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Reforming the law

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**Leasehold home ownership: buying your  
freehold or extending your lease  
Consultation paper  
Summary**

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**Consultation Paper 238  
20 September 2018**

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# LEASEHOLD HOME OWNERSHIP: BUYING YOUR FREEHOLD OR EXTENDING YOUR LEASE

## A CONSULTATION PAPER

### SUMMARY

#### The Consultation Paper

- 1.1 The Consultation Paper, which this summary accompanies, discusses reform of the law of leasehold enfranchisement and seeks views on our provisional proposals for a new, single enfranchisement regime designed to benefit leaseholders of houses and flats. Leasehold enfranchisement is the process by which people who own property on a long lease may extend the lease, or buy the freehold.
- 1.2 It is important to make clear that the proposals contained in this consultation paper are only provisional. At this stage, we are not making recommendations for law reform. It is during this open public consultation that we are inviting views on our provisional proposals. These views will be carefully considered and taken into account when forming our final recommendations, which will be published in a subsequent report. We are keen to receive comments from as many stakeholders as possible, whether they agree or disagree with our provisional proposals.
- 1.3 This summary explains what the project is about, provides some context, and then outlines the main provisional proposals and questions that we set out in the Consultation Paper. Of necessity, this summary offers only an overview of our key provisional proposals and questions. Before responding, consultees are encouraged to read our full Consultation Paper or the relevant parts of it. References in this summary are to the chapters of the Consultation Paper.

#### Responding to the Consultation Paper

- 1.4 The Consultation Paper is available online at [www.lawcom.gov.uk/project/leasehold-enfranchisement/](http://www.lawcom.gov.uk/project/leasehold-enfranchisement/). The deadline for responses is 20 November 2018.
- 1.5 Comments may be sent to us using the online response form at [www.lawcom.gov.uk/project/leasehold-enfranchisement/](http://www.lawcom.gov.uk/project/leasehold-enfranchisement/). Where possible, it would be helpful if this form was used.
- 1.6 Alternatively, comments may be sent:
  - (1) by email to [propertyandtrust@lawcommission.gsi.gov.uk](mailto:propertyandtrust@lawcommission.gsi.gov.uk); or
  - (2) by post to Leasehold Enfranchisement Team, Law Commission, 1st Floor, Tower, 52 Queen Anne's Gate, London, SW1H 9AG.
- 1.7 Our website also includes a short survey which we invite individual leaseholders to complete in order to share with us their experiences of the enfranchisement process.
- 1.8 For further information about how the Law Commission conducts its consultations, and our policy on the confidentiality of consultees' responses, please see page iii - iv of the Consultation Paper.

## INTRODUCTION (CHAPTER 1)

### What is leasehold ownership?

- 1.9 Leasehold enfranchisement law is concerned with those who own property on a long lease. What, then, does leasehold ownership mean? Many people own, or aspire to own, a home. But 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).
- 1.10 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 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: its value tends to reduce over time, as its length (the “unexpired term”) reduces.
- 1.11 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. As well as a division of control, a landlord may have different interests from the leaseholders. For instance, the landlord may see leasehold 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.
- 1.12 As a consequence of these features of leasehold ownership, legislation has been enacted that gives leaseholders “enfranchisement rights”.
- (1) Leaseholders have a right to extend their lease (“the right to a lease extension”), which provides them with longer-term security in their home and goes some way to overcoming the problem of owning a wasting asset. Leaseholders’ security in their home, and the value of their asset, is far better protected if they can extend, say, a 40-year lease to 130 years.
  - (2) Leaseholders of houses have a right to purchase their freehold, and leaseholders of flats have a right, acting with the other leaseholders in their building, to purchase the freehold of their block. Freehold acquisition provides leaseholders with the same advantages as a lease extension (namely, security in their home and protecting the value of their asset), but also allows leaseholders to gain control of their property from an external landlord.
- 1.13 Our enfranchisement project is a wide-ranging examination of leaseholders’ enfranchisement rights.

