

A Guide to the Leasehold of Residential Properties

There are three ways of purchasing property: leasehold, freehold and less commonly commonhold.

Leasehold

Leasehold is where someone buys the right to use land and property for a fixed number of years. Usually, this is 99 years, but it can be as many as 999. The lease is agreed with the freeholder, or landlord, who owns the property outright.

Most flats are sold as leasehold (freehold flats can create issues with mortgage lenders when trying to secure mortgage borrowing) meaning that a buyer will own the property subject to the terms of the Lease but not the entire building/block of flats. Houses can also be purchased using leasehold, which is where a buyer owns the building but not the land it is on and owns the property subject to the terms of a lease. Leasehold tenure for houses is becoming more popular for new-build houses and there has been much information regarding this in the press as of late.

Freehold

Freehold is where the buyer owns the property and land it stands on, which makes them solely responsible for the property as they own the 'title absolute'.

Commonhold

Commonhold came into force on 27 September 2004 (so is still relatively new) and created a new way of owning freehold properties which have communal facilities. The unit-holder as they are known owns the freehold estate in the unit. The unit-holder is a member of the commonhold association which owns and manages the common parts. Land can only be commonhold if it is already registered with an absolute freehold title.

As residential property law experts, our specialist team at Butcher & Barlow LLP has put together a useful guide in respect of residential leasehold properties as per below.

Buying

Buying a leasehold property essentially involves taking over the lease from the previous owner or in the case of a new build property entering into a brand new lease with the landlord/freeholder. This previous owner could be another tenant (also known as the lessee or leaseholder) or the landlord (also known as the landlord or lessor or freeholder).

Before you buy a leasehold property, you should consider a few factors that can affect the value and marketability of the lease, the charges involved, and any other terms:

The remaining number of years left on the lease (low remaining lease terms can affect mortgage lenders lending against the property or the value of the property should you sell)

The amount of ground rent and how frequently any future increases are calculated

The service charge and other costs associated with the lease/property (such as transfer fees on sale or notice fees payable under the lease)

Does Lease Length Matter?

Yes it does! Mortgages are harder to obtain against properties with leases that have fewer than 70 years remaining. Lenders usually want to mortgage leases that are up to 30 years longer than the mortgage itself. Different lenders have different requirements here.

It can be increasingly difficult to sell property with a lease that has fewer than 70 years remaining. **This is partly due to mortgage lenders' stances on shorter leases. Even a cash buyer will not want to find themselves restricted upon re-sale due to a short lease term.** You should, therefore, pre-empt the length of the lease if you are planning on selling the leasehold in the future.

Changing the Lease

You may be able to negotiate changes to your lease directly with your landlord/freeholder, which is known as 'varying the lease'. If the tenant and the landlord cannot agree, they may be able to apply to a tribunal.

Extending the Lease

At any time of lease ownership, you may request to extend the lease. After two years, you have the right to extend the lease by 90 years, providing you qualify. To qualify for a lease extension after two years, you usually have to have a lease that was longer than 21 years before extending.

The price for extending a lease depends on a range of factors that are unique to each property. This is why you will usually need the help of a solicitor or a conveyancer when extending a lease.

If you cannot agree on a price with your landlord, you may be able to appeal to a Leasehold Valuation Tribunal.

Ending the Lease

It is rare that a landlord ends your lease and evicts you, but they may look to do this **under 'forfeiture** proceedings (examples here could be due to a breach of covenant in the lease or non-payment of service charge and/or ground rent). Court permissions and a formal letter are required for this, however.

Lease Runs Out

When a lease runs out, the tenant does not have to renew the lease; they do not have to do anything if they wish to continue the arrangement. The lease will continue on the same terms as before unless the tenant or the landlord decides to end it.

The lease can be ended if the tenant decides to surrender it, the landlord serves notice gained with a court order, or the landlord provides notice of a periodic tenancy (where the tenant pays monthly rent). If none of these channels have been followed, it may still be possible for the tenant to extend the lease or buy the freehold.

