

# Response to Consultation Paper: “Tackling unfair practices in the leasehold market”

By the HomeOwners Alliance

September 19th, 2017

## **The HomeOwners Alliance**

The HomeOwners Alliance is an independent consumer organisation providing help and assistance to our members. We campaign for policies that help homeowners and publish free advice and guidance on everything to do with buying, selling and owning your home.

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## Background

The HomeOwners Alliance has long campaigned for a fairer leasehold system, which is one of the biggest areas of concern for our members. Many members suffer what can only be described as extortion from unscrupulous freeholders, leading to huge costs, stress and uncertainty, and even potentially to a substantial loss of value of their home. In reports such as [\*Homes Held Hostage\*](#) (April 2017), we have highlighted the problems, illustrated by case studies, showing how the extreme unfairness of the antiquated leasehold system can turn the dream of owning your own home into a nightmare. Some of the situations homeowners find themselves in are so contrary to natural justice that people have difficulty believing it is actually legal in 21<sup>st</sup> century Britain. Many of the injustices are the result of deliberate attempts by freeholders, property investors, and some major property developers, to use the complexity of the leasehold system to maximise the money they can extract from leaseholders. In many cases there is anecdotal evidence that the freeholders have deliberately misled leaseholders, in what would make it a massive mis-selling scandal, as happened with pensions and PPI.

We have previously analysed why earlier reforms – such as commonhold – haven't had the full desired impact, and suggested other practical reforms to ensure a fairer system, such as abolishing leasehold houses and addressing onerous ground rents. That said, we believe government should go much further, and set out a plan to abolish the leasehold system over time as has been done overseas. There are no redeeming qualities to the leasehold system, which is so complex and confusing to the public that partial reforms will mean it will remain a vehicle for unscrupulous landlords and investment companies to unfairly make money from homeowners.

Our starting point is that in the vast majority of cases when homebuyers understandably believe they have bought their own home, they should actually have done so in the eye of the law, and not be merely a tenant with a long lease subject to an unfair agreement with a freeholder. Leaseholders should be presumed by government to be the actual owners of the property, rather than temporary tenants. In the case with houses, homeowners shouldn't have to deal with a third party or ask their permission to do work to their house. The primary role of an alternative system should be to ensure good upkeep of properties with common areas, not to provide an income for investors or developers.

As we showed in *Homes Held Hostage*, and as your consultation paper recognises, that far from fading into feudal history, the leasehold system has been growing in significance in recent years, making up an increasing proportion of new homes sold. Anecdotally, there is also an increase in unscrupulous practices from freeholders who see an opportunity to make extortionate profits at the expense of leaseholders.

Against this background, we welcome the government's recognition of the injustices in the current system, and its plan to ban the sale of new build leasehold houses. But we also need to deal urgently with those already caught in this scandal, by curbing extortionate ground rents and ensuring they can buy their freehold at a reasonable cost with no punitive strings attached. There is sufficiently strong evidence of mis-

selling, that the government should set up a Leasehold Mis-selling Commission, to establish the scale of the problem and propose remedies.

We urge the government to accept that this is only one particular set of reforms, and that far more extensive reforms will be necessary to bring an end to the feudal leasehold system. We outline some other reforms at the end.

In summary, the HomeOwners Alliance calls on the government to:

**General:**

- State its commitment to ending the leasehold system and ground rents, and to set out a plan to do that

**To protect those buying new build houses:**

- Ban the sale of new leasehold houses
- Ban the sale of freehold of houses to third parties without giving the leaseholder the right of first refusal. This right currently exists for leaseholders of flats, but not for houses

**To protect leaseholders already suffering onerous ground rents:**

- For all leasehold properties, set a statutory cap on existing ground rents as a proportion of the value of a home (to be set by government, but could be 0.1%). Ground rents above that level would have to be reduced to the cap, and disputes would have to be referred to the leasehold tribunal
- Establish a Leasehold Mis-selling Commission

**Limiting ground rents on all new leases:**

- Set ground rents at a peppercorn for all new leases for all properties, and lease extensions. This currently applies to all formal leasehold extensions, but it should also apply to informal extensions and new leaseholds

**Other reforms:**

- Make commonhold tenure mandatory for all newly-built blocks of flats or apartments (with a possible exception for shared ownership tenure)
- Ban freeholders from selling the freehold to the leaseholder while still imposing restrictive covenants which require leaseholders to continue making certain payments to and asking for consents from the original freeholder
- Protect freeholders on estates from unreasonable service charges for communal services, just as leaseholders are
- Make the statutory extension of leasehold flats longer (currently outstanding term plus 90 years)
- Ensure enforcement of the law requiring estate agents and developers to state whether the properties they are marketing are leasehold or freehold and to include information on the length of lease and service charges

Our detailed comments follow.

