

E-Update

Autumn 2017



Welcome to Hewitsons Residential Property E-Update

Welcome to the Autumn edition of our update. There has been a lot of media interest recently surrounding the sale of leasehold residential property and, in particular, leasehold houses. We are therefore dedicating the majority of this Update to this thorny issue.

Why do we have leases at all?

Covenants in a lease are enforceable against both the original and all future holders of that lease. This includes covenants to do something "positive", such as maintain, decorate and insure or to contribute towards the costs of doing so (if the landlord provides these services).

However, covenants relating to freeholds are generally only enforceable against future owners if they are "restrictive" in nature e.g. not to build or alter or cause a nuisance.



Tim Middleton
Head of Residential Property

When should a lease be used?

Leases must be used for flats, where there will always be common parts which need maintaining or repairing and all those who benefit from them must pay their share of the costs.

In contrast, houses seldom benefit from shared facilities and, if they do, this can usually be dealt with by putting in place appropriate covenants and a means of enforcing them against future owners. It should therefore virtually never be necessary to sell a house on a leasehold basis.



Clare Martin
Partner

So, why have houses been sold on leases?

Developers have claimed that this enables

houses to be sold at cheaper prices, but little or no evidence has been provided to support this assertion. The conclusion generally reached is that it enables developers to sell the freehold once all the houses are built, often at a very attractive price.

And this return is maximised by requiring leaseholders to pay hundreds of pounds of ground rent each year which then rises regularly (sometimes as frequently as every 10 years). Not only does this make the cost to individual leaseholders of subsequently buying their freeholds prohibitive, it has also made some houses unsaleable - locking the owners into a financial stalemate. At present the issue of leasehold houses is of such concern that it is under review by Parliament, with an expected ban to come.

Is the problem confined to leasehold houses?

No it isn't. Again developers have taken to selling on the freeholds of blocks of flats to third parties and to maximise the price they will obtain by having frequent and substantial ground rent rises. And sometimes the level of rent is such that these "long leases" are getting caught by legislation intended to apply to short term tenancies. This legislation provides that, if there are arrears of rent and the landlord takes action to recover them, then a court must grant possession of the flat to the landlord with no discretion to give the tenant more time to pay. This is of concern to both the leaseholders themselves but also, of course, to their mortgage lenders (since it is the leases of flats which represent the security for their loans).

An imbalance of power

How have so many buyers of leasehold properties been allowed by their lawyers to purchase an asset which has turned out, in some cases, to be unsaleable and unmortgageable? The answer lies in the inherent imbalance of power between developers and their buyers. It is not uncommon for our team to be asked if we can act for both buyer and seller in a property transaction and it is often possible for us to do



Beverley Henderson
Solicitor



Bradley Armorgie
Solicitor



Paul Ross
Residential Property Executive

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so, provided that we carry out a strict risk assessment. This is to establish that there is no real prospect of a conflict of interest (usually a disagreement) arising between the two parties during the course of that transaction. One of the issues to be considered in that risk assessment is whether there is any "difference in bargaining power" between the two parties. This is seldom an issue if the prospective clients are both private individuals, but where one of the parties is a developer the imbalance is such that it will virtually never be possible for us to act on both sides.

So what has been happening with these leasehold properties? In these cases many buyers are purchasing for the first time and so the difference in bargaining position between them and developers is even more stark than usual. Consequently the need for them to have genuinely independent advice on what they are buying is even greater. But in practice what they get is a "pet lawyer" recommended to them by the developer who, by dealing with large numbers of purchases on the same development, can use economies of scale to offer a cheap price. There are two fundamental problems with this:

1. The fact those lawyers are receiving large amounts of work "fed" to them by the developer must cast doubt on their ability to act genuinely independently and only in the interests of their buyer clients.
2. The reports provided on the (usually voluminous) paperwork tend only to inform these naïve buyers what the terms of the sale are and do not advise on the implications of them. For instance, a summary of the lease terms is provided, but no advice on why a house is being sold leasehold and what might it cost to buy the freehold in the future.

The voluminous paperwork referred to lies at the heart of the problem. For it is simply not possible for buyers' lawyers to charge a realistic price for going through the hundreds of pages of legal documents involved in a typical new build purchase unless economies of scale are applied. And to achieve that they are dependent upon the developer sending these buyers to them. If problems like this are to be avoided in future, a way must be found to break this vicious circle.

Should I buy a leasehold property?

There is nothing fundamentally wrong with leasehold property. It has served its purpose for many years without any great problems. However, if you are purchasing a leasehold (and, in particular, a newbuild) here are some things to consider:

- Do not be put off a Leasehold, just be wary and thorough
- Make sure your lawyer advises on the ground rent and mechanisms for this to increase
- Find details about who will own the freehold. Will the developer retain it (or perhaps transfer it to a company which the residents control) or will it be sold to a third party?

Leasehold still has its place, especially for social housing or retirement developments you just need to be sure it is not subject to any adverse provisions.

Is there an alternative to Leasehold?

Strangely enough there is, but it is virtually unused. It is called 'Commonhold'. and was introduced in 2002 by the Commonhold and Leasehold Reform Act. However, as at June 2009 only 12 Commonhold developments had been built in England. This is partly because some Lenders refuse to lend on commonhold properties but mostly because developers decided not to adopt commonhold on newbuild developments (where no ground rent can be charged and there is no freehold to sell on).

If Parliament is considering the whole issue of leaseholds once more, it is to be hoped that it will consider forcing developers to use commonholds as an alternative in future.

Highlighted Lawspot

Every week, Partner Clare Martin writes a law article for the Cambridge Property News. This update's Lawspot focuses on cost.

I have obtained several quotes from Solicitors all at varying prices. How do I choose what is right for me?

It is a difficult situation and one that needs carefully considering as you are entrusting someone to look after your most valuable asset – your home.

Generally speaking you get what you pay for however it isn't ever as simple as 'higher cost means higher service.'

Typically, a Firm charging a higher fee tends to have a good, respected history with a good level of experience in the field. It is usual for you to have direct access with the Fee Earner and the PA. Generally speaking those charging less do not offer this and instead your contact tends to be limited to people in a junior position or a secretary.

Often if you pay a lower fee you are just a number in a scheme of stack them high, sell them cheap. Often paying a little bit extra means you get a more intimate experience.

You should also consider your personal needs. Are you a first time buyer who needs a little extra guidance and reassurance; are you a well adverse in the property world or somewhere in-between? Typically a first time buyer needs extra guidance in what can be a daunting process – paying extra tends to offer this service, although there is of course a balance between what you can afford and the service you require.

Whilst paying extra doesn't guarantee and good service, and paying less doesn't guarantee a poorer service you generally, especially in the Cambridge market, get what you pay for.

I would advise you speak to each Firm and find out exactly how they deal with a residential transaction.



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Reg No: OC334689