

## **LONG LEASES (SCOTLAND) ACT 2012**

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### **EXPLANATORY NOTES**

#### **PART 4: COMPENSATION FOR LOSS OF LANDLORD'S RIGHTS**

##### *Overview of Part 4 of the Act*

183. **Part 4** sets out a scheme under which the landlord of a lease converting to ownership under Part 1 may claim compensation. A landlord may claim a general payment for the loss of rights. This is termed a compensatory payment and is based on the capitalised value of the rent (see sections 45 to 49).
184. Exceptionally a compensatory payment may not be enough. In certain cases, therefore, a landlord may claim a further payment, termed an “additional payment”, for the loss of the right in question (see sections 50 to 55).
185. **Part 4** also contains provisions in relation to the landlord serving a preliminary notice where a claim is likely to exceed £500 (see section 56); the tenant making payments by instalments when the amount due is £50 or more (see section 57) and the disclosure of information (see sections 58 and 59).

##### *Compensatory payment*

##### *Section 45: Requiring compensatory payment*

186. To claim a compensatory payment, the former landlord must serve on the former tenant a notice in the prescribed form within 2 years of the appointed day, accompanied by a copy of a prescribed explanatory note (subsection (4)).
187. The sum due by the tenant is calculated in accordance with section 47 and is an ordinary unsecured debt. The claim is against the immediate former tenant of the person making the claim.
188. If the sum being claimed is £50 or more, an instalment document has to be served along with the notice (subsection (5)). This gives the former tenant the option of paying by instalments in accordance with the scheme set out in section 57. If an instalment document is not served, the notice has no effect.
189. Subsection (6) provides that the section is subject to section 56, the effect of which is to restrict the amount of compensatory payment to no more than £500 unless a preliminary notice has been served.

##### *Section 46: Making compensatory payment*

190. If the landlord has followed the notice procedure correctly, the former tenant must, unless entitled to pay by instalments (see sections 45(5) and 57), make the compensatory payment within 56 calendar days beginning with the day on which notice is served.

## ***Calculation of compensatory payment***

### ***Section 47: Calculation of the compensatory payment***

191. This section sets out how the compensatory payment by tenants to landlords is to be calculated. The method of calculation is based on the compensation scheme under the Abolition of Feudal Tenure etc. (Scotland) Act 2000, which abolished feudal tenure. The compensation is designed to deliver the same economic benefit to the landlord as the ongoing income from rent paid under the ultra-long lease being converted to ownership. Additional payments may also be due – see sections 50 to 55.
192. The compensatory payment is first calculated by working out the Annual Income (AI). As outlined in Step 1, the AI is calculated by determining the annual rent, in accordance with section 48, and then, as outlined in Step 3, by adding any notional annual renewal premium (NARP) calculated under section 49. Under Step 2 and section 49, the NARP is any renewal premium of £100 or less, divided by the renewal period (RP) (see section 49). Renewal premiums of over £100 may give rise to a separate claim for an additional payment – see section 51(1)(d).
193. To give an example, if the annual rent is £2.50 and the renewal premium is £2.50, with a renewal period of 99 years, the AI is £2.50 plus 3p (£2.50 divided by 99, rounded to the nearest penny). Therefore, the AI is £2.53.
194. The next step, as outlined in Step 4, is to calculate the sum of money which would, if invested in 2.5% Consolidated Stock, produce an annual sum equal to AI. This sum is the compensatory payment.
195. The price of Consolidated Stock varies. At 2 November 2012 the price was £58.76 (to buy £100 of nominal stock yielding 2.5% interest). Therefore, the compensatory payment is £58.76 (price of stock yielding £2.50 a year) multiplied by £2.53 (AI) divided by £2.50 (annual sum produced by investing £58.76 in 2.5% consolidated stock). This gives a compensatory payment of £59.47.
196. To give another example, if the annual rent is £20 and there is no NARP, the compensatory payment is £58.76 (price of stock) multiplied by £20 (AI) divided by £2.50 (annual income from the stock). This gives a figure of £470.08
197. Another way of carrying out the calculation is to use a variable multiplier (variable as the price of 2.5% Consolidated Stock varies). Therefore, if the price of 2.5% Consolidated Stock is £58.76, the variable multiplier is 23.5 (£58.76 divided by £2.50). This variable multiplier can then be multiplied by the AI to produce the compensatory payment.

