

# An End to “Fleecehold”?

## Report Recommends a New Era of Accountability for UK Developers and a Commonhold Regime

In December 2017, in response to a government consultation on leasehold practices, the then Communities Secretary Sajid Javid announced:

*“It’s unacceptable for home buyers to be exploited through unnecessary leaseholds, unjustifiable charges and onerous ground rent terms.*

*It’s clear from the overwhelming response from the public that real action is needed to end these feudal practices. That’s why the measures this government is now putting in place will help create a system that actually works for consumers.”*

An internet search for “fleecehold” reveals pages and pages of entries highlighting what has been dubbed the “next PPI” scandal in a headline-winning sensation that has spanned more than two years. Just a few pages in, however, it is clear that some of the earliest coverage was more than seven years ago, indicative of very real and damaging problems over an increasingly long period of time.



What lies at the heart of the headlines? Serious concerns have arisen around:

- Developers selling new houses with leasehold, rather than freehold, title, allowing them an ongoing income even after they have sold the properties
- New homes sold on a freehold basis but still attracting a service charge for shared services or communal areas with few or no controls over charging and accountability
- Escalating and excessive administration costs

- High and rapidly increasing ground rents that threaten long leaseholders’ security and ability to sell and mortgage their properties
- A lack of transparency in marketing practices such that buyers were misled as to the nature of their occupation and financial commitments
- Unfair practices that reward buyers for using a developer’s preferred legal adviser

Aside from the very tangible financial cost, any one of these factors can affect how easily a tenant or owner can deal with their own property.

What, if anything, has changed since the 2017 announcement?

### “Leasehold Reform”: Report by Housing, Communities and Local Government Committee (HCLGC)

The most significant development is the recent report delivered by HCLGC (the Report): a frank and damning exposé that condemns the development structures and marketing practices that the leasehold system has allowed to perpetuate. But is there a problem with the system, or just some of the people who use it? And how far does the HCLGC go in its recommendations to right the wrongs unfairly visited on the affected?

### Key Recommendations

The recommendations are wide ranging and all designed to create a fairer landscape for leaseholders and freeholders subject to service charges. It is difficult to resist the temptation to list them all, significant and deserving of attention as they all are. Key proposals, however, include:

- Competition and Markets Authority to investigate mis-selling of leaseholds and to give a view on whether or not onerous lease terms are unenforceable.
- Fairer marketing practices to be employed, including use of a standardised “key features document” setting out tenure and cost implications at the start of the sales process and the prohibition of financial incentives to induce buyers to use a particular legal adviser.
- Removal of onerous ground rents in leases (an onerous ground rent being one that is disproportionate to the value of the property, adversely affecting the ability to sell or mortgage) with a limit imposed on existing ground rents.

- Maximum ground rent of a peppercorn on all new leases (zero financial value).
- Restrictions on permission fees and use of a standardised form for invoicing of service charges.
- New consultation process for leaseholders affected by major works with a cap of £10,000 per leaseholder. Above this cap, the majority of leaseholders must agree to the works going ahead.
- Freeholders' tribunal costs should not be recoverable where a leaseholder has won its case.
- Reformation of forfeiture laws to enable leaseholders to dispute large bills without fear of losing their homes.
- Implementation of processes to make it easier and cheaper for leaseholders to acquire the freehold or extend their leases, including the introduction of low-cost loans to facilitate this.

These are all significant changes responding to serious and justified criticisms of the current regime.

The proposals will make a material and beneficial difference to the lives of existing and future leaseholders. One of the most radical suggestions, however, is the proposal to favour a commonhold model over leasehold.

## What Is Commonhold?

A commonhold model of ownership requires residents to take responsibility for the block within which they live, facilitating ownership of a freehold (rather than leasehold) flat and responsibility for shared areas and services. The model is successfully employed in other countries around the world, including Germany, the US, Australia, France and Belgium.

Some 15 years ago, the government introduced commonhold as an alternative form of tenure, envisaging that it would replace leasehold as the “go-to” tenure for new-build flats. That has not happened. Fewer than 20 commonholds have been registered in the years following the introduction of the system in 2004, when the enabling law came into force. There are a number of reasons cited for the lack of take-up. These include issues with the legislation itself that affect confidence in the system around:

