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23<sup>rd</sup> November 2018

Dear Sir/Madam,

## Implementing reforms to the leasehold system

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. This response has been prepared by the Land Law Committee, the details of which are on the CLLS website herewith:-

[http://www.citysolicitors.org.uk/index.php?option=com\\_content&view=category&id=142&Itemid=469](http://www.citysolicitors.org.uk/index.php?option=com_content&view=category&id=142&Itemid=469)

### Response to Implementing reforms to the leasehold system

*Question 1: Do you have views on any further means to implement the ban on unjustified new residential long leases being granted on non-exempt houses?*

The landlord could be penalised for granting an unjustified new residential long lease. A precedent for this could be the approach taken to penalties for landlords granting unlawful leases under the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015. So where the landlord is or has been in breach of the prohibition on letting substandard domestic private rented property, a penalty notice can be served on the landlord. The landlord can appeal against the notice on specified grounds. If no appeal is made or it fails, the landlord has to pay a financial penalty of up to £5,000 for the unlawful lease (this is a civil, not a criminal fine). Where a landlord is in breach of the requirements of a penalty notice, the 2015 Regulations also provide for a publication penalty. Under this, the local authority may publish information about the defaulting landlord such as the landlord's name (but not if an individual); details of the breach; and the amount of the financial penalty imposed. It is worth noting that even though a lease under the Regulations is unlawful, its provisions remain enforceable between the parties to the lease.

The ban should not affect pre-existing contractual rights. So if a contract or agreement has been exchanged to grant a new residential long lease on a non-exempt house prior to the ban coming into force, the ban should not affect the contract or agreement, nor the lease granted pursuant to it. There should be no statutory restriction on the registration of such contract, agreement or lease at HM Land Registry. The landlord should not be penalised for granting a lease pursuant to such a contract or agreement, nor for entering into such a contract or agreement.

*Question 2: Do you have any views on how to provide appropriate redress for the home owners should (a) a long lease be incorrectly granted upon a house or (b) a long lease be granted at a ground rent in excess of the cap, after the legislation has taken effect?*

Great care must be taken in relation to interfering with a contractual bargain freely negotiated between independently and professionally advised landlords and tenants. The Committee notes that the Consultation states the tenant should be able to cancel the lease and have the freehold transferred to them together with any necessary rights and obligations included in the lease. The nature of a transfer document is very different from a lease and precise mechanisms need to be included in the relevant legislation to ensure that the unravelling of the lease and the replacement transfer of the freehold fully protects both the landlord and the tenant and any mortgagees.

If the landlord themselves has only a leasehold interest, then they cannot transfer the freehold to the tenant. The freehold is held by a third party who may not be involved with the transaction between the landlord and the tenant. The Committee notes paragraph 2.40 of the Consultation but considers that no landlord can transfer a freehold if they only have a leasehold interest to give, regardless of when the landlord acquired its leasehold title. So in relation to the suggestion at paragraph 2.42 ii that the ban will apply to any leasehold land acquired from 22 December 2017 onwards and to the suggestions at paragraphs 2.43 and 2.44, how will the transfer of the freehold be effected where the owner of the freehold title is a separate party not involved in the transaction between the seller and buyer of the leasehold land? Or will the legislation force the third party to transfer its freehold?

As an alternative to a transfer of the freehold, the enlargement rights under section 153 of the Law of Property Act 1925 could be extended to enable the tenant home owner to obtain a freehold.

In terms of a ground rent in excess of the cap, the legislation can provide that the ground rent is limited to the permissible statutory level (which the Consultation suggests is £10 a year). So limited, the ground rent should be valid.

*Question 4: With the exception of community-led housing, do you agree that any exemptions provided which allow the continued granting of new long leases on houses should have their ground rents restricted as proposed?*

Yes. However, it is important to bear in mind the implications of capping the ground rent. From conversations with developers, while such restrictions may not have a direct impact on the long-term supply of housing, it would be likely to increase the price of new homes. Ground rent income has been and can be used to fund housing developments and there may also be a negative effect on registered providers and other providers of public sector housing, who rely on ground rent income.

The ground rent cap also needs to take account of the wide divergence in the amount of ground rent that has been charged across the UK. Since there are significant disparities nationally in market values, a threshold for a cap in one part of the country may be too high or too low for other parts. Also ground rent increases are needed to preserve its value in monetary terms even if its initial level is capped at £10. The increase should be neutral to the home owner and the Committee would suggest increases every 10 years linked to the RPI, CPI or other relevant Index.

The question refers to community-led housing as an exception, but the Committee considers that the exception should extend to shared ownership, retirement properties and mixed use leases for the reasons specified in the Consultation.

*Question 11: Are you aware of any other exceptional circumstances why houses cannot be provided on a freehold basis that should be considered for an exemption, in order to protect the public interest or support public policy goals?*

The most obvious circumstance is when the house builder only has a leasehold interest. Where houses are built on developments, with common facilities, such as landscaped areas and private roadways or underground facilities, it is important to have a legal structure that places obligations on the homeowners to contribute to the maintenance of the common areas and ensures that the maintenance is carried out. The existing traditional freehold and leasehold structure achieves this. It is possible to set up a scheme of management, but this requires governmental input and is a slow and cumbersome process. A better solution is to allow leasehold houses to continue to be sold and to set up proper regulation of service charges and ground rents in the relevant leases. A leasehold structure is a much more effective way of ensuring that obligations relating to the provision of services and payment of money are passed on to the successors (this happens automatically in relation to leasehold properties but as a matter of law not in relation to freeholds).

Modern housing estates, particularly in urban areas, are increasingly complicated. Take the example of a development where the estate was set up on a leasehold basis because the vast majority of the homes are apartments. However, in a later phase the developer built some 20 or so houses. They were quite distinctly houses, with their own front door at ground level and no other accommodation above them. However, the houses were built – in part – above the underground car park serving the whole of the development and their own parking was in an underground garage beneath the houses. The houses sat on the concrete slab which formed the roof of the underground car park at ground level. The garage for the house and some utility areas were located in part underneath the slab. It would have been wholly impractical for these houses to have been sold on a freehold basis. The lease included positive covenants on the part of the tenant to pay towards a service charge for the upkeep and maintenance of the grounds in the estate, the estate roads, the cleaning and maintenance of the underground car park and in the long term for the maintenance of the structure of the underground car park. It would have been impractical to divide the freehold horizontally here in order to sell the houses on a freehold basis.

Whilst the Government may ultimately introduce improvements to commonhold, at the moment leasehold structures are the only solution.

It may also be appropriate to have exemptions for timeshare leases, Sharia compliant financing arrangements and equity release products.

*Question 12: Do you agree that there should be no further transitional arrangements after the commencement of the legislation to permit the sale of leasehold houses?*

The new legislation must not affect leases entered into after the legislation commences where the agreement to grant the lease was exchanged before the legislation commenced. See our earlier comments in response to Question 2.

*Question 20: Do you agree with the circumstances set out above in which a capped ground rent will apply in replacement leases?*

The Committee agrees with the circumstances mentioned. The Committee would reiterate the point that if the description of the property has in substance altered or the terms of the lease have been varied significantly, the changes need to constitute at law a surrender and re-grant of the lease for the cap to be introduced for the altered/varied lease.

*Question 21: Do you agree there should be no further transitional period after commencement of the legislation permitting ground rents above £10 per annum?*

The new legislation must not affect leases entered into after the legislation commenced where the agreement to grant the lease was exchanged before the legislation commenced.

If you have any queries about this response, please do not hesitate to contact us.

**Jackie Newstead**  
**Chair, Land Law Committee**  
**City of London Law Society**

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