# Response to Questions

## 1. Introduction

Q1: We are responding as the HomeOwners Alliance, Britain's only consumer group for homeowners and those who aspire to own.

Q2: N/A

Q3: The interest of our organisation is as a representative of homeowners. Our most recent Homeowners Survey found that 50% of UK adults see the current leasehold system (including service charges and ground rent) as a very serious or serious problem, up from 42% in 2016

Q4: We operate nationally, and have members in all parts of the UK

## 3. Limiting the sale of new build leasehold houses

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

The government should take immediate steps to ban outright the sale of leasehold houses. As an immediate first step, the government should stop offering Help To Buy on leasehold houses. Many of the arguments for a ban are set out in the consultation paper, although there are other concerns. For example, new build houses are being sold on a leasehold basis not just to create an income stream from ground rent (paragraph 3.8) but also from other charges, such as for permissions to make changes to the property, leasehold extensions etc. Not only is the leasehold discount not passed on to the consumer, but there is widespread confusion and ignorance about leasehold issues, as illustrated by our survey carried out for *Homes Held Hostage*. Probably the majority of new home buyers are unaware of the value of owning a freehold, and that ignorance is being taken advantage of by sellers. Our research found that of a sample of 100 flats listed for sale, 51 of them didn't show them as being leasehold, even though estate agents are required to display not only tenure but the length of the lease<sup>1</sup>. Often this legally required information cannot even be obtained from developers' show homes.

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

We do not think there are any other circumstances where it is justified.

### **Q7: Are any of the exceptions listed in 3.2 not justified? Please explain**

We do not accept that the exceptions set out in paragraph 3.2 are justifiable reasons for allowing someone to sell a new build home as leasehold. Many, if not all, the concerns can be addressed by the planning system, or other local authority powers. For example, if a house is sold adjoining a property of architectural interest, there is

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<sup>1</sup> The Property Ombudsman, Code of Practice for Residential Sales Estate Agents

no justification for them to have to pay ground rent to a freeholder; any changes to the house that could compromise the architectural integrity could be controlled by other local authority powers, such as through the use of conservation areas. Likewise, there is no justification for a local authority or university to retain the freehold of new build houses built on their land where they want to do further development – it is simply unfair to the homeowner to make them tenants and charge ground rent to make life easier for the authorities in future. If the local authority is unsure about its future plans, it should simply rent out the properties on short leases rather than sell them as homes. Private developers can cope without such powers, and so should public ones.

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

The claim that sale of new build homes is increased by selling them as leasehold is an entirely self-serving argument by property developers. As stated above, the leasehold discount is often not passed on to consumers, so selling as leasehold does not reduce the price and thus increase demand for the home. Indeed, if having a leasehold discount increased demand for houses that they could not otherwise sell, then developers would make sure that homebuyers knew they were buying a home at a discount because it is leasehold. The opposite is the case: there is strong evidence that when homebuyers know that a house is leasehold, and know the problems that can cause, they are less likely to buy it. There is stronger demand for the homes if they are freehold, which is why developers can be poor at making clear to homeowners when houses are leasehold or market them as ‘virtually freehold’.

**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

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

None

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

N/A

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

N/A

**4. 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 have no data on the prevalence of onerous ground rents, but it is a regular source of complaints from homeowners, suggesting that it is widespread. We have encouraged our members and visitors to our website to complete the survey conducted by the The Leasehold Knowledge Partnership in association with the All Party Parliamentary Group (APPG) on Leasehold and Commonhold reform, and the Facebook group the “National Leasehold Campaign”. The practice is certainly continuing.

