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19th April 2018

Dear Rachel

Law Commission Consultation on Commonhold Law

The City of London Law Society ("CLLS") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

A full list of the CLLS corporate members may be found on the CLLS website at <http://www.citysolicitors.org.uk/attachments/category/81/Corporate%20Membership%202017%2001.pdf>

The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees. This response, prepared by the CLLS Land Law Committee, is in respect of the Law Commission Consultation on Commonhold Law.

The Law Commission asks:

- What are the difficulties in creating or converting to commonhold?
- What issues make commonhold unattractive to homeowners?
- What issues make commonhold unattractive in the wider property sector?

1. What are the difficulties in creating or converting to commonhold?

The problems which have caused disincentives to the creation of commonhold schemes on new developments have been mainly:

- inertia on the part of the housebuilding industry owing to familiarity with leasehold tenure and its use on selling flats and houses; commonhold is a voluntary scheme and so few developers have felt any incentive to undertake a departure from customary residential unit disposal models;
- the benefits of retention of ground rents and ability to sell the investment;
- prospective receipts from tenants enfranchising to freehold tenure;
- the reluctance of lenders to finance commonhold development and offer mortgages to potential buyers;
- the lack of rights of re-entry (forfeiture) for serious breaches of obligation on the part of unit owners that are available in respect of leases;
- the prescriptive and bureaucratic nature of the commonhold model; it is “over-engineered”, lacks simplicity and needs simplification;
- the conversion of existing blocks of flats has proved often to be impossible, due to the inability of, or extreme difficulty in, obtaining the requisite consent of lenders and lessees;
- the commonhold association is subject to company law which, it is understood, is regarded as too complicated for that purpose, particularly as failure to comply with the filing of accounts and other rules can lead to criminal prosecutions; homeowners often have limited or no knowledge of company law.

Those few developers who have promoted commonhold schemes may be able to provide additional examples of disadvantages, whatever the advantages may have been. Some further disadvantages and difficulties have been reported to the Law Commission and are set out in the Call for Evidence. It is assumed that the paucity of schemes (fewer than 20 since the introduction of the legislation in September 2004) begs the question of whether there are other disadvantages which actual experience of using the scheme has revealed.

If the Government’s intent is to prohibit the grant of leases of more than 21 years of flats and houses, then this would be a spur towards the promotion of commonhold schemes; but that in turn might be regarded as an infliction of restraint and lead to a reduction in developers committing to residential business. House builders are concerned to ensure the marketability of the homes that they build and there is a concern that buyers would be put off purchasing homes which are being offered for sale on a common hold basis, as they and their lawyers are not familiar with it. Radical interference with the market has rarely provided a satisfactory answer to problems where more measured responses would suffice.

2. What issues make commonhold unattractive to homeowners?

To a large extent, the response to this question is speculative. Again, the lack of commonhold schemes in respect of multiple occupancy developments leads to little reliable information. The following matters are suggested:

- foremost must be the unwillingness of major lenders to finance purchases of residential units in commonhold schemes of development. The lack of ready access to mortgages is a major disincentive to unit buyers;
- the commonhold scheme mirrors the well-known private schemes of flat-owner sales which have been successfully used in dealing with small blocks of flats often of luxury standard and usually in prestigious residential urban areas. Under these schemes
 - a private company limited by guarantee set up by the developer acquires the property under which a share is allotted to each buyer of a flat;
 - the developer sells the flat by the grant of a long lease at a premium and reserves a ground rent (often a peppercorn) to the buyer;
 - the developer retains control of the company until the last of the flats in the block is sold, at which point control passes to the shareholders (the respective flat-owners); and
 - on transfers of flats, the transferor must also transfer the share in the company to the transferee of the flat.

These schemes have been shown to work reasonably in high quality comparatively small blocks of flats where the flat owners are business orientated, well-placed in the “wealth-scale” and who appoint and supervise capable managing agents; disagreements on repair and maintenance issues nevertheless produce difficulty;

- It is not clear that commonhold schemes produce desirable social models for lower-paid and first-time buyers and flat owners less well-placed in the “wealth scale”. Such evidence as there is suggests that:-
 - long leaseholders in large blocks of flats show a marked reluctance to consent to conversion to commonhold;
 - obtaining the consent of all has been a major stumbling block to attempts on the part of developers to convert to commonhold, which suggests a tendency of leaseholders not to want to be involved in management, reluctance to obtain professional advice and incur the cost of doing so;
 - developers and property owners have been sensitive to the poor reputation of those commonhold schemes that have been set up;
 - without an accountable property manager, default of house and flat-owners in paying costs and disagreements between them causes the standard of maintenance and repair to deteriorate: and
 - difficulties in recovering contributions to maintenance and repair expenses lead to a deterioration of the conditions of the building and common parts.

In large blocks of flats, these problems multiply.

- the lack of simplicity in the commonhold model has, it is thought, generated reluctance on the part of potential buyers;

- lack of understanding of remedies and inconsistent methods of resolution of disputes with those applying to leasehold schemes.

3. What issues make commonhold unattractive in the wider property sector?

In spite of the attractions of positive covenants being enforceable against successors in title to residential property and the freehold tenure of a residential unit not being a wasting asset, commonhold has proved thoroughly unattractive to the property sector and the scheme is regarded as having so far been a resounding failure. The following issues, as reflected in the responses given in paragraphs 1 and 2 above, would seem to be relevant:

- the reluctance of institutional lenders to lend generally on commonhold development schemes and to unit buyers;
- the prescriptive nature of the commonhold model and its lack of simplicity;
- the voluntary nature of the commonhold scheme and the inertia of the industry to move away from tried and tested leasehold models.

While bad practices, which lead to unfairness in relation to tenants of long leases of residential units, should be counteracted, it is feared that absolute prohibition of the use of leases of more than 21 years on the sale of residential units, as advocated by the Government, is far too drastic. Such a measure is quite likely to lead to many developers looking away from residential development at a time when there is a loud political call for much more development of owner-occupied housing. It is suggested that the resort to the commonhold model of residential development would be too far-reaching to ensure that such a streamlined pattern of development immediately ensues. It remains to be seen how the commonhold model can be improved. The Government's statements that the commonhold model would, subject to some adjustment, immediately provide a satisfactory alternative, need some compelling substantiation.

It is not clear that the Government has been looking at any alternative, or perhaps additional, approach. The Law Commission has reported (Law Com 327 – "Making Land Work") on changes that should be made to real property law including:

- the draft of a "Law of Property" Bill, which recommends a number of very important changes to real property law, such as positive covenants that touch and concern land to be enforceable against successors-in-title, and powers to modify and discharge easements; and
- a separate Bill making changes to the ancient law of rights to light which obstruct development.

Neither of these suggested changes has been taken forward by the Government, in spite of some encouragement that they will in due course be adopted.

By bringing forward these measures, alternative schemes of freehold development could be adopted with greater flexibility and simplicity than is now afforded by commonhold schemes.

Yours faithfully

Jackie Newstead
Chair, Land Law Committee

City of London Law Society

A full list of the Land Law Committee members is herewith:-

http://www.citysolicitors.org.uk/index.php?option=com_content&view=category&id=142&Itemid=469