FACV Nos. 1, 2, 3, 4, 5, 6, 7, 8 & 9 of 2017

IN THE COURT OF FINAL APPEAL OF THE HONG KONG SPECIAL ADMINISTRATIVE REGION
FINAL APPEAL NOS. 1, 2, 3, 4, 5, 6, 7, 8 & 9 OF 2017 (CIVIL)
(ON APPEALS FROM CACV NOS. 13, 14, 15, 16, 115, 116, 119 & 120 of 2015)

BETWEEN

PENNY'S BAY INVESTMENT COMPANY LMITED Applicant
(Appellant in FACV 1/2017)

and

DIRECTOR OF LANDS Respondent
(Appellant in FACV 2-9/2017)

APPELLANT'S CASE
of
DIRECTOR OF LANDS
(APPELLANT IN FACV 2-9 / 2017)

Reference[1]

1. This appeal by the Director of Lands ("the Director") concerns the following question on which this Court has given leave to A2/18/365-366 A2/19/392-401

[1] References to "A/…" and "B/…" are respectively references to Part A and Part B of the Record. Page references to Part B of the Record will be added when the index to that Part of the Record is finalised.

appeal against the decision of the Court of Appeal ("the CA"):- A2/25/403

> "*Whether the Court of Appeal were correct in holding that, although the Court of Final Appeal had directed that different factual assumptions were to be made for the purposes of the before and after valuations, most of those assumptions could not as a matter of law lead to any difference in the two values*".

Introduction

2. The facts are fully set out in a number of previous judgments in this protracted litigation including in the previous judgment of Lord Hoffmann in this Court of 26 March 2010 so that only a short summary is needed here.

3. The essential background facts are as follows. Lot 22 at Penny's Bay was held by Penny's Bay Investments Limited ("PBIL") under a lease granted on 2 January 1970 for a term of 99 years less 3 days from 1 July 1898, extended to 30 June 2047. It was 2,010,000 sq. ft. in area with a sea frontage. It had no land access except by pedestrian tracks. Under Special Condition 3(a) of the lease the land could be used only for general industrial and/or godown purposes and at least 285,000 sq. ft. could be used only for shipbuilding purposes. The land was sub-let in 1975 to an associated company of PBIL. A part of the land was used by PBIL or its sub-tenant as a shipyard. No other use was ever carried out on the land and the greater part of the land was unused. A draft Outline Zoning Plan ("OZP") was published on 24 March 1995 in which much of the land was zoned for industrial use.

4. In the mid-1990s the Government proposed to carry out a scheme of reclamation of the sea at Penny's Bay in order to construct a container port. An essential part of that scheme was the construction of a new link road to run northwards, across a small part of Lot 22, to join the proposed North Lantau highway. No land of Lot 22 was to be acquired for the scheme save for the part needed for the road.

5. On 11 March 1994 the Director of Lands published a notice in the Gazette under s.5 of the Foreshore and Sea-bed Reclamations Ordinance, Cap 127 ("the FSRO") describing the proposed reclamation and its purpose. On 25 April 1995 the Secretary of Transport published in the Gazette details of the proposed new road under the Roads (Works, Use and Compensation) Ordinance Cap 170. On 5 May 1995 the then Governor in Council published in the Gazette the authorisation of the reclamation of 1,260 hectares of foreshore and sea-bed. The effect under s.10(1)(a) of the FSRO was that on 5 May 1995 all marine rights (the rights of passage between the land and the sea) of Lot 22 were extinguished. Under s.12(1) of the FSRO PBIL became entitled to compensation for any injurious affection to land caused by the reclamation.

6. Subsequently the Government changed its proposals and a new reclamation was carried out so as to create the Hong Kong Disneyland currently in operation at Penny's Bay. In April 2001 PBIL voluntarily surrendered its lease to the Government in return for a payment of $1,506,098,750. These events did not

affect the entitlement of PBIL to compensation under s.12 of the FSRO.

7. There were proceedings in the Lands Tribunal ("the Tribunal") and the Court of Appeal ("the CA") and this Court ("the CFA") on a preliminary issue concerning the method of the assessment of compensation. Following the decision of this Court on 26 March 2010 the proceedings were remitted to the Lands Tribunal for the assessment of compensation. The Tribunal determined the compensation in the sum of $10,925,500 (subsequently amended to $9,431,000 as a result of an agreed minor error). Both parties again appealed to the CA and both appeals were to some extent allowed so that the matter was remitted to the Tribunal for further consideration in accordance with the decision of the CA. Accordingly the question on which leave to appeal to this Court has been given to the Director is one of the holdings of law of the CA.

A1/1/150, §480
A1/1/152
A1/3/169, §50
A2/10/286-287, §§4-5
A2/12/312

<u>The declaration</u>

8. This Court in its unanimous judgment of 26 March 2010 declared that the compensation was to be assessed in the following way, as stated in paragraph 47 of the judgment of Lord Hoffmann:-

> *"The compensation payable to the claimant is the difference between (a) the price which Lot 22 would have fetched on a sale in the open market between a willing seller and a willing buyer on 5 May 1995 on the assumption that it enjoyed access to the sea as it had done up to that date and (b) the price which it would have fetched on such a sale on the assumption*

that access to the sea had been lawfully interrupted by the completion of the proposed reclamation."

