



**Law
Commission**
Reforming the law

In more detail: the future of home ownership

Introductory chapter to all three of our reports

21 July 2020

In more detail: the future of home ownership

This is the introductory chapter to all three of our reports. It explains how our reports fit with Government's own reforms and sets out the future of home ownership after reform.

INTRODUCTION

- 1.1 Our homes are hugely important. It is no surprise, therefore, that housing policy is high up the political agenda. Problems that we experience with our homes can become particularly pronounced. Many leaseholders of flats would point to issues with cladding that were brought into focus following the Grenfell Tower fire tragedy as an illustration of this impact. A recent report from the UK Cladding Action Group found that 9 out of 10 leaseholders surveyed said their mental health had deteriorated as a direct result of the situation in their building.¹ For all of us, the COVID-19 pandemic, and consequential requirement to “stay at home”, has emphasised how much we depend on our homes.
- 1.2 Broadly speaking, we occupy our homes either as owners or as renters.
 - (1) Owners: Many people own, or aspire to own, a home.² The focus of our projects, and of Government's work on leasehold and commonhold reform, is on owners.
 - (2) Renters: There have been significant reforms to the way in which homes are rented in Wales,³ and Government intends to provide tenants with greater security in their homes in England.⁴ Renters are not the focus of our reports.
- 1.3 Reforms concerning home ownership have been discussed for some time, and the future of home ownership is set to change.

¹ UK Cladding Action Group, *Cladding and internal fire safety: mental health report 2020* (May 2020), p 6, at <https://drive.google.com/file/d/1ezKSaJqO3bVyG9-eH58SoiT2bH4D8PjW/view>.

² In the 2010 British Social Attitudes survey, 86% of respondents expressed a preference for buying a home and 14% preferred to rent: Department for Communities and Local Government, *Public attitudes to housing in England: Report based on the results from the British Social Attitudes survey* (July 2011), at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/6362/1936769.pdf.

³ Renting Homes (Wales) Act 2016. The 2016 Act was enacted following recommendations made by the Law Commission in its reports, *Renting Homes* (2003) Law Com No 284 and *Renting Homes in Wales* (2013) Law Com No 337.

⁴ See proposal for a Renters Reform Bill, which would remove the current right of landlords in the private rented sector to evict their tenants by giving two months' notice to leave: *The Queen's Speech, December 2019*, pp 46-47, at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/853886/Queen_s_Speech_December_2019_-_background_briefing_notes.pdf. See also temporary measures whereby landlords will have to give all renters 3 months' notice if they intend to seek possession of a property in the Coronavirus Act 2020, s 81 and sch 29.

- 1.4 In our Reports, we recommend reform to the law of commonhold, to the right to manage (“RTM”) and to leasehold enfranchisement. We have already published our report setting out the options for reducing the price that leaseholders must pay to make an enfranchisement claim.⁵

Enfranchisement is the right for people who own property on a long lease (“leaseholders”) buy the freehold or extend their lease.

The right to manage (“RTM”) is a right for leaseholders to take over the management of their building without buying the freehold.

Commonhold allows for the freehold ownership of flats, offering an alternative way of owning property which avoids the shortcomings of leasehold ownership.

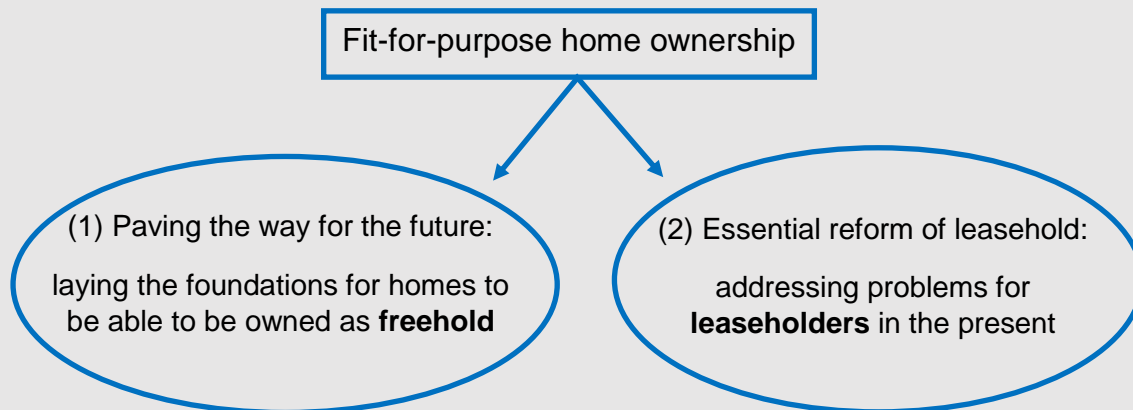
- 1.5 Before we explain our recommendations for reform, it is important to consider the overall purpose of reform, to explain how our three reports fit together, and to explain their relationship with Government’s work on leasehold and commonhold reform.
- 1.6 In this chapter, we start by looking to the future and explaining what the future of home ownership could look like after reform. We then discuss the route to get there.
- (1) In Part A, we summarise how home ownership currently works and its problems.
 - (2) In Part B, we discuss our recommended reforms and Government’s reforms.
 - (3) In Part C, we explain how all the proposed reforms fit together.

⁵ Leasehold home ownership: buying your freehold or extending your lease – Report on options to reduce the price payable (2020) Law Com No 387 (“the Valuation Report”).

HOME OWNERSHIP AFTER REFORM: A SUMMARY

1.7 The reforms proposed by the Law Commission and by Government are intended to create fit-for-purpose home ownership. They are about making our homes ours, rather than someone else's asset.

1.8 The reforms fall into two categories.



(1) Owners of future homes

1.9 For owners of future homes:

- (1) houses will always be sold on a freehold basis – because Government intends to ban the sale of houses on a leasehold basis.⁶
- (2) flats will:
 - (a) be sold *solely* on a freehold (that is, “commonhold”) basis – if Government requires commonhold to be used and bans leasehold; or
 - (b) sometimes be sold on a commonhold basis and sometimes on a leasehold basis – if Government actively incentivises commonhold, but does not go as far as to ban leasehold; or
 - (c) continue (as is presently the case) to be sold on a leasehold basis – if Government takes no action to require or incentivise the use of commonhold and/or does not ban leasehold.
- (3) commonhold will be a viable alternative to leasehold – because our recommendations will make commonhold workable.
- (4) insofar as any homes are sold on a leasehold basis, they will not contain any ground rent obligations – because Government intends to restrict ground rents to zero.⁷

⁶ Subject to exceptions.

⁷ Subject to exceptions.

1.10 As a consequence, for owners of future homes:

- (1) the right for leaseholders to buy the freehold of their house will be largely redundant – because houses in the future will already have been sold freehold;
- (2) if flats are *only* sold on a commonhold basis, the right for leaseholders (i) to extend their lease, (ii) to buy their freehold, or (iii) to take over the management of their block of flats (the RTM), will be redundant – because the flats will already have been sold freehold;
- (3) if flats continue to be sold on a leasehold basis:
 - (a) it will be significantly cheaper for leaseholders to extend the lease of their flat – because (i) restricting ground rents to zero, and (ii) our options for reducing enfranchisement prices, will limit the amount that leaseholders have to pay;
 - (b) it will be significantly cheaper for leaseholders (with their neighbours) to buy the freehold of their block – because (i) restricting ground rents to zero, and (ii) our options for reducing enfranchisement prices, will limit the amount that leaseholders have to pay.
 - (i) Those leaseholders would then be able to convert to commonhold, if they wanted to do so.
 - (ii) Those leaseholders are less likely to want or need to exercise the RTM (which involves taking over the management of a block but not buying the freehold) – because the cost of purchasing the freehold will be significantly cheaper than it is now.

(2) Leasehold owners of existing homes⁸

1.11 While there can be an ambition for freehold to be the basis of home ownership in the future, it is crucial to recognise that leasehold will continue to exist for some time. Many people already own a leasehold home. And some homes may be granted on a leasehold basis in the future – namely (i) any flats granted on a leasehold basis (if commonhold is not required, or sufficiently promoted), and (ii) any houses which are exempt from the leasehold house ban. For those leaseholders:

- (1) it is necessary for various problems with leasehold ownership to be resolved; and
- (2) they will need to have the improved rights that we recommend:
 - (a) to extend their lease or to purchase their freehold, and – in the case of flats – to convert to commonhold; and
 - (b) to take over the management of their block.

⁸ Including leasehold owners of future homes, to the extent that leases are still granted of future homes.

1.12 The recommendations that we make in our reports on enfranchisement and the right to manage will considerably improve the position of existing leaseholders, and any future leaseholders, in a number of respects. In particular:

- (1) a lease extension will result in a lease being extended by 990 years at a peppercorn rent, so that the need to extend a lease only arises once and no ground rent is payable;
- (2) more leaseholders will be able collectively to purchase the freehold of their block or take over the management of the block: leaseholders cannot currently do so if more than 25% of the block is commercial property, and we recommend raising the threshold to 50%;
- (3) it will be possible to purchase the freehold or take over the management of multiple buildings (for example, in an estate);
- (4) the process for making an enfranchisement or RTM claim will be easier, quicker, and cheaper, with procedural traps removed;
- (5) leaseholders making an enfranchisement or RTM claim will no longer have to pay their landlord's costs (in the case of enfranchisement, if Government sets premiums at market value); and
- (6) leaseholders making an enfranchisement claim will be better able to convert from leasehold to commonhold, if they wish to do so.

