your Lordships' House.

The Leasehold Reform Act 1967

52. Tenants under long leases, i.e. leases granted for more than twenty-one years, were first given the right to acquire new leases or to buy their freeholds under the Leasehold Reform Act 1967, which applies only to houses. Section 1 of that Act originally contained a number of requirements which had to be satisfied before the right arose, including that the value of the house be below a certain level. Section 9 of the 1967 Act contained the formula for assessing the price which the tenant would have to pay to enfranchise – i.e. to buy the freehold. So far as relevant, in its original form, it was in these terms:

> "9(1) [T]he price payable … shall be the amount which … the house …, if sold in the open market by a willing seller, might be expected to realise on the following assumptions:-
>
> (a) on the assumption that the vendor was selling for an estate in fee simple, subject to the tenancy but on the assumption that this Part of this Act conferred no right to acquire the freehold …"

53. Following the passing of the 1967 Act, a number of tenants promptly sought to exercise their right to enfranchise. This occasionally led to disputes as to the purchase price, which at that time were referred to the Lands Tribunal pursuant to section 21. In the first of those cases, *Custins v Hearts of Oak Benefits Society* (1969) 209 EG 239, the Lands Tribunal decided that the actual tenant could be treated as being in the market as a potential purchaser of the freehold when assessing a price payable under section 9(1). The correctness of that conclusion appears to me to be inescapable. The landlord's interest has a special value to the tenant, as he is the only person who can unite it with his leasehold interest, thereby producing an unencumbered freehold. Further, given that he has served a notice seeking to enfranchise, the tenant has made it clear that he is indeed interested in acquiring the landlord's interest..

54. The assumed presence of the actual tenant as a potential purchaser would accordingly serve to enhance the price payable for the landlord's freehold interest, in many cases quite substantially. This was not the intention of Parliament, which swiftly acted to reverse the decision. Section 82 of the Housing Act 1969 amended section 9(1) of the 1967 Act to insert "after the words 'a willing seller' the words '(with the tenant and members of his family who reside in the house not buying or seeking to buy)' ".

55. The 1967 Act has subsequently been amended by a number of subsequent statutes, almost all of which included provisions which widened its scope by removing or cutting down the requirements in section 1 (although the long lease requirement has always subsisted). In particular, the Housing Act 1974 brought many, more valuable, houses within its scope. The 1974 Act also introduced a new subsection 9(1A), which contained a different formula for assessing the price payable for the freehold by the tenant for higher value houses. So far as relevant, section 9(1A) was in these terms:

> "… [T]he price payable for a [higher value] house … shall be the amount which … the house …, if sold in the open market by a willing seller, might be expected to realise on the following assumptions:
>
> (a) on the assumption that the vendor was selling for an estate in fee simple, subject to the tenancy, but on the assumption that this Part of this Act conferred no right to acquire the freehold …"

Thus, for present purposes, the only difference between the two provisions was that section 9(1A), unlike section 9(1), did not require one to assume that the actual tenant was excluded from the market.

56. For completeness, it should be added, that more leases, including those involved in the *Pitts and Wang* and *Atlantic Telecasters* appeals, were brought within the ambit of the 1967 Act by the Leasehold Reform, Housing and Urban Development Act 1993. In relation to such leases, sections 9(1C) and 9A, added by the 1993 Act, apply. However, it is unnecessary to set out those sections out, as they incorporate the above-quoted part of section 9(1A).

57. Although the determination of the price payable under section 9 was originally entrusted to the Lands Tribunal, section 21 as amended by section 142 of the Housing Act 1980 now requires the issue to be referred to a Leasehold Valuation Tribunal ("LVT"), against whose decision an appeal lies to the Lands Tribunal.

Marriage value

58. In three reported decisions over a period of ten years, the Lands Tribunal effectively set the tone for future valuation cases under section 9(1A) of the 1967 Act. In the second of those cases, *Lloyd-Jones v Church Commissioners for England* [1982] 1 EGLR 209, the tenant's lease had about twelve years unexpired and was at a rent of £45 per annum. The valuation of the landlord's reversionary freehold interest involved two stages. The first stage was to assess the so-called investment value of the landlord's interest. This had two components. The first was the right to receive the rent over the remaining 12 years of the lease, which involved capitalising that future rental stream. The second component was the value of the landlord's deferred right to possession of the house at the end of the 12 years, which involved applying an appropriate annual deferment rate to the present value of the unencumbered freehold interest.

59. The second stage of the valuation was required because the tenant was assumed to be in the market. As already mentioned, when it comes to marketing the landlord's reversion to a long lease, the tenant under the lease can normally be expected to be a special purchaser. It is accordingly clear, if at first sight somewhat counter-intuitive, that, in almost every case, the aggregate of (a) the investment value of the

landlord's interest and (b) the market value of the tenant's interest is significantly less than the value of the two interests if combined in a single ownership. In *Lloyd-Jones* [1982] 1 EGLR 209, the market value of the tenant's interest was £45,000, and the investment value of the landlord's interest was £84,257, while the value of what the tenant would end up owning, namely the unencumbered freehold interest, was £187,500, which is £58,243 more than the aggregate of those two figures. Accordingly, combining the two interests released a so-called marriage value of £58,243. The question which then arose was the effect of the potential release of the marriage value on the value of the landlord's freehold interest.

60. After careful consideration of the evidence and arguments, the Lands Tribunal decided, contrary to the tenant's case, that the marriage value should be divided equally between the parties, so that the value of the landlord's interest was increased by £29,121. The Tribunal's reasoning was expressed in these terms at [1982] 1 EGLR 211M by reference to the evidence of the landlord's surveyor:

> "Mr Hopper's addition … represents the actual amount which the lessee in friendly negotiations with the lessor would be willing to bid above the amount which any other purchaser would pay: that amount would take his bid well above that of any other potential purchaser. Mr Hopper assumed that the parties were of equal bargaining strengths. I agree: neither can unlock the marriage value without the other. In friendly negotiations they would agree to divide it equally as they had done in the 57 settlements [as between landlords and tenants of other houses where the tenant was seeking to enfranchise]."

61. In reaching the conclusion that the value of the landlord's freehold interest should be increased by half the marriage value, the Lands Tribunal was following the approach which it had adopted in *Norfolk v Trinity College, Cambridge* [1976] 1 EGLR 215. Precisely the same approach was followed in a subsequent Lands Tribunal decision, *Lowther v Strandberg* [1985] 1 EGLR at 203. In all three cases, the tenant's argument, that the landlord should receive a smaller proportion than 50% of the marriage value, failed.