**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.**

- i) Given that leaseholders get nothing in return for the ground rent, we strongly believe that it should be set at a peppercorn for all new leases for all properties, as it currently is for formal lease extensions. The price of buying a new home should be transparent, simple to understand, inclusive and not open to abuse. In the overwhelming majority of homes, there is no intellectual or commercial justification for ground rents, which are a much abused legacy of a feudal system. In flats, ground rent is a meaningless concept, and it is impossible to justify a separate charge for the ground that the block is built on. In houses, where people have sole use of their house and garden, there is no justification to charge a rent for the land when you are not charging rent for the house itself. When a homebuyer buys a leasehold, they are buying the right to use the property, which inevitably includes use of the land that the property is built on. A large proportion of leaseholds in England are already set at peppercorn rents, without any adverse consequences. Freeholders already charge annual administration fees, as well as a range of other fees. The very existence of the ground rent system leads to unproductive bureaucracy and disputes between leaseholders and freeholders. It encourages abuse by freeholders who are incentivised to see it as an opportunity to make money at the expense of the homeowner. The existence of profits from ground rents as well as making the freehold more expensive to buy incentivises freeholders and property developers to resist moves to fairer systems, such as commonhold. The government should aim to make freehold financially unattractive as an investment, to accelerate the move to commonhold. The government should be aiming to phase out ground rents, rather than letting new ground rents be established.

In addition, the government should ensure ground rent is set at a peppercorn for all types of lease extensions, including those done informally. Informal lease extensions by their nature are problematic

because leaseholders often do not have the proper legal advice needed in what can be a costly and complex transaction. They are at real risk of being taken advantage of by the freeholder. Ground rent having to be set at a peppercorn could be enforced by Land Registry refusing to register informal lease extensions which are subject to ground rent.

- ii) Given the strong arguments for setting all new ground rents at zero, we do not think that the government should allow ground rents on new leases to be increased at all. However, if the government does not ensure all new ground rents are set at a peppercorn, it should restrict increases to CPI (now the measure of inflation used for most annual increases, rather than the invariably higher RPI). There can be no justification for allowing automatic exponential increases in ground rents, such as doubling every set period. Although doubling every 25 years in a period of high inflation would not amount to a substantive increase, doubling it every 10 years in a period of low inflation would rapidly become extortionate. There is no rationale for doubling ground rents, other than to trap leaseholders in extortionate contracts, and the practice should be banned.
- iii) Up-rating in line with CPI every year would be bureaucratically burdensome, and we suggest that up-rating it every 5 years should be the norm.

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

We cannot see why there should be any exemptions for Right to Buy, shared ownership or other leases – the arguments are the same.

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

We do not believe that restrictions on ground rent levels will have any impact on the supply of new build homes. Like the claim that banning leasehold houses will impact sales, it is an entirely self-serving argument put forward by developers who want to continue making unjustifiable incomes from homebuyers. Our construction industry is almost unique in selling products with a regular and rising annual income stream legally attached to them, which they can then sell to third parties to make a one-off capital gain. Almost all other sectors just sell their products for an upfront payment, and there is no reason the construction industry should be different. It is also an economically fallacious argument. In a fully transparent and competitive market, the income from ground rents would reduce the price that developers sell homes at (the leasehold discount), so the overall profit levels are normalised. If developers argue that curbing ground rents reduces house building because it reduces profitability, they are admitting that the lack of transparency and competition around ground rents enables them to make excess profits. The mix of payments (the balance between upfront payments and amortised annual payments) should not have an impact on the average profitability of the industry. In the final analysis, there is clearly an excess of demand over supply for new housing, and that is likely to last decades.

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

It would be unfair to protect new homebuyers, but not to provide any support for those already trapped in extortionate or exponentially rising ground rents. If the ground rent provisions are extortionate, it is hard to justify to homeowners stuck in essentially a life-long contract that it was legal under the law at the time and nothing can be done about it. There is strong anecdotal evidence that many of the leaseholds were mis-sold, with developers telling homebuyers they could buy the freehold within a couple of years for a reasonable price, but then selling the freehold to a third party investment company without telling the leaseholder. We note that Taylor Wimpey accepts it has responsibility to help those in existing onerous leaseholds, and has now set up a ground rent fund to help them. However, that fund does not cover second-owners, who have bought the property from the new home owner. There are also precedents in other industries, where action has been taken against widespread mis-selling (eg. pensions and PPI).