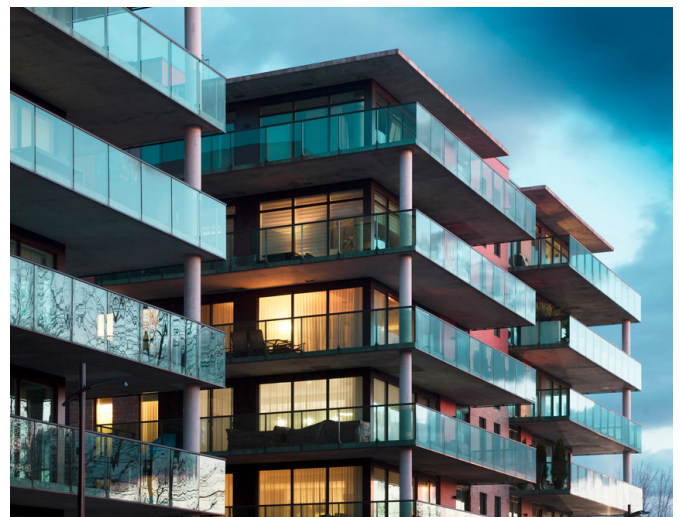
- Creation and conversion of commonholds
- Shared ownership generally
- Dispute resolution
- Enforcement

How effectively these issues can be addressed will influence the likelihood of a commonhold system being put into practice. There is also a real perception and concern that commonhold is not suitable for mixed-use developments due to a misalignment between the interests of residential and commercial occupiers.

It is also argued that a commonhold system reduces incentive for developers, as they lose the valuable income stream that has been so heavily criticised by the HCLGC.

A key consideration is also likely to be the role of professional freeholders which they, themselves, say “cannot be underestimated” or if, in fact, occupiers really would be better off looking after their investments themselves.

In a previous article, we explored some of the criticisms of the leasehold structure, looking at the challenges of commonhold<sup>1</sup> and identifying some changes to the current regime that might support a less radical change to the legislative structure we have today. However, in the year that has followed, we have seen a rapidly changing political landscape that appears to welcome the prospect of an overhaul. The findings of the HCLGC have highlighted legitimate and serious reservations about an industry that has failed to regulate itself effectively. The Report sets out abuses of a system that is simply not working for the end user: the homeowners who have made probably the biggest financial commitment of their lives. Whilst concerns remain around the effectiveness of commonhold for all development structures, the recent findings give merit to serious consideration of commonhold as an alternative to what we now have. The challenges remain, however, and must be addressed.



## Challenges Arising From Commonhold Structures

Several factors are viewed as being potential blocks to a more widespread introduction of the commonhold system:

- Lender willingness: the key issue being lack of precedent by which lenders can assess risk
- Occupier co-operation, expertise and involvement
- Suitability for large or complex developments, such as mixed-use

Comments made by UK Finance indicate that if developers will build commonhold, lenders will lend. Some 50% of UK lenders are currently willing to lend against a commonhold tenure.

Occupier co-operation and expertise may be the greatest challenge, perhaps. There are strong arguments that a responsible freeholder plays a valuable role in protecting the investment and ensuring harmony between the residents.

<sup>1</sup> “[Commonhold – It Is Broke, But Let’s Not Fix It](#)” – Michael Shaw, April 2018

But this assumes a responsible and diligent freeholder or management company operating with integrity. The HCLGC saw evidence that this was often not the case. Despite the arguments put forward, the HCLGC remained sceptical that professional freeholders provided a more reliable and cost-effective service that leaseholders could, themselves, provide, saying that:

“...we recognise that there are complexities in larger, especially mixed-use developments. The high premiums leaseholders are required to pay ... are paid regardless of the level of oversight the freeholder provides, and do not provide an obvious financial incentive for freeholders to work in the interests of leaseholders or promote the long-term condition of a building.”

The challenge for commonhold occupiers will be finding the time, resources and expertise to enable the development to run smoothly.

There was a clear recognition that some structures, such as mixed-use and retirement communities, may need special consideration, as they do not readily lend themselves to a commonhold model. The National Trust, too, has particular considerations in relation to the status of its inalienable land that will need to be addressed. However, the sentiment was clear – the current state of affairs cannot continue.

## The Future

We are awaiting, with a great deal of interest, the government's response to this report. Will it give substance to its promise to “tackle unfair practices in the leasehold market” and “end feudal practices”, or will we see an altogether more watered-down approach to resolving the issues that have been identified? Whatever the solution is, we need to see a response that protects both the vulnerable end user and the legitimate business interests of developers, who provide a much-needed resource in a climate where shortage of housing remains a perennial problem.

Either way, the issue of commonhold will remain central to the debate, and one of the key questions must be whether the other recommendations, alone, can resolve the unfair practices visited upon leaseholders, or is it the case that we really do need to abolish leasehold and start again?

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