62. In *Hague on Leasehold Enfranchisement* (2nd edition, 1987), at para 9-55, this was described as "correct as a matter of logic, because the bargaining powers of the freeholder and the tenant…are equal, and the agreement of both of them is required in the hypothetical sale postulated by section 9(1A)", although it was pointed out that, in the end, "the question is properly one of valuation". This view was repeated in the subsequent edition of *Hague*: 3rd edition, 1999, at para 9-40. Nonetheless, it appears clear that some tenants' surveyors (and, indeed, when they felt they could justify it, some landlords' surveyors) continued to argue, albeit unsuccessfully, for an unequal apportionment of the marriage value.

63. The longer the lease, the smaller the investment value of the landlord's interest. The proportion of the total value of the landlord's interest attributable to marriage value increases as the unexpired residue of the lease reduces; it reaches a maximum when the lease has about 35 to 40 years to run, and then the proportion decreases over time. It should also be mentioned that marriage value is released when a tenant under a lease negotiates an extension (or a new long lease) with his landlord. The calculation is a little more complex, but the release of the marriage value is normally a significant feature in the exercise.

64. By sections 145 and 146 of the Commonhold and Leasehold Reform Act 2002, two further subsections were added to section 9 of the 1967 Act, namely:

> "(1D) Where in determining the price payable for a house … in accordance with this section, there falls to be taken into account any marriage value arising by virtue of the coalescence of the freehold and leasehold interests, the share of the marriage value to which the tenant is to be regarded as being entitled shall be one-half of it.
>
> (1E) But where at the relevant time the unexpired term of the tenant's tenancy exceeds 80 years, the marriage value should be taken to be nil."

Section 9(1D) thus put an end to any attempts to split the marriage value other than equally between landlord and tenant under section 9(1A); where section 9(1E) applies, it simply removes marriage value from the valuation exercise.

Hope value

65. Having discussed marriage value and its treatment under section 9(1A), it is convenient to deal with "hope value". If a landlord is selling his freehold interest subject to a lease, at a time when the tenant is not interested in purchasing the freehold, there is no immediate prospect of releasing the marriage value. That is because the only way in which it can be released is either by the tenant acquiring the freehold interest or by the landlord acquiring the leasehold interest. As it is the landlord who is assumed to be selling, the latter possibility could not arise, and the former possibility is excluded by the fact that the tenant is not, on this hypothesis, in the market at the time of the sale.

66. However, where the landlord is selling his interest when the tenant is not in the market, a potential purchaser may well think that, in addition to its investment value, the freehold interest carries with it the potential benefit of a possible future sale of the freehold to the present tenant or a successor in title (or indeed the acquisition of the leasehold interest), thereby enabling a release of the marriage value in the future. In such a case, therefore, it can be said that, even though the tenant is not in the market at the time of the sale, the value of the freehold subject to the lease is greater than the aggregate of the capitalised rental stream and the deferred right to possession at the end of the term, and that something should be added for the possibility of a purchaser benefiting from a release of the marriage value. That additional sum is known as "hope value".

67. In *Lloyd-Jones* [1982] 1 EGLR 209, the landlord's surveyor argued that hope value should be included in the investment value of the freehold. The Tribunal accepted that surveyor's valuation in its entirety, and, while it is not clear precisely what effect, if any, the inclusion of the hope value had on the valuation, it appears to have been through the medium of a downward adjustment in the rate of deferment (see at [1982] 1 EGLR 210M and 211H).

68. In a number of subsequent cases (your Lordships were told it was over twenty, most of which were under schedule 6 to the 1993 Act), the Lands Tribunal and the LVT accepted that hope value can be included even where marriage value is taken into account. In *Blendcrown Ltd v Church Commissioners for England* [2004] 1 EGLR 143, at para 77, the Lands Tribunal described hope value as "a speculative element that does not lend itself to objective assessment" and "essentially a matter of

informed opinion" (although 5% of the marriage value was then accorded to the landlord as hope value). And in a number of cases, hope value has not been established on the evidence – see e.g. *Gesso Properties (BVI) Ltd v SCMLLA Ltd* LRA/13/2003.

69. In some cases, hope value has been held to justify an increase in the investment value of the freehold by around 15% of the marriage value – see e.g. *In Shulem B Association Ltd's Appeal* [2001] 1 EGLR 105. In other cases, the same approach was taken as in *Lloyd-Jones* [1982] 1 EGLR 209, so the deferment rate was adjusted downwards to allow for hope value – see e.g. *Arbib v Earl Cadogan* [2005] 3 EGLR 139, para 188. However, in several conjoined appeals from the LVT, including three of the instant cases, *Sportelli*, *Grandeden* and *27/29 Sloane Gardens*, a three-member Lands Tribunal, presided over by the President, Mr Bartlett QC, convincingly concluded at [2007] 1 EGLR 153, para 112 that, where hope value could be included, it was the former approach which was appropriate.

The Leasehold Reform, Housing and Urban Development Act 1993

70. Having examined the relevant provisions of the 1967 Act, and explained the nature of marriage value and of hope value, I must now refer to the rather more complex provisions of the Leasehold Reform Housing and Urban Development Act 1993. Whereas the 1967 Act benefited long leaseholders of houses, the 1993 Act benefited long leaseholders of flats. Chapter I of part I of the 1993 Act is entitled "Collective enfranchisement in case of tenants of flats", and chapter II is entitled "Individual right of tenant of flat to acquire new lease". Many of the provisions of part 1 of the 1993 Act to which it is necessary to refer are complicated by the fact that they have to cover cases where there are intermediate interests between the freehold and the leases of individual flats, and cases where the building includes business premises or flats let for short terms. When quoting those provisions, I shall omit or modify them to delete such complicating factors (indicating where I have done so).

71. It is convenient to deal first with chapter II. Section 39 imposed various conditions which had to be satisfied by a tenant before he could seek a new lease, and, as with section 1 of the 1967 Act, subsequent legislation has removed or modified most of those conditions. The right to acquire a new lease is exercised by the tenant serving a notice under

section 42. By virtue of section 56, the price payable by the tenant for the new lease is assessed in accordance with Schedule 13.