## Leasehold home ownership in England and Wales

- 1.14 The number of residential leasehold properties (houses and flats) that are owned on a leasehold basis is the subject of some debate. The latest Government estimates are that there are over 4.2 million leasehold properties in England alone, comprising 18% of all housing stock. Of those, 2.2 million are owner-occupied, 1.8 million are privately owned and let to tenants in the private rented sector, and 0.2 million are owned by social landlords and let in the social rented sector. Other estimates, however, suggest that there are far more leasehold owners than these statistics suggest – the Leasehold Knowledge Partnership estimates that there are 6.6 million flats and leasehold houses in England, and a further 0.2 million in Wales. On any basis, however, it is clear that leasehold ownership is a matter that directly impacts on the lives of millions of people and families.
- 1.15 Flats are almost universally owned on a leasehold, as opposed to freehold, basis. That is because, for historic reasons, 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. There are therefore good reasons, under the current law, why flats are sold on a leasehold basis.
- 1.16 But leasehold ownership is not limited to flats. Sometimes houses are (and for many years have been) sold on a leasehold basis.<sup>1</sup> The first piece of enfranchisement legislation enacted in 1967 – the Leasehold Reform Act 1967 (“the 1967 Act”) – granted enfranchisement rights to leaseholders of houses. More recently, concerns have been raised about the sale of houses on a leasehold basis, and the UK Government has announced its intention to ban the sale of leasehold houses.<sup>2</sup>
- 1.17 The 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. The reasons why, for legal purposes, houses may be sold on a long lease do not, however, require the lease to provide income streams to the landlord, beyond those needed to maintain the property or the estate.

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<sup>1</sup> Historically, the sale of houses on a leasehold basis became widespread practice in particular areas of the country. More recently, new build houses have been sold on a leasehold basis (at least in part) to allow developers to sell the property subject to an ongoing obligation to pay a ground rent. The right to receive a ground rent (in respect of both houses and flats) is a valuable asset, which can then be sold to an investor. The UK Government has announced its intention to ban ground rents in future leases: see fn 2 below.

<sup>2</sup> Department for Communities and Local Government (now Ministry of Housing, Communities and Local Government), *Tackling unfair practices in the leasehold market: A consultation paper* (July 2017) available at <https://www.gov.uk/government/consultations/tackling-unfair-practices-in-the-leasehold-market>, and *Tackling unfair practices in the leasehold market: Summary of consultation responses and Government response* (December 2017) available at [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/670204/Tackling\\_Unfair\\_Practices\\_-\\_gov\\_response.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/670204/Tackling_Unfair_Practices_-_gov_response.pdf).

## The background to the project

- 1.18 In July 2016, we launched a public consultation asking which areas of law should be included in our Thirteenth Programme of Law Reform. We identified residential leasehold law as an area which might benefit from reform and sought views on the problems being faced in practice. We received over 150 responses to our consultation from a wide range of stakeholders which supported a review of one or more aspects of residential leasehold law.
- 1.19 Following discussions with Government, a project on residential leasehold and commonhold reform was included in our Thirteenth Programme, published in December 2017.<sup>3</sup> In the first instance, our project focusses on reform to enfranchisement and commonhold. Following further discussions with Government, a review of the right to manage – introduced in 2002 – has been added to our project.

## Welsh devolution

- 1.20 The extent to which leasehold enfranchisement is devolved to the Welsh Assembly is unclear. However, our project is supported by the Ministry of Housing, Communities and Local Government (“MHCLG”), and by the Welsh Government in so far as it relates to devolved matters, under our statutory Protocols with both Governments.<sup>4</sup> Our project therefore covers both England and Wales, and is intended to result, where reasonably possible, in a uniform set of recommendations that are suitable for both England and Wales. Nevertheless, after outlining the new scheme that we provisionally propose in this Consultation Paper in Chapter 3, we ask consultees whether any specific considerations in England or in Wales call for particular issues to be treated differently in England and in Wales.