## ***Annual rent***

### ***Section 48: Determination of the annual rent***

198. This section lays down how the annual rent should be determined for the purposes of calculating the compensatory payment. In some cases, rent may be paid on a *cumulo* basis. *Cumulo* rent is defined in section 38 and refers to a single rent payable in relation to two or more leases. In these cases, the annual rent is allocated under section 40.
199. In other cases, a lease may be “partially continuing” (a definition of “partially continuing lease” is laid down in section 37). In these cases, the annual rent is allocated under section 41.
200. Where the lease does not involve *cumulo* rents or partially continuing leases, the annual rent is as laid down in the lease, excluding any non-monetary payments.

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201. Subsection (2) provides that any rent expressed in non-monetary terms is to be excluded from the calculation of the compensatory payment. Provision is made for non-monetary rents to be the basis of a claim for an additional payment – see section 51(1)(a).

### ***Renewal premiums***

#### ***Section 49: Calculation of notional annual renewal premium***

202. This section applies if a renewal premium of £100 or less is payable under the lease and it is necessary to include the renewal or more than one renewal in order to meet the durational requirements for conversion.
203. Subsection (2) directs the former landlord to divide the amount of the renewal premium by the number of years between each renewal. This gives a sum which represents the “notional annual renewal premium” or NARP. The NARP is added to the annual rent payable under the lease in order to calculate compensation under section 47.
204. Subsection (3) provides that that where there is a partially continuing lease, the renewal premium for leases converting to ownership is as allocated under section 43. Where there is not a partially continuing lease but there is a *cumulo* renewal premium, the renewal premium is as allocated under section 42. And in all other cases the renewal premium is the amount payable under the lease.
205. If a renewal premium of more than £100 is payable, the landlord can claim compensation under the additional payments regime set out in sections 50 to 55.

### ***Additional payment***

#### ***Section 50: Claiming additional payment***

206. To claim an additional payment for the loss of a right, the former landlord must serve a notice in the prescribed form on the former tenant within two years of the appointed day (subsections (2) and (4)). The amount claimed is calculated in accordance with section 52. The claim is against the immediate former tenant of the person making the claim except in the circumstances set out in subsection (3).
207. Under subsection (3), where the right lost by the former landlord of a superior lease is one specified in section 51(1)(e) to (g), the former landlord is directed to serve the notice claiming an additional payment on the former tenant of the qualifying lease rather than on the former tenant of the superior lease.
208. Subsection (4) sets out various requirements for the form and content of the notice. The notice must be accompanied by a copy of the explanatory note.
209. Under subsection (5), if the sum being claimed is £50 or more an instalment document has to be served along with the notice. This gives the tenant the option of paying by instalments in accordance with the scheme set out in section 57. If an instalment document is not served the notice has no effect.
210. Subsection (6) provides that the section is subject to section 56 the effect of which, in the case of a qualifying lease, is to restrict the maximum amount that can be claimed by way of additional payment to £500 unless a preliminary notice has been served.

#### ***Section 51: Extinguished rights***

211. This section identifies the rights the loss of which may found a claim for an additional payment. In the notice making the claim it will be for the landlord to nominate, and to justify, the particular ground of claim (see section 50(4)).
212. Subsection (1)(a) refers to a right to a non-monetary rent. Paragraph 6.29 of the Scottish Law Commission report indicated that in around 1% of the leases it surveyed it found

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non-monetary rents such as six fat hens, oat farm meal and the services of a labourer for three days to work on the roads in a town.

