An introduction to compulsory purchase valuation principles spanning 150 years

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Lucy Clements Smith is a commercial property specialist and has particular experience in high value and complex claims. Her recent cases range from claims arising out of all types of property valuation including a logistics warehouse in Hungary, residual and gross development appraisals of development sites, office blocks and convenience stores as well as residential investment property. Because Lucy’s clients have a global presence, she is well versed in dealing with multi-jurisdictional issues. Lucy also has considerable experience of disputes within the UK involving bricks and mortar and business valuations, property management, disputes relating to service charge provisions, rent reviews and the interpretation of lease terms. Lucy advises insurers, agents, surveyors, mortgage brokers, fund managers and other property professionals in relation to all aspects of their professional responsibilities including such diverse issues as their obligations in relation to town planning regulations, conflicts of interest and other questions of ethics and consumer regulations. Together with David Vaughan, Lucy recently delivered a series of lectures to RICS members throughout the country. The topics of the seminars included an overview of basic valuation principles for compensation matters arising out of compulsory purchase orders, Lands Chamber procedure and an overview of the Electronic Communications Code.

Abstract
Compulsory purchase compensation law is an enormously complex, increasingly specialist, but very relevant area of law. It is an area of law that is unfortunately not well understood. With major public projects such as HS2 on the horizon, Members of Parliament and local councillors have had to engage with compulsory purchase concepts...
that have been in urgent need for reform for some time. The widespread application of compulsory purchase principles as a result of the enormous HS2 project is unprecedented. It is hoped that, whilst compulsory purchase has the attention of so many MPs, that the Government will at long last consider some of the reforms suggested by the Law Commission in its excellent report.

Keywords: compulsory purchase, valuation, Rule 2, Rule 6, Land Compensation Act, No Scheme World Valuation.

INTRODUCTION

Originating from the 19th century, Compulsory Purchase Orders (CPOs) allow public bodies to acquire land or property without the owner’s consent. The public body wishing to use a CPO will have to demonstrate that taking the land is necessary for the completion of a major project that is in the public interest. CPOs have been used as a tool to allow construction of and improvements to the motorways, to regenerate town centres, build bridges, develop social housing, implement major transport schemes, and, of course, will be used to clear the way for HS2.

It is fair to say that the compensation rules are notoriously complex, and their application can be unjust at times. To understand the present state of the law it is necessary to go back 150 years to the Lands Clauses Consolidation Act 1845, and it is beyond the scope of this short paper to carry out that exercise. The Law Commission (the body created to keep the law under review and to recommend reform where needed) published two reports in 2002 and recommended the adoption of a Compensation Code that would provide clarity, consistency and accessibility. It is worth noting that despite some minor amendments to the rules through the Planning and Compulsory Purchase Act 2004, and most recently through the Localism Act 2011, there has not been a huge appetite to implement overdue reforms.

This is despite strong and repeated requests by the Court of Appeal and the House of Lords to parliament to urgently reform compulsory purchase law (see Spirerose Limited v Transport for London [2009] 1 WLR 1797 and Waters and others v Welsh Development [2004] 1 WLR 1304).

Indeed, when the Waters case was before the Court of Appeal, Carnwath LJ said:

The right to compensation for compulsory acquisition is a basic property right. It is unfortunate that ascertaining the rules upon which compensation is to be assessed can involve such a tortuous journey, through obscure statutes and apparently conflicting case law, as has been necessary in this case. There can be few stronger candidates on the statute book for the urgent reform, or simple repeal, than section 6 of and Schedule 1 to the Land Compensation Act 1961.

Having explained that the rules are complex and conflicting, this paper will discuss the core valuation principles and rules that govern the assessment of compensation payable to landowners whose properties are compulsorily acquired.

THE CORE VALUATION RULES

The underlying principle is that compensation following a compulsory acquisition of land is the principle of equivalence. This principle has been developed through case law spanning hundreds of years. Courts have determined the compensation by ensuring that the property owners are in no better and no worse position financially than they would have been if the interest had not been compulsorily acquired.

Where land is compulsorily acquired, courts will try and ensure that property owners were fairly and fully compensated for the loss arising. It is important to highlight
the fact that the basis of compensation is the value to the owner of the land being acquired not the value to the public authority acquiring the land (Stebbing v Metropolitan Board of Works [1870] LR 6 QB 37).