## Leasehold reform in the spotlight

- 1.21 Residential leasehold has, for some time, been hitting the headlines and is the subject of an increasingly prominent policy debate.
- 1.22 Concerns have been raised about many aspects of the leasehold market. For example:
- (1) high and escalating 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;
  - (2) leasehold homes being unmortgageable as a result of high and escalating ground rents, making the properties unsaleable and trapping the owners in their homes;

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<sup>3</sup> Thirteenth Programme of Law Reform (2017) Law Com No 377, available at <https://www.lawcom.gov.uk/project/13th-programme-of-law-reform/>.

<sup>4</sup> Protocol of 29 March 2010 between the Lord Chancellor (on behalf of the Government) and the Law Commission (Law Com No 321), available at <https://www.lawcom.gov.uk/document/protocol-between-the-lord-chancellor-on-behalf-of-the-government-and-the-law-commission/>; Protocol of 10 July 2015 between the Welsh Ministers and the Law Commission, available at <https://www.lawcom.gov.uk/document/protocol-rhwng-gweinidogion-cymru-a-comisiwn-y-gyfraith-protocol-between-the-welsh-ministers-and-the-law-commission/>.

- (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 charging by landlords of unreasonable permission fees to carry out alterations to a property; and
- (5) 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.

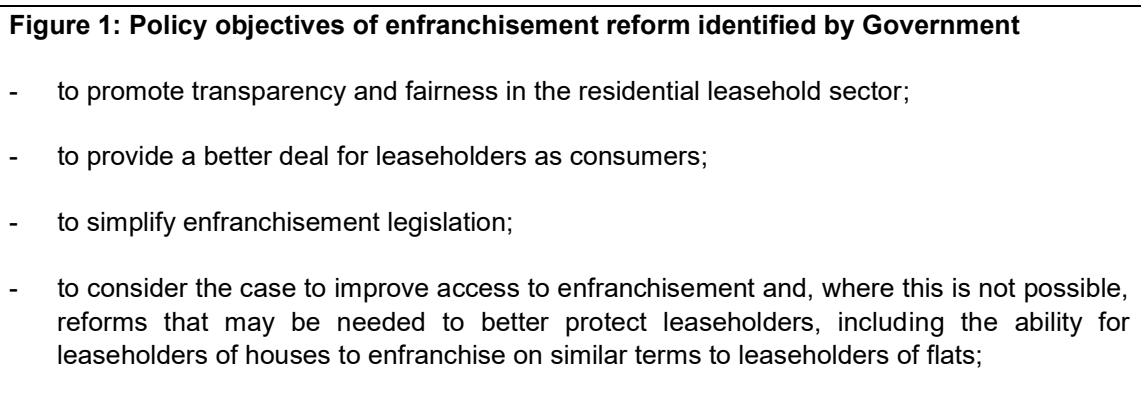
1.23 Conversely, we would emphasise that, while there have been abusive practices in leasehold, there are other landlords who operate fairly and transparently.

1.24 While abusive practices have been a focus of concern (particularly in media reports), the reform of leasehold law, including of enfranchisement, is not intended simply to remove abuse. Those practices have served to highlight long-standing concerns with leasehold. Our project is therefore not confined simply to removing abuses. Our Terms of Reference refer generally to providing “a better deal for leaseholders as consumers”. Our proposals for reform of enfranchisement are therefore intended to make the law work better for all leaseholders.

1.25 Improving and facilitating home ownership is a priority for Government, and – as part of that – reform of residential leasehold law has become an increasing priority. In December 2017, following a consultation, the UK Government announced various reforms, including proposals to ban the sale of houses on a leasehold basis, and the reservation of ground rents with any financial value when homes (whether houses or flats) are sold on a leasehold basis.<sup>5</sup> Measures to address problems faced by leaseholders have also been announced by the Welsh Government.

### Our Terms of Reference

1.26 The Law Commission's role is to ensure that the law is fair, modern, simple and cost-effective. While we work independently from Government, our project is designed to pursue certain policy objectives, which have been laid down for our work by Government and which are set out in our Terms of Reference. The objectives of reform that we have been asked to achieve are set out in Figure 1.