1.13 In addition, the options for reducing enfranchisement prices in our earlier report would reduce the amount that leaseholders have to pay to extend their lease or purchase their freehold.

Home ownership after reform	Existing homes	Future homes
Houses	Improved rights for leaseholders Existing leaseholders can buy the freehold – and it will be cheaper to do so	New houses are freehold
Flats	Improved rights for leaseholders Existing leaseholders can buy the freehold and convert to commonhold – and it will be cheaper to do so	Government to decide whether commonhold is compulsory, incentivised, or optional Even if leasehold continues, the right to buy the freehold (including converting to commonhold) will be significantly cheaper

PART A: HOW HOME OWNERSHIP CURRENTLY WORKS AND ITS PROBLEMS

Freehold and leasehold ownership

- 1.14 What does “ownership” mean? When an estate agent markets a house or flat as being “for sale”, what is the asset on offer? In England and Wales, property is almost always owned on either a freehold or a leasehold basis.
- (1) Freehold is ownership that lasts forever, and generally gives fairly extensive control of the property.
 - (2) Leasehold provides time-limited ownership (for example, a 99-year lease), and control of the property is shared with, and limited by, the freehold owner (that is, the landlord).
- 1.15 So we refer to “buying” or “owning” a house or a flat. But when we buy on a leasehold basis, we are in fact buying a lease of a house or flat for a certain number of years (after which the assumption is that the property reverts to the landlord). A leasehold interest is therefore often referred to as a wasting asset: while it may increase in value in line with property prices, its value also tends to fall over time as its length (the “unexpired term”) reduces. There comes a point when the remaining length of the lease makes it difficult to sell, because purchasers cannot obtain a mortgage since lenders will not provide a mortgage for the purchase of a short lease.⁹
- 1.16 In addition, leasehold owners often do not have the same control over their home as a freehold owner. For example, they may not be able to make alterations to their home, or choose which type of flooring to have, without obtaining the permission of their landlord. The balance of power between leasehold owners and their landlord is governed by the terms of the lease and by legislation. Recently, concerns have been raised that the lack of control historically associated with leasehold ownership has – in some cases – become a feature of freehold ownership. We return to that issue below.
- 1.17 As well as a division of control, landlords may have different interests from leaseholders. For instance, the landlord may see a leasehold property solely as an investment opportunity or a way of generating income, while for leaseholders the property may be their home as well as a capital investment.

Different types of ownership	Freehold	Leasehold
Duration of ownership	Lasts forever	Time-limited
Control	Generally extensive	Shared with landlord

⁹ If a lease is unmortgageable, and if the leaseholder cannot afford to extend the lease, the leaseholder might be able to sell the lease to a cash-buyer who can afford to pay the landlord to extend the lease. The purchase price would be reduced by (at least) the cost of a lease extension.

- 1.18 In summary, therefore, leasehold does not provide outright ownership. The experience of leasehold owners has been described as being that of “owners yet tenants”.¹⁰ On the one hand, they are homeowners, with some of the benefits that ownership brings, such as a financial stake in the home. On the other hand, they have a landlord who maintains some control over their use of their home, who has a financial interest in their home, and who will ultimately take back the home on the expiry of the lease.

The inherent features of leasehold “provided the impetus for the development of commonhold, and remain at the heart of many criticisms of leasehold. They do not simply suggest the need for tighter regulation of developers and landlords in the interests of their leaseholders. Instead, they call into question the ability of the landlord-tenant relationship to deliver home-ownership, and provide an imperative for a radical increase in the control held by individuals over their homes. This change, which is reflected in the Law Commission’s three residential leasehold and commonhold projects, arguably marks a renewed focus on the home as a vital element in people’s financial and personal autonomy”.¹¹

Leasehold as a valuable asset for landlords

- 1.19 As we go on to explain below, these inherent features of leasehold ownership are the root cause of many criticisms that have been levelled at it as a mechanism to deliver home ownership. Conversely, these features of leasehold ownership are the very reason that it is an attractive investment opportunity, and a valuable asset, for landlords.

- (1) Since a lease is a *time-limited interest*, there will come a point when the leaseholder needs to extend the lease or buy the freehold in order to retain the property. The leaseholder has to pay the landlord in order to do so. In addition, throughout the term of the lease, the leaseholder will usually have to pay ground rent to the landlord, which provides a source of income for landlords.
- (2) The landlord’s *control* over the property provides a further source of income. For example:
 - (a) landlords can charge leaseholders a fee for certain actions, such as giving consent to alterations to a flat, or for registering a change of ownership when a leaseholder sells his or her flat; and
 - (b) landlords can receive income indirectly through the service charge that leaseholders are required to pay for the costs of maintaining their block or estate. For example, the premium for insuring a block will be paid by the leaseholders, but when arranging the insurance policy the landlord might receive a commission from the insurance company. Similarly, the landlord might arrange for the services at a block (such as for

¹⁰ I Cole and D Robinson, “Owners yet tenants: the position of leaseholders in flats in England and Wales” (2000) 15 *Housing Studies* 595.

¹¹ N Hopkins and J Mellor, ““A Change is Gonna Come”: Reforming Residential Leasehold and Commonhold” (2019) 83(4) *Conveyancer and Property Lawyer* 321, 331-322 (“*A Change is Gonna Come* (2019)”).

management, for cleaning, or for repair work) to be undertaken by an associated company.

Why are homes owned on a leasehold basis?

Flats

- 1.20 Flats are almost universally owned on a leasehold, as opposed to freehold, basis. There is a good legal reason for that: certain obligations to pay money or perform an action in relation to a property (such as to repair a wall or a roof) cannot legally be passed to future owners of freehold property. These obligations are especially important for the effective management of blocks of flats. For instance, it is necessary that all flat owners can be required to pay towards the costs of maintaining the block, which is important since flats are structurally interdependent. There are therefore good reasons, under the current law, why flats are sold on a leasehold basis.

Houses

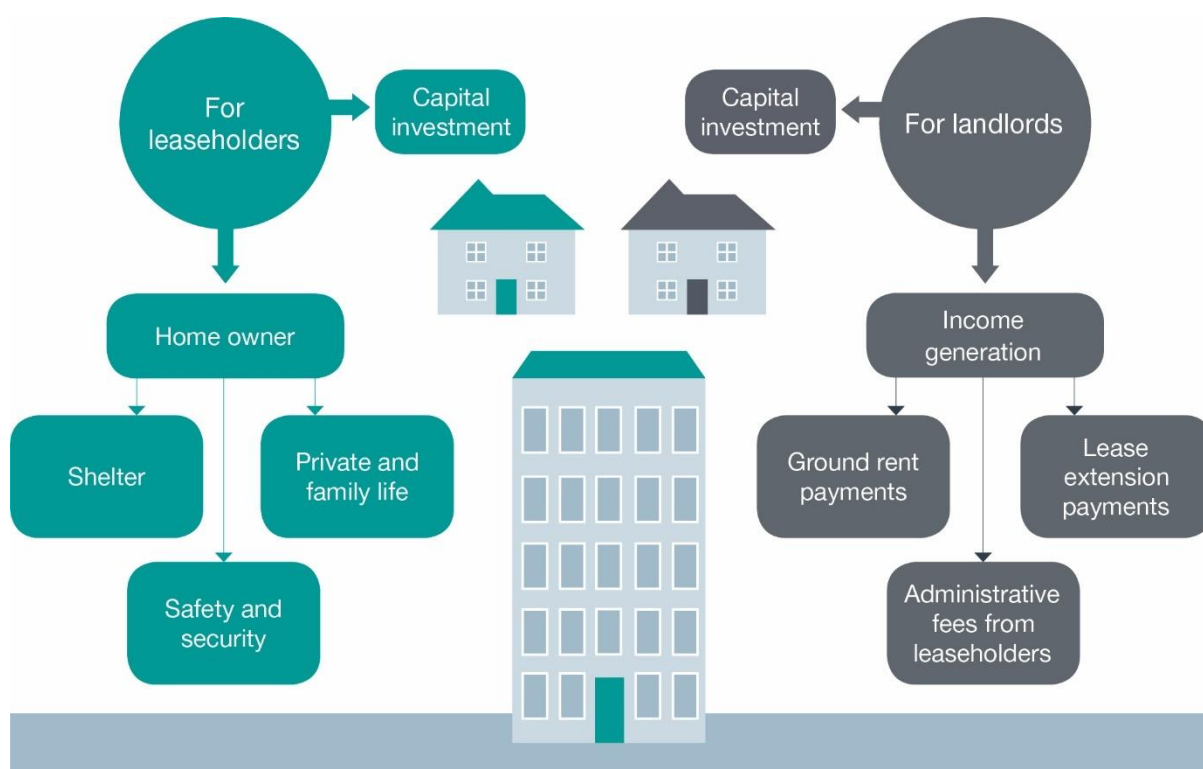
- 1.21 But leasehold ownership is not limited to flats. Sometimes houses are sold on a leasehold basis. That has been the case for some years.¹² More recently there has been an increase in new-build houses being sold on a leasehold basis. That allows developers to sell the property subject to an ongoing obligation to pay a ground rent.
- 1.22 The legal reasons for selling houses on a leasehold basis are less apparent than those for leasehold flats. One reason might be the need to impose positive obligations on house owners in relation to the upkeep (management) of an estate, but that does not apply in all cases.