What is the valuation date?
Many years often pass between the date that the acquiring authority serves a notice to treat (the traditional notice pursuant to which the authority confirms that the property may be required for the major project) and the date that possession of the property is taken. During that period, the value of the land may fluctuate, and it is important to establish the correct date for the purposes of assessing the compensation payable to the owner deprived of his/her property. The statutory definition of the valuation date is set out in Section 103 of the Planning and Compulsory Purchase Act 2004, which inserts a new Section 5A into the Land Compensation Act 1961. The statutory definition accords with that established by case law, and in particular with the House of Lords decision in the case of Birmingham Corporation v West Midlands Baptist (Trust) Association [1970] AC 874. The relevant date for the purpose of valuation is the date the acquiring authority entered onto the land and took possession (in compulsory purchase language, this is known as the date of entry) or, if earlier, the date when the assessment is made (ie, is agreed or is assessed by the Lands Chamber). It is important to bear this in mind as a reference must be taken out at the Upper Tribunal (Lands Chamber) within six years of the date of entry in order to prevent the claim from being statute barred under the Limitation Act.

The case of Pointe Gourde and the ‘no scheme’ rule
It is necessary to value the property on the basis of its open market value without any increase or decrease that could be attributed to the CPO scheme. Compensation should not include an increase in value that is entirely due to the scheme underlying the compulsory acquisition.

The principle that provides that compensation for the compulsory acquisition of land cannot include an increase in value that is entirely due to the scheme underlying the compulsory acquisition was set out in the Court of Appeal case of Pointe Gourde Quarrying and Transport Company Limited v Sub Intendent of Crown Lands [1947] AC 565. The Pointe Gourde principle — known as the ‘no scheme rule’ — was enacted in the Land Compensation Act 1961 and codified in Rule (3).

What if the ‘no scheme’ rule valuation produces unfair results?
Rather helpfully, Lord Nicholls, giving the leading judgment in Waters v Welsh Development Agency [2004] 1WLR 1304 offered the following useful pointers:

(1) The Pointe Gourde principle should not be pressed too far. The principle is soundly based but it should be applied in a manner that achieves a fair and reasonable result.
(2) A result is not fair and reasonable where it requires a valuation exercise that is unreal or virtually impossible.
(3) A valuation result should be viewed with caution when it will lead to a gross disparity between the amount of compensation payable and the market values of comparable adjoining properties that are not being acquired.

The six rules
Statutory provisions relating to compulsory purchase compensation are contained in the Land Compensation Act 1961, which effectively was a consolidation statute. The six rules of compulsory purchase compensation that are found in Section 5 of the Land Compensation Act 1961 are as follows:
(1) No allowance shall be made on account of the acquisition being compulsory.

(2) The value of land shall, subject as hereinafter provided, be taken to be the amount which the land if sold in the open market by a willing seller might be expected to realise.

(3) The special suitability or adaptability of the land for any purpose shall not be taken into account if that purpose is a purpose to which it could be applied only in pursuance of statutory powers, or for which there is no market apart from the requirements of any authority possessing compulsory purchase powers.

(4) Where the value of the land is increased by reason of the use thereof or of any premises thereon in a manner which could be restrained by any court, or is contrary to law, or is detrimental to the health of the occupiers of the premises or to the public health, the amount of that increase shall not be taken into account.

(5) Where land is, and but for the compulsory acquisition would continue to be, devoted to a purpose of such a nature that there is no general demand or market for land for that purpose, the compensation may, if the Lands Tribunal is satisfied that reinstatement in some other place is bona fide intended, be assessed on the basis of the reasonable cost of equivalent reinstatement.

(6) The provisions of Rule (2) shall not affect the assessment of compensation for disturbance or any other matter not directly based on the value of land.

Rule (2)

Rule (2) is perhaps the most commonly used rule. It is known as the market value rule. It envisages a hypothetical sale of the property in the open market by a willing seller.

No allowance should be made for the fact that the property is being compulsorily acquired. Market value does not, however, mean simply the existing use value. A willing seller would expect to receive recognition of any additional value due to the development potential of the land, which will not be negligible simply because, in practice, there is only one potential buyer.