213. Subsection (1)(b) refers to a right to have the rent reviewed or increased. Paragraph 6.30 of the Scottish Law Commission report indicated that provision for rent reviews was rare in ultra-long leases but the possibility should be acknowledged. Paragraph 6.31 of the report indicated that it is possible for rent to increase by way of a fixed formula rather than by virtue of a review.
214. Subsection (1)(c) refers to a right to a rent to the extent that the amount payable is variable from year to year. This might, for example, be relevant where rent is based on the turnover of a business.
215. Subsection (1)(d) refers to a right to receive a renewal premium of more than £100 (rights to receive lesser amounts can be recovered under the compensatory payment regime (see sections 47 and 49)).
216. Subsection (1)(e) relates to a landlord's right of reversion, so long as the lease would expire no later than 200 years after the appointed day. Reversionary rights occasionally may have a value over and above the income stream from rent. Rights falling into this category are to be valued in accordance with section 52(3) and (4).
217. Subsection (1)(f) refers to a right to bring a lease to an end before its normal expiry. The right has to be within the full control of the landlord and exercisable within 200 years of the appointed day. A break clause exercisable at regular intervals or a right of redemption or resumption exercisable at the landlord's discretion would be included but not a right to terminate on breach. A right (such as a right of redemption) which is converted into a real burden under sections 16,19 or 23 is excluded.
218. Subsection (1)(g) refers to a right to development value provided that the right has not been converted into a real burden under sections 16 or 19. "Development value" is defined in subsection (2) as is the expression "right to development value".

***Section 52: Calculating additional payment***

219. This section sets out some general and some specific rules for determining the amount of an additional payment. Subsection (2) provides that the right is to be valued as at the appointed day.
220. Subsections (3) and (4) contain specific rules relating to the valuation of a landlord's reversionary interest in a claim under section 51(1)(e). In particular, the value is deemed to be the value of the right if sold on the open market by a willing seller to a willing buyer, with special buyers and special sellers (i.e. those with a particular interest in the property) disregarded.
221. Subsections (5) to (7) provide that any obligations on the landlord which are extinguished by conversion have to be taken into account (but not insofar as such obligations are preserved as a counter obligation to a real burden) as has any other entitlement of the landlord to recover in respect of the loss. "Any other entitlement" refers primarily to the compensatory payment calculated under section 47.
222. Subsection (8) caps a claim for the loss of the right to development value. In some cases, ultra-long leases may have been granted cheaply on the basis that the property was used for some limited purpose, such as the building of a church or a community hall.
223. Paragraph 6.45 of the Scottish Law Commission report said that if any leasehold conditions preserving development value were discharged by the Lands Tribunal, any compensation would be limited to a sum to make up for the effect the leasehold condition produced in reducing the consideration paid for the interest in the property. No account is taken of inflation. In other words, the loss of the right to development

value is limited to the reduction in the price paid for the interest in the property at the time.

***Section 53: Additional payment: former tenant agrees***

224. This section applies where, following service of an additional payment notice under section 50, the former tenant agrees to make the payment specified in the notice. Unless the former tenant is entitled to pay by instalments (see section 57), payment must be made to the former landlord within 56 calendar days beginning with the day on which the notice was served on the former tenant.
225. There may be cases where the former tenant does not agree to pay the amount specified in the notice. In these cases, the former tenant and the former landlord may agree that a different amount should be paid (see section 54) or where agreement cannot be reached, the matter may be referred to the Lands Tribunal (see section 55).

***Section 54: Additional payment: amount mutually agreed***

226. Following service of an additional payment notice under section 50, the former landlord and former tenant may agree that a different amount be paid. This section regulates the procedure to be followed.
227. Subsection (2) requires the former landlord to serve a further notice in the prescribed form on the former tenant specifying the agreed amount and requesting payment. The notice must be served within 5 years of the appointed day to be valid. If a notice is not served, the obligation to pay does not arise and the landlord loses the right to collect the payment.
228. Subsection (3) sets out requirements for the form and content of the notice. The notice must be accompanied by a copy of the explanatory note (to be prescribed by the Scottish Ministers in regulations).
229. If the agreed sum is £50 or more, subsection (4) requires that an instalment document is served along with the notice. This gives the tenant the option of paying by instalments in accordance with the scheme set out in section 57. If an instalment document is not served, the notice has no effect.
230. Unless entitled to pay by instalments, subsection (5) requires the former tenant to make payment to the former landlord within 28 calendar days, beginning with the day on which the notice is served.