A source of income

- 1.23 We have explained that there can be good legal reasons why homes are sold on a leasehold basis. The reasons why, for legal purposes, houses and flats may be sold on a long lease do not, however, require the lease to provide income streams to the landlord (see paragraph 1.19 above), beyond those needed to maintain the property, the block, or the estate.

¹² Historically, the sale of houses on a leasehold basis became widespread practice in particular areas of the country.

Figure 1: The purpose of a leasehold home



Leasehold and feudalism

1.24 Leasehold is often referred to as “feudal”. In fact, leasehold developed outside of the main feudal tenures and later in time. Leases began as contracts, not interests in land. But while “feudal” is a misdescription of the landlord-tenant relationship, it is not necessarily a mischaracterisation. The language of “feudalism” reflects the power imbalance experienced by leaseholders, and concerns that the tenure has too readily facilitated the extraction of excessive monetary payments from those leaseholders.¹³

What is wrong with leasehold home ownership?

1.25 Residential leasehold has, for some time, been hitting the headlines and is the subject of an increasingly prominent policy debate. There is a growing political consensus that leasehold tenure is not a satisfactory way of owning residential property.

“too often leaseholders, particularly in new-build properties, have been treated by developers, freeholders and managing agents, not as homeowners or customers, but as a source of steady profit. The balance of power in existing leases, legislation and public policy is too heavily weighted against leaseholders, and this must change”.¹⁴ Housing, Communities and Local Government Select Committee

¹³ *A Change is Gonna Come* (2019).

¹⁴ Housing, Communities and Local Government Committee, Leasehold Reform (2017-19) HC 1468, para 25, at <https://publications.parliament.uk/pa/cm201719/cmselect/cmcomloc/1468/1468.pdf>.

Criticisms based on leasehold ownership being inherently unfair

- 1.26 Many people have a fundamental objection to leasehold being used as a mechanism for delivering home ownership. They argue that the fact that external investors have a financial stake in a person's home – which arises from the time-limited nature of the leaseholder's interest and the control enjoyed by the landlord – creates an inappropriate, unbalanced and inherently unfair starting point for home ownership. Leasehold, it is argued, is fundamentally flawed as a mechanism to deliver the type of home ownership that people want and expect. The solution is said to be for home ownership – of both houses and flats – to be delivered through freehold (including commonhold) ownership.
- 1.27 Arguments about inherent unfairness are compounded by the inequality of arms that exists, broadly speaking, between leaseholders and landlords in the current leasehold regime. It is a systemic inequality between leaseholders (as a whole) and landlords (as a whole), as opposed to an individual inequality as between particular people within those groups. We discussed the inequality of arms, the opposing views on whether leasehold ownership is inherently unfair, and competing arguments about reform in our earlier report on valuation in enfranchisement.¹⁵

Criticisms of ways in which the leasehold market operates

- 1.28 While there is a strong voice that leasehold is inherently unfair and should be replaced with freehold (including commonhold), there are also criticisms of specific aspects of how the leasehold market operates.¹⁶ To those who have a fundamental objection to leasehold, they are all symptoms of what they consider to be an inherently unfair system. But these criticisms are not made solely by those who have a fundamental objection to leasehold; many who do not object to the use of leasehold nevertheless have concerns about aspects of the way that it operates. For example, concerns have been raised about:
- (1) legal, practical and financial obstacles for leaseholders seeking to exercise their statutory rights, including:
 - (a) their right to extend their lease or buy their freehold (that is, their enfranchisement rights);
 - (b) their right to take over management of their block (that is, the RTM);
 - (c) their right to challenge the reasonableness of service charges that have been levied by landlords;

¹⁵ Valuation Report, para 1.71 and 3.45 onwards (on the inequality of arms), para 3.4 onwards (on inherent unfairness), and Ch 3 generally on competing views about reform.

¹⁶ We summarise the wider policy debate in Ch 1 of our Enfranchisement, Commonhold and Right to Manage Consultation Papers, where we refer to media coverage, the activities of campaign groups, Government announcements, the work of the All-Party Parliamentary Group on Leasehold and Commonhold, and various Parliamentary debates about leasehold.

- (d) the “right of first refusal”, which is intended to allow leaseholders whose landlord proposes to sell the freehold of their block of flats to step in to the purchaser’s shoes and themselves purchase the freehold instead;
 - (e) the right to apply to the Tribunal for a manager to be appointed to manage the block instead of the landlord;¹⁷
 - (f) the right to form a recognised tenants’ association, and acquire the contact details of the leaseholders in a block in order to do so;
- (2) high and escalating onerous ground rents, with a particular concern about the imposition of ground rents which double at periodic intervals (generally ten years) during the term of a lease; such obligations can make properties unmortgageable and unsaleable, trapping the owners in their homes;
 - (3) houses being sold on a leasehold, as opposed to freehold, basis, for no apparent reason other than for developers to extract a profit from owning the freehold;
 - (4) the absence of any compulsory regulation of managing agents, either in terms of their qualifications or the quality of their work;
 - (5) excessive service charges levied by landlords;
 - (6) the ability of landlords to require leaseholders to pay all or some of the landlord’s legal costs when there has been a dispute between the parties, including in cases where the leaseholder has “won” a legal challenge against their landlord;
 - (7) the legal entitlement of landlords to “forfeit” (that is, terminate) a lease if the leaseholder breaches a term of the lease;
 - (8) the charging by landlords of unreasonable permission fees for leaseholders to carry out alterations to their property; and
 - (9) close relationships between property developers and particular conveyancers which may threaten the latter’s independence in advising clients seeking to buy leasehold properties from the referring developers.

1.29 The concerns set out above lie against a background, generally speaking, of leasehold purchasers not understanding what leasehold ownership involves.

“For most consumers, buying a house or flat will be their largest purchase and investment. Because it is a relatively infrequent purchase consumers are unlikely to accumulate significant knowledge of the process or of the salient characteristics of different forms of property ownership. Further, while the value of the purchase may make the consumer cautious, the sheer magnitude of the purchase price will typically

¹⁷ The First-tier Tribunal (Property Chamber) in England and the Leasehold Valuation Tribunal in Wales.

make other amounts of money involved seem insignificant by comparison”.
Competition and Markets Authority¹⁸

- 1.30 Further, even when purchasers do understand what leasehold ownership involves, there is often no choice over the form of ownership. As we explained above, flats are almost invariably owned on a leasehold basis.
- 1.31 Some criticisms outlined above can fairly be described as abusive practices by landlords or developers. The Competition and Markets Authority (“CMA”) launched an investigation into leasehold home ownership in 2019 and published an interim report in 2020.¹⁹ The CMA expressed concerns about ground rents in leases, about mis-selling of leasehold houses, about service charges and permission fees, and about a failure of “checks and balances” in the leasehold system. The CMA stated that it intended to take enforcement action in relation to the mis-selling of leasehold property, and in relation to leases containing high and escalating ground rents.
- 1.32 While there have been abusive practices in leasehold, we would emphasise that there are other landlords who operate fairly and transparently. But however fairly the system is operated, inherent limitations of leasehold remain.
- 1.33 All of the criticisms summarised above derive, at least to some extent, from those inherent limitations – namely that the asset is time-limited, and that control is shared with the landlord. Those limitations are compounded by the fact that the landlord and leaseholder have opposing financial interests – generally speaking, any financial gain for the landlord will be at the expense of the leaseholder, and vice versa. Accordingly, the leasehold system has been reformed over the years in an attempt to create an appropriate balance between those competing interests. Given their opposing interests, it is very unlikely that leaseholders and landlords will agree that the balance that has been struck between their respective interests is fair. Their interests are diametrically opposed, and consensus will be impossible to achieve.

“For landlords, property is fundamentally about money: both the capital value in the freehold and the income that is generated from ground rent payments, commissions, enfranchisement premiums and other fees. That is not to say that the profit generated cannot be used for good ends, and landlords come in many guises. ... But the fact remains that the primary value of property to many landlords is financial. And whether a particular landlord has observed better or worse practices does not alter the fact that, systematically, leaseholders still lack autonomy and control over their homes.

For homeowners, the home is also about money, but in a very different sense. It is about having a financial stake in the property in which we live; a stake we are increasingly being asked to draw upon to support us financially into retirement, as well as to support the next generation. But the more a person’s home is used as a financial asset to benefit their landlord, the less it is an investment for the individual. The more a leaseholder’s money is providing an investment for their landlord, the less their

¹⁸ Competition and Markets Authority, *Leasehold housing: update report* (February 2020) para 33, at <https://www.gov.uk/cma-cases/leasehold>.

