

DEPARTMENT FOR COMMUNITIES AND LOCAL GOVERNMENT

TACKLING UNFAIR PRACTICES IN THE LEASEHOLD MARKET

RESPONSE OF ANTHONY COLLINS SOLICITORS LLP (“ACS”)

INTRODUCTION AND BACKGROUND TO THE ACS RESPONSE

ACS is one of the leading law firms in the country delivering services to the social housing sector. We contribute nationally to the regeneration, governance and management of social housing, offering a full range of services to over 200 private registered providers (“PRPs”),

ALMOs and local authorities (“LAs”). The feedback in this response is based on strategic discussions with our clients and sector contacts.

Our initial starting point is that the mischief is not so much in the fact that properties are leasehold per se, but in excessive ground rent increases, fees for consents and the price of exercising the right to buy the freehold. The focus should therefore be less on the nature of the tenure and more on the control of unfair terms. If these aspects were addressed, then the market would self-correct, as that would significantly reduce the point of leasehold sales.

Alternatively, there is a question as to whether the impact of these terms is being valued properly on the initial purchase of the lease, compared with a freehold valuation of the same property; if not, whether valuation principles should be reviewed to reflect this. Also, does the basis of valuation on enfranchisement need to be reviewed?

In this response we use as shorthand “good” leasehold houses (where ground rents are necessary for covenant compliance) to “bad” leasehold houses (where the ground rents are generated for investment returns).

LIMITING THE SALE OF NEW BUILD LEASEHOLD HOUSES

Q5: What steps should the Government take to limit the sale of new build leasehold houses?

We think it will be challenging to define what are “good” leasehold houses and “bad” leasehold houses; we suggest the overriding principle is to ensure that the value of the freehold of new leasehold houses is so restricted that in practice, selling “bad” leasehold houses is uneconomic; providing that provision is retained for innovative affordable leasehold housing schemes where the value of the freehold is separated from the building *and that reduction passed onto the leaseholder*.

We think the most straightforward way to do this is to amend the Leasehold Reform Act 1967 so the valuation formula of the enfranchisement after such amendment (for all new leases) would be EITHER:

- a. to apply section 9(1) of that Act (i.e. to restrict the valuation to the site so there is no marriage value) b) have assumptions that would be applied in all cases that: -



- i. the annual ground rent is £10 per annum in place of the actual ground rent
 - ii. the yield rate is set at 6% and the reversion rate at 5% (the current accepted norms); OR
- b. the initial lease sets out its own enfranchisement formula that is ascertainable at the time of the grant.

These proposals would give certainty to parties.

We acknowledge this means in the case of A) that if a leaseholder wished to purchase the freehold of their house within the first two years (when the Act doesn't apply) they would have to accept what the freeholder offered; clearly the Act could be further amended so that for new leases the qualification period would be, say, two months (or even no qualification period).

Q6: What reasons are there that houses should be sold as leasehold other than under the exceptions set out in paragraph 3.2?

Where the value of the freehold is separated from the building and that reduction passed on to the leaseholder – we consider the best way to make that explicit is when the enfranchisement methodology is set out in the lease.

Q7: Are any of the exceptions listed in 3.2 not justified? Please explain. These should all stand.

These should all stand.

Q8: Would limiting the sale of new build leasehold houses affect the supply of new build homes? Please explain.

With the exception of models which separate out the value of the freehold, we do not see how supply can be affected.

Q9: Should the Government move towards removing support for the sale of new build leasehold houses through Help to Buy Equity Loan, unless leasehold can be justified and where ground rents are reasonable (which could be a nominal or peppercorn ground rent), and if not, why not?

Yes unless there is the valuation separation which would directly support the purpose of HTB.

Q10: In what circumstances do you consider that leasehold houses supported by Help to Buy Equity Loan could be justified?

Our suggestions above should be supported by HTB.

Q11: Is there anything further the Government could do through Help to Buy Equity Loan to discourage the sale of leasehold houses?

The Government could limit funding to leasehold houses where the rationale is covenant compliance and the ground rent nominal or where the value of the freehold is separated – in the case of HTB there could be a further restriction that sellers could only be either PRPs/local authorities or any landlord where such landlords had a stake of at least 50 per cent.

HTB should also impose a condition that there must be no charge for any consent (such as for alternations approval) only the reimbursement of reasonable costs.



Q12: What measures, if any, should be considered to minimise the impact on the pipeline of existing developments?

We consider the Government should provide maximum publicity to the difficulties to persuade developers to sell units on a different basis. Legislation could, following a clear announcement, be backdated to the date of that announcement.

Limiting the reservation and increase of ground rents on all new residential leases over 21 years

Q13: What information can you provide on the prevalence of onerous ground rents? We are keen to receive information on the number and type of onerous ground rents (i.e. doubling, or other methods) and whether new leases are still being sold with such terms.

We are unable to contribute.

Q14: What would a reasonable ground rent look like, in terms of i) the initial annual ground rent, ii) the maximum rate of increase in annual ground rent, and iii) how often the rate of increase could be applied to an annual ground rent? Please explain your reasons.