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<sup>5</sup> See fn 2 above.

- to examine the options to reduce the premium (price) payable by existing and future leaseholders to enfranchise, whilst ensuring sufficient compensation is paid to landlords to reflect their legitimate property interests;
- to make enfranchisement easier, quicker and more cost effective (by reducing the legal and other associated costs), particularly for leaseholders, including by introducing a clear prescribed methodology for calculating the premium (price), and by reducing or removing the requirements for leaseholders (i) to have owned their lease for two years before enfranchising, and (ii) to pay their landlord's costs of enfranchisement;
- to ensure that shared ownership leaseholders have the right to extend the lease of their house or flat, but not the right to acquire the freehold of their house or participate in a collective enfranchisement of their block of flats prior to having "staircased" their lease to 100%; and
- to bring forward proposals for leasehold flat owners, and house owners, but prioritising solutions for existing leaseholders of houses.

1.27 In summary, our project is designed to provide a comprehensive review of enfranchisement with a view to improving the position of leaseholders as consumers.

1.28 In the Consultation Paper, we make proposals to rationalise, streamline and expand the existing enfranchisement rights and to improve the procedure for claiming enfranchisement rights. These reforms would help leaseholders, but in many cases would not do so at the expense of landlords who would also benefit from clarity and efficiency in the system.

1.29 In respect of valuation, however, our Terms of Reference are different. We have been asked to set out the options for reducing the premium payable by existing and future leaseholders to enfranchise, whilst ensuring sufficient compensation is paid to landlords to reflect their legitimate property interests. Lower premiums would be beneficial to leaseholders, at the expense of the landlord who would receive less money for the lease extension or the freehold.

### **The impact of reform**

1.30 The different options for reform that we present will have financial and non-financial implications for landlords and leaseholders, and for the wider property market and economy. Government will undertake impact assessments in relation to any reform options that it pursues. Our consultation provides an opportunity to gather evidence and data which can be used in the preparation of impact assessments.

1.31 We therefore ask various questions throughout the Consultation Paper about the impact of problems under the current law and about the potential impact of reform. In addition, we have created an online survey which we are inviting individual leaseholders to complete in order to share their experiences of the enfranchisement process.

### **CRITICISMS OF THE CURRENT LAW**

1.32 We have heard numerous, and often detailed and technical, criticisms of the enfranchisement regime. We summarise some of the specific criticisms of each aspect of the enfranchisement regime below. Broadly speaking, the key concerns we have heard fall into five broad categories.



## **(1) Inherent unfairness of leasehold tenure**

- 1.33 Underlying some criticisms of the enfranchisement regime is the view that leasehold ownership is inherently unfair for leaseholders. That perceived underlying unfairness then exhibits itself during the enfranchisement process.
- 1.34 Leaseholders who are bringing an enfranchisement claim are doing so as a result of having previously acquired an interest which is diminishing in value over time. Many leaseholders, when they acquired their lease, will have paid a premium that was not substantially different from the value of a freehold interest in the property. They would say that they had no choice but to acquire a leasehold interest, and consider that they are being asked to pay again for the home they have already bought. And many leaseholders will not have been aware of, or have understood, the diminishing value of their interest, or that the cost of extending their lease or acquiring the freehold would increase substantially over time.
- 1.35 We have also been told that many prospective purchasers of houses and flats – particularly first-time buyers – do not have a full understanding of the terms of the lease or of the implications of owning a leasehold property. In some cases, buyers of leasehold houses may not even realise when purchasing a leasehold house that they will not become its outright owner. As one stakeholder said to us, people have set their heart on a home and are measuring for curtains and furniture before the lease is explained to them.
- 1.36 Leaseholders often find themselves compelled to make an enfranchisement claim, either (i) because they wish to sell their lease and a purchaser can only be found (or will only be able to obtain a mortgage) if the length of the lease is increased, or (ii) because they know that the cost of doing so in the future will likely be higher than it is at present. They are compelled to make a claim in order to be able to protect the value of their interest from reducing further. And in many cases, that interest is not only an asset but also their home.
- 1.37 The mere fact that leaseholders have to engage with the enfranchisement process – no matter how simple, quick and cheap it is – can, therefore, be a cause of frustration and anger. Leaseholders will often feel that they have been treated unfairly.
- 1.38 By contrast, landlords would argue that they only ever granted – and were only ever paid for – a time-limited interest. Those who purchased such an interest would have known, or ought to have known, that its expiry in the future would entail a process, and a sum of money being paid, in order to extend the interest. Landlords, they would argue, are entitled to the assets that they own. To some, the very existence of a compulsory purchase regime that entitles leaseholders to force landlords to hand over their asset is objectionable. To others, such a power of compulsory purchase must be accompanied by an obligation to pay full compensation for the deprivation of the landlord's interest.
- 1.39 So to landlords, any feeling of unfairness amongst leaseholders is caused by a lack of consumer awareness about the nature of leasehold ownership, rather than by a systemic failure of the leasehold regime. Landlords are merely seeking to protect their legitimate property interests.