72. Part II of Schedule 13 sets out the basis upon which that price is to be calculated. Paras 2 to 4 were originally in these terms:

> "2 The premium payable by the tenant in respect of the grant of the new lease shall be the aggregate of –
>
> (a) the diminution in value of the landlord's interest in the tenant's flat as determined in accordance with para 3,
>
> (b) the landlord's share of the marriage value as determined in accordance with para 4 …
>
> 3(1) The diminution in value of the landlord's interest is the difference between –
>
> (a) the value of the landlord's interest in the tenant's flat prior to the grant of the new lease; and
>
> (b) the value of his interest in the flat once the new lease is granted.
>
> (2) Subject to the provisions of this paragraph, the value of any such interest of the landlord … is the amount which … that interest might be expected to realise if sold on the open market by a willing seller (with the tenant not buying or seeking to buy) on the following assumptions –
>
> (a) …
>
> (b) on the assumption that Chapter I and this Chapter confer no right to acquire any interest in any premises containing the tenant's flat or to acquire any new lease;
>
> (c) on the assumption that any increase in the value of the flat which is attributable to an improvement carried out at his own expense by the tenant … is to be disregarded …
>
> …
>
> 4(1) The marriage value is the amount referred to in sub-paragraph (2), and the landlord's share of the marriage value is –
>
> (a) [to be determined by agreement, or in default of agreement by the LVT], or

(b) 50 % of that amount,

whichever is the greater.

(2) The marriage value is the difference between the following amounts, namely —

(a) the aggregate of —

(i) the value of the interest of the tenant under his existing lease, [and]

(ii) the value of the landlord's interest in the tenant's flat prior to the grant of the new lease …, and

(b) the aggregate of —

(i) the value of the interest to be held by the tenant under the new lease, [and]

(ii) the value of the landlord's interest in the tenant's flat once the new lease is granted ….”

73. Chapter I of part I of the 1993 Act contains provisions whereby long leaseholders of flats in a block of flats can, through a so-called nominee purchaser, acquire the freehold interest in the block – or building as I will refer to it. A specified proportion of tenants – currently at least 50% according to section 13(2)(b) – of flats in the building have to be “participating tenants”, that is, they have to join together to exercise their rights under the chapter through the nominee purchaser.

74. By virtue of section 32, the price payable for the freehold of the building is to be determined in accordance with Schedule 6, part II of which was originally in the following terms:

“2(1) Subject to the provisions of this paragraph, the price payable by the nominee purchaser for the freehold [of the building] shall be the aggregate of –

(a) the value of the freeholder's interest in the [building] as determined in accordance with paragraph 3,

(b) the freeholder's share of the marriage value as determined in accordance with paragraph 4 …

3(1) Subject to the provisions of this paragraph, the value of the freeholder's interest … is the amount which at the valuation date that interest might be expected to realise if sold on the open market by a willing seller (with neither the nominee purchaser nor any participating tenant buying or seeking to buy) on the following assumptions –

(a) …

(b) on the assumption that this Chapter and Chapter II confer no right to acquire any interest in the [building] or to acquire any new lease (except that this shall not preclude the taking into account of a notice given under section 42 with respect to a flat contained in the [building] where it is given by a person other than a participating tenant);

(c) on the assumption that any increase in the value of any flat held by a participating tenant which is attributable to an improvement carried out at his own expense … is to be disregarded...

…

4(1) The marriage value is the amount referred to in sub-paragraph (2), and the freeholder's share of the marriage value is –

(a) [the proportion determined by agreement or by the LVT], or

(b) 50 % of that amount,

whichever is the greater.

(2) The marriage value is any increase in the aggregate value of the freehold…[of the building], when regarded as being (in consequence of their being acquired by the nominee purchaser)…under the control of the participating tenants, as compared with the…value of [the freehold] when held by the [freeholder], being an increase in value –

(a) which is attributable to the potential ability of the participating tenants, once [the freehold has] been so acquired, to have new leases granted to them without payment of any premium and without restriction as to length of time, and

(b) which, if [the freehold was] being sold to the nominee purchaser on the open market by [a] willing [seller], the nominee purchaser would have to agree to share with the [seller] in order to reach agreement as to price.

… "

75. Sections 109 and 110 of the Housing Act 1996 made some amendments to para 2 of Schedule 6 and para 3 of Schedule 13. More significant amendments were made by section 109 to para 3 of schedule 6. First, in para 3(1), the words "(with neither the nominee purchaser nor any participating tenant buying or seeking to buy)" were effectively replaced with the words "(with no person who falls within sub-para 1(A) buying or seeking to buy)". Secondly, a new para 3(1A) was added, in these terms:

> "A person falls within this sub-paragraph if he is –
>
> (a) the nominee purchaser, or
>
> (b) a tenant of premises contained in the [building],
>
> … "

76. Further amendments were made to Schedules 6 and 13 to the 1993 Act by the 2002 Act. In particular, para 4(1) of each Schedule was amended so that, in effect, it reflected the amendments made by the addition of subsections (1D) and (1E) to section 9 of the 1967 Act. A new para 4(2A) was added to each Schedule, which provides that, where a lease has more than 80 years to run, marriage value is to be ignored, and para 4(1) was amended so that it provides that, in any other case, "the landlord's share of the marriage value is 50% …".

The issues on these appeals

77. These appeals require your Lordships to consider whether, when determining the prices to be paid by the tenant under section 9(1) of the 1967 Act, section 9(1A) of the 1967 Act, para 3 of Schedule 13 to the 1993 Act, and para 3 of Schedule 6 to the 1993 Act (in each case in their respective current forms), hope value can, as a matter of principle, be taken into account as a component of the price to be paid to the landlord.

78. It is (in my view quite rightly) common ground between the parties that:

> 1. Under section 9(1), marriage value cannot be taken into account because the tenant is expressly assumed not to be in the market;

2. Under section 9(1A), marriage value can be taken into account because there is no requirement that the tenant is not in the market;
3. Under Schedule 13, marriage value cannot be taken into account under para 3 because the tenant is assumed not to be in the market, but it is to be taken into account as directed by para 4;
4. Under Schedule 6, no tenant of any part of the building is assumed to be in the market for the building under para 3, but at the para 4 stage marriage value is to be taken into account, to the limited extent of the participating tenants being able to enjoy the marriage value through the medium of being granted new leases of their flats.