¹⁹ Competition and Markets Authority, *Leasehold housing: update report* (February 2020).

money is providing an investment for their own future, their family and their next generation.

For homeowners, however, the home is about more than money. Britain has famously been described as a nation of homeowners. Fulfilling the dream of home-ownership has long been many people's ambition. Much of this ambition can be attributed to the non-financial, "x-factor" values that home-ownership encompasses, and which have become embedded in an ideology of home ownership. Our home is the focal point of our private and family lives; it is integral to our identity, reflecting who we are and the community we belong to. Bad law and bad practice that affect people's experience in their home therefore have a particular impact on them. The current programme of law reform marks an opportunity to reform the law so that it can better deliver both the financial and non-financial benefits of home ownership".²⁰

Freehold ownership of flats: commonhold

- 1.34 In many countries, leasehold ownership does not exist. Instead, forms of "strata" or "condominium" title are used so that flats can be owned on a freehold basis.
- 1.35 In England and Wales, commonhold was introduced as an alternative to leasehold in 2002, to enable the freehold ownership of flats.²¹ Commonhold allows the residents of a building to own the freehold of their individual flat (called a "unit") and to manage (or appoint someone to manage) the shared areas through a company. For many blocks, the homeowners would not themselves carry out the day-to-day management but would instead appoint agents to manage the block. Crucially, however, the homeowners (rather than an external landlord) would control the appointment of those agents.
- 1.36 For homeowners, commonhold offers a number of advantages over leasehold ownership. In particular:
- (1) it allows a person to own a flat forever, with a freehold title – unlike a leasehold interest, which will expire at some point in the future;
 - (2) no ground rent is payable;
 - (3) it gives the homeowner greater control of their property than leasehold; and
 - (4) it is designed to regulate the relationship between a group of people whose interests are broadly aligned. That is in stark contrast to the leasehold regime, which has to attempt to balance and regulate the competing interests of landlord and leaseholder.

²⁰ *A Change is Gonna Come* (2019), 330-331.

²¹ Commonhold was created by the Commonhold and Leasehold Reform Act 2002. While primarily designed to enable the freehold ownership of flats, commonhold is equally capable of applying in a commercial context. It can, for example, regulate the relationship between individually owned offices within an office block.

- 1.37 Despite these apparent advantages, however, commonhold has not taken off – fewer than 20 commonholds have been created since the commonhold legislation came into force.²²

Why has commonhold failed?

- 1.38 Various suggestions have been made as to why commonhold has not taken off.

- (1) Some have suggested that shortcomings in the law governing commonhold can make it unworkable in practice and have led to a lack of confidence in commonhold as a form of ownership.
- (2) Some ascribe commonhold's low uptake to an unwillingness of mortgage lenders to lend on commonhold units.
- (3) Some think that there may be a lack of consumer and sector-wide awareness of what is a relatively unfamiliar form of ownership.
- (4) Others point out that commonhold remains less attractive to developers than leasehold because of the opportunities that leasehold offers to secure ongoing income-streams on top of the initial purchase price paid by the leaseholders.
- (5) Others point out that Government provided no incentives for developers to use commonhold – and no disincentives to them continuing to use leasehold (for example, by removing the financial advantages for developers of selling leasehold flats).
- (6) Others suggest that the low uptake is more the result of inertia among professionals and developers. Moreover, we have been told that there is insufficient incentive (financial or otherwise) for developers of homes and commercial property to change their practices and adopt a whole new system while the existing one (from their perspective at least) does the job.

Stewardship and culture change²³

- 1.39 A common thread that runs through all three of our projects is moving management and control from a third-party landlord to homeowners. But it is in relation to commonhold that the management of land has come under the greatest scrutiny, because of the removal of the relationship of landlord and tenant. This shift from leasehold to freehold tenure has raised questions as to the stewardship of land and the utility of the landlord-tenant relationship in the residential context. Stewardship is not always defined, but in this context, we use the term to mean the management of land over time and for the next generation of owners. It has been suggested that landlords are necessary to provide stewardship over residential property. Institutional landlords are said to act as custodians who take a long-term view of the investments needed in a building or estate.²⁴ Such landlords are also said to have superior

²² L Xu, "Commonhold Developments in Practice" in W Barr (ed), *Modern Studies in Property Law: Volume 8* (2015) p 332.

²³ Taken from *A Change is Gonna Come* (2019), 328-329.

²⁴ Housing, Communities and Local Government Committee, Leasehold Reform (2017-19) HC 1468, para 81.

expertise in overseeing insurance, maintenance, health and safety, fire risks, planning obligations, building regulations and anti-social behaviour.²⁵

- 1.40 But this argument must address the following challenge: if owners of houses are trusted to be the stewards of their house, why can owners of flats not be similarly trusted? While leaseholders have a shorter-term interest than their landlords, it is the term of the lease granted by the landlord that so constrains them. There is no reason to assume that leaseholders would not have the same incentives as landlords presently do if they had the same enduring financial stake.²⁶ The management of a block is undoubtedly more complex than that of an individual house. It is not suggested that commonhold unit owners themselves will personally take charge. In all but small blocks, where self-management is a realistic choice, the expectation is that professional managers will be appointed.
- 1.41 This insistence on the necessity of landlord freeholders to provide inter-generational stewardship of a building or estate is symptomatic of a broader issue. The reform of leasehold, and particularly the reinvigoration of commonhold, bring about a need for cultural change, and for all participants in the housing market to re-think fundamental assumptions on which the market currently operates.
- 1.42 It has been suggested, for example, that developers will not build unless there is a professional landlord in place to manage the development. This ignores the fact that commonhold structures are used around the world and that large, mixed-use developments are built in those jurisdictions. It is also argued that commonhold owners will not take an active interest in the management of their block. Such arguments operate on the assumption that flat owners are ultimately apathetic about how their buildings or estates are run.²⁷ While commonhold is about empowering and giving responsibility to owners of flats, it is also about owners of flats being ready to accept responsibility and therefore being ready to take on that cultural change. Law reform must be matched by changes in people's expectations of what home-ownership will involve. It should not be assumed that apathy generated in a leasehold system – where the long-term financial investment and control of a building lie with an external third party – will carry over into a system in which, from the outset, investment and control lie with the unit owners.
- 1.43 In summary, therefore, commonhold should not be looked at through the lens of leasehold. Commonhold involves a culture change. It moves away from an “us and them” mindset, towards “us and ourselves”.

²⁵ See, for example, <https://wslaw.co.uk/wp-content/uploads/2019/07/LR-December-Bulletin-2018.pdf>, p 3.

²⁶ S Bright, “Do freeholders provide a unique and valuable service?” (2019) at <https://www.law.ox.ac.uk/housing-after-grenfell/blog/2019/04/do-freeholders-provide-unique-and-valuable-service>.

²⁷ Housing, Communities and Local Government Committee, Leasehold Reform (2017-19) HC 1468, para 17.

PART B: LAW COMMISSION AND GOVERNMENT RECOMMENDATIONS FOR REFORM

The impact of COVID-19

- 1.44 The final stage of the preparation of our reports has been undertaken against the backdrop of the COVID-19 pandemic. In common with many people in England and Wales, Law Commission staff and Commissioners found themselves working from, as well as living in, their homes, as everybody limited contact with others to benefit the health of their communities. It is a reminder of the huge importance that a home plays in a person's life, and that individuals must work together to build and get the most out of a community. A significant part of our current work reforming leasehold and commonhold has been aimed at making sure that there exist the right tools to ensure homeowners have the comfort and certainty that they need to enjoy their homes into the future, and, where homes form part of bigger developments, the right people are involved in the decisions that enable their communities to flourish.

Law Commission recommendations for leasehold and commonhold reform

- 1.45 We have published a suite of final reports on our three projects:

- (1) leasehold enfranchisement;
- (2) the right to manage; and
- (3) commonhold.

- 1.46 Our three projects fall into two categories.

- (1) Improving leasehold: our recommendations about leasehold enfranchisement and the right to manage are aimed at improving the existing system of leasehold ownership, to make it easier, quicker and cheaper to exercise leasehold rights.

Our starting point in these projects is the fact that leasehold ownership exists. Our recommendations are aimed at improving the law governing leasehold ownership.

- (2) Reinvigorating commonhold, so that leasehold is no longer needed: our recommendations about commonhold are aimed at creating a workable alternative to leasehold ownership, with a view to its widespread use in the future.

Once we have commonhold in a way that works ... we do not need long residential leases. Commonhold solves the two underlying concerns that we hear about leases. ... Once commonhold is there and it is working, if you want a system of ownership that removes those underlying concerns with leasehold,

you can use commonhold”. Professor Nick Hopkins, evidence to the Housing Select Committee²⁸

Our starting point in this project is that it is not necessary for leasehold to be used as the mechanism for delivering home ownership. Rather, commonhold can be used instead, and we would go as far as to say that it should be used in preference to leasehold, because it overcomes the inherent limitations of leasehold ownership set out above. But commonhold can only replace leasehold if it is workable in practice.

