

Insights

## **LONGER LEASES, LOWER GROUND RENTS AND LEASEHOLD LIBERATION: RESIDENTIAL REFORMS IN THE KING'S SPEECH EXPLAINED**

Nov 14, 2023

### SUMMARY

The King's speech announced a new Leasehold and Freehold Reform Bill *'to reform the housing market by making it cheaper and easier for leaseholders to purchase their freehold and tackling the exploitation of millions of homeowners through punitive service charges'*. It also addressed some key points in the Renters (Reform) Bill. This note sets out some of the key proposals and commentary in respect of the same.

The King's speech announced a new Leasehold and Freehold Reform Bill, which the King hails as:

*'A bill to reform the housing market by making it cheaper and easier for leaseholders to purchase their freehold and tackling the exploitation of millions of homeowners through punitive service charges'*.

It is the latest in a series of long awaited and much debated residential leasehold reforms, which are slowly starting to trickle through parliament.

So what does this latest announcement mean, and what is being proposed in practice?

### **LEASEHOLD AND FREEHOLD REFORM BILL ("LFRB")**

The key features of the LFRB, outlined in the briefing notes to the King's speech, are as follows:

#### **Cheaper and easier for leaseholders to extend their leases or buy their freehold**

There are minimal details on how this will be achieved. The briefing notes do confirm that the LFRB will:

- remove the requirement for leaseholders to have owned their interest for two years in order to extend their lease or acquire their freehold, and
- further limit the mixed-used property exemption (see below).

## Mixed-use property exemption

Under current legislation, where more than 25% of the internal floor space of a 'building' is non-residential (excluding common parts), the collective rights of residential tenants to acquire their freehold or manage their property **do not** apply. The LFRB proposes increasing this threshold to 50%, so that going forwards, provided **at least 50%** of the internal floor space of a 'building' is residential (rather than the current 75% threshold), such collective rights **will** now apply.

It is unclear if this will retrospectively apply to existing developments, but if it does, landlords could unexpectedly be left exposed to these rights in schemes where they had previously thought they would not apply. It remains to be seen if in the future, landlords will seek to mitigate against this, especially in true mixed-use schemes (rather than residential-led with ancillary commercial), by changing the make-up of their schemes to retain 51% as non-residential. This could have the unintended consequence of further lowering housing stock.

## Lease extensions

The standard lease extension term will increase from 90 years for flats and 50 years for houses to 990 years for both (with ground rent reduced to £0 on extension, as is currently the position).

## Ground Rent caps on existing long leases

With ground rents already abolished for all **new** qualifying long residential leases, a consultation has now been launched regarding capping ground rents in all **existing** qualifying long residential leases (those which pre-date the recent Leasehold Reform (Ground Rent) Act 2022 ("**GRA**") (see BCLP insight: [Leasehold Reform \(Ground Rent\) Act 2022 - Ground Rents Banned on New Residential Leases from 30 June 2022](#)). The purpose of this proposal is *"to ensure that all leaseholders are protected from making payments that require no service or benefit in return, have no requirement to be reasonable, and can cause issues when people want to sell their properties"*. This would prevent a two-tier system developing in residential leasehold properties between leases granted before and after ground rents were abolished. In addition, the Competition and Markets Authority has already been carrying out much publicised investigations into ground rents in leases which pre-date the GRA, which have led to various voluntary commitments by landlords and revised approaches in respect of such leases.

However, any new proposals must be considered against the impact on landlords and ground rent investors whose pre-existing business models relied on such ground rent as an income stream, or as a means of covering service charge gaps. Whilst previous government statements referenced a

proposed cap at 0.01% of freehold value, the current consultation is seeking views on much wider proposals. These range from capping ground rents at a fixed value (a peppercorn, the original amount when a lease was first granted, or at current levels) with no increase allowed, to capping them at an absolute maximum value or a percentage of the property value, with allowance for an increase mechanic (by either fixed or index linked increments or open-market review). Whether any leases should be exempt is also being considered.

Such measures are seen by some as going too far in interfering with the contracts reached between landlords and tenants. Arguably, the premium paid by the leaseholders reflected the ground rent payable and if ground rents are abolished the tenants will achieve an unanticipated benefit at the expense of their landlords. The valuation impact on existing portfolios could be far-reaching, and affect a wide range of stakeholders including pensions funds, local authorities and charities. The consultation on these caps closes to responses on 21 December 2023. Those affected will no doubt wish to have their say.