The principles

9. In the light of the declaration and general principles of compensation law there are six principles of law which provide the framework for the assessment of the compensation in this case. We propose in this document to set out the principles and then to explain how these principles were applied in a generally correct fashion by the Tribunal but were disregarded in important respects by the CA. It is that error by the CA which has led to the question on which leave to appeal has been granted by this Court.

(i) The first principle

10. The first principle is the obvious one that the compensation is to be assessed as the difference between two values, as set out in the CFA declaration, called for convenience the before value and the after value. It is important to note that each value is the price which would have been paid for Lot 22 on the same date but in different factual circumstances as a result of a hypothetical negotiation between a willing seller and a willing buyer. These hypothetical parties are not actual persons and are not PBIL as a seller and not some actual person as a buyer; instead they are sensible and reasonable people who wish to reach agreement and do so with each doing all that is reasonable to obtain what is for each of them the best result; see *Executors*

of Lady Fox v. Inland Revenue Commissioners [1994] 2 EGLR 185 at 186E, per Hoffmann LJ. In the event of disagreement the sum which the hypothetical negotiators would arrive at as the agreed price in the two different sets of assumed circumstances is to be determined by the Tribunal on the basis of expert evidence and submissions.

11. These are basic and well-established rules of valuation, normally applicable to the statutory valuation of all assets for all purposes. As we will explain the CA abandoned these rules and imposed upon the valuers and the Lands Tribunal a rigid rule of law that fundamental components of the two prices or values had to be the same for the before and after values irrespective of what valuation evidence was given and irrespective of any differences between the assumptions underlying the two valuations. Such a rule of law and imposed process is unprecedented in valuation law and was supported by no authority and no satisfactory reasoning. It is contrary to this first principle since it pays no heed to what the hypothetical parties would have done but imposes the valuation judgments of the CA.

A1/5/220-223, §§82-91

(ii) <u>The second principle</u>

12. The second principle is that different factual assumptions were directed to be made for the before and after valuations. Since the two valuations were of the same land and as at the same date these differences are crucial since had they not been different the two values would have necessarily been the same. The

declaration of course specified the different assumptions.

13. The factual assumptions to be made for the before valuation, as stated in the declaration or as a necessary consequence of what was so stated, are as follows.

(a) Lot 22 continued to enjoy access to the sea on 5 May 1995.

(b) No extinguishment of the marine rights of the Lot had been brought about prior to or at that date under the FSRO.

(c) Those marine rights, and thus access to the sea, would continue for the remaining 52 years of the lease unless they were removed at some future time by some future and different process of legal extinguishment under the FSRO.

(d) In the absence of such a future extinguishment the land could be used in accordance with the lease conditions as a shipyard and for godown purposes dependent on sea access only.

(e) The carrying out of general industrial development on the land beyond the 285,000 sq. ft. shipbuilding area could only occur if a new link road was built.

(f) That new link road would only be built if there was a future reclamation of the sea-bed accompanied or followed by a future container port development, or some other future

valuable development, of the reclaimed and other land. That reclamation and new road could themselves not have occurred without a future extinguishment of marine rights under a future and different FSRO process.

14. The factual assumptions to be made for the after valuation, again as stated in the declaration or as a necessary consequence of what was so stated, are as follows.

(a) Access to the sea had been interrupted on 5 May 1995.

(b) That interruption was brought about by the publication on that date in the Gazette of the authorisation of the Governor in Council of the proposed reclamation under the FSRO, something which under s.10(1)(a) brought about on that date the extinguishment of marine rights.

(c) The proposed reclamation was completed by 5 May 1995.

(d) The ability to use any part of Lot 22 for shipbuilding or godown purposes ceased on 5 May 1995 since those uses were dependent on marine rights or sea access which had been extinguished on that date.

(e) An industrial development of much of the Lot, beyond the 285,000 sq. ft. which could be used only for shipbuilding purposes, could be carried out in the future in accordance with the industrial zoning in the draft OZP but only as and

when a new link road was built so providing vehicular land access.

15. There are two explanatory addenda to be made in connection with the above assumptions. The first is that certain of the circumstances described as factual assumptions were in truth the reality such as existed on 5 May 1995 as opposed to being assumptions. For example, the interruption of access to the sea for the purposes of the after valuation (paragraph 14(a)) was what really happened on 5 May 1995 as well as being an assumed fact. Other assumptions were assumptions as opposed to the reality, for example the assumption for the purposes of the before valuation that marine access continued to exist on and after 5 May 1995 (paragraphs 13(a) and (b)).

16. The second addendum is the assumption for the purposes of the after value that the reclamation had been physically completed by 5 May 1995 (paragraph 14(c)). The CA held that this assumption had to be made but that it was to have no valuation consequences or effect. The Director was refused leave by this Court to appeal against this element of the CA decision. Consequently we proceed, as we must for the purposes of this appeal, on the footing that whereas this particular assumption has to be made it has no further relevance to the two values or the difference between them.