1.40 These competing views are genuinely held and irreconcilable. Decisions about which side to favour, and how to strike the balance between the competing interests, depend to a large extent on political judgement.

## **(2) An inconsistent, disjointed and unclear regime**

1.41 The current enfranchisement regime is the product of over 50 Acts of Parliament, totalling over 450 pages. There are numerous anomalies and unintended consequences resulting from piecemeal changes over time. Certain terms in the legislation create much uncertainty, and scope for litigation. For example, there is still no clear definition of a “house”. And there are different rules for leaseholders of houses and of flats, often with no logical reason for the distinction. The most significant difference concerns the right to a lease extension, the substance of which differs significantly between houses and flats,<sup>6</sup> but there is a catalogue of further, more detailed and technical, inconsistencies between the enfranchisement rights for leaseholders of houses and those of flats.

## **(3) Complexity and uncertainty**

1.42 Many aspects of the regime are incredibly complex. It can be difficult even to work out whether a leaseholder qualifies for enfranchisement rights. In the case of houses, eligibility may depend on historic rateable values. These values may be difficult, or in some cases impossible, to find. The procedure for exercising enfranchisement rights is not straightforward, and varies depending on the enfranchisement right being claimed. In some circumstances, strict deadlines apply, which can be a trap for the unwary. The valuation process is complicated. There are various different valuation formulae for the purchase of a house, and which of them is applicable again depends on historic rateable values. The valuation process is difficult to understand, and also involves an element of artificiality. That brings with it uncertainty for leaseholders, since valuation is not an exact science, involving a number of known and unknown variable factors.

## **(4) Costly procedure**

1.43 The complexity of the process gives rise to legal costs, and the complexity of valuation gives rise to valuation costs. Both sets of costs can be significant, and can be disproportionate to the property value. In some cases, the costs involved actually exceed the premium payable. These costs are borne by both leaseholders and landlords, though leaseholders are required to pay towards their landlords’ costs so will often feel the burden of costs more acutely.

## **(5) Undesirable incentive structures**

1.44 Various aspects of the enfranchisement regime create undesirable incentive structures. For example, there is no incentive for leaseholders in a block of flats to encourage all of their neighbours to participate in the collective purchase of the freehold. Instead, one group of leaseholders can – without justification but without negative consequences – deliberately exclude other leaseholders in the block from the process, which is unlikely to foster harmonious relations in the ongoing management of the block.

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<sup>6</sup> See para 1.53 below. Leaseholders of houses would generally prefer to acquire the freehold, rather than a lease extension, but in some circumstances they are not permitted to do so, and some may prefer a lease extension in order to avoid having to pay a premium up front.

1.45 The regime can encourage an unhelpful tactical “gaming” approach to negotiations, which tends to favour more experienced landlords over leaseholders. The complexity of the regime gives plenty of scope for parties to disagree, or to argue different positions. The threat of litigation about those points, and the time it can take to resolve disputes, can be used tactically against a party who is seeking to complete the process speedily and at minimal cost. The consequence can be an incentive for leaseholders to agree to voluntary lease extensions (that is, outside the statutory regime) which can expose them to significant risks, such as onerous terms in the lease extension.