“The right to manage and enfranchisement ... mitigate the systemic difficulties with leasehold. But commonhold alone removes those difficulties, delivering freehold ownership of individual flats or units, and collective freehold ownership and management of the common parts”.²⁹

1.47 We summarise our three projects below.

Our Terms of Reference

1.48 The Terms of Reference for all three of our projects include two general policy objectives identified by Government, which are:

- (1) to promote transparency and fairness in the residential leasehold sector; and
- (2) to provide a better deal for leaseholders as consumers.

1.49 Our Terms of Reference include specific provisions for each of our projects, which we set out in the following chapter and in Appendix 1 to our reports.

1.50 Our Terms of Reference are not neutral. They require us to make recommendations that would alter the law in favour of leaseholders. They indicate a policy conclusion reached by Government that the leasehold system in its current form is not a satisfactory way of owning homes.

1.51 We set out many criticisms of leasehold above. Some amount to abusive practices, which have often been a focus of concern (particularly in media reports). But the reform of leasehold is not intended simply to remove abuse. Those practices have served to highlight long-standing concerns with leasehold. Government’s work and our recommendations for reform are therefore not confined simply to removing abuses. Our Terms of Reference refer generally to providing “a better deal for leaseholders as consumers”. Our recommendations for reform are therefore intended to make the law work better for all leaseholders.

²⁸ Housing, Communities and Local Government Committee, Oral evidence: Leasehold reform (2017-19) HC 1468), response to Question 456, at <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housing-communities-and-local-government-committee/leasehold-reform/oral/95161.pdf>.

²⁹ *A Change is Gonna Come* (2019), 328.

Improving leasehold: reform of leasehold enfranchisement

- 1.52 Leasehold enfranchisement is the process by which leaseholders may extend the lease, or buy the freehold. In order to exercise enfranchisement rights, leaseholders must pay a sum of money (“a premium”) to their landlord.³⁰
- 1.53 We make recommendations for a brand-new, reformed enfranchisement regime. We recommend that the enfranchisement rights, and the leaseholders who qualify for them, should be expanded, improved, simplified and rationalised. And we recommend that the process that leaseholders must follow to exercise enfranchisement rights should be improved and simplified, and that the costs that leaseholders incur doing so should be reduced.
- 1.54 We previously published our final report concerning one aspect of leasehold enfranchisement, namely the amount that leaseholders must pay to their landlords in order to make an enfranchisement claim.³¹ As required by our Terms of Reference, we set out the options for Government to reduce the premiums paid by leaseholders.

Improving leasehold: reform of the right to manage

- 1.55 The right to manage is a right for leaseholders to take over the management of their building without buying the freehold. They can take control of services, repairs, maintenance, improvements, and insurance.
- 1.56 We make recommendations which will make the RTM more accessible, less confusing, and more certain. Our recommendations would simplify and liberalise the criteria that govern which properties may be subject to an RTM claim. We have designed a new process by which information and claims are exchanged between leaseholders, landlords, and RTM companies to clear the procedural thicket which currently plagues the regime but also will facilitate better communication between all parties. We also recommend that RTM companies should not be required to cover any non-litigation costs incurred by the landlord as a result of an RTM claim.

The alternative to leasehold: reinvigorating commonhold

- 1.57 We explain above that commonhold allows for the freehold ownership of flats (and other interdependent properties), offering an alternative way of owning property which avoids the shortcomings of leasehold ownership.
- 1.58 We also summarised some of the reasons why commonhold is said to have failed in paragraph 1.38 above.
- 1.59 Our project seeks to address the first suggested barrier to the uptake of commonhold in paragraph 1.38 above: perceived shortcomings in the legal design of the commonhold scheme. Our project analyses which aspects of the law of commonhold have so far impeded commonhold’s success, for example by affecting market confidence, or making it unworkable. In accordance with our Terms of Reference, we

³⁰ There is an exception: leaseholders of houses can extend their lease without paying a premium but instead paying a higher annual rent. See para 2.8(2) of the Enfranchisement Report.

³¹ Valuation Report.

recommend reforms to reinvigorate commonhold as a workable alternative to leasehold, for both existing and new homes.

- 1.60 Other barriers to the uptake of commonhold, including those identified in paragraph 1.38 above, are not problems with the law and do not fall within our Terms of Reference.³² They are issues which Government is considering – and Government therefore has a crucial role in seeking to reinvigorate commonhold as a mechanism for delivering home ownership.

Government proposals for leasehold and commonhold reform

- 1.61 Improving and facilitating home ownership is a priority for Government, and – as part of that – reform of residential leasehold and commonhold law has become an increasing priority. The UK Government and Welsh Government have announced various proposals for reform. Our recommendations for reform will be considered by both Governments as part of their overall programmes of reform.
- 1.62 We summarise Government’s current proposals for reform below. We do not comment on those proposals. They are all matters which fall outside the scope of our projects. Nevertheless, it is important to explain those proposals in order to explain how all proposed reforms (including those that we recommend) fit together.

Ministry of Housing, Communities and Local Government

- 1.63 The Ministry of Housing, Communities and Local Government (“MHCLG”) has announced its intention to bring forward the following measures.³³
- (1) For the future, banning the sale of houses on a leasehold basis, other than in exceptional circumstances.³⁴ As we explain further below, the only good legal reason for selling houses on a leasehold basis – namely ensuring that owners on an estate will contribute to (reasonable) shared costs – would be provided by the creation of “land obligations”: see paragraph 1.63(11) below.

³² Our project did, however, provide an opportunity to gather evidence on these wider measures to reinvigorate commonhold, and we report on them in our Commonhold Report.

³³ See: (1) Department for Communities and Local Government (“DCLG”), *Tackling unfair practices in the leasehold market: A consultation paper* (July 2017) (“*Tackling unfair practices consultation, July 2017*”); (2) DCLG, *Tackling unfair practices in the leasehold market: Summary of consultation responses and Government response* (December 2017) (“*Tackling unfair practices response, December 2017*”); (3) MHCLG, *Implementing reforms to the leasehold system in England: A consultation* (October 2018) (“*Implementing reforms consultation, October 2018*”); (4) MHCLG, *Implementing reforms to the leasehold system in England: Summary of consultation responses and Government response* (June 2019) (“*Implementing reforms response, June 2019*”); and (5) MHCLG, *Government response to the Housing, Communities and Local Government Select Committee report on leasehold reform* (July 2019) (“*Response to Select Committee, July 2019*”). (1) and (2) are at <https://www.gov.uk/government/consultations/tackling-unfair-practices-in-the-leasehold-market>; (3) and (4) are at <https://www.gov.uk/government/consultations/implementing-reforms-to-the-leasehold-system>; (5) is at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/814334/CS0519270992-001_Gov_Response_on_Leasehold_Reform_Web_Accessible.pdf.

³⁴ *Implementing reforms response, June 2019*, Ch 2. The ban would apply, predominantly, to houses that are built in the future. The ban on the grant of leases of houses would, however, also prevent the grant of a *new* lease over an *existing* house. The ban would not apply to existing leases of houses.

- (2) For the future, when homes are sold on a leasehold basis (which, following the leasehold house ban, will predominantly be flats), restricting ground rents to zero in those leases.³⁵
- (3) Regulation of the property agent sector, including letting, managing and estate agents through mandatory licensing, mandatory codes of practice, new qualifications provisions and a new regulator with a range of enforcement options.³⁶
- (4) Consideration of reform of the regulation of the service charges that leaseholders must pay, including the requirements to consult with leaseholders before incurring expenditure on major works or on long-term contracts.³⁷
- (5) Reviewing the ability of landlords to charge leaseholders permission fees under long leases, such as fees for permission to make alterations to the property.³⁸
- (6) Reviewing the circumstances in which leaseholders are required to contribute to their landlord's legal costs.³⁹
- (7) Requesting that the Law Commission update its previous recommendations to abolish forfeiture.⁴⁰
- (8) Protecting leaseholders from losing their homes for small sums of rent arrears.⁴¹
- (9) Reviewing loopholes in the "right of first refusal".⁴²
- (10) Implementation of most of the Law Commission's recommendations on fees charged in leasehold retirement properties ("event fees"), including limiting the

³⁵ *Implementing reforms response*, June 2019, Ch 3.

³⁶ The proposals included plans for a mandatory code of practice covering letting and managing agents and nationally recognised qualification requirements for letting and managing agents to practise. In addition, an independent regulator was proposed which would oversee both the code of practice and the delivery of the qualifications: DCLG, *Protecting consumers in the letting and managing agent market: call for evidence* (October 2017), and MHCLG, *Protecting consumers in the letting and managing agent market: Government response* (April 2018). A working group chaired by Lord Best was subsequently tasked with "considering the entire property agent sector to ensure any new framework, including any professional qualifications requirements, a Code of Practice, and a proposed independent regulator, is consistent across letting, managing and estate agents": see: *Regulation of property agents working group – final report* (July 2019), at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/818244/Regulation_of_Property_Agents_final_report.pdf.

³⁷ *Response to Select Committee*, July 2019, pp 25-29.