A1/5/217-220, §§73-80

A2/21/373-374, §3

(iii) The third principle

17. The third principle is in effect explanatory of the operation of the second principle. The second principle is that certain assumptions of fact (which may or may not correspond with the reality) have to be made as at the valuation date. These assumptions are succinctly set out in the CFA decision. Certain of the assumptions for both values as set out above are a direct repetition of the terms of the declaration, for example the assumption for the after valuation (paragraph 14(a)) that access to the sea has been lawfully interrupted on 5 May 1995. Other assumptions are logical and inevitable consequences of such directly stated or primary assumptions. For example, the assumption that for the before value a shipbuilding and godown use of the land could have been carried out at and after the valuation date (paragraph 13(c)) is an inevitable consequence of the primary assumption that the land continued to enjoy access to the sea on 5 May 1995. This third principle, as well as being backed by common sense, is the subject of high authority. In *East End Dwellings Co Ltd v. Finsbury Borough Council* [1952] AC 109 Lord Asquith said at pg.132:-

> *"If you are bidden to treat an imaginary state of affairs as real, you must surely, unless prohibited from doing so, also imagine as real the consequences and incidents which, if the putative state of affairs had in fact existed, must inevitably have flowed from it or accompanied it".*

All of the assumptions set out in paragraphs 13 and 14 are set out in the CFA judgment or are logical and inevitable consequences of those assumptions.

18. It is important here to draw a distinction between an assumption or state of facts which inevitably flows from an expressly directed assumption and that which is merely a possible or expected consequence of an expressly directed assumption. Where a consequence is only a possibility or probability that assumption does not have to be made as a matter of law or principle but rather the prospect of its occurrence has to be determined by the Tribunal on the evidence. Strictly speaking the question is whether the willing buyer would regard the possible consequence as certain or virtually certain or would regard it as having some degree of risk or uncertainty. For example, the construction of a new link road was not an inevitable consequence of the extinguishment of marine rights but may have been regarded by a willing buyer in the after situation as a virtually certain consequence or only as a likely consequence of the extinguishment. The question of into which category a particular consequence falls is a matter for expert evidence and the judgment of the Tribunal. The CA flouted this third principle by holding that the degree of risk and the period of delay attendant on a road being built and industrial development becoming possible had to be the same irrespective of considerations of common sense or of the expert evidence.

A1/5/220-223, §§82-91

(iv) The fourth principle

19. The fourth principle is that for both the before and the after valuations all relevant facts and information must be taken into account save for the assumptions as stated in the declaration and the consequences of those assumptions as just mentioned. There is, so to speak, a background of reality into which these assumptions, with their differences for the two valuations, are imposed. The Court said just this at paragraph 46 of Lord Hoffmann's judgment.

> *"The valuation must take into account all the information which was public knowledge at the time and (apart from the assumptions about marine rights) not be based on any artificial assumptions."*

This is no more than the application to the assessment of compensation under the FSRO of the "presumption of reality" which permeates the law of compensation. The principle was put as follows by Megaw LJ in *Trocette Properties Ltd v. GLC* (1974) 28 P & CR 408 at pg.416:-

> *"If the assessment of the value for the purpose of compensation is to be on the basis of ignoring a proven or admitted fact which would have affected the price of an actual site on the open market, the use of such basis must, I think, be justified by reference to some specific provision of the legislation."*

20. This principle was correctly applied by the Tribunal. For example, the before value was ascertained on the basis that since

the marine rights continued to exist on and after the valuation date the before value included the value of the land on the valuation date for a continued shipbuilding use and a new godown use. Both of these uses were dependent on access to the sea and thus the continuation of the marine rights. In the same way the provisions of the draft OZP and the publication on 25 April 1995 of the provisions for a new road under the Roads (Works, Use and Compensation) Ordinance formed part of the factual background for both valuations. The CA ignored this principle in that it held that irrespective of any actual expectation of the hypothetical parties the expected deferment period for industrial development had to be the same in two substantially different situations.

A1/1/43-47, §§108-118

A1/5/220-223, §§82-91

(v) The fifth principle

21. The fifth principle is that Lot 22 has to be valued by reference to facts as they were at the valuation date. The hypothetical parties when they reach agreement on the price cannot know what will or will not happen in the future. The principle is an aspect of all land valuations which are anchored to a valuation date and is supported by abundant authority. Unless the governing statute, or a court interpreting that statute, states otherwise there cannot be total and absolute certainty about the future. This rule was explained by this Court in the present case in paragraph 43 of the judgment of Lord Hoffmann where he said:-

> *"The value of property means the price which it would have fetched on a sale in the open market between a willing seller and a willing purchaser on*

the relevant date. That decision cannot be affected by what happened afterwards".

22. Consequently absolute certainty must be differentiated from expectations at the valuation date. Many land transactions are arrived at on the expectation of what will happen after the sale and on what may subsequently be able to be done on the land. Such expectations may vary from a near certainty with no appreciable risk to a remote possibility. The art of the valuer is to ascertain what additions to, or deductions from, the value (if any) he considers the willing buyer would make by reason of such expectations. Lord Hoffmann stated the principle at paragraph 44 of his judgment where he referred to the possibility of lively expectations existing about how the value of land on Lantau Island would be enhanced by the proposed works. He added:-

> *"Whether such expectations existed and the extent, if any, to which they would have affected the open market value of the land is a matter for evidence when the valuation comes to be done. But if they did exist and would, as a matter of reality, have affected the price which the land would have fetched, they cannot be ignored."*

The important principle which Lord Hoffmann stated is that such expectations are a matter for evidence and their existence and effect on values are not to be imposed in a mechanistic fashion by any court as though they were questions of law. The CA acted in a way which was directly contrary to this principle.