## Summary

1.46 The problems with the current enfranchisement regime outlined above cause unnecessary conflict, stress, uncertainty, costs, and delay. Ordinary leaseholders tend to be less able to shoulder the costs and delays than landlords.

## OUR PROPOSED NEW ENFRANCHISEMENT REGIME

1.47 The criticisms of the current enfranchisement regime are summarised above. It is imperative that the legislation is simplified, and that the exercise of enfranchisement rights is made easier, quicker and cheaper. Our project is a root-and-branch review of enfranchisement law. It considers the fundamental questions of the availability of enfranchisement rights and the calculation of the premium that must be paid to a landlord in order to avail of them, as well as the technicalities of how those rights can be exercised.

1.48 Our project asks four key questions:

- What should the enfranchisement rights be?
- Who should be entitled to exercise enfranchisement rights?
- How should enfranchisement rights be exercised?
- What should it cost to enfranchise?

1.49 Each of these questions is addressed in separate Parts of the Consultation Paper. However, we do not approach all of these questions in the same way. Our overall task is to devise an improved enfranchisement regime, and so, in most cases, we put forward provisional proposals for, and ask open questions about, a new regime. In relation to the cost of enfranchising, however, our Terms of Reference are different. We have been asked to provide Government with options for reducing the premiums payable by leaseholders when they enfranchise, while ensuring sufficient compensation is paid to landlords. We therefore set out a number of options for reducing premiums which we propose to put before Government, and seek views on these options.

## WHAT SHOULD THE ENFRANCHISEMENT RIGHTS BE? (CHAPTERS 4 TO 6)

### Current law and criticisms

1.50 Leaseholders who meet certain qualifying criteria have various enfranchisement rights.

## Freehold acquisition

- 1.51 Leaseholders of houses can purchase the freehold of their house. Leaseholders of flats can purchase the freehold of the building containing their premises; they must join together to make the purchase collectively via a nominee purchaser (a process known as “collective enfranchisement”).
- 1.52 The legislation does not cater for the needs of many modern housing estates. For example, when the leaseholder of a house acquires the freehold, services that are provided across a wider estate should continue to be provided, and paid for, for the benefit of that owner and his or her neighbours. But the legislation makes no provision for an ongoing relationship. Similarly, where an estate comprises houses, multiple blocks of flats, or a mixture of houses and blocks of flats, the leaseholders of all of the homes on the estate might wish to join together to acquire the freehold of the entire estate from their landlord.<sup>7</sup> Currently, the legislation only allows a group of leaseholders to purchase a freehold interest in their properties collectively if they are leaseholders within a single block of flats. It does not allow the leaseholders of a wider estate to acquire the freehold of the whole estate.

## Lease extension

- 1.53 Leaseholders of houses and of flats who meet certain qualifying criteria have a right to a lease extension, which provides them with longer-term security in their home. Leaseholders of flats are entitled, on payment of a premium, to be granted a 90-year lease extension without an obligation to pay any ground rent. There is no limit to the number of lease extensions that can be obtained. Leaseholders of houses are also entitled to a lease extension, but on very different terms. They are entitled to a single 50-year lease extension. No premium or purchase price is paid for the lease. While that may suggest that a lease extension is attractive, that is not in fact the case. The lease extension is subject to what is known as a “modern ground rent”, which can be very high. In effect, the modern ground rent means that what would have been paid as a premium is instead paid over time in rent.

## Proposals for reform

- 1.54 In Chapters 4, 5 and 6 of the Consultation Paper, we provisionally propose a new, coherent and streamlined regime comprising the following enfranchisement rights, which no longer turn on the distinction between houses and flats:
- (1) a universal right to a lease extension which is available to all leaseholders, whether they own a house or flat (“the right to a lease extension”);
  - (2) a right for leaseholders to acquire the freehold of a building individually, or of a building or estate collectively (“individual freehold acquisition” and “collective freehold acquisition” respectively); and
  - (3) a new right for leaseholders who did not participate in a previous collective freehold acquisition to do so at a later date (the “right to participate”).