³⁸ *Response to Select Committee*, July 2019, pp 23-24.

³⁹ *Response to Select Committee*, July 2019, p 29.

⁴⁰ *Response to Select Committee*, July 2019, pp 29-30. We have previously recommended that forfeiture be abolished and replaced with a regime to enforce the terms of leases in a proportionate way: *Termination of Tenancies for Tenant Default* (2006) Law Com No 303.

⁴¹ *Tackling unfair practices response*, December 2017, Ch 4.

⁴² *Response to Select Committee*, July 2019, p 13. We explain the right of first refusal in para 1.28(1)(d) above.

circumstances in which event fees can be charged and requiring the disclosure of information to prospective purchasers.⁴³

- (11) To support the leasehold house ban, relying on the implementation of the Law Commission's recommendations to reform property law, including introducing "land obligations" and reforming the way in which rights over land are created, varied, terminated and regulated.⁴⁴
- (12) Extending mandatory membership of a redress scheme to landlords who do not use managing agents.⁴⁵
- (13) Setting a cap on what leaseholders can be charged for the provision of information about the lease to potential purchasers, and a minimum time within which the information must be provided.⁴⁶
- (14) Extending rights currently enjoyed by leaseholders to freeholders of houses – in particular:
 - (a) extending the right to challenge charges for the maintenance of an estate where they are unreasonable, as well as allowing freeholders of houses to apply to change their managing agent;⁴⁷
 - (b) protecting freeholders from losing their homes for unpaid service charges which are owed as "rentcharges";⁴⁸
 - (c) reforming the "right of first refusal" by extending the right to leaseholders of houses;⁴⁹ and
 - (d) considering regulating the ability of developers and others to charge homeowners permission fees, such as to make alterations to their property.⁵⁰

⁴³ Letter from Heather Wheeler MP, then Minister for Housing and Homelessness, to the Rt Hon Lord Justice Green, Chair of the Law Commission, 27 March 2019, at <https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jsxou24uy7q/uploads/2017/03/Letter-from-Mrs-Heather-Wheeler-MP.pdf>.

⁴⁴ *The Queen's Speech 2016*, p 61, at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/524040/Queen_s_Speech_2016_background_notes_.pdf; *Tackling unfair practices response, December 2017*, para 36; and *Implementing reforms consultation*, October 2018, para 2.21. See also *Making Land Work: Easements, Covenants and Profits À Prendre* (2011) Law Com No 327.

⁴⁵ MHCLG, *Strengthening consumer redress in the housing market* (January 2019), para 123, at <https://www.gov.uk/government/consultations/strengthening-consumer-redress-in-housing>.

⁴⁶ *Implementing reforms response, June 2019*, Ch 5, which sets out proposals for a cap of £200 plus VAT and a timeframe of 15 working days.

⁴⁷ *Tackling unfair practices response, December 2017*, Ch 5; *Implementing reforms response, June 2019*, Ch 4.

⁴⁸ *Tackling unfair practices response, December 2017*, para 81.

⁴⁹ *Implementing reforms response, June 2019*, paras 2.34-2.35; *Response to Select Committee, July 2019*, p 13.

⁵⁰ *Response to Select Committee, July 2019*, pp 23 to 24.

- (15) Ensuring the New Homes Ombudsman is created and requiring developers of new-build homes to belong to it, which would provide new-build homebuyers with an effective route to resolve disputes, avoiding the need to go to court.⁵¹
- (16) Considering the case for creating a Single Housing Court, to see whether it could make it easier for all users of court and tribunal services to resolve disputes, reduce delays and to secure justice in housing cases.⁵²

1.64 Some measures have already been implemented.

- (1) Changes have been made to the recognition of residents' associations, to require landlords to provide residents' associations with information about leaseholders.⁵³
- (2) A Government-backed pledge, designed to help leaseholders with onerous ground rent terms, has been agreed by many landlords, developers, conveyancers and managing agents.⁵⁴
- (3) Restrictions are to be placed on the properties that qualify for support from the Help to Buy scheme in England, reflecting the leasehold house ban and the restriction of ground rents to zero.⁵⁵
- (4) Government has committed that no new scheme will fund the building of leasehold houses.⁵⁶

⁵¹ MHCLG, *Redress for purchasers of new build homes and the New Homes Ombudsman: technical consultation* (June 2019) and *Government response* (February 2020), at <https://www.gov.uk/government/consultations/redress-for-purchasers-of-new-build-homes-and-the-new-homes-ombudsman>.

⁵² MHCLG, *Considering the case for a Housing Court – A Call for Evidence* (November 2018), at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/755326/Considering_the_case_for_a_housing_court.pdf.

⁵³ The Tenants' Associations (Provisions Relating to Recognition and Provision of Information) (England) Regulations SI 2018 No 1043. The regulations are intended to make it easier for residents' associations to contact leaseholders, increasing the likelihood of those leaseholders becoming members of the association. This affects the chances of the association being formally recognised under s 29(1) of the Landlord and Tenant Act 1985, which improve if a higher percentage of the leaseholders are members. For background, see s 130 of the Housing and Planning Act 2016; DCLG, *Recognising residents' associations, and their power to request information about tenants* (July 2017), at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/632116/s130_HPAAct_consultation.pdf.

⁵⁴ MHCLG, *Public pledge for leaseholders* (27 June 2019), at <https://www.gov.uk/government/publications/leaseholder-pledge/public-pledge-for-leaseholders>.

⁵⁵ *Tackling unfair practices response, December 2017*, para 47; MHCLG, *Leasehold axed for all new houses in move to place fairness at heart of housing market* (27 June 2019), at <https://www.gov.uk/government/news/leasehold-axed-for-all-new-houses-in-move-to-place-fairness-at-heart-of-housing-market>; MHCLG, *Housing Secretary clamps down on shoddy housebuilders* (24 February 2020), at <https://www.gov.uk/government/news/housing-secretary-clamps-down-on-shoddy-housebuilders>

⁵⁶ MHCLG, *Funding for new leasehold houses to end* (2 July 2018), at <https://www.gov.uk/government/news/funding-for-new-leasehold-houses-to-end>.

1.65 In addition, commonhold has been brought back on to the political agenda. MHCLG has stated that, in addition to pursuing leasehold reform:

we also want to look at ways to reinvigorate commonhold. ... This will help ensure that the market puts consumers' needs ahead of those of developers or investors. We will also look at what more we can and should do to support commonhold to get off the ground working across the sector, including with mortgage lenders.⁵⁷

Welsh Government

1.66 The Welsh Government has imposed restrictions on properties that qualify for support from the Help to Buy Wales scheme, namely that houses should generally be sold on a freehold basis and that ground rents should be restricted.⁵⁸ At the same time, a Help to Buy Wales conveyancer accreditation was introduced, and the use of an accredited conveyancer was made mandatory for sales through the scheme, to ensure a minimum level of information is given to purchasers on a range of issues, including information about leasehold. In addition, the major developers operating in Wales pledged not to use leasehold for new-build houses, whether sold through the Help to Buy scheme or otherwise.⁵⁹

1.67 In addition, the Welsh Government established a working group on leasehold reform. The group's report, published in 2019, made a wide range of recommendations, including recommendations to:⁶⁰

- (1) legislate to ban the unjustified use of leasehold in new-build houses, with some exceptions;
- (2) legislate to ban onerous ground rents and implement the reduction of future ground rents to a nominal financial value;
- (3) improve education and awareness for all participants in the property market;
- (4) improve transparency for consumers with respect to the obligations that burden a leasehold or freehold property at the point of sale; and
- (5) introduce an updated Code of Practice in Wales for the licensing and accreditation of managing agents.

1.68 The Welsh Government has also published a Call for Evidence to better understand how private housing estates are maintained through the payment of estate service charges by homeowners and residents. The evidence base collected by this process

⁵⁷ *Tackling unfair practices response*, December 2017, p 25.

⁵⁸ Developers have to present genuine reasons for a house to be marketed as leasehold. In addition, starting ground rents need to be limited to a maximum of 0.1% of the property's sale value and leasehold agreements have to have a minimum term of 125 years for flats and 250 years for houses.

⁵⁹ *Written Statement: Leasehold Reform in Wales* (6 March 2018), at <https://gov.wales/written-statement-leasehold-reform-wales>.

⁶⁰ *Residential Leasehold Reform – A Task and Finish Group Report*, pp 21-22, at <https://gov.wales/independent-review-residential-leasehold-report>. See also *Written Statement: Response to Report of the Task and Finish Group on Leasehold Reform* (6 February 2020), at <https://gov.wales/written-statement-response-report-task-and-finish-group-leasehold-reform>.

will then be used by the Minister for Housing and Local Government to consider the case for reform.⁶¹

PART C: THE BIG PICTURE – HOW THE VARIOUS REFORM PROPOSALS FIT TOGETHER

Introduction

1.69 In Part B, we have summarised the areas in which we are recommending reform, and we have summarised (without commenting on) Government’s proposals for reform. We now explain how all those proposed reforms fit together.