79. The nature of the dispute between the parties may be best appreciated by identifying the landlords' arguments on these appeals, which are, in summary terms, as follows:

1. Although marriage value is excluded under section 9(1), hope value is not excluded;
2. The fact that marriage value is taken into account under section 9(1A) does not prevent hope value being included in addition;
3. Under Schedule 13, the fact that marriage value is specifically included by virtue of para 4 similarly does not exclude hope value being included in para 3;
4. Under Schedule 6, in addition to the marriage value included in the price through the medium of para 4 in relation to participating tenants, hope value in relation to participating tenants and/or hope value in relation to the non-participating tenants can be included under para 3.

In fact, none of the instant appeals concern section 9(1), but it is sensible to consider that provision, as it was the first of the statutory valuation hypotheses in this field, and the issues raised by these arguments are connected.

80. Before turning to these four issues, it should be recorded that the questions raised in each of these appeals are whether the landlords are entitled, as a matter of law, to have hope value taken into account as an element in the valuation of their respective interests. If any of these appeals succeed, it would be for the LVT (or, on appeal, for the Lands

Tribunal) to decide whether, and if so to what extent, the landlord is entitled to hope value in any particular case.

Section 9(1) of the 1967 Act and hope value

81. The issue under section 9(1) is whether the words "(with the tenant and members of his family who reside in the house not buying or seeking to buy)", added by the 1969 Act, exclude hope value. In my opinion, the words mean that, not only marriage value, but also hope value, is excluded from being taken into account when assessing the price to be paid by a tenant for the freehold of the house. This conclusion is based on the natural meaning of the words and common sense, which together powerfully justify the conclusion that it is inherently improbable that Parliament, when enacting section 82 of the 1969 Act, intended the landlord to be able to seek hope value.

82. As to the language, the words inserted into section 9(1) by the 1969 Act are linguistically capable of having the effect that, although the tenant is not interested in acquiring the freehold on the valuation date, he could be interested in a future date. However, the participles "buying" and "seeking" are not necessarily limited to the present, and, in their context, the more natural meaning of the words is that the tenant is not, and will not be, so interested. Even if the verbs had been expressed in the present tense, my view would have been the same. That is best demonstrated by reference to the assumption in section 9(1)(a), that the 1967 Act "conferred" (as at the valuation date) no right to acquire the freehold. Those words cannot mean that it can be assumed that the tenant nonetheless has that right the day after the valuation date.

83. Common sense confirms this view, even if, as I am prepared to accept, the exclusion of marriage value does not logically and necessarily require the exclusion of hope value. As Carnwath LJ said in the Court of Appeal at [2008] 1 WLR 2142, para 49 (when dealing with the same point under para 3 of Schedule 13 to the 1993 Act), the notion that "the market would disregard the prospect of a bid by the tenant himself on the valuation date, but not the prospect of exactly the same bid the following day" is something of an "absurdity". Further, section 9(1) has always applied to relatively low value houses, and it seems likely that the valuation exercise it gives rise to was intended to be relatively simple. It is clear from many of the Lands Tribunal and LVT decisions in which hope value was an issue that it is a potentially controversial factor, which is often hard to quantify.

84. Accordingly, I consider that, in relation to a valuation under section 9(1), a landlord is not entitled to seek hope value.

Section 9(1A) of the 1967 Act and hope value

85. The respondents' argument, which was accepted by the Court of Appeal, is that, under section 9(1A), the landlord cannot claim hope value in addition to marriage value because it is subsumed by marriage value. At first, that contention seemed to me to be unanswerable, particularly now that the landlord is entitled to half the marriage value under section 9(1D). As half the marriage value is what the tenant would pay if he was in the market (as explained in *Lloyd-Jones* [1982] 1 EGLR 209, 211L-M), it seems logically inconsistent that he should have to pay yet more on the basis that, although not in the market, he might be in the future. To put the point another way, if it is right to split the marriage value equally between the parties, it would, at first blush at any rate, seem to give the landlord more than half the marriage value, through the medium of an additional sum for hope value, which can fairly be characterised as a sum in respect of deferred contingent marriage value. In other words, as Carnwath LJ put it at [2008] 1 WLR 2142, para 48 in the Court of Appeal, the argument is that, as the landlord is entitled to half the marriage value, "[t]o include a further element of hope value would involve double counting".

86. I have come to the conclusion that this conclusion is correct, although I have found the point more difficult than it initially seemed. Although hope value can be characterised as deferred marriage value, and including hope value in the valuation of the freehold interest will reduce the marriage value, and although one might quantify the hope value by reference to the amount of the marriage value (as in *Shulem B* [2001] 1 EGLR 105), there is considerable force in the point that hope value is not the same as marriage value. It is something which (at least if the surveyors' evidence in the particular case supports it) the market will pay for when a landlord is selling his freehold reversion at a time when the tenant is not in the market. It therefore could be said to follow that, provided it was justified on the evidence, a landlord in the hypothetical friendly negotiations with his tenant for the sale of the freehold reversion, as described in *Lloyd-Jones* [1982] 1 EGLR 209, 211L-M, would negotiate on the basis that (a) the investment value of his interest should include hope value (as that is how the price would be calculated if the tenant was not in the market), and (b) he should be able to seek half the marriage value in addition, as that reflects the special value of the freehold to the tenant.

87. Such an approach to the inclusion of hope value under section 9(1A) appears to be largely consistent with the views of the Lands Tribunal in *Pitts v Earl Cadogan* [2007] 3 EGLR 86. At para 14, the Tribunal said that, at least in the absence of section 9(1D), "there would be no obvious constraint on the method of valuation", and that it could not be "a matter of law as to what constitutes marriage value and whether the value of the landlord's interest can include hope value". However, in para 20, the Tribunal concluded that, by providing in section 9(1D) that marriage value must be divided equally, it was "likely" that Parliament intended hope value to be disregarded.

88. Although I have concluded that the Tribunal reached the right conclusion in para 20, my conclusion, like that of the Court of Appeal, is based on the fact that the price payable under section 9(1A) includes a proportion of the marriage value, and is reached irrespective of the provisions of section 9(1D). The contention that the landlord can have both hope value and half the resultant marriage value is, I think, based on two assumptions, which, on analysis, appear to me to be unsound. The first assumption is that one can build up the valuation of the landlord's interest in two stages (the investment value stage and the marriage value share) on the assumption that each stage is wholly independent of the other. The second assumption is that the tenant is the hypothetical buyer of the landlord's interest, which is to be found in the otherwise impeccable reasoning of the Lands Tribunal in the passage quoted above from *Lloyd-Jones* [1982] 1 EGLR 209, 211L-M, and supported by the extract from the 2nd edition of *Hague*.