A1/5/217-220, §§73-80

(vi) The sixth principle

23. This leads to the sixth principle which is to an extent a matter of procedure but is vital to the question in this appeal. It is for a court assessing the two values (including of course on points of law an appeal court) to state any relevant principles of law to be applied in the valuation process. It is then for the court of first instance (usually a specialist tribunal) to hear evidence on valuation matters and to determine the values in accordance with those principles of law and on the basis of the evidence and its own specialist expertise. If the Tribunal has got the law wrong an appellate court will correct it. However, it is, we submit, not for an appellate court to usurp the task of the Tribunal and tell it how to value or, still less, to tell it precisely what detailed valuation judgments it has to make. To take an example from the fifth principle, it is not for an appellate court, whose jurisdiction is confined to questions of law, to tell a tribunal of first instance that it must make one assessment and not another of the risk of some future event, such as the building of a road, not happening or, still less, to direct that tribunal what its assessment of some matter such as the likely date of the road being available must be on different factual assumptions in different valuations which are relevant to determining that date. As we will explain it is the direction by the CA on such a matter which underlies the present appeal.

The Lands Tribunal's decision

24. The Lands Tribunal followed and applied these six cardinal principles in its decision. It was the CA which, on the point now under further appeal, flouted certain of the principles. The logical way in which to explain this submission is therefore first to state how the Tribunal followed the principles and then to explain what we submit was the error of the CA on the question under appeal.

25. The decision of the Tribunal is a long and somewhat complex document including its assessment of four before values and the selection of one of them as the before value to be applied. In order to assist the CA we put before that Court a summary and analysis of the decision which attempted to follow, without comment, the steps in the reasoning, and this document is being put before this Court. In the end the essence of the Tribunal's decision can be stated quite briefly. A1/1/1-152

26. For the purposes of the before value (called the fourth before value) the Tribunal proceeded by five steps. We omit in this summary minor aspects of the valuation, such as the receipt of a small amount of rent from the sub-tenant, which have no bearing on the substance of the question now under appeal.

    (a) It determined the value on the assumption that the marine rights could continue until 2047. This allowed a shipbuilding and godown use to be carried out. The value was A1/1/109, §345

$551,157,000.

(b) It determined the value on the assumption that the container terminal scheme would certainly have gone ahead. This would have required the new road to be constructed and would have allowed an industrial development on much of Lot 22 which could have been commenced eight years after the valuation date. This value was $841,828,000. A1/1/128, §§403-405

(c) The additional value created by the prospect of industrial development was therefore $841,828,000 less $551,157,000 = $290,671,000. A1/1/129, §408

(d) It decided that the prospect of the container terminal scheme proceeding, with the before value assumption of no extinguishment of marine rights on the valuation date, was 50%. Thus the additional value due to the prospect of industrial development became 50% of $290,671,000 = $145,335,500. A1//1/129, §408

(e) The before value was therefore the value of Lot 22 with no prospect of industrial development plus one half of the additional value which industrial development would give, i.e. $551,157,000 + $145,335,500 = $696,492,500. A1/1/129, §§408-409

27. There are two observations to be made on this process which are important for the question presently under appeal.

(a) The before value as determined depended on a prospect of industrial development. This in turn depended on a reclamation and a new road to serve the reclaimed area. Given the assumption dictated by the CFA declaration that marine rights remained at the valuation date these events could only have occurred if there was in the future a new FSRO process bringing about the extinguishment of marine rights. It was of course the obvious uncertainty of this which largely created the 50% deduction for risk. A1/1/118, §§371-372

(b) The industrial value of land for an immediate start on industrial development (the "dead ripe" value) was not in dispute. The deferment of the value for eight years was, of course, that which the Tribunal determined as the expectation of a willing buyer since before industrial development could start there would have to be a new FSRO extinguishment of marine rights, the carrying out of the reclamation, and the construction and opening of the new road (which might have been contemporaneous with or following the reclamation). A1/1/127, §401

28. The Tribunal assessed the after value by fundamentally the same process. There were two major differences which stemmed from the different assumptions as described in the CFA's declaration. Obviously no sum could be attributed to a shipbuilding or godown use since those uses became impossible with the extinguishment of the marine rights on which they depended. The other difference was that the extinguishment of marine rights under a completed FSRO legal process, taken to have occurred at A1/1/147-148, §§469-474

the valuation date, obviously increased the expectation that a new road would be built and that industrial development would become possible and, additionally, it reduced the likely period which would have to elapse before a start on that development became possible.