1.70 It is important to look at existing and future home owners. Reform must cater for the needs of:

- (1) Leaseholders of existing homes: reform must cater for the needs of the leaseholders of existing houses and flats, as well as the future owners of those homes.⁶² It is estimated that there are at least 4.3 million leasehold homes in England alone.⁶³
- (2) Owners of future homes: reform must cater for the needs of the owners of houses and flats that are built in the future: 178,000 new-build properties were completed in England in 2019, of which 78% were houses and 22% were flats.⁶⁴

“The work of the Law Commission and of the Government brings onto the horizon an unprecedented level of reform of residential leasehold and commonhold. Lying at the heart of the work is an acknowledgement that leasehold home ownership has failed to deliver the benefits associated with being an owner, and that the systemic problems with leasehold mean that the tenure is ill-equipped to do so”.⁶⁵

Overall aim: fit-for-purpose home ownership

1.71 The aim of all the proposed reforms can be summarised as seeking to create fit-for-purpose home ownership.

1.72 There are two strands to that work:

⁶¹ Welsh Government, *Estate charges on housing developments: call for evidence* (February 2020), at <https://gov.wales/sites/default/files/consultations/2020-02/estate-charges-on-housing-developments.pdf>.

⁶² In addition, it is necessary to consider leasehold owners of future homes, to the extent that leases are still granted in the future.

⁶³ MHCLG, *Estimating the number of leasehold dwellings in England 2017-2018* (26 September 2019), at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/834057/Estimating_the_number_of_leasehold_dwellings_in_England__2017-18.pdf.

⁶⁴ MHCLG, *House building: new build dwellings, England: December Quarter 2019* (26 March 2020), at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/875361/House_Building_Release_December_2019.pdf.

⁶⁵ *A Change is Gonna Come* (2019), 330.

- (1) paving the way for the future: laying the foundations for homes to be able to be owned as freehold; and
- (2) essential reform of leasehold: addressing problems for leaseholders in the present.

(1) Paving the way for the future: laying the foundations for homes to be able to be owned as freehold

Owners of future homes

- 1.73 MHCLG's proposed ban on *houses* being sold on a leasehold basis (see paragraph 1.63(1) above) will ensure that, in the future, houses will be sold on a freehold basis (subject to exceptions). Accordingly, houses that are built in the future will predominantly be owned on a freehold basis.
- 1.74 By implementing our recommendations for the creation of land obligations, there would no longer be any reason – from a legal point of view – for selling houses on a leasehold basis. That is because land obligations would allow for freehold owners to be subject to positive obligations. Land obligations would be a rational and controlled mechanism for requiring payments to be made.
- 1.75 Turning to future *flats*, as recorded in our Terms of Reference, Government wishes to reinvigorate commonhold as a workable alternative to leasehold. Our recommendations to reform the law of commonhold will overcome the defects in the current legal regime so that commonhold can be used with confidence.
- 1.76 In the future, the sale of all flats could be on a commonhold basis, rather than as leasehold (as is invariably the case currently).⁶⁶ The Law Commission's reforms will ensure that commonhold is workable and flexible enough to cater for the wide range of modern-day developments.

We urge the Government to ensure that commonhold becomes the primary model of ownership of flats in England and Wales, as it is in many other countries. ... there is no reason why the majority of residential buildings could not be held in commonhold; free from ground rents, lease extensions, and with greater control for residents over service charges and major works. We are unconvinced that professional freeholders provide a significantly higher level of service than that which could be provided by leaseholders themselves". Housing, Communities and Local Government Committee⁶⁷

- 1.77 If commonhold is not used (or if it is used only in some cases), the 40,000 or so flats built each year (or some of them) will continue to be sold on a leasehold basis, with the inherent limitations of leasehold.
- 1.78 Developers and other property-owners are currently incentivised to sell flats on a leasehold basis. As we explained in paragraph 1.19 above, the freehold is a valuable asset for the developer because it provides a steady income from ground rents,

⁶⁶ We refer to the sale of flats to cover (a) the sale, for the first time, of new-build flats, and (b) the sale of *existing* flats which are not already subject to a long lease, such as where a freehold owner splits a house into multiple flats and sells the individual flats.

⁶⁷ Housing, Communities and Local Government Committee, Leasehold Reform (2017-19) HC 1468, p 3.

income from lease extension premiums, and other income from the leaseholders. Developers can therefore sell the flats that they build twice: they sell a long lease to the homeowner, and they can sell the freehold to an investor. By contrast, commonhold flats can only be sold once – to the homeowner. Developers therefore have no incentive to adopt commonhold. The restriction of ground rents to zero will remove one significant incentive to sell flats on a leasehold basis, since a developer will not receive (or be able to sell) a steady ground rent income. However, the freehold will continue to be valuable, because enfranchisement premiums might be paid and there may be additional income to be gained from owning the freehold. Accordingly, the incentive will remain to sell flats on a leasehold basis. Moreover, given the limited consumer awareness about commonhold, there may not be sufficient consumer demand to act as a catalyst for change. Even if such demand were to exist, the fact that demand for housing outstrips supply means that prospective homeowners do not have the bargaining power to demand commonhold flats.⁶⁸

- 1.79 We summarise in Appendix 3 to our Commonhold Report what consultees said about the steps that would be necessary to reinvigorate commonhold.
- 1.80 Based on the evidence that we have gathered during our projects, we have concluded that commonhold will not be used unless (a) it is made compulsory, or (b) adequate incentives are put in place to make it more attractive to developers than leasehold (or conversely that leasehold is disincentivised sufficiently to make it less attractive than commonhold). Commonhold will not take root on its own. There is no reason why developers will start selling commonhold flats for so long as there is more money to be made by selling leasehold flats.
- 1.81 Developers have had the option of using commonhold or leasehold for over 15 years, but have almost invariably used leasehold. Commonhold was not pushed by Government. Unless it is encouraged, or mandated, there is no reason to believe that the outcome will be any different from when it was first introduced. But the consequences may be even graver. For those who object to commonhold, and prefer leasehold, a second apparent “failure” of the commonhold model is likely to be claimed to be a reason that commonhold cannot and will not work. That, in our view, would be a very unfortunate outcome, and would do a great disservice to current and future homeowners. Commonhold is used around the world; it can and does work. But for so long as there is more money to be made from leasehold, and unless initial impetus can be given to overcome inherent inertia and a lack of awareness, it is not going to take root on its own. Without Government intervention, commonhold simply cannot compete with leasehold.
- 1.82 Accordingly, while implementation of our recommendations on commonhold reform is necessary for the reinvigoration of commonhold, it will not be sufficient on its own to do so.

⁶⁸ House of Commons Library Briefing Paper, *Tackling the under-supply of housing in England* (2020), <http://researchbriefings.files.parliament.uk/documents/CBP-7671/CBP-7671.pdf>; Welsh Government, *Delivering More Homes for Wales: Report of the Housing Supply Task Force* (2014), at <https://gov.wales/sites/default/files/publications/2019-04/delivering-more-homes-for-wales-recommendations.pdf>.

- 1.83 For houses, Government has decided to ban the use of leasehold, so that freehold ownership is used.⁶⁹ That policy can be pursued because the legal mechanisms for owning houses on a freehold basis already exist (subject, to some extent, to the creation of land obligations: see paragraph 1.63(11) above). It would be a logical extension of that policy to ban the use of leasehold for flats, so that commonhold (freehold) ownership is used instead – once a workable legal mechanism exists. Our recommendations to reform commonhold would create that workable legal mechanism, and so banning the use of leasehold for flats becomes a realistic possibility.
- 1.84 As well as the direct loss of income that developers would suffer by selling flats on a commonhold basis, they would also have to adapt to an unfamiliar ownership model. This was one of the other barriers to the success of commonhold noted in paragraph 1.38 above, alongside inertia amongst professionals, a lack of sector-wide and consumer awareness, and caution on the part of mortgage lenders. These barriers to the uptake of commonhold all require Government intervention if they are to be overcome.
- 1.85 Government must therefore decide:
- (1) whether there should be an equivalent of the leasehold house ban for flats, so that flats cannot be sold on a leasehold basis in the future but must instead be sold on a commonhold basis. Put another way, commonhold could be made compulsory; or
 - (2) whether developers and other property-owners should (as is currently the case) be left to choose between using leasehold or commonhold for the sale of flats, and if so:
 - (a) whether – and how – the sale of flats on a commonhold basis should be incentivised; and/or
 - (b) whether – and how – the sale of flats on a leasehold basis should be disincentivised; and
 - (3) what measures it will adopt in order to overcome the other practical barriers to commonhold, in particular a lack of awareness, and caution and inertia amongst developers, lenders and professionals.

Leaseholders of existing homes

- 1.86 For leaseholders of existing houses,⁷⁰ our recommendations to reform the enfranchisement regime will provide improved rights to acquire the freehold (an “individual freehold acquisition”), and therefore move away from leasehold ownership to freehold ownership.

⁶⁹ Subject to exceptions.

⁷⁰ Including leaseholders of any future houses that are sold on a leasehold basis.