89. So far as the second assumption is concerned, the existence of a special purchaser does not actually mean that one assumes that he is the buyer in the hypothetical sale one is required to postulate. The seller of the landlord's interest under section 9(1A) is expressly not assumed to be the actual landlord, but a hypothetical "willing seller" (whereas, of course, the landlord is very rarely anything of the kind). The buyer is similarly a hypothetical person, not an actual person; section 9(1A) makes no express reference to a "willing buyer", but it is implied by the assumption of a sale in the "open market" – see per Fox LJ in *Dennis & Robinson Ltd v Kiossos Establishment* [1987] 1 EGLR 132, at 134K, and see also the analysis of Donaldson J in *F R Evans (Leeds) Ltd v English Electric Co Ltd* (1977) 36 P & C R 185 (affirmed 11 November 1977), relying on the reasoning in *Inland Revenue Commissioners v Clay* [1914] 3 KB 466. The notion that the buyer is a hypothetical person, rather than the actual tenant, also accords with practical sense, as otherwise the tenant could argue that he would not have been prepared, or able, to pay more than a certain sum.

90. Once one considers a hypothetical prospective buyer negotiating with the landlord, one can see that, if the landlord sought hope value at the first, investment, stage, and then sought half the marriage value at the second stage, he would be seeking to have his cake and eat it. That is because the price he would be seeking for his interest would assume both the fact that the tenant was in the market (as the landlord is seeking half the marriage value) and that the tenant was not in the market (as the landlord is seeking hope value on the basis that the tenant is not in the market, but may be in the market in the future). Thus, as Carnwath LJ said, at [2008] 1 WLR 2142, para 48, taking account of hope value when assessing the investment value, when the landlord is also to be accorded half the marriage value, would involve double counting.

91. In fact, the same analysis would apply if the actual tenant were assumed to be the hypothetical buyer, although it is harder to appreciate that there is double counting in such a case. That is, I think, because it is less obviously illogical that the landlord should be able to build up the value of his interest on the basis of two inconsistent assumptions, when those assumptions concern the hypothetical activities of the very person with whom he is assumed to be negotiating.

92. Although it does not directly arise on these appeals, it is sensible to deal with the question whether hope value can be claimed in those section 9(1A) cases where marriage value is excluded by virtue of the provisions of section 9(1E). In my opinion, the purpose of those provisions is the same as that of the words added to section 9(1) by section 82 of the 1969 Act. Although I accept that hope value is not the same as marriage value, it appears to me unreal to attribute to Parliament the intention to allow for the prospect of marriage value being taken into account, when it has specifically excluded marriage value from the valuation exercise. Just as it is unrealistic under section 9(1) to assume that the tenant might be in the market the next day, if the section excludes the tenant from the market on the valuation date, so is it unrealistic to allow for hope value where the statute specifically excludes marriage value.

93. There is a potential complicating factor I should mention. In a case where the marriage value is shared equally, just as the landlord's interest should be valued excluding hope value, so, I am inclined to think, should the tenant's leasehold interest. In some cases, the valuation of the tenant's interest may include hope value, as the President recognised in *Pitts* [2007] 3 EGLR 86, para 16, where he said that "hope value does not necessarily exclusively reside in the landlord's interest".

It may well be unfair on the landlord if he is precluded from seeking hope value in circumstances where, for the purpose of assessing the marriage value, the tenant's leasehold interest is valued including hope value. So, while, as a matter of principle, it appears to me that, under section 9(1A), the valuation of the landlord's interest should not include hope value, if it could be shown that the valuation of the tenant's interest included hope value and that this was illogical and unfair on the landlord, then an adjustment would have to be made.

Schedule 13 to the 1993 Act and hope value

94. The arguments about marriage value and hope value where a tenant is seeking a new lease of his flat under Schedule 13 to the 1993 Act are similar, in valuation terms, to those which can be raised in relation to the tenant's acquisition of the freehold of his house under section 9 of the 1967 Act, although the calculation is a little more complex as the tenant is acquiring a new lease rather than the freehold.

95. In those circumstances, it seems to me that the arguments which establish that the words "(with the tenant not buying or seeking to buy)" in para 3(2) of Schedule 13 have the same force as the very similar words inserted into section 9(1) of the 1967 Act by section 82 of the 1969 Act. There is no doubt that they bar marriage value from being included in the valuation of the landlord's interest, and, for the same reasons as contained in the section of this opinion dealing with section 9(1), I consider, in agreement with the Court of Appeal, that they also bar the inclusion of hope value. For completeness, I should add that, for the reasons discussed in para 92, the effect of the new para 4(2A) is to exclude hope value as well as marriage value in the case of leases with more than eighty years to run.

Schedule 6 to the 1993 Act and hope value

96. It is clear from the bracketed words in para 3(1), "with no person who falls within sub-paragraph (1A) buying or seeking to buy", and the provisions of para 3(1A), with its reference to "a tenant of premises contained in the [building]", that every tenant of a flat in the building, whether or not participating in the proposed purchase, is deemed to be out of the market. It is also seems clear from the wording of sub-paras (a) and (b) of para 2(1), the opening part of para 4(2), and the unambiguous terms of para 4(2)(a) that marriage value can only be

taken into account in so far as it is attributable to the ability of the participating tenants, through the nominee purchaser, to grant new long leases of their respective flats to themselves. The way in which paras 2(1)(a) and (b) are worded also confirm that the only aspect of marriage value in respect of which the landlord can claim is that identified in para 4. But that does not necessarily exclude hope value: as I have explained, it may be similar to, and based on the existence of, marriage value, its inclusion may serve to reduce any marriage value and it may be assessed by reference to marriage value, but it is not marriage value.

97. The Court of Appeal concluded that hope value could not be taken into account under the para 3 valuation, whether it is attributable to the ability of either participating tenants or non-participating tenants to acquire new leases of their respective flats. This conclusion was primarily based on their view that the exclusion of all such tenants, whether participating or not, from the market under para 3(1) and 3(1A)(b) meant that they were excluded for the purposes of any hope value, consistently with their conclusion in relation to Schedule 13.