29. In these circumstances the Tribunal assessed the after value by essentially two steps.

(a) It included only a nominal value for the land over the period from the valuation date until the expected start of the industrial development. A1/1/141, §449

(b) It then included the industrial value as it had done for the before valuation but with two differences as just explained, namely (i) that no deduction for risk or uncertainty was needed and (ii) that the deferment period was reduced from eight to six years. A1/1/147, §472 A1/1/148, §474 A1/1/147, §471 A1/1/148, §474

In carrying out the second step the Tribunal accepted but only in part the expert valuation evidence of Mr Mok and others for the Director. The Director adduced expert evidence of industrial values and costs so as to arrive at a dead ripe industrial value. For reasons which we have never understood PBIL adduced no evidence of their own on industrial values and the Tribunal accepted the evidence of the Director. However, on deferment Mr Mok opined that a four year deferment was correct for the after value situation but the Tribunal found that six years was more A1/1/147-48, §471-474

appropriate. This was, of course, their task in assessing the evidence. The after value determined at the end of these steps was $685,540,000. A1/1/148, §475

30. The compensation as determined by the Tribunal was therefore (after small and agreed amendments were made to it) $694,971,000 less $685,540,000, i.e. $9,431,000. A1/3/169, §50

31. In reaching its decision the Tribunal applied each of the principles described as the first to sixth principles as described above and in particular applied the second principle which contained the assumptions as directed by this Court and the consequences of those assumptions.

The decision of the Court of Appeal

32. The CA corrected the reasoning of the Tribunal on a number of points, some of minor import such as that the Tribunal had on occasions misstated the cost of removing unauthorised structures on the land. There were two important respects in which the CA altered the approach of the Tribunal. The first was that it held as a matter of law that the risk of the industrial development not becoming possible and the period of the deferment of that development and its value had to be exactly and numerically the same for the before and after valuations. It is this holding of law which is the question on which the Director was given leave to appeal and which is the subject of this document. The second alteration was that the CA held that a godown use necessarily A1/5/241, §147

A1/5//220-223, §§82-91

A1/5/232-236, §§117-129

involved a warehouse such that the Tribunal was wrong to value an open storage use as a godown use. This matter is the subject of the question on which PBIL were given leave to appeal. The two questions are entirely unrelated and this document addresses only the first question.

A2/17/360-364

The error of the CA

33. The Tribunal carried out the traditional process of land valuation. It clarified and stated the assumptions of fact on the basis of which it then carried out each of the necessary two valuations. Of course those assumptions differed in ways material to the valuation and have been stated in paragraphs 13 and 14 above. The source of the assumptions was of course the content of sub-paragraphs (a) and (b) of paragraph 47 of the CFA judgment. We are not aware of any material respect in which the CA thought that the Tribunal got its assumptions wrong. Once the Tribunal had stated the before and after value assumptions it assessed the expert evidence, including evidence about expectations at the valuation date for both valuations, and carried out the two valuations with their results as described earlier. As far as we can see there was no holding by the CA of any significant technical errors by the Tribunal. Since the assumptions for the two valuations were different it was likely, probably inevitable, that certain of the important components of the Tribunal's valuations would be different. They were different including the risk and period of delay connected with future industrial development on Lot 22. Yet the CA took it upon itself to hold as a matter of

strictly imposed law that, irrespective of the different assumptions and irrespective of the expert evidence, the risk and deferment factors applicable to industrial development had to be numerically and precisely the same for both values. The CA did not say what these factors were to be in numerical terms. All it said was that the factors had to be exactly the same for both valuations. The identical factors were then to be fed into a formula which the Court said had to be applied uniformly to the two valuations.

A1/5/220-223, §§82-91

A1/5/220, §80

34. The formula was P = [(H – L) x R] + L. This may seem more akin to physics than law or valuation but there is of course no legal rule that such an algebraic formula cannot be used where appropriate. The difficulty of the law as stated by the CA is that in the radically different assumed circumstances of the before and after valuations the two vital components of the formula, H (the deferred industrial value) and R (the risk associated with future industrial development), had to have exactly the same numerical values irrespective of whether they would in fact have been the same or the evidence was that they would have been different. We submit that this imposed rule is incorrect in law for four reasons.

A1/5/220, §82

A1/5/220, §80

(i) The first reason

35. The first reason is that the imposed rule of law defies common sense.

(a) Industrial development depended on the building and opening to traffic of the new link road. This in turn depended on a reclamation taking place since a new road would have to be built to serve the development (for a container port or anything else) on the reclaimed land. Nobody had ever suggested that there was any prospect of a new road being built otherwise than in order to serve development on the reclaimed land, or possibly to facilitate the reclamation work itself. It is a matter of common sense that any risk that the road would not be built would become less if the FSRO process and the extinguishment of marine rights, necessary preliminaries to the building of the road, had been completed at the valuation date.

(b) In the after value situation any marine rights were extinguished at the valuation date under the FSRO. In the before value situation the only way in which a reclamation and new road could take place was by a new FSRO legal process. Even if the new process had been put in hand at the valuation date (a bold and optimistic assumption for any purchaser to make) the history of the actual process from the first drawing up of proposals as needed to initiate the FSRO process to final extinguishment of marine rights took about two years. It is therefore simply a matter of common sense that in the before value situation a buyer of Lot 22 would have expected a longer period of deferment before industrial development could start than he would in the after value situation. The Tribunal applied common sense and determined

A1/1/147, §471
A1/1/148, §474

a shorter period of deferment (six years and not eight years) for the after valuation. We submit that the rule of law imposed by the CA on the deferment period also defies common sense.

