

Joint Industry Guidance on Determining Compensation at Way-Go

published jointly by the
**National Farmers Union of Scotland
Scottish Land and Estates
Scottish Tenant Farmers Association**

in association with
The Scottish Government's Independent Adviser on Tenant Farming

Final Version 21st June 2016

NB: Every care has been taken to ensure that this guidance accurately reflects the provisions of current legislation. It is essential, however, that users obtain independent legal advice relevant to their particular circumstances before deciding to implement any part of the procedures outlined. Please note that the new relinquishment and assignation for value provisions contained within the Land Reform (Scotland) Act 2016, which are not yet in force, will in future offer an additional option for those seeking to end their tenancy.

Introduction

Uncertainty over compensation due at way-go is frequently cited as a major disincentive to investment in tenant's improvements on a holding, and as the reason why some tenants remain on their farms long after the normal age of retirement commonly found among owner occupiers. Many tenants have no clear idea of the way-go value of their business, and therefore no ability to engage meaningfully in discussions where an understanding of this may be important (estate and tax planning for example).

In some instances the main cause of this is the lack of an agreed and up to date record of tenant's improvements, and/or the lack of an up to date record of condition (to clarify any dilapidations). In many, however, the reasons have more to do with an incorrect belief that an accurate valuation of way-go compensation can only be obtained after an irrevocable notice of intention to quit has been given by the tenant. A lack of clarity around additional compensation for voluntarily yielding vacant possession is also sometimes given as a cause of uncertainty.

The Agricultural Holdings Legislation Review Group (AHLRG) considered these issues in 2014, noting that it held the view that the tenant has a property right in the tenancy but not in the land. Although it concluded that no direct legislative change was required, it recommended that a Code of Practice be brought in by a new Tenant Farming Commissioner so that uncertainty relating to way-go compensation could be minimised. In the light of this the three industry bodies have decided to bring into effect joint industry guidance on a voluntary basis, and to keep this under review.

The industry bodies believe that this guidance may provide a helpful model for an incoming Tenant Farming Commissioner, but they also recognise that provisions in the Land Reform (Scotland) Act 2016 will create potential alternatives to way-go whereby the tenant may be able to realise the value in his tenancy. The guidance will be updated once it is known when the provisions in the Act will come into effect.

Core Principles

The guidance is underpinned by six core principles that broadly reflect current legislation –

1. The landlord may at any time require the making or updating of a record of condition at shared expense, and the tenant should assist with this.
2. The tenant may at any time require the making or updating of a record of condition and/or of tenant's improvements at shared expense, and the landlord should assist with this.
3. The landlord may at any time indicate to the tenant that he is interested in obtaining vacant possession subject to agreeing satisfactory way-go compensation, and the tenant should cooperate in exploring whether terms might be agreed for such an arrangement.
4. The tenant may at any time indicate to the landlord that he is interested in quitting subject to agreeing satisfactory way-go compensation, and the landlord should cooperate in exploring whether terms might be agreed for such an arrangement.
5. The landlord may under certain circumstances issue the tenant with a notice to quit, in which case both parties should collaborate in determining the amount of way-go compensation to be paid.

6. The tenant may at any time issue the landlord with a notice of intention to quit, in which case both parties should collaborate in determining the amount of way-go compensation to be paid.

Basis of the Guidance

The guidance is built on an assumption of reason and reasonableness among all involved. It builds on existing legislative provisions and applies to 1991 Act tenancies.

The industry bodies believe it **essential** that, before deciding to implement the guidance, landlords and tenants should obtain their own independent professional advice relevant to their particular circumstances.

Tenants should note that provisions in the Land Reform (Scotland) Act 2016 may offer alternative ways of realising the value in a secure 1991 Act tenancy once those provisions come into effect, and it is strongly recommended that independent professional advice is sought before agreeing any way-go valuation in order to fully assess the different options that may be available.

The Process in Practice

The recommended process involves alternatives according to circumstances. Sometimes a landlord or tenant will want to explore the possibility of the tenant quitting in return for an agreed amount of compensation, while in others there may be no option about quitting – for example where a landlord has served a notice to quit under part III of the 1991 Act or a tenant has died and his executors have served a notice of intention to quit because there are no eligible successors.

Note that normally a tenant who is considering quitting should only serve a notice of intention to quit after a satisfactory provisional valuation for way-go compensation has been agreed under step 3a below. This should include consideration of the alternative options that may be available to the tenant once the Land Reform (Scotland) Act 2016 comes into force.

Note also that where the tenant only requires an approximate valuation (for example for estate planning purposes), it will usually be possible for a professional valuer to undertake this without reference to the landlord so long as the tenant has a copy of the original statement of condition.

