The Leasehold Advisory Group

news UPDATE

Edition 7

ACTIONS SPEAK LOUDER THAN WORDS

Michael Tims + Company a founder member of the Leasehold Advisory Group has since the introduction of the Leasehold Reform legislation back in 1993 handled countless cases for both tenants and landlords alike. Following recent research it is estimated the Company has provided advice during the 17 years on some 2000 cases. Furthermore, in circumstances of the Company acting for tenants they have saved its clients about £68m in negotiating reductions in the premiums quoted by the landlords. A single case recently has seen a saving of £1.2m on a freehold enfranchisement.

Michael Tims commented "that we see our role as striking a balance between the landlords and the tenants both of whom openly over value or under value the freehold or lease extension that they are seeking". He added, "the legislation is not perfect and the valuation procedure is too complex and has been cleverly manipulated by some to maximise the value of their investments. This is why there are consistent referrals of aspects of the legislation to the Courts which has unfortunately in same cases given rise to legal precedent which is inappropriate in some areas. The prime example of this has been the matter of deferment rates. The valuation of short to mid-term leases in Central London is far removed from a similar process being undertaken outside of London where the market for short leases etc is far smaller".

Investment yields will also vary as a result of a number of factors which would have a bearing on deferment rates. The Courts are consistently looking at these issues and further amendments may result in time.

At last an estate agent licensing scheme

Despite strenuous efforts on the part of the industry to persuade Government to introduce licensing for estate agents, all efforts over many years have failed. Government has preferred that trading standards legislation should provide sufficient comfort in circumstances of the consumers finding themselves in the grip of unscrupulous estate agents. Controls over the taking of rental deposits etc have assisted, but frankly the industry has always felt that trading standards was not the appropriate body to provide consumers with the safeguards they need.

Therefore, the National Association of Estate Agents has launched its own licensing. The scheme is open to all NAEA members and it was launched at the House of Commons recently by the Housing Minister, Mr Grant Shapps. It appears that several politicians are now getting on the bandwagon and are all saying that they have for years been calling for better standards throughout the industry, but previous requests for licensing fell on deaf ears, until now.

The aim of licensing is that members of the NAEA will be able to set themselves aside as a professional organisation within the estate agency field and will offer security and integrity to its customers.

It is so important however, that estate agents who are not part of the NAEA should be singled out and be given the opportunity to qualify which is only now by appropriate study and exams.

It is hoped that people will appreciate the new professionalism of the body and trust those selling their homes to conduct themselves in a far more professional way than perhaps they have in some instances in the past.

By Michael Tims, Director, Michael Tims + Company

INSIDE

The Liechtenstein Law
on Administrative Assistance In Tax Matters

New Law
If you represent any of those listed below you need to be aware that a new law in Liechtenstein will mean that your **Liechtenstein Bank** or **Intermediary** will be asking you for a certificate of compliance with your clients UK tax obligations or they will have to close the bank account or cease acting for the entity concerned and you will be asked to remove their assets from Liechtenstein.

Do you represent or act for:
- Any person with a Liechtenstein bank account.
- A Foundation/Stiftung.
- An Establishment/Anstalt.
- Any form of trust.
- Any form of partnership.
- Any other legal entity.

Where a person who has an UK connection:
- Provided money to the account or entity.
- Is the settlor of any of the above or has provided funds to them.
- Is a beneficiary or is intended to be a beneficiary or capable of benefitting or has benefitted from any such entity.

Then – your Liechtenstein Bank or Intermediary will need:
- An opinion from an UK tax expert that the structure and all UK connections are tax compliant; or
- A disclosure to HMRC which leads to a certificate of compliance from HMRC.

What happens if neither of these is available?
If neither of these is available then the **Liechtenstein Bank** or **Intermediary** must close the account and stop acting and remove the assets from Liechtenstein.

BE WARNED! BE PREPARED!

Check your files for clients with **UK connections** and make sure you know what has happened.

The UK tax laws are complex
Under certain circumstances income and capital gains are attributable to UK settlors or persons who have transferred assets to the entity or structures.

Any UK resident beneficiary who has received a capital or income benefit from the entity or structure will have an UK tax liability.

You will need to ensure that all these people are UK tax compliant.

The benefits of the LDF are:
- Tax will only be payable for the period from 5th April 1999 for individuals and from the 1st April 1999 for companies.
- Interest on unpaid tax will be limited to this period as well
- Only a 10% penalty will be payable.
- There will be no prosecution by HMRC unless your client has been involved in crimes other than the non-disclosure of tax.

The Liechtenstein Disclosure Facility

In Brief
- Liechtenstein and HMRC have agreed to the introduction of a 5-year 'taxpayer assistance and compliance program'.
- Liechtenstein financial intermediaries will be under a duty to identify clients who may have a liability to UK tax.
- If a client cannot provide evidence of his or her compliance with UK tax, the financial intermediary will have to cease acting for the client
- HMRC has offered a special disclosure facility with reduced penalties: The Liechtenstein Disclosure Facility ("LDF").