***Section 55: Claim for additional payment: reference to Lands Tribunal***

231. This section applies in cases where no agreement has been reached under section 53 or section 54.
232. Subsection (1) gives both the former tenant and the former landlord the right to refer any matter relating to a claim for an additional payment to the Lands Tribunal.
233. Subsection (2) gives the Lands Tribunal a wide discretion to determine the matter and make such order as it thinks fit.
234. Subsection (3) requires the Lands Tribunal to provide the former tenant with the option of paying by instalments in accordance with the statutory instalment scheme if the additional payment is fixed at £50 or more. This subsection makes certain amendments to the instalment scheme to take account of the fact that no instalment document will be served on the former tenant in such circumstances.
235. Subsection (4) provides that all references to the Lands Tribunal must be made within 5 years of the appointed day.

## **Supplementary**

### **Section 56: Claims in excess of £500: preliminary notice**

236. A landlord who intends to claim a sum which is likely to exceed £500 by way of compensatory or additional payment from the tenant of the qualifying lease has to serve a preliminary notice. This notice must be served no later than six months before the appointed day on the person who is registered at that time as the tenant. Separate notices have to be served in respect of each type of payment. If a notice is not served the amount of compensatory or additional payment that can be claimed is capped at £500.

### **Section 57: Making payment by instalments**

237. Where the compensatory payment or additional payment is £50 or more the former landlord has to serve an instalment document along with the relevant notice. This section sets out the rules of the instalment scheme.
238. Subsection (2) provides that the instalment document must be completed in the prescribed form and accompanied by a copy of the explanatory note.
239. Subsection (3) requires that to obtain the option to pay by instalments, the former tenant has to sign, date and return the instalment document along with payment of a 10% surcharge. The tenant has to do this within the period allowed for payment of the compensatory or additional payment, which is either 56 or 28 calendar days.
240. Subsection (4) provides that the option of paying by instalments is lost by the former tenant of a qualifying lease in the event of a sale of the whole or part of the land now owned.
241. Subsections (6) and (7) set out the details of the instalment scheme. Whitsunday is 28 May and Martinmas is 28 November.
242. Subsection (8) provides for immediate payment of the balance if an instalment is unpaid for forty two calendar days.
243. Subsection (9) makes clear that in other cases the balance can be repaid at any time.

### **Section 58: Collecting third party to disclose information**

244. This section requires any third party collector of rent (e.g. where rent has been on a *cumulo* basis) to disclose to the landlord information about the tenants from whom the rent has been collected and, where the rent remitted is part of a *cumulo* rent, the amount so collected, so far as this is practicable.

### **Section 59: Duty to disclose identity etc. of former tenant**

245. This section requires a person on whom a notice was mistakenly served claiming a compensatory or additional payment to disclose the name and address of the former tenant or, failing that, such other information as will enable the former tenant to be traced.

### **Section 60: Prescription of requirement to make payment**

246. This section provides that the obligation to pay the compensatory or additional payment prescribes (i.e. extinguishes) after 5 years. Prescription starts to run from the date the obligation to pay arises.

### **Section 61: Interpretation of Part 4**

247. Subsection (1) defines former landlord and former tenant for the purposes of Part 4. It has to be read alongside the definitions of landlord and tenant in section 80(1). The definitions include a person who has a right to the interest but who has not completed

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title. If more than one person comes within the definition the latest such person is treated as the landlord or the tenant.

248. Subsection (2) provides where there are co-tenants their liability is joint and several as regards the compensatory or additional payment in a question with the former landlord and also among themselves. It also makes clear that for the purposes of Part 4 such tenants are to be treated as a single tenant except for the provisions regarding service of a notice.