Step 1 – Initiating a Valuation

Either the landlord or the tenant may initiate a valuation, depending on which party is considering triggering a formal way-go process. The initiating party should first contact the other informally to discuss the matter in as much detail as possible. In particular the two parties should thoroughly explore their expectations with respect to any voluntary compensation payment over and above that required by statute. The outcome of step 1 will either be agreement to proceed to step 2 or a decision to take the matter no further.

Step 2 - Creating a Reliable Basis for Valuation

Unless the record of tenant's improvements is up to date it may be difficult to undertake a robust valuation of compensation due for improvements. At the very least the tenant must be able to show that the correct statutory consent or notice procedure was followed for each improvement for which compensation is sought.

The original record of condition provides the basis for assessing payments that may be due by the tenant for any dilapidations. This should be compared against current condition, through an updated record of condition or otherwise, so that any dilapidations can be identified and payments agreed.

Unless this information is already available the parties should agree to update relevant records, with the cost being shared in whatever proportions the two parties agree is appropriate. In default of agreement the cost should be shared equally. The outcome of step 2 will be agreed records sufficient to enable the parties to proceed to either step 3a (if quitting is optional) or 3b (if quitting is inevitable).

Step 3a – Obtaining a Provisional Valuation

Where the two parties are willing to consider an agreement to quit subject to confirming mutually satisfactory way-go compensation, they should obtain a provisional valuation on which to base further discussions. The valuation will comprise an element that is the net value of tenant's improvements less any dilapidations, and can also include (but not always) an additional element that is viewed as compensation for yielding vacant possession.

The former element will normally be calculated by assessing the value of any tenant's improvements to a hypothetical incoming tenant, and then subtracting from that any costs that may be necessary in order to rectify dilapidations that may have occurred as a result of a failure by the tenant to fulfil all of his repairing and maintenance obligations. The latter element can be calculated by reference to section 55 of the 2003 Act, it may be agreed "in kind" (for example in the form of retirement housing), or it may be agreed through any other settlement that the two parties consider to be reasonable.

A period of negotiation may be required between the parties for a provisional valuation to be agreed. If agreement cannot be reached then the two parties should consider the use of mediation to resolve the matter, but ultimately an irresolvable inability to reach agreement will normally mean that the matter cannot be taken any further.

The outcome of step 3a will usually be a decision to enter into an agreement to quit or renounce the tenancy, failing which the tenancy will continue. Tenants should note, however, that provisions in the Land Reform (Scotland) Act 2016 will in due course offer them alternative ways of realising their value in the tenancy, for example through assignation or conversion to an LDT.

Step 3b – Obtaining a Firm Valuation

Where the landlord has already issued a notice to quit or the tenant has already issued a notice of intention to quit, the two parties should agree a firm valuation in accordance with the law as to the way-go compensation that will be payable. A period of negotiation may be required for an agreed valuation to be reached. If agreement cannot be reached the two parties should consider the use of mediation and/or arbitration to resolve the matter, but either party may refer the dispute to be settled by the Land Court if they wish.

Where quitting is inevitable this formal valuation step will take into consideration any discussions which have taken place regarding the voluntary payment of additional compensation for the relinquishment of the tenancy.

The outcome of step 3b will usually be either an agreed or an imposed valuation, and the tenant quitting on those terms.

Maintaining a Record of Process

The industry bodies are aware that under the terms of the Land Reform (Scotland) Act 2016 there will in due course be established a position of Tenant Farming Commissioner with a remit to prepare codes of practice, including a code relating to the determining compensation at way-go. The industry bodies see their new guidance as potentially providing a basis for such a code, and they are anxious that it operates in an equivalent manner.