A1/5/220, §80

(ii) The second reason

36. The second reason is that we submit that it is not for an appellate court to impose as a rule of law a particular valuation process on a tribunal of first instance. This is particularly so where the jurisdiction of an appellate court is statutory and is confined, as in this case, to appeals on questions of law. Even when there is an appeal not confined to questions of law it has been held by the Court of Appeal of the Cayman Islands in a compensation case that an appellate court will confine itself to matters of law and principle and not engage in the detailed valuation process: see *National Roads Authority v. Bodden* 2013 (1) CILR 389. This is what we have described in paragraph 23 as the sixth valuation principle.

37. The Tribunal used for the before value assessment a formula akin to that favoured by the CA. It did not use such a formula for the after value assessment. It is, we suggest, for an expert tribunal of first instance to decide whether and when it finds it useful to apply a formula in arriving at a value of land. It is, we suggest, not for an appellate court to apply its own formula to every aspect of the valuation unless there is some reason of law requiring that that should be done (none was put forward in this case). We suggest also that, as we have said, it is particularly inappropriate

A1/1/122-124, §§385-392

for an appellate court dealing with matters of law not only to impose a particular formula but where there have to be two contrasting valuations to direct that the main components of the formula must be numerically the same for both valuations. In the present case the FSRO prescribes that there shall simply be compensation for injurious affection and does not prescribe any formula for determining it. This Court did determine a valuation framework which is set out in paragraph 47 of the judgment of Lord Hoffmann and its two contrasting sub-paragraphs. We submit that it is not thereafter satisfactory that any court should insert a further judge-made assumption into that framework when it is complete and self-contained in itself.

38. The question which is the subject of this appeal was in effect considered by the House of Lords in England in *Transport for London Ltd v. Spirerose* [2009] 1 WLR 1797. That decision concerned compensation payable as the market value of old industrial premises in London which had been compulsorily acquired and the issue was the expectation of obtaining planning permission for a new mixed office and residential development on which the value of the land largely depended. Sections 14-18 of the Land Compensation Act 1961 contained a framework or formula specifying what assumptions as to planning permission were to be made. The English Court of Appeal held, for reasons which nobody has understood, that an assumption of the certainty of a planning permission had to be made as a matter of law where there was a 50% or greater expectation of that permission being granted even though no such assumption was mentioned in the

statute. This was the insertion of a Judge-made assumption into the statutory formula and was rejected by the House of Lords. As Lord Neuberger put it at paragraph 50: "To put the point another way, the courts below appear to have inserted a Judge-made assumption into a statutory formula, which seems to be complete and self-contained". There is an obvious and considerable similarity between the issue in *Spirerose* and the question in this appeal. In *Spirerose* the English Court of Appeal took a 50% or greater probability as found on the evidence and converted it, as a matter of law and irrespective of the self-contained statutory formula, into a 100% certainty. In the present appeal the CA took what was found on the evidence to be a 50% probability and converted it, as a matter of law and irrespective of the self-contained formula stated by this Court, into a 100% certainty. We submit that both processes disclose the same error and were wrong in law.

A1/5/220, §80

39. The imposition of this CA-made formula, and the imposition of identity of components within it when applied to the two valuations, mean that the Tribunal was required as a matter of law to disregard expert evidence on what would have been the expectation in the market at the valuation date of the period before which a new road was opened. If the Tribunal is not permitted to make its own assessment of this matter, and any differences between the two contrasting valuations, it is not easy to see what exactly is the function of the Tribunal.

(iii) The third reason

40. If a Court is to impose a new and absolute rule of law which will to a considerable extent determine the valuation process one would expect that solid reasons would be given for the imposition of that rule. The rule would normally be justified by reasons of justice or the language of the underlying statute or general principles of valuation law such as we have set out above. In the present case no such reasoning was advanced by the CA. In this case the basic direction which dictates the form of the two valuations is the declaration in paragraph 47 of the CFA decision. There is nothing in that decision which suggests that two of the most important components in the two valuations, risk and deferment of industrial value, must as a matter of law be the same for the two valuations. Indeed Lord Hoffmann said the opposite. He pointed out in paragraph 45 that the before value was dependent on a sea access whereas the prospect of a new use dependent on a road access might have heavily influenced the price the land would have fetched in the after valuation. Put in its simplest terms if this Court had wanted to say that in law the risk or deferment attached to a future industrial use had to be exactly the same for the two contrasted valuations it would surely have expressly said so and not left such a crucial factor in the air to be somehow inferred.

41. Doing the best we can with paragraphs 86-90 of the CA decision it appears that that Court attributed the supposed legal error of the Tribunal in finding different risk and deferment factors for the A1/5/222-223

two values to an assumption supposedly made by it that for the purposes of the after value, but not the before value, the physical reclamation was completed by the valuation date. This reasoning of the CA is plainly incorrect for two reasons.