## **Banning the sale of new leasehold houses**

The LFRB proposes banning the sale of houses by way of leasehold interest other than in exceptional circumstances. This means that all houses sold after the LFRB comes into effect will need to be freehold from the outset. A combination of the GRA banning ground rents and the general market sentiment about leasehold tenure, has led to a substantial decrease in the practice of selling leasehold houses, so this proposal will have limited effect and comes as no surprise. However, further clarification will be needed regarding the scope of 'exceptional circumstances', for example whether it will include houses built on land with specific restrictions, or within an estate containing predominantly leasehold flats and a number of shared estate facilities and amenities, or retirement communities where leasehold houses are still a common operating model.

## **Service and estate charges**

The LFRB proposes to improve leaseholders' consumer rights and give freehold owners on private and mixed tenure estates the same rights of redress in respect of their service charge equivalent (estate charges), which are not currently regulated in the same manner as leasehold service charges. Proposals include:

- improving service charge transparency by using standardised formats (that can easily be compared);
- replacing building insurance commissions for managing agents, landlords and freeholders with transparent administration fees;
- extending access to 'redress' schemes to challenge poor practice; and

- removing the presumption that leaseholders pay their freeholders' legal costs for such challenges.

It is worth noting that the Competition and Markets Authority also has an ongoing review into this area, including a recent working paper on the private management of public amenities on housing estates. It seems likely that some of the suggestions proposed in the working paper will be considered for the detailed LFRB.

## **RENTERS (REFORM) BILL (“RRB”)**

Alongside the introduction of the LFRB, the King's speech also re-iterated the government's commitment to and intentions for the RRB (which had its second reading in the House of Commons on 23 October 2023), although it did not create any further certainty on its timescale.

The Renters (Reform) Bill will only apply to England, whereas the LFRB applies to England and Wales.

Our June insight: [Residential Rented Sector Reset: The Renters \(Reform\) Bill](#) covers the original scope of the RRB, and various industry concerns in respect of it. Below are the further key points that have now been addressed:

### **Student accommodation**

A key concern with the draft RRB was its interplay with the student accommodation sector, and the necessary ability to sync lettings with the academic year. Whilst falling short of committing to allow fixed term tenancies in all student residences (the Bill already provides for fixed term tenancies for 'PBSA'), a new ground for possession will be introduced to facilitate the student academic year. Details of what this will include and who it will apply to are awaited.

### **Benefits and Babies**

The revised RRB will make it illegal to have blanket bans on renting to tenants in receipt of benefits or with children, which was a notable omission from its original form.

### **Section 21 'no reason' evictions**

It has been confirmed that the implementation of this widely discussed and central proposal in the RRB will be *'aligned with reform of the courts'*. It is unclear whether this means that the specific provision that deals with section 21 will become operative post reform or whether the entire Bill will be delayed. Either way, this will come as a relief to landlords who need the practical ability to reclaim possession of their properties in the appropriate circumstances without being hindered by excessive court delays.

## EPC ratings

The initial proposals for landlords to be required to meet EPC Rating C in their private rented domestic properties from 2025 will be dropped.

## THE MISSING PARTS

Alongside those proposals that *were* included in the briefing notes to the King's speech, those that were not are also of interest. The ***abolition of marriage value*** is not directly mentioned, although the worked examples for lease extension premiums in the briefing notes do indicate that the premiums payable will be substantially reduced – without explaining how. ***Banning leasehold flats*** seems off the agenda (unsurprisingly), and there is also silence on any proposals for ***reworking commonhold legislation*** to make it a more viable alternative to leasehold ownership and encourage its wider adoption.

In conclusion, the King's speech clearly confirms a commitment to the ongoing pursuit of reform in the residential leasehold market, and contains some information for those in the industry to start mulling over in the context of their specific portfolios. However, the jury is out on how, or if, either Bill will strike the right balance between the rights of landlords and tenants, ensuring consumers are well informed and protected whilst also ensuring that the living sector continues to thrive and entice investment. We can be sure that there will be clarifications, retractions, amendments and much lively debate, but whether either Bill will make it through parliament before the next election remains to be seen.

## RELATED PRACTICE AREAS

- Real Estate
- Real Estate Sector

## MEET THE TEAM



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