98. It would be both arbitrary and unfair, in my judgment, if a landlord, who can recover marriage value in relation to the participating tenants' flats, could not recover hope value in respect of the non-participating tenants' flats. It would be arbitrary because, in so far as they are purchasing the reversion to non-participating tenants' leases, the participating tenants are acquiring an investment, whereas, in so far as they are purchasing the reversion to their own leases, they are acquiring greater security in their homes. They are plainly anxious to enhance the value of their interests in their respective flats, as otherwise they would not be exercising their chapter I rights. It is therefore quite logical to oblige them to pay a share of the resultant marriage value, as envisaged by para 4: Parliament could have decided to release them from that obligation, as it did to tenants under section 9(1) of the 1967 Act, but it did not do so. Given that it was thought to be fair to make the participating tenants pay a true market price for the reversion to their own flats, it would be surprising if they did not have to pay a true market price for the investment part of their purchase, and that would include paying for any hope value in respect of the prospect of negotiating new leases of their flats with non-participating tenants. By the same token, it would be unfair on the landlord.

99. In the Court of Appeal, at [2008] 1 WLR 2142 para 54, Carnwath LJ accepted that the denial of hope value to the landlord under Schedule 6 result "seem[ed] unfair". However, he said that hope value "may have

been thought so speculative that it could be disregarded without injustice". I am not convinced by that argument. It has some force in a valuation dispute involving a single relatively low-value house under section 9(1) of the 1967 Act, but not to a dispute under Schedule 6, which applies to collective enfranchisement, and extends to very valuable flats and buildings. In most of the cases where hope value has been found to be allowable in principle under schedule 6, it has been included in the investment value of the landlord's interest in some form, and has had a significant effect on the price payable, in percentage terms or in the actual amount, or indeed in both.

100. In the following paragraph of his judgment, Carnwath LJ referred to the submission (repeated before your Lordships) that there was a counterbalancing benefit for the landlord, in that it would suffer no discount for improvements effected by non-participating tenants to their flats (as para 3(1)(c) of Schedule 6 only applies to participating tenants) whereas if such tenants then sought extended leases under chapter II, para 3(1)(c) would entitle them to a discount on the price payable, to take into account their improvements. I am unpersuaded by that argument also: there is no correspondence between the two factors, save that they could suggest a rough and ready approach to valuation. However, in the case of flats subject to long leases, there must be very few cases indeed where improvements by the tenant have much effect on the value of the reversion.

101. Excluding hope value in respect of non-participating tenants would be unfair on a landlord for another reason. In many cases, all, or at least the great majority, of the tenants of flats in a building wish to buy the freehold, but, if they are well-advised, they would ensure that only the minimum number of them formally participate in the purchase under Schedule 6 (on the basis that they agreed appropriate terms with the other tenants). Such an arrangement would artificially reduce the price that they would have to pay for the freehold under Schedule 6, as there would be neither marriage value nor hope value in respect of non-participating tenants' flats.

102. I have seen, in draft, my noble and learned friend Lord Hoffmann's opinion, which, as always, I have read with pleasure and admiration. Despite his cogently expressed reasons to the contrary, I consider that, on a fair reading of para 3 of Schedule 6, hope value can be taken into account in so far as it is attributable to the possibility of non-participating tenants seeking new leases of their respective flats by

negotiation (and not, it should be emphasised, as of right under chapter II).

103. I agree with the Court of Appeal that the bracketed words in the opening part of para 3(1), when read together with para 3(1A), exclude all flat tenants from the market, and they exclude hope value as well as marriage value because the words "buying or seeking to buy" are, for the reasons given when considering section 9(1), apt to cover the future as well as the present. But this conclusion begs the question of what precisely it is that the flat tenants are not buying or seeking to buy. The natural meaning of the opening part of para 3(1) is that they are not buying, or seeking to buy, that which is described immediately before as being "sold on the open market", namely the freehold of the building. At least as a matter of words, that would not extend to excluding from account the possibility of flat tenants seeking in the future to acquire new long leases of their respective flats: they would not be "buying" anything, let alone the building. On that basis, there is nothing in para 3 which excludes the hope value for which the appellants contend in these appeals.

104. However, I accept that, as Carnwath LJ said at [2008] 1 WLR 2142, para 50, such a literal reading of the bracketed words in the opening part of para 3(1) will not do. The words "buying" and "buy" in para 3(1) must cover seeking a 999-year lease at a peppercorn or any similar interest: otherwise they would have no real effect; for the same reasons, the bracketed words would extend to buying (or acquiring a 999-year lease at a peppercorn of) all but a small part of the building. However, those considerations by no means necessarily require one to construe the bracketed words so as to exclude the possibility of the flat tenants acquiring any interest in any part of the building, especially if there are good reasons, based on other provisions of the 1993 Act, to hold that they should not be so construed. In my opinion, when one turns to provisions other than the opening part of para 3(1) and para 3(1A)(b), it is apparent that such hope value is not to be excluded.

105. Of course, as Lord Hoffmann implies, if one accepts (as I do) that the bracketed words in the opening part of para 3(1) of Schedule 6 should be given a wide meaning, any cutting down of that wide meaning must be on a principled and clear basis, and must be justified by the provisions of the Schedule. In this connection, para 3(1)(b) and para 4 are important. First, if, as the respondents contend and the Court of Appeal held, the bracketed words in the opening part of para 3(1) require one to assume that none of the flat tenants are or will ever be

interested in acquiring new leases of their flats, there would be no point in including the requirement in the opening part of para 3(1)(b) that one disregards the fact that they have the right to do so. That therefore suggests that, for para 3 purposes, one should not disregard the possibility of the market taking into account at least some of the flat tenants seeking to negotiate new leases of their respective flats. It is perfectly true that words such as those in the opening part of para 3(1)(b) are commonplace compulsory acquisition valuation assumptions (as evidenced by para (a) of sections 9(1) and 9(1A) of the 1967 Act). However, that does not invalidate the point, although I accept that, if it stood on its own, it would be a shaky foundation for my conclusion that hope value can be included in relation to non-participating tenants' flats.

106. However, the bracketed words of para 3(1)(b), which permit taking into account a notice under section 42 – i.e. a notice seeking a new lease under chapter II – served by a non-participating tenant, are also of significance in this connection. Lord Hoffman suggests that they merely indicate that the valuation can take into account the fact that such a tenant has exercised his chapter II right, in the same way as one can take into account the fact that such a tenant has actually been granted a new lease pursuant to chapter II. However, it appears to me that this is inconsistent with an interpretation of the opening part of para 3(1) which requires one to assume that such a tenant does not wish to acquire any further interest in his flat. That point is reinforced by the fact that sub-para (b) is intended to be an "assumption" – see the end of the opening part of para 3(1) and the start of sub-para (b) - not an exception to the opening part of para 3(1).