We have three recommendations to help those trapped in existing unfair leaseholds:

- a statutory cap on all existing ground rents for all leasehold properties, set as a proportion of the property price (to be determined by government, but for example 0.1%). This would help homeowners already trapped in leaseholds with unreasonable ground rents, against which they currently have no legal recourse. It would curb the practice of doubling ground rents, as they would quickly hit the cap, and protect leaseholders from having the value of their homes destroyed by excessive ground rents. This would mirror the existing rights that leaseholders have that maintenance charges should be reasonable. There is no justification for freeholders being allowed to charge unreasonable ground rents but not unreasonable maintenance charges. The practical application of the cap would need to be carefully thought through, but at its simplest could just be a right given to leaseholders, who can appeal to the freeholder, and if unsuccessful take the freeholder to the tribunal for resolution (as currently happens with disputes on maintenance fees).
- Give leaseholders of houses the right of first refusal to buy the freehold when it is put on the market, giving them the same right as leaseholders of flats. This would prevent developers selling freeholds on houses to investment companies without the leaseholder having a chance to buy it.
- Establish a Leasehold Mis-selling Commission. As stated earlier, there is strong anecdotal evidence that some housebuilders deliberately mislead homebuyers into buying leasehold houses, in order to profit from selling the freehold. There are examples of homebuyers being told by the housebuilder that they can buy the freehold after two years at a low price, only for the housebuilder to sell the freehold to a third party who then requires a far higher price for the freehold. Homebuyers have been pressured into using solicitors provided by the housebuilder, who then fail to warn the homebuyer about the onerous terms such as exponentially rising ground rent. Homebuyers have ended up getting independent legal advice on their options, and have been told that they should sue their original solicitors for professional negligence – an expensive and



uncertain course of action. If housebuilders did deliberately mislead homeowners in order to increase profits from them, then that would be fraud (legally defined as gaining financial advantage by deception). The Leasehold Mis-selling Commission should establish the facts of the matter, and if there is any mis-selling ensure that homebuyers can get access to any compensation due without having to resort to the courts.

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

The government should as a matter of principle not legislate whenever there are effective voluntary solutions. However, in the case of leasehold, the abuse by the property industry has been so egregious that we believe that no voluntary solutions will work and legislation is necessary. Housebuilding is a very fragmented industry, and any voluntary agreement would be difficult to enforce.

**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?**

We have seen a member’s legal advice on this – technically such leaseholders are indeed assured tenants and so can be subject to these possession orders. The legislation needs to change. It is clearly egregious if a homeowner is subject to repossession because they fall three months behind on ground rent. The basic principle of the law should be that leaseholders are the owners of their homes, not the freeholders. We would support the proposed amendment of the Housing Act 1988.

**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?**

Yes, freeholders on private estates should have the same rights to protect them against unreasonable charges as leaseholders. It is an issue of growing concern among homeowners, and regularly raised with the HomeOwners Alliance. Freeholders and leaseholders on private estates should also have the right to remove a management company if they have cause for complaint, similar to the right to manage given to leaseholders in flats. New homebuyers also need to be made well aware of these proposed charges, as in the past these common parts of estates (eg green spaces) would have been adopted by the council.

## 7. Future issues

**Q21: The Housing White Paper highlights that the Government will consult on a range of measures to tackle abuse of leasehold. What further areas of leasehold reform should be prioritised and why?**

There are other areas of reform to the leasehold system that are needed, to ensure it is transparent and fair. Other issues to look at include:

- The government should make it mandatory that all new flats are sold commonhold rather than leasehold, as is usual in other countries. Commonhold tenure has failed to take off in new built flats and conversions because developers are strongly financially incentivised to sell the flats as leasehold, and so the government should make it mandatory.
- Stopping opportunistic charges from freeholders. We have come across cases where freeholders have imposed charges on leaseholders for changing a carpet or changing the mortgage, for which there is no feasible justification. The tribunal should be empowered to prevent such charges.
- Stopping restrictive covenants from freeholders. When freeholders sell the freehold to the leaseholder, they should be banned from imposing restrictive covenants which require the new freeholder to continue making payments to the previous freeholder. Some freeholders have been imposing restrictive covenants as a way of continuing to generate an income even when they sell the freehold. When the freeholder sells the freehold to the leaseholder, they should no longer get any payments of any form, nor should their consent be required (eg for alterations or remortgaging).
- The Land Registry should hold a public register of all freeholders, so there is more visibility of the ultimate ownership. At present, many freeholds are owned by offshore companies, which can hide the beneficial owner.
- Leaseholders should not have to wait two years before being allowed to extend the freehold. There is no justification for this waiting period. They should be able to extend as soon as they want to and for longer than the current practice of outstanding term plus 90 years.
- The government should ensure enforcement of the requirement that estate agents and developers should advertise both the tenure of a property (whether it is leasehold or freehold), and the length of the lease



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