However
The LDF is not limited to tax payers who already have assets in Liechtenstein.

Who can use the Facility?
- Anyone with UK tax liabilities in respect of financial interests in Liechtenstein structures, including bank accounts, companies, trusts and foundations, which are formed, administered, or managed in Liechtenstein.
- An individual with UK tax liabilities who moves financial interests into Liechtenstein. This could include opening a bank account or relocating a trust.

The advantages of the Facility
- Only 10% penalty of unpaid tax, plus unpaid tax and interest.
- Tax liabilities pre 5th April 1999 fall out of account.
- No prosecution.
- No "naming and shaming".
- Option to have "no-names" discussion with HMRC prior to disclosure.
- Option to use a simplified composite rate of tax of 40% – beneficial if PAYE and NIC involved.

Who should use the Facility
- Any UK resident with unassessed tax liabilities connected with Liechtenstein.
- A person with a UK tax issue who can move their financial interests into Liechtenstein.
- Individuals who have inherited assets that have a tax liability.
- Anyone at risk of prosecution.

How Rooks Rider can help
- We have a multi-disciplinary team of tax specialists.
- We are experienced in advising on the LDF.
- We are experienced in dealing with HMRC on contentious and non-contentious matters.
- We have extensive contacts in Liechtenstein.
- We are well known in the Offshore Trusts and Tax world.

If you would like any more information or would like to discuss any of the issues raised, please contact:
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NEWS FROM THE BUDGET

There was plenty for the property industry to consider in the Spring budget.

Chancellor George Osborne announced plans to disaggregate stamp duty on bulk home purchases. Changes will be made in the Finance Bill later this year to allow the rate of stamp duty to be determined by the mean value of the dwellings purchased – subject to a 1% minimum rate rather than by their aggregate value. Therefore on a £10m portfolio of flats where the average value of each individual property is less than £175,000, this would make the stamp duty just 1% as opposed to the 5% currently charged, and would save the purchaser some £400,000.

This "long campaigned for" move is expected to finally make the rented residential sector an attractive asset class to institutions.

A Government review of stamp duty tax relief for first time buyers will be published in the Autumn.

The Government are also cracking down on stamp duty avoidance schemes which have been used to attempt to avoid tax on both residential and non residential property transactions.

There will also be consultations on proposals to make it easier to convert premises into homes. The consultation will focus on allowing a change of use to C3 (homes) with no need of a planning consent for classes B1, B2 and B3 which covers small offices through to industrial warehouse.

The Government are also introducing in September a £250m first buy direct scheme to help around 10,000 buyers earning under £73,500 per annum for Londoners (£60,000 elsewhere). The buyer contributes a 5% deposit and the Government and the house builder will contribute 10% each. The purchaser will pay the mortgage on the remaining 75%.

The loans will be interest-free for the first five years, with the rate rising to 1.75% in the sixth year and then 1% above the retail price index after that. The loan can be paid back at any time or deducted from the proceeds when the property is sold.

The scheme is exclusively for new build properties. Large housebuilders who will be delivering FirstBuy are advising buyers to register with them now and earmark a suitable property ahead of September. Developers expect to have their allocations in place by July. Critics have said that the scheme would not "scratch the surface" of the problems faced by first time buyers.

Moves to increase the housing stock follows the Department for Communities and Local Government revealing that the number of new homes built in England had fallen in 2010 to 102,570 – the lowest level during peacetime since 1923!

For further information on the budget proposals contact Stephen Phillips FNAEA Michael Tims + Company and Company and Anthony Shalet, Partner, Rooks Rider.

Assured Shorthold Tenancy Rent Threshold Increase

In Brief

From 1 October 2010 a tenancy cannot be an Assured Tenancy or an Assured Shorthold Tenancy (AST) if the annual rent exceeds £100,000, an increase from the previous threshold of £25,000. This recent change has implications both during a current tenancy which finds itself below the current threshold, and also for tenancy renewals.

Deposit Protection for AST's

A landlord under an AST must protect the tenant's deposit by using an authorised tenancy deposit scheme operated by an approved scheme administrator. This obligation was introduced by the Housing Act 2004 for tenancies that were entered into on or after 6 April 2007

Landlords with existing common law tenancies that became AST's on 1 October 2010 will not need to protect their tenants' deposits in a recognised scheme immediately because these were not taken in connection with an AST and therefore do not meet the criteria for protection under the Housing Act 2004 However, landlords will need to protect the deposit if the AST is renewed on or after 1 October 2010, or if a new deposit is taken.

The Department for Communities and Local Government (DCLG) has, however, pointed out that ultimately it is for the Courts to decide when deposits should be protected

Termination

Care must be taken on serving notice where a tenancy has become an AST. This is because if the notice expires on or after 1 October 2010, it will be ineffective unless it is not less than two months notice served in accordance with section 21 of the Housing Act 1988.