(a) The CA seems to have believed that the different risk/uncertainty factors for the two valuations "were all attributable to the legal assumption on reclamation" (see paragraph 88), i.e. that in the after value the Tribunal assumed that the reclamation had been physically completed by the valuation date. This is in fact the exact opposite of what the Tribunal found and reasoned. The Tribunal said in paragraphs 416 and 417 of its decision:- A1/5/222 A1/1/132

> *"416. From the summary above, it is crystal clear that it was never the findings by the CFA that the Tribunal has to assume that the reclamation has* [been] *already completed at the date of authorisation, i.e. the date of valuation. Rather, it is only to assume that the marine access had been extinguished in fact and in law even before the reclamation had taken place.*
>
> *417. Furthermore, we agree with the Applicant's contention and found that the assumption in the After Situation that the reclamation had been completed at the valuation date is not allowed under the CFA Judgment".*

What we do not understand is how the CA could have based its reasoning and the alleged error of the Tribunal on the belief that the Tribunal found that in the after situation it had to assume that the reclamation had been physically completed at A1/1/132, §§416-417

the valuation date when, in the passages just cited, the Tribunal said in the simplest and clearest terms the precise opposite. With due respect to the CA this is profoundly unsatisfactory as an explanation for its reasoning. If the CA had been in any doubt it only had to read on to paragraph 418 of the Tribunal's decision where the Tribunal said; "Any assumption about the reclamation being completed is an artificial assumption which is specifically disallowed in the words of Lord Hoffmann". We have just never understood how the CA could have believed that the Tribunal had made an assumption as to the reclamation being physically completed at the valuation date when, in the above sentence, it said in the plainest and most explicit terms that it had not done so because such an assumption was disallowed in the words of Lord Hoffmann.

A1/1/132-133

(b) The actual reason given by the Tribunal for the different factors in the industrial values in the two valuations was also set out clearly by it. It was the fact that in the before valuation the marine rights continued to subsist at the valuation date whereas in the after situation they had been extinguished at that date by the completion of the legal and administrative process under the FSRO. In its explanation of its after valuation the Tribunal said as follows in paragraph 472:-

A1/1/14-15, §22

A1/1/147

> *"In the After Situation, although the resumption notice has been announced and the road scheme has been stipulated in the OZP, there is still uncertainty that the entire scheme will be delayed. How long the delay would be was still an outstanding question. However,*

> *relative to the situation in the Before Value, the uncertainty should definitely be lower in view of the fact that the marine access had been extinguished."*

We fail to understand how the Tribunal could have explained with greater clarity its reasons for the difference between the risk and deferment factors in the two valuations, namely that in the before valuation the marine rights still subsisted at the valuation date and in the after situation they had ceased to exist by extinguishment under the FSRO. The CA chose to ignore this as the reason although this was the reason which the Tribunal had given and although the reason attributed by the CA to the Tribunal was the direct opposite of what the Tribunal had actually said.

42. Perhaps the most important issue on the question under appeal is what reason or justification the CA could have had for dictating the inflexible rule of valuation as a purported rule of law which it did dictate. For reasons explained in the last two paragraphs we submit (a) that there is nothing in the declaration or in any other part of the judgment of the CFA which justified the inflexible rule, (b) that there is no general principle of the law and practice of valuation which justified such a rule (indeed as we have explained the imposed rule is contrary to a number of basic principles), and (c) that the only supposed justification for its rule enunciated by the CA was founded on a radical misunderstanding by that Court of what the Tribunal had itself reasoned and explained in the clearest terms.

A1/5/220, §80

(iv) The fourth reason

43. The fourth reason is that the rigid new rule of the CA, if it is correct, is likely to have unsatisfactory and unjust general consequences. An initial effect of the loss of marine rights appurtenant to land is likely by itself to be a loss of value to that land. However, reclamations are nearly always the harbinger of some substantial development scheme. That scheme may decrease the value of the land with the extinguished rights (e.g. a new road on the reclaimed land causing noise and pollution) or may increase the value of that land (e.g. the prospect of new transport facilities or new amenities). Taking the first case, if the law says that the prospect and timing of the new road must be the same in the before and after valuations it is difficult to see how the real loss caused by the reclamation scheme to the land affected can ever be truly compensated. The reality of the difference between the before and after values is largely removed, or at least is elided, by the rigid rule that the prospect and timing of the new road are the same in the before and after situations. In the same way an increase in value caused by the reclamation is largely removed by the rigid rule since, if the prospect and timing of the expected development have to be the same for both values, the resultant benefit to the landowner from the scheme is largely ignored and the compensation is therefore unjustly increased. Both possible situations lead to injustice and an unsatisfactory outcome. The CA seems to have introduced its new rule haphazardly and without any consideration of generally unjust potential results. However, if the reality of the prospect

A1/5/220, §80

A1/5/220, §80

and timing of the reclamation scheme and subsequent development consequent upon that scheme are fed into the before and after valuations without any unreal but legally enforced equality of prospect and timing then these potential injustices to landowners and the public are avoided. We do ask this Court to sit back and take a longer view of these problems.

44. The matter does not end there. Compensation for injurious affection to land can arise in many circumstances where land is deprived of valuable rights such as access to the sea or access to a highway or is damaged in some other way in the interests of the public. In many cases consideration has to be given, as in the present case, both to the adverse impact of the loss of the rights removed and to the other effects of the public project which justifies the removal of rights on the value of the land affected. These other effects may be further damage to the value of the land or may by themselves increase the value of the land. The effect of what is said by the CA seems to be that the impact of the public project and its consequences must apply to the valuation impact both before and after the removal of the rights in question and that the prospect of that project and its consequences occurring and the delay involved must always be the same in the before and after situations, i.e. whether or not the private rights the removal of which give rise to the claim for compensation are taken away. We submit that this is an artificially imposed legal straitjacket which will be inimical to the proper assessment of compensation in many cases. There seems no logical reason why the rule imposed by the CA, if it applies to injurious affection

A1/5/220, §80

caused by the removal of marine rights under the FSRO, should not apply to compensation for injurious affection caused by the removal of any other rights under any other legislation which can cause injurious affection to land.