107. There are two reasons why, in my opinion, the bracketed words in para 3(1)(b) are significant for present purposes. First, all that the service of a section 42 notice does is to give the tenant a right to acquire a new lease: he can pull out at any time – see section 52. Accordingly, para 3(1) permits some hope value attributable to non-participating tenants' flats to be included on any view. Secondly, the bracketed words in para 3(1)(b) require one to take into account the "notice", not the rights and obligations which accrue pursuant to it. That suggests to me that the purpose of sub-para (b) is to entitle the landlord to argue that the section 42 notice is evidence that the tenant concerned is interested in acquiring a new lease of his flat. Where a non-participating tenant has served such a notice, the hope value attributable to his flat may well be increased because he has made it clear that he is interested in acquiring a new lease of his flat. In other words, by serving a section 42 notice, a non-participating tenant has, in my view, assisted any contention that he would be in the market, because he has evinced a desire to acquire a

new lease of his flat at market value, which is what Schedule 13 effectively means that he would have to pay.

108. Accordingly, para 3(1)(b) appears to me to indicate that, while the bracketed words in the opening part of para 3(1) are to be construed widely, they do not prohibit taking into account the possibility of non-participating tenants seeking to negotiate new leases of their respective flats. This view is reinforced by the contents of para 4, under which marriage value must be taken into account in relation to the participating tenants' ability to take new leases of their respective flats. On this basis, there would be a symmetry between para 4, which requires marriage value to be taken into account in relation to participating tenants, limited to their obtaining new leases of their respective flats, and para 3, which entitles the landlord to seek hope value in relation to the non-participating tenants, again limited to the prospect of their seeking new leases of their respective flats. Para 4 also explains why, under para 3, hope value can only be taken into account as against non-participating tenants: if the landlord is entitled to marriage value as against participating tenants, then he is not entitled to hope value as well: see the discussion in relation to section 9(1A).

109. Further, I have already referred to the unfairness and arbitrariness of excluding hope value arising from the possibility of non-participating tenants seeking new leases of their flats in the para 3 valuation, when marriage value arising from the rights of participating tenants to obtain new leases of their flats can, indeed must, be taken into account under the para 4 valuation. While it is right to give the bracketed words in the opening part of para 3(1) an extended meaning so that they have commercial efficacy, it does not follow that one cannot limit that extension, particularly where the limitation is supported by other provisions elsewhere in paragraphs 3 and 4, and by commercial fairness, and where the limitation in question is clear and logical.

110. Some further support for the notion that hope value can be sought in respect of non-participating tenants' flats is to be found in section 18 of the 1993 Act, which requires disclosure to the landlord of any agreements made between participating tenants and non-participating tenants. This seems to me to represent an acknowledgment that such agreements could affect the assessment of the price payable for the freehold of the building. While such agreements could provide comparable evidence of general value, it appears to me that, if such agreements were not envisaged as assisting in the assessment of hope value in respect of non-participating tenants' flats, then it is "difficult to

explain fully the legislative intentions in respect of the disclosure of agreements under section 18", as Carnwath LJ accepted at [2008] 1 WLR 2142, para 56.

111. The interpretation of Schedule 6 is difficult, and this is attributable to its original complexity, the subsequent amendments which have been made to it, and the fact, pointed out by my noble and learned friend Lord Walker of Gestingthorpe in his opinion, which I have had the privilege of reading in draft, that it is perhaps unfortunate that its drafting was based on Schedule 13, which is concerned with a far simpler construct. In reaching the conclusion that hope value in respect of non-participating tenants' flats is excluded, Lord Hoffmann relies in part on the drafting history of the present paras 2 to 4 of Schedule 6. The original drafting of at least parts of chapter I of part I of the 1993 Act left much to be desired, and subsequent amendments have in some cases made things worse. The poorness of the drafting means that, in my opinion, it is safer to construe the paragraphs as they now stand, rather than seeking to identify what purpose or errors may be revealed at earlier stages. I should add that the inept drafting of the 1993 Act is unfair on landlords, who are being deprived of their property, and on residential tenants, the very people who are intended to benefit from the legislation.

112. Where does the conclusion that hope value as against non-participating tenants in respect of their flats may be taken into account leave hope value in relation to participating tenants and their flats? If, as I have concluded, the bracketed words in the opening part of para 3(1) do not exclude the possibility of taking into account hope value arising from non-participating tenants seeking new leases of their flats, the same conclusion must apply to participating tenants. However, the effect of para 4 means that, for the reasons I have given when considering hope value under section 9(1A), it is not possible to include hope value in relation to participating tenants' flats under para 3, as it has already been subsumed into the marriage value exercise mandated by para 4. That is clear not only as a matter of commercial sense and justice, but also because para 2 envisages the purchase price consisting of the aggregate of the sums in sub-paras (a) and (b), and it cannot have been envisaged that the same sum be included under both sub-paragraphs.

113. My conclusion that the hope value attributable to non-participating tenants' flats may be taken into account under para 3 is consistent with a clear statement made in this House by Lord Strathclyde, the Minister promoting the bill which became the 1993 Act.

On 18 May 1993, in relation to what became Schedule 6 in its original form, he said:

> "When valuing the landlord's present interests, any hope value element in the open market value of non-participating tenants' flats is included, as it is only nominee and participating tenants who are assumed not to be in the market…[N]on-participating tenants are outside the marriage-value, but they do come into hope value" (*Hansard* ,18/5/93, col 1679).

114. The force of any argument based on this observation is, however, reduced by the fact that no such statement was made in relation to the bill which became the 1996 Act, which, crucially for present purposes, amended para 3(1) and added para 3(1A). However, there had been no change of government between the passing of the two statutes, and there is no suggestion that the amendments effected to Schedule 6 by the 1996 Act were intended to reverse the effect described so clearly by Lord Strathclyde. In the light of the amendments made in 1996, however, I have not thought it right to rely, as part of my reasoning, on what was said by Lord Strathclyde in 1993, but I do draw some comfort from it.

115. Accordingly, for these reasons, as well as those articulated by Lord Walker, I consider that hope value can be taken into account under para 3 of Schedule 6, in so far as it is attributable to the possibility of non-participating tenants wishing to obtain new leases of their flats in the open market (and not pursuant to Schedule 13).