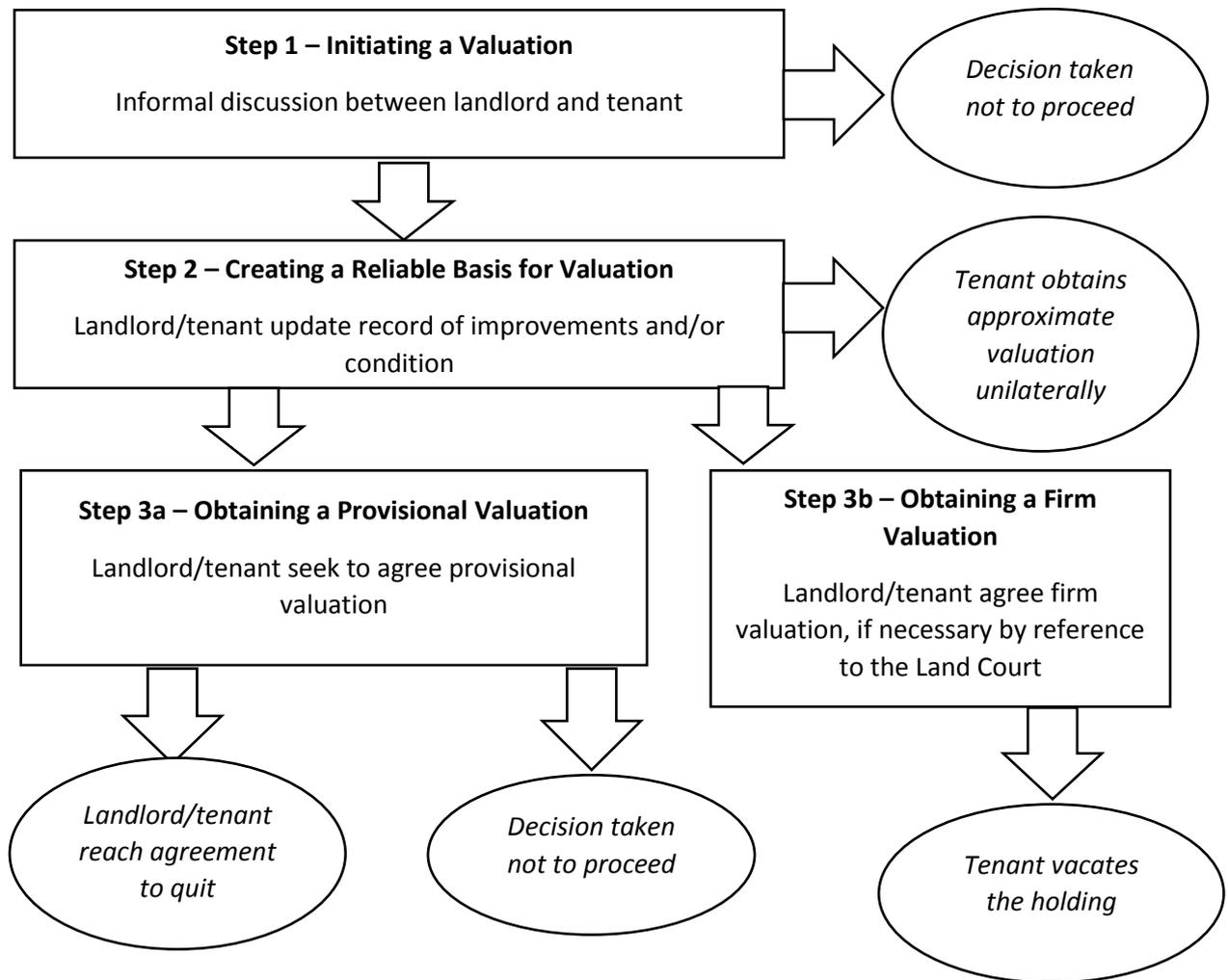
All landlords, tenants and professional intermediaries are therefore asked, while following this guidance, to maintain a concise written record of key dates and associated notes for stages 1 – 3 and to be willing on request and in confidence to make this record available to the Scottish Government's Independent Adviser on Tenant Farming so that he is in a position to undertake a risk based compliance audit should the industry bodies collectively ask him to do so. A pro-forma Record of Procedure is given in appendix B.

In Summary

The guidance sets out a simple process whereby a valuation for the way-go compensation payable in different circumstances can be determined. It recognises that while some tenants will simply require a reasonably reliable estimate for planning purposes, others will want an accurate figure on which to base a decision as to whether or not they wish to quit the holding. In some cases the tenant may have no choice over whether or not to quit, and the valuation process applicable in such circumstances is also outlined. The guidance is based on current legislative provisions.

Statutory arrangements for way-go continue to apply. Landlords' and tenants' statutory rights are unaffected, and the **essential** importance of both parties obtaining independent legal advice is emphasised. The guidance seeks simply to provide an effective framework whereby uncertainty with regard to the value of potential way-go compensation can be minimised.

Appendix A – Flow Chart Showing Procedure for Determining Way-Go Compensation



Appendix B – Pro-Forma Record of Procedure

Step 1 – Initiating a Valuation

- Date of informal discussions?
- Decision to proceed to step 2?

Step 2 - Creating a Firm Basis for Valuation

- Date of request/agreement to update record of condition and/or improvements?
- Copy of updated record(s) on file?
- Decision to proceed to step 3a/b? Reasons?

Step 3a – Obtaining a Provisional Valuation

- Date net valuation of tenant's improvements less dilapidations agreed?
- Date any additional compensation for vacant possession agreed?
- Copy of valuations attached or on file?
- Decision taken to quit?

Step 3b – Obtaining a Firm Valuation

- Date net valuation of tenant's improvements less dilapidations agreed?
- Date any additional voluntary compensation agreed (if appropriate)?
- Copy of valuations attached or on file?