Deferment and risk

45. A final word is necessary on the different assessments made by the Tribunal on risk and deferment for the before and after values. The position is as follows.

Tribunal's decision on deferment and risk

	Deferment	**Risk**	
Before value	8 yrs (466) [(a)]	50% (407)	A1/1/145-146 A1/1/129
After value	6 yrs (474)	Nil (118, 464)	A1/1/148
			A1/1/47, 145

Note

[(a)] The figures in brackets are the most relevant paragraph numbers in the Tribunal's decision explaining the numerical assessments.

46. The two year difference in the deferment factor was attributable to the difference that in the after valuation the FSRO extinguishment of marine rights had already been completed by the valuation date whereas in the before valuation it had not even started resulting in a further delay in realising this value of at

least two years. On this the Tribunal accepted in part the expert evidence of the Director but reduced the difference of four years stated in that evidence to one of two years.

A1/1/145-148, §§465-467, 472-474

47. In determining the risk factor, and particularly the risk factor for the after value, the Tribunal used the same reasoning and justification, namely that for the after value assessment marine access is assumed to have been extinguished on the valuation date. Thus, given the extinguishment of marine rights and the expectation at the valuation date that the container terminal scheme would proceed as planned, the latter found by the Tribunal as a fact to exist, the Tribunal considered that for the after value the only uncertainty would be the delay in carrying out the scheme and thus a delay in the opening of the new road. While this is a matter of fact or a valuation judgment for the Tribunal on the evidence it was a conclusion which was in effect required by the decision of the CFA in paragraph 41 of the decision.

A1/1/140-141, §§445, 446
A1/1/143, §456
A1/1/145, §463
A1/1/147, §472
A1/1/145, §464

> *"In my opinion this* [the language and scheme of the FSRO] *can only mean that for the purposes of assessing the compensation, it must be assumed that on the date of authorisation it was certain that the reclamation would take place."*

Therefore in addition to it being an ordinary conclusion on the facts and the evidence the decision of the Tribunal on a nil risk of the reclamation not taking place in the after value accords exactly with what this Court directed. If in the after valuation there was an expectation amounting to a certainty that the physical

A1/1/47, §118A/1/145, §464

reclamation would take place then there as an equal expectation amounting to a certainty that a new road would be built to serve the use of the reclaimed land. There was therefore no risk for the after value of there not being a new road and therefore no risk of the industrial development not being possible. That is what this Court said. The CA simply ignored this direction and this aspect of the judgment of this Court.

Conclusion

48. The issue before the Court is whether the CA was correct and justified in ordering the Tribunal to carry out the before and after valuations in strict accordance with an algebraic formula with the two decisive components of the formula having as a matter of law to be precisely the same in both valuations despite the important differences in factual assumptions between the two values as directed by this Court. We submit that in issuing this direction to the Tribunal the CA erred in law for the following four reasons. (a) As a matter of common sense the different factual assumptions would almost inevitably lead to differences in the two components. (b) In the absence of an error of law or a manifestly unsupportable decision it was not for an appellate court, whose jurisdiction was confined to correcting errors of law, to alter the valuation judgment of a specialist tribunal of first instance reached on the evidence. The only reason given by the CA for its decision was a misrepresentation of the actual reasoning of the Tribunal which was clearly and explicitly explained by that Tribunal. (c) There was nothing in the

judgment of this Court or in any general principle of valuation law which constituted a reason for the rule of law erected by the CA. Indeed in ordaining that the risk factor must be the same in both valuations the CA appears to have ignored a specific part of the judgment of this Court and a specific direction made by this Court. The conclusion of the CA on the question under appeal also flouts a number of basic principles of the law of valuation which we have explained. (d) The application of the CA's new rule of law can lead to potential injustice to either party in cases under the FSRO and more generally in cases of compensation for injurious affection under any legislation.

Dated the 6th day of June 2017.

Michael Barnes QC

Valentine Yim
Counsel for the Appellant

FACV Nos. 1, 2, 3, 4, 5, 6, 7, 8 & 9 of 2017

IN THE COURT OF FINAL APPEAL OF THE HONG KONG SPECIAL ADMINISTRATIVE REGION
FINAL APPEAL NOS. 1, 2, 3, 4, 5, 6, 7, 8 & 9 OF 2017 (CIVIL)
(ON APPEAL FROM CACV NOS. 13, 14, 15, 16, 115, 116, 119 & 120 of 2015)

BETWEEN

PENNY'S BAY INVESTMENT COMPANY LMITED Applicant
(Appellant in FACV 1/2017)

and

DIRECTOR OF LANDS Respondent
(Appellant in FACV 2-9/2017)

APPELLANT'S CASE
of
DIRECTOR OF LANDS
(APPELLANT IN FACV 2-9 / 2017)

Filed on the 6th day of June 2017

Department of Justice
6th Floor, Main Wing and East Wing,
Justice Place, 18 Lower Albert Road,
Central, Hong Kong
Tel No.: 3918 4323
Fax No.: 3918 4525
(File Ref.: FACV 1-9/17)