Disposal of these five appeals

116. In *Earl Cadogan and Cadogan Estates Ltd v Sportelli and Sportelli*, Mr and Mrs Sportelli sought a new lease of Flat 14, 85 Cadogan Gardens London SW3, pursuant to chapter II of the 1993 Act. The parties could not agree the price payable and that issue was referred to the LVT. One of the issues was whether the price should be assessed taking into account hope value. The LVT held that it should not, in the light of the bracketed words in the opening part of para 3(1) of Schedule 6 - LON/NL/2788/04, paras 142 to 148.

117. In *Earl Cadogan and Cadogan Estates Ltd v Grandeden Property Management Ltd*, tenants of some of the flats in a building, 59 Cadogan Square and 105 Cadogan Gardens London SW1 sought to acquire the freehold of the building pursuant to chapter I of the 1993 Act. Before the LVT there were a number of valuation issues, including the landlord's claim for an allowance in respect of hope value. The LVT decided that "no quantified sums should be added for 'hope value' and that this aspect should be regarded as taken into account as an element in the yield" – LON/ENF/1370/05, para 20.

118. In *Earl Cadogan and Cadogan Estates Ltd v 27/29 Sloane Gardens Ltd and Mahdi*, tenants of some of the flats in a building, 27/29 Sloane Street London SW1, sought to acquire the freehold of the building pursuant to chapter 1 of the 1993 Act. By agreement between the parties, an agreed sum for hope value in respect of the two flats held by non-participating tenants was included in the sum assessed by the LVT, which had to resolve other valuation issues between the parties – LON/ENF/1102/04.

119. The LVT decisions in *Sportelli* and *Grandeden* were appealed to the Lands Tribunal, which also gave permission to the tenants in *27/29 Sloane* Gardens to withdraw the concession that the landlord was entitled to claim any hope value, and to mount an appeal on that issue. The Lands Tribunal heard the three appeals together (with other appeals). In its illuminating decision, at [2007] 1 EGLR 153, paras 98 to 108, the Lands Tribunal concluded that, as a matter of law, no hope value could be included in valuations under para 3 of Schedule 13 or under para 3 of schedule 6, essentially because of the express exclusion of the tenant or the flat tenants, respectively, from the market.

120. The Court of Appeal agreed with the Tribunal's conclusions in relation to schedule 6 and schedule 13, for reasons given in the closely reasoned judgment of Carnwath LJ (with which Ward LJ and Sir Peter Gibson agreed) – [2008] 1 WLR 2142, paras 43 to 59. While accepting, in para 54, that the issue was less clear in relation to schedule 6, where the absence of any right to hope value would give rise to "some problems", he concluded that under neither Schedule was the landlord entitled to hope value.

121. In *Earl Cadogan v Pitts and Wang*, the tenants were seeking to acquire the freehold of a house, 35 Hans Place, London SW1, and the valuation was effected pursuant to section 9(1C) of the 1967 Act, which

incorporates the relevant provisions of section 9(1A). The LVT's economically expressed determination (LON/LVT/1815/05) did not make it entirely clear whether hope value had been allowed for in its assessment of the investment value of the landlord's interest, although the deferment rate it adopted suggested that it was.

122. In *Earl Cadogan v Atlantic Telecasters Ltd*, the tenant was also seeking to acquire the freehold of a house, namely 10 Holbein Mews London SW1 pursuant to section 9(1C) of the 1967 Act. In a fully reasoned decision, the LVT decided that, hope value was already "subsumed into the full marriage value reflected in the value of the interest at the valuation date" and that no additional amount was payable by way of hope value – LON/LVT/1957/05, paras 101 to 104.

123. These two LVT decisions under section 9(1A) were appealed to the Lands Tribunal, which heard the appeals together. As I have mentioned, in a clearly expressed decision, [2007] 3 EGLR 86, the Tribunal concluded that hope value should not be taken into account under section 9(1A) as a matter of principle – LRA/79/2006.

124. This decision was upheld by the Court of Appeal – see [2007] EWCA Civ 1280 – by Carnwath LJ, sitting on his own. In a very short judgment, he simply applied his conclusion on the point in *Sportelli* [2008] 1 WLR 2142, paras 58 and 59, where, although there was no appeal in relation to hope value under section 9(1A), he had said that hope value was excluded in the section 9(1A) valuation. (This course, adopted under section 54(2) of the Supreme Court Act 1981 with the agreement of the Master of the Rolls, seems to me to have been very sensible.)

125. In the light of the conclusions expressed earlier in this opinion, I consider that the appeal in *Sportelli* must be dismissed, as the landlord has no right to claim hope value under para 3 of Schedule 13, and that the appeals in *Pitts and Wang* and *Atlantic Telecasters* must similarly be dismissed as the landlord has no right to claim hope value under section 9(1A). However, the appeals in *Grandeden* and in *27/29 Sloane Gardens* must be allowed, as the landlord is entitled to claim hope value under para 3 of Schedule 6 in relation to non-participating tenants' flats, albeit not in relation to participating tenants' flats.

126. Two further points should be made. First, in relation to the two appeals under section 9(1A), it is right to acknowledge that it is possible that there could, at least in theory, be an inconsistency as a consequence. When it comes to assessing the marriage value, the value attributable to the relevant tenants' interests might have included hope value, which may be inappropriate if the investment value of the landlord's interest must ignore hope value, as I have concluded. However, the point is one of valuation, not law, and anyway the landlords raised no argument to that effect before your Lordships' House. Indeed, so far as I can detect, there was no evidence that the valuation of the tenants' interests included hope value.

127. The second point is that the landlords argued that, if their appeals, and in particular if the appeals in *Grandeden* and *27/29 Sloane Gardens* would otherwise have failed, their rights under article 1 of the First Protocol to the Convention would be infringed. Because I consider that hope value is subsumed into marriage value, and because the appeals in *Grandeden* and in *27/29 Sloane Gardens* have succeeded, no point can arise in that connection. However, it is right to add that I agree with the observation of Lord Walker in this connection.

128. Accordingly, for my part, I would propose that we dismiss the landlords' appeals in the *Sportelli*, *Pitts and Wang*, and *Atlantic Telecasters* cases, but allow the appeal in the *Grandeden* and in *27/29 Sloane Gardens* cases to the extent indicated. I would also suggest that the parties should have fourteen days to agree any issue relating to costs and the terms of the order in each appeal, and, in default of agreement in any appeal, they should have a further seven days to make written submissions.