Tenancies entered into before 28 February 1997

Before 28 February 1997, if a landlord wanted to grant an AST rather than an assured tenancy he had to serve notice on the tenant before the tenancy commenced. If a common law tenancy began before 28 February 1997, the landlord could not have served the tenant with such a notice Consequently, the tenancy will have become fully assured on 1 October 2010 if the rent is below the new threshold

If a tenancy becomes fully assured on the introduction of the new threshold, rather than becoming an AST, the landlord will not be able to recover possession without a ground set out in Schedule 2 of the Housing Act 1988. To do this, the landlord will need to serve notice of that ground on the tenant before the tenancy commences.

The DCLG anticipates that this will only affect a minority of tenancies, as the majority will have become AST's on 1 October 2010 and the landlord will be able to recover possession by giving notice of expiry of any fixed term.

By Lucy Riley, Associate Solicitor, Rooks Rider

Cadogan Square Properties Limited v The Earl Cadogan [2010] UKUT 427 (LC)

The Leasehold Advisory group are delighted that Piers Harrison has contributed to this issue of Update. Piers, a barrister, is a member of Tanfield Chambers, where his property practice covers all areas of property law and clients include property development companies, local authorities, government agencies, private companies and individuals. He has a particular interest in leasehold enfranchisement.

In *Sportelli* the Court of Appeal gave guidance on the deferment rate to be applied in the majority of leasehold enfranchisement cases, but left the door open for further argument as to what the appropriate deferment rate should be in respect of leases which have less than 20 years to run at the valuation date. In this case a number of cases were heard together by a specially constituted Upper Tribunal chaired by Morgan J to determine what the appropriate rate should be for short leases.

For the non-valuers reading this let's revise what is meant by deferment rate. In a collective enfranchisement claim or a lease extension one is required to value the landlord's interest in the subject premises. One component of his interest is the right to vacant possession at the term date. The latter is valued by ascertaining the open market value of the freehold interest with vacant possession as at the valuation date and then adjusting that value to reflect the fact that vacant possession will not be available until the end of the term. The adjusting factor is called the "deferment rate". It is the annual discount applied, on a compound basis, to an anticipated future receipt (the vacant possession value of the house at the term date assessed at current prices) to arrive at its market value at the valuation date.

In *Sportelli* the Lands Tribunal approved the following formulation for calculating the deferment rate. The deferment rate is to be calculated from the addition of (i) an appropriate risk free rate and (ii) an appropriate risk premium, with (iii) a deduction for capital growth. The deferment rate was determined on the basis of a risk free rate of 2.25%; a risk premium of 4.5% for houses and 4.75% for flats (to compensate for the extra hassle of managing flats); and a real growth rate (based on evidence of long term growth) of 2%.

As the deferment rate is used to discount an anticipated future receipt a high rate will result in a lower value at the valuation date and vice versa. Thus tenants push for high rates and landlords for low rates.

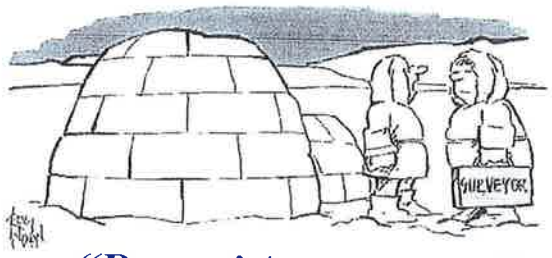
The argument used by the tenants in this case had been foreshadowed by the Lands Tribunal in *Sportelli*. At paragraph [85] of the decision it accepted the view of several experts that below 20 years the deferment rate would need to have regard to the property cycle at the time of valuation.

One of the experts who had given evidence to that effect was Professor Lizieri who again gave evidence for the tenants in this case. His argument essentially was that if the valuation date followed a period of above trend growth in property prices it could be assumed that there was a good chance that in any subsequent period there would be a reversion to the mean, thus suggesting that growth until the term date may be below the 2% growth rate used in the standard *Sportelli* calculation. The Upper Tribunal accepted that argument.

The Professor suggested the use of a mathematical model to calculate the appropriate adjustment to the growth rate. The Tribunal rejected the use of such a model but accepted instead the "valuation approach" suggested by the valuer giving evidence for the tenants. Essentially the valuation approach means relying on the evidence of valuers as to the stage in the property cycle at the valuation date and market expectations as to growth during the relevant period.

Comment

The decision has the benefit of common sense in that the shorter the period until the term date the less likely it is that a growth rate of 2% based on the long term growth rate will relate to reality. The decision is likely to be welcomed by valuers as it means an increased role for them in valuations. The downside for litigants is that there will be less certainty and more scope for disagreement between valuers. At any given point in time it is difficult to fathom where one is in the property cycle and it is much easier to recognise a bubble in retrospect. As at the date of writing it would be comparatively easy to find experts predicting substantial falls in property prices in the coming years and others who would predict growth at 2% or above. It also seems unlikely that the approach adopted in this case is suitable for very short leases of less than 10 years.



"Dry rot! Are you sure?"

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