The authoritative interpretation of the ‘market value’ principle is set out in *Vyricherla Nanayana Gajapatinaju v Revenue Divisional Officer, Vizagapatnam (the Indian case)* [1939] AC 302). Lord Romer said:

The compensation must be determined, therefore, by reference to the price which a willing vendor might reasonably expect to obtain from a willing purchaser. The disinclination of the vendor to part with his land and the urgent necessity of the purchaser to buy must alike be disregarded. Neither must be considered as acting under compulsion. This is implied in the common saying that the value of the land is not to be estimated at its value to the purchaser. But this does not mean that the fact that some particular purchaser might desire the land more than others is to be disregarded. The wish of a particular purchaser, though not his compulsion, may always be taken into consideration for what it is worth.

Applying the Pointe Gourde rule to Rule (2), the ‘market value rule’, this means that the landowner would not be entitled to enhanced value attributable solely to the particular use proposed to be made of the land under a scheme of which compulsory acquisition of the land is an integral part. This element of value is not part of market value because the owner could not realise it in the open market.

Rule (6)

Rule 6 is also known as ‘Disturbance’ compensation, but it is important to note that it
has two limbs: (a) disturbance and (b) other matters not directly based on the value of the land. It is only available to occupiers of the properties. It represents the costs and losses that the property occupiers incurred as a result of being disturbed from their occupation of the property.

The exception to this is investment owners, who would be entitled to reimbursement of incidental costs incurred in acquiring a replacement investment property, as a result of being disturbed from owning the acquired property. In the case of investment owners, they would be able to recover any legal or other professional costs reasonably incurred in connection with the acquisition of the property.

The starting point when determining compensation payable under Rule (6) is the principle of equivalence as set out by Lord Nicholls in the case of Director of Buildings v Shun Fung Ltd [1995] 2 AC 111 PC:

Fair compensation requires that he should be paid for the value of the land to him, not its value generally or its value to the acquiring authority. as already noted, this is well-established. If he is using the land to carry on a business, the value of the land to him will include the value of his being able to conduct his business there without disturbance. Compensation should cover this disturbance loss as well as the market value of the land itself. The authority which takes land on ... compulsory acquisition does not acquire the business, but the ... acquisition prevents the claimant from continuing his business on the land. So the claimant loses the land and, with it, the special value it had for him as the site of his business ... in practice it is customary and convenient to assess the value of the land and the disturbance loss separately, but strictly in law these are no more than two inseparable elements of a single whole in that together they make up the value of the land to the owner. Rule (6) specifically excluded compensation for any matter directly based on the value of land. The purpose of this was clearly to avoid any potential overlap with the market value principle, introduced by rule (2). The general principle of the assessment of rule (6) compensation claims was set out by Scott LJ in Horn v Sunderland Corporation [1941] 2 k.b. 26.

The principle of compensation will include in the price of the land, not only its market value, but also personal loss imposed on the owner by the forced sale, whether it be the cost of preparing the land for the best market then available, or incidental loss in connection with the business he has been carrying on, or the cost of reinstatement, because otherwise he will not be fully compensated. The statutory compensation cannot, and must not, exceed the owner’s total loss ... [as this] will transgress the principle of equivalence which is at the root of statutory compensation, the principle that the owner shall be paid neither less nor more than his loss.

Relocation or extinguishment?
Compensation payable under Rule 6 would include the costs of relocating the business or the cost of extinguishing it. A proprietor will usually be expected to seek to relocate his/her business. The burden of proof will be on the business owner, who will need to show that the business cannot practically be relocated to another premises, in order to succeed in a claim for extinguishment.

Under the ‘relocation’ basis, the owners of the businesses are able to claim the costs of relocation and any temporary losses. The ‘extinguishment’ basis assumes that the business is closed down and compensation is
based on the value of the business. In most cases, relocation will be the preferable option for both parties; but provision needs to be made for those cases where the claimant wishes to relocate, even though total extinguishment would be the cheaper option for the authority.

A business owner will have to show that the property that is being acquired is so unique that the business cannot possibly carry on at alternative premises, or that the costs of relocating the business are greater than the value of the business and that no prudent business owner would incur the costs of relocating the business, if these far exceeded the end value of the business.

In addition, it should be noted that under Rule (6) landowners are entitled to recover reasonable surveyors’, legal and other professional fees incurred as a direct result of the compulsory purchase.

CONCLUSION

It has been beyond the scope of this paper to provide anything other than a brief overview of the compulsory purchase valuation principles. Compulsory purchase compensation law is an enormously complex, increasingly specialist but very relevant area of law. It is an area of law that is unfortunately not well understood. With major public projects such as HS2 and Crossrail on the horizon, it is hoped that the government will at long last consider some of the reforms suggested by the Law Commission in its excellent report.