- a. Restricting new ground rents to a nominal sum (£10 per annum) would “work” for “good” leases but again would destroy the value of “bad” leases. We don’t see how there could be a “reasonable” ground rent since that implies an element of investment return which would permit “bad” leases; the issue is one of principle. The only exception to this is where the ground rent truly reflects the value of the freehold AND the purchase price paid by the leaseholder deducts that value.
- b. We do not consider there is any benefit of permitting increases (save in the case of the exception referred to in (a)) – no doubt this issue was considered when the right to buy legislation was drafted and the decision then was to have a “fixed” £10 per annum.

Q15: Should exemptions apply to Right to Buy, shared ownership or other leases? If so, please explain.

Yes exemptions should continue to apply. There are few RTB leases of houses and in any event these are restricted to £10 pa fixed ground rent. Shared ownership leases must be excluded to retain the value of the freehold. There must be a further exclusion to protect innovative models as referred to above where the leaseholder is purchasing just the building and the land value is retained (or alternatively the lease must have a transparent enfranchisement formula).

Q16: Would restrictions on ground rent levels affect the supply of new build homes? Please explain.

We cannot see why ground rent levels would affect supply since high ground rents are a relatively new phenomenon.

Q17: How could the Government support existing leaseholders with onerous ground rents?

We consider maximum publicity should be given to leaseholders so they are aware of their right to enfranchise under the 1967 Act.



Research needs to be undertaken to ascertain whether generally valuers acting for purchasers and lenders properly took into account ground rent and increases in the initial valuation. We believe it is likely that few valuers took into account such factors and therefore such valuers were negligent. Lenders (who would always employ a valuer) might well have an action in negligence against such valuers – and leaseholders as a minimum would have a defence to any possession proceedings and a claim against any valuer who had given such an opinion.

Invite the Competition and Markets Authority (CMA) to consider issuing guidance on what ground rents and onerous consent terms would amount to unfair terms (and therefore void).

Q18: In addition to legislation what voluntary routes might exist for tackling ground rents in new leases?

We consider maximum publicity should be given to leaseholders so they are aware of their right to enfranchise under the 1967 Act. Invite the Competition and Markets Authority (CMA) to consider issuing guidance on what ground rents would amount to unfair terms (and therefore void).

5. EXEMPTING LEASEHOLDERS POTENTIALLY SUBJECT TO 'GROUND 8' POSSESSION ORDERS

Q19: Should the Government amend the Housing Act 1988 (as amended by the Housing Act 1996) to ensure a leaseholder paying annual ground rent over £1,000 in London or over £250 in the rest of England is not classed as an assured tenant, and therefore cannot be issued with a Ground 8 mandatory possession order for ground rent arrears? If not, why not?

The following should be excepted: -

Where the value of the freehold is retained and the leaseholder only purchases the building. An exception is needed to protect innovative models as referred to above where the leaseholder is purchasing just the building and the land value is retained (or alternatively the lease must have a transparent enfranchisement formula).

Shared ownership leases because:-

- There is detailed joint guidance agreed between the Council of Mortgage Lenders (CML), National Housing Federation (NHF), Homes and Communities Agency (HCA) and the Building Societies Association (BSA): <https://www.cml.org.uk/policy/guidance/all/guidance-for-handling-arrears-and-possession-sales-of-shared/>
- That joint guidance sets out protections for all parties.
- Shared Ownership leaseholders, by their nature, are more likely to go into rent arrears and those arrears (given they relate to the “retained” equity share) can quickly become significant; the current forfeiture provisions are too slow and too costly to be borne by PRP, who are not for profit (mainly charitable) organisations where any additional cost is effectively borne by their beneficiaries.



6. SERVICE CHARGES FOR MAINTAINING COMMUNAL AREAS AND FACILITIES ON FREEHOLD AND MIXED TENURE ESTATES

Q20: Should the Government promote solutions to provide freeholders equivalent rights to leaseholders to challenge the reasonableness of service charges for the maintenance of communal areas and facilities on a private estate? If not, what management arrangements on private estates should not apply?

Freeholders who purchase from local authorities and PRPs do have existing rights under section 45 – 51 Housing Act 1985 <https://www.legislation.gov.uk/ukpga/1985/68/section/45>

In our view these rights should be shared with all freehold service charge payers.

The value of such service charges are generally on the low side so we do not consider there is a case for having any challenges brought via the First Tier Tribunal (Property Chamber) but to the courts so that only claims of a material amount are brought OR any claim must be in respect of a service charge over a minimum amount, linked to inflation.

7. FUTURE ISSUES

There is a widespread perception that when selling leasehold flat developers make over optimistic assumptions in the calculation of the initial service charges estimates; this leads purchasers to make incorrect assumptions about their ability to manage their finances.

Shared ownership leaseholders by their very nature are at the margins of affordability. Shared owners they pay 100% of service charges and therefore service charges which increase dramatically would have a significant effect on their finances.

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18th September 2017