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<sup>7</sup> Doing so can provide the leaseholders with the ability to control the management of their estate, as well as providing them with long-term security in their homes (overcoming the problem of owning a wasting asset).

- 1.55 All of the existing enfranchisement rights are retained under our proposed new regime, though in streamlined form and without some of the existing technical problems. That includes retaining the possibility of a leaseholder of a house extending the lease. While many leaseholders of houses will, of course, want to buy the freehold, a lease extension will be appropriate in some cases. Some leaseholders of houses are unable to acquire the freehold. Others may prefer to have a lease extension. Our proposal therefore ensures that consumer choice is maintained, while providing that the lease extension is on more favourable terms than under the current law.
- 1.56 We make provisional proposals for reform, and consult on other possible changes, that would have the following key effects.
- (1) All leaseholders who qualify for a lease extension would have a uniform right to a lease extension, as often as they so wish, at a nominal ground rent. We seek consultees' views as to the appropriate length of that lease extension – it could, for example, be 125 or 250 years.
  - (2) An extended lease would be on the same terms as the existing lease, except where either party elects to adopt non-contentious modernised terms drawn from a prescribed list. That would remove scope for unfavourable terms to be added to a lease during the enfranchisement process.
  - (3) Where a freehold is acquired in circumstances where the landlord does not retain any surrounding land:
    - (a) In relation to individual freehold acquisitions, we are seeking consultees' views on whether leaseholders should acquire the freehold subject to the rights and obligations that applied to the freehold prior to its acquisition, or on terms that reflect the rights and obligations contained in the existing lease or leases. Additional terms may only be added if the leaseholder decides that they ought to be, and these terms will be drawn from a prescribed list of non-contentious, modernised terms.
    - (b) In relation to collective freehold acquisitions, we propose that the rights and obligations that applied to the freehold prior to the exercise of enfranchisement rights should continue once the freehold has been acquired. We also propose that the landlord and the leaseholders should only be able to add additional covenants to that conveyance from a prescribed list.
  - (4) By contrast, where the landlord does retain surrounding land, there are certain circumstances in which ongoing obligations should continue following the freehold acquisition. However, retaining these obligations may not simply mean replicating the terms of the existing lease.
    - (a) In relation to individual freehold acquisitions we are seeking consultees' views on whether the leaseholder should acquire the freehold on terms replicating those set out in the existing lease (where there is no estate management scheme in place) or whether the terms should be drawn from a prescribed list of appropriate covenants.

- (b) In relation to collective freehold acquisitions, we seek consultees' views as to whether the freehold should be acquired on terms that replicate the terms set out in their existing leases (where there is no estate management scheme in place), but only in so far as those terms relate to the landlord's retained land, or, alternatively, only on terms drawn from a prescribed list.
- (5) In respect of collective freehold acquisition:
- (a) all acquisitions (save in limited circumstances) would be carried out by a nominee purchaser which is a company limited by guarantee;
  - (b) the right would not be limited to leaseholders in a single block of flats. It would also be possible for leaseholders on an estate comprising multiple buildings – whether those buildings are houses or blocks of flats or a combination of the two – to purchase the entire estate collectively (which we refer to as “estate enfranchisement”);
  - (c) participating leaseholders would be able to require the landlord to take a leaseback of any parts of the property being acquired (other than common parts) which are not let to the participating leaseholders. Such parts would include residential units which have not been let on long leases, residential units which are let on long leases but to non-participating leaseholders, and non-residential units. The effect of this proposal would be to reduce the cost of the enfranchisement since the participating leaseholders would not have to obtain finance to cover the costs that are attributable to parts of the premises that are not owned by the participating leaseholders; and
  - (d) the right would be available only where the building or estate in question has not been the subject of a prior collective freehold acquisition within the last five years. While a new collective freehold acquisition will not be possible in that period, leaseholders who did not participate will be able to join the previous collective freehold acquisition through the new “right to participate” (which we explain below).