- 1.87 For leaseholders of existing flats,⁷¹ our recommendations to reform the enfranchisement regime will provide improved rights both to extend the lease and to acquire the freehold of the block – a “collective freehold acquisition”. In addition, our recommendations to reform the law of commonhold will allow leaseholders to then convert the block to commonhold, if they wish to do so. We recommend that leaseholders should have a choice whether (1) to undertake only a collective freehold acquisition, retaining the leasehold structure, or (2) replace the leasehold structure by converting to commonhold.
- 1.88 As commonhold becomes more prevalent, it is likely to be more desirable for leaseholders to convert to commonhold, rather than merely purchase the freehold by making a collective freehold acquisition claim. In time, Government might decide that leaseholders should only be able to convert to commonhold, rather than carry out a collective freehold acquisition claim and retain the leasehold structure.

Ensuring freehold ownership itself is fit-for-purpose

- 1.89 We have summarised above the measures that would pave the way to home ownership – of both houses and flats, and of both existing and future homes – to be freehold rather than leasehold.
- 1.90 That ambition does, however, rest on an assumption that freehold ownership is preferable to leasehold ownership. Generally speaking, for the reasons we set out in paragraphs 1.14 to 1.18 above, freehold ownership is preferable to leasehold ownership. Freehold ownership, however, is not without its own problems.
- (1) Concerns have been expressed about some features of freehold ownership. For example, freehold house owners can be required to pay estate management charges,⁷² and there have been concerns about such charges being high or about difficulties challenging the charges. When sums are due under a “rentcharge”, any failure by the freeholder to pay the sums due can result in them losing the property.⁷³
 - (2) There has been growing concern that certain undesirable features of leasehold ownership have been replicated in freehold ownership. The term “fleecehold” has been used to describe this phenomenon. Examples include obligations imposed on freehold homeowners to pay permission fees to make alterations to

⁷¹ Including leaseholders of any future flats that are sold on a leasehold basis.

⁷² The legal position is that positive obligations cannot bind future owners of the land (see para 1.20 above). However, freehold land can be subject to a requirement to pay an “estate rentcharge”, and there are various “workarounds” which can be effective to bind future freehold owners such as a “chain of covenants” protected by a restriction at HM Land Registry.

⁷³ See *Roberts v Lawton* [2016] UKUT 395 (TCC), [2017] 1 P & CR 3, which featured the method of enforcing rentcharges implied by s 121(4) of the Law of Property Act 1925 whereby the holder of a rentcharge that is in arrears may grant a lease of the charged land to a trustee to raise money to discharge the outstanding debt. See MHCLG’s work on fees and charges (paras 1.63(14)(a) and (b) above) and the Welsh Government Call for Evidence (para 1.68 above).

their home and inappropriate charges for the upkeep of neighbouring land and facilities.⁷⁴

- (3) As home ownership moves away from leasehold, the opportunity for developers and investors to make money from leasehold will evaporate. It is quite possible that they will look for ways to make money instead through freehold ownership. There is, therefore, a risk that the problems currently seen in leasehold may appear in freehold.

1.91 Put another way, moving from leasehold to freehold ownership is not a complete solution to the problems currently faced by homeowners, and nor does it guarantee that practices decried in the context of leasehold ownership will not also emerge as part of freehold ownership.

1.92 Certain reforms to freehold ownership are therefore necessary:

- (1) Government's plans to extend certain rights currently enjoyed by leaseholders to freeholders will provide protections that do not currently exist (see paragraph 1.63(14) above); and
- (2) the implementation of our recommendations on property law reform – including the creation of land obligations – will improve the operation of freehold ownership, and introduce a more streamlined, proportionate and controlled mechanism for homeowners to contribute towards maintenance costs: see paragraph 1.63(11) and 1.74 above.

1.93 As well as resolving existing problems with freehold ownership, it will be necessary to continue to monitor the way in which freehold ownership is working in practice in order to address any future problems as they arise. In particular, freehold is not free from the risk of abuse, and it is necessary to ensure that bad practices in leasehold do not creep back in under the disguise of freehold ownership.

1.94 In the case of commonhold, our recommendations for reform are designed to ensure that this form of freehold ownership is fit-for-purpose. There are various problems with the current commonhold model, and they would be resolved by our recommendations for reform. We have said that it is important that the practical operation of freehold ownership is monitored, and commonhold is no different. In our Commonhold Report, we conclude that the law of commonhold should be kept under review – just as it is in other countries which adopt a similar ownership model – in order to identify and resolve any problems as they emerge in the future.

⁷⁴ See, for example, BBC News, '*Fleecehold*': *New homes hit by 'hidden costs'* (20 March 2019), at <https://www.bbc.co.uk/news/uk-england-46279048>. See also MHCLG's work on permission fees (para 1.63(14)(d) above).

Summary: reforms that lay the foundations for home ownership to be freehold

Laying the foundations for home ownership to be freehold	Existing homes	Future homes
Houses	<u>Improved enfranchisement rights</u> : existing leaseholders can buy the freehold	<u>Leasehold house ban</u> : new houses to be sold on a freehold basis
Flats	<u>Improved enfranchisement rights</u> : existing leaseholders can buy the freehold and convert to commonhold	<u>Commonhold is available</u> . Government to decide whether commonhold should be compulsory, incentivised, or optional.

(2) Essential reform of leasehold: addressing problems for leaseholders in the present

1.95 While there can be an ambition for freehold to be the basis of home ownership in the future, it is crucial to recognise that leasehold currently exists, and will continue to exist – certainly in the short term, and probably for many years to come.

- (1) There are millions of existing leaseholders of houses and flats. Even if those leaseholders transition to freehold (or commonhold) ownership, that process will be gradual.⁷⁵ Unless and until existing leaseholders become freeholders, they need suitable protection as leaseholders.
- (2) Similarly, if and in so far as leasehold continues to be used in the future, there needs to be suitable protection for leaseholders.
 - (a) For owners of future houses, leasehold generally ought not be relevant, since Government proposes to ban leasehold houses (subject to exceptions).
 - (b) For owners of future flats, leasehold would not be relevant if commonhold becomes the norm, either because it is made compulsory or because it is sufficiently incentivised over leasehold (see paragraphs 1.75 to 1.85 above).

⁷⁵ Although we are recommending the expansion of enfranchisement rights, some leaseholders would remain unable to buy the freehold. For example, while we recommend increasing the threshold for commercial use from 25% to 50% (see para 1.12(2) above), leaseholders will not be able to buy the freehold to their block if more than 50% of the block is in commercial use.

- 1.96 It is therefore necessary for various problems with leasehold ownership to be resolved. Of the various reforms discussed in Part B above,⁷⁶ those intended to improve the position of existing leaseholders and any future leaseholders include:
- (1) improving the enfranchisement regime, so that it is easier, quicker and cheaper for leaseholders to extend their lease or buy their freehold: see paragraphs 1.52 to 1.54. We recommend the creation of an improved right to a lease extension, and improved rights for leaseholders to acquire their freehold (either individually or with their neighbours). Exercising enfranchisement rights removes the ground rent in existing leases, whether the claim is for a lease extension or for the purchase of the freehold. We have already published our report on the options that are available to Government to reduce the premiums that leaseholders must pay in order to exercise enfranchisement rights;
 - (2) improving the right to manage, so that it is easier, quicker and cheaper for leaseholders to take over control of the management of their block. We recommend improvements to the right to manage: see paragraphs 1.55 to 1.56;
 - (3) (for leaseholders of future homes only) restricting ground rents to zero in future leases: see paragraph 1.63(2).⁷⁷ Having said that, houses built in the future will not generally be leasehold (as a result of the leasehold house ban) and flats built in the future would not be leasehold if commonhold is used in preference to leasehold.⁷⁸ Put another way, once the restriction on ground rents is effective, there might be very few leases to which it would apply – houses will generally be sold freehold, and flats could always be sold commonhold;
 - (4) regulating property agents and requiring landlords who do not use managing agents to be members of a redress scheme: see paragraphs 1.63(3) and 1.63(12);
 - (5) consideration of the reform of the regulation of service charges, permission fees, and legal costs: see paragraphs 1.63(4), 1.63(5) and 1.63(6);
 - (6) reviewing our previous recommendations to abolish forfeiture in leasehold: see paragraphs 1.63(7) and 1.63(8);
 - (7) reviewing loopholes in the “right of first refusal”: see paragraph 1.63(9);
 - (8) reforming the regulation of event fees: see paragraph 1.63(10) above;
 - (9) regulating the provision of information by landlords to prospective purchasers of leases: see paragraph 1.63(13); and

⁷⁶ See paras 1.45 to 1.68 above.

⁷⁷ The restriction on ground rents will not change the ground rents in existing leases, so this measure will only affect leaseholders of future homes. Removing ground rent in existing leases can be done through an enfranchisement claim: see para 1.96(1) above.

⁷⁸ Indeed the restriction of ground rents to zero is one of the measures that would remove the current incentive to use leasehold, and might therefore go some way to encourage the use of commonhold.

- (10) improving the process for recognising residents' associations: see paragraph 1.64(1) above.

1.97 In the following diagram, we summarise how the various reforms fit together.

Figure 2: The big picture: how the various reform proposals fit together