Charges

There are a number of charges applicable to leased properties, which will be set out in the lease. The following are common to see: –

Service Charges

Service charges are used to share the cost of maintaining land/a building that the leaseholder does not own and is not responsible for, but contributes to financially with the service charge.

These costs vary from property to property and might be used to cover matters such as parking, bin storage areas, and the maintenance of communal areas in the building. Service charges might also cover the maintenance of communal gardens and exterior walls and services for common parts used by the properties (such as electricity supplies etc).

You need to be aware of the service charges associated with a property before you enter into the lease because these costs may take the property out of your budget.

Ground Rent

Where a property is held on a long lease ground rent usually has to be paid to the landlord/freeholder of the property.

Unlike service charges, ground rent is not applicable to all properties; you will not have to pay ground rent unless the landlord sends a formal, written demand.

If you still do not pay ground rent after receiving a formal, written demand from the landlord, the landlord may decide to take legal action against you.

Up to 6 years of unpaid ground rent can be recovered by the landlord, and the tenant may also be asked to pay in one go.

The amount of the ground rent is set out in the lease as is the method by which it can increase (if not for a set amount throughout the lease term). Ground rent can only be increased if it is agreed between the tenant and the landlord, or if the increase is detailed in the lease.

Escalating or doubling ground rents will not be acceptable to most mortgage lenders and we would advise you against proceeding with the purchase of a property with an escalating or doubling ground rent. This is because the ground rent can increase rapidly making the property quickly unaffordable and not good security for a mortgage lender to lend against.

Ground rents that are above £250 per annum (or above £1,000 per annum in London) can also create issues in long leases. This is because under the Housing Act 1988 the **definition of "assured tenancies" in section 1 of such Act does not exclude long leases.** The problem here is that under this Act a landlord can seek possession of the property if certain grounds are established. One of these grounds (Ground 8) relates to arrears of rent.

Provided that Ground 8 is met then the landlord can serve a notice seeking possession of the property relying on Ground 8 and once that notice has expired can commence possession proceedings in respect of the rent arrears.

As Ground 8 is a mandatory ground this means that if it is proven then the Court has no option but to make the order, meaning that the tenant would lose their property.

As Ground 8 is not a forfeiture route this means that the usual route by which a tenant can apply for relief (such as paying the arrears) does not apply.

Please note that if a property is owned by a corporate tenant (so a Company for example) or if the property is not occupied by the tenant as their only or main home then the lease cannot be classed as an assured tenancy.

Buildings Insurance

The landlord is usually responsible for the insurance of the building/property itself, (this is more common where the property is a flat). This does not include the contents **of the building/property, which are the tenant's responsibility, and the cost of Buildings Insurance is included in the service charge.**

As the tenant, you can ask for a summary of the Buildings Insurance policy, and then challenge the cost if it seems unreasonable.

Reserve/ 'Sinking' Funds

Designed as cover for unexpected maintenance costs, landlords or management companies can sometimes collect from tenants monies to be used as a reserve, or **'sinking fund'**. **There are rules for how landlords manage these funds, however.**

A tenant is not able to recover reserve funds, even if the money is not used for unexpected maintenance. There can, therefore, be a risk that a tenant may pay into a **'sinking fund' and not benefit from it. Likewise, a new tenant may take the benefit of** certain works to a building, paid for out of the reserves built up by a landlord even though the tenant has not contributed much to the fund.

Responsibilities (also known as 'covenants')

A lease will contain conditions that detail the responsibilities of both parties, which may include a number of different matters, such as:

Whether permission is needed to make alterations, and which alterations/type of changes specifically will require permission from the landlord

The cost of the service charge for the property

The landlord's responsibility regarding repairs and other conditions of the property, such as dealing with difficult neighbours

Any restrictions on what a tenant may or may not do in the property (such as keeping pets)

Who is to insure the property

Conclusion

Residential leasehold properties can be complicated, so having it broken down and put into simple terms digestible sections may take some of the worry out of your experience in buying a leasehold property.. It is recommended that you work closely with a legal professional, such as a solicitor or a surveyor, in order to ensure your leasehold transaction proceeds smoothly.

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