1.57 Additionally, as we explained in paragraph 1.44 above, one group of leaseholders can currently deliberately exclude other leaseholders in the block from the process of collective freehold acquisition. We therefore propose the creation of a new enfranchisement right, available where a building has already been the subject of a collective freehold acquisition in which all leaseholders did not participate. We suggest that the leaseholders who did not participate at the time of the collective freehold acquisition should be able, subsequently, to purchase a share of the freehold interest held by those who did participate. We call this new right “the right to participate”.

1.58 The new regime would have the effect of enhancing and adding to the rights available to leaseholders; they would have a suite of comprehensive rights, which are standardised, practically useful and coherent.

## WHO SHOULD BE ENTITLED TO EXERCISE ENFRANCHISEMENT RIGHTS? (CHAPTERS 7 TO 9)

1.59 In Chapters 7 and 8 of the Consultation Paper, we consider the criteria that a leaseholder must satisfy in order to qualify for enfranchisement rights. We refer to these as “qualifying criteria”.

### Current law and criticisms

1.60 The current legislation setting out the various criteria that leaseholders must satisfy in order to qualify for enfranchisement rights is complex. The relevant provisions are scattered across several statutes and subject to many exceptions, provisos and qualifications. The criteria can also be difficult to apply in practice. For example, for leaseholders of houses, eligibility for enfranchisement rights and for a particular valuation basis may depend on historic rateable values, which can be difficult to find, and which for some properties do not exist at all. Leaseholders may be required to satisfy the “low rent test”, which is set out in a number of convoluted, confusing statutory provisions. More fundamentally, certain terms in the legislation create much uncertainty, and scope for litigation. There is still no clear definition of a “house”, despite the issue having been considered by the highest appeal court on five occasions. In the collective enfranchisement regime, what is meant by a “self-contained building” has been the source of frequent dispute. These kinds of difficulties can lead to additional costs and delay for leaseholders seeking to enfranchise, who may need to obtain specialist legal advice, or even in some cases to assert their rights through litigation.

1.61 It has also been said that the qualification criteria can be arbitrary or lead to unfair outcomes. For example, in some cases, leaseholders must have owned their leasehold property for two years before they can make an enfranchisement claim. During this waiting period, the price to be paid by the leaseholder to enfranchise might rise. There are also distinctions between the qualification criteria which must be met by leaseholders of houses and those which apply to leaseholders of flats, for which there is not always a good justification.

### Proposals for reform

1.62 To simplify matters, and to address particular problems, we make the following key provisional proposals.

- (1) The replacement of the current two-track approach to the question of availability of enfranchisement rights (which requires premises to be categorised as a “house” or “flat”) with a single set of criteria (based around the new concept of a “residential unit”, which can be applied to any leasehold premises). This proposal would overcome the difficulties encountered in the current law in determining whether a building is a house.
- (2) The application of these criteria in two logical stages to identify the enfranchisement rights available to any particular leaseholder:
  - (a) first, to establish whether a lease extension is available to the leaseholder in question; and

- (b) if so, to establish whether the leaseholder has the additional ability to acquire the freehold, either individually or collectively.
- (3) The abolition of qualifying criteria based on financial limits – both the “low rent test” and other financial limitations based on historic rateable values. The regime would therefore be simpler, easier to understand, and practically workable.
- (4) The extension of the 25% limit on non-residential use (which currently applies only to collective freehold acquisition claims) to all freehold acquisition claims, which ensures the new scheme is coherent and standardised.
- (5) The removal of the requirement (currently applicable to all lease extension claims, and claims to acquire the freehold of a house) that the leaseholder must have owned the lease for the last two years. Leaseholders would not, therefore, be required to delay their claim, and watch the premium rise, while they are waiting to satisfy a minimum ownership requirement.
- (6) In collective freehold acquisition claims:
  - (a) the removal of the requirement, where a building contains only two flats, for the leaseholders of both flats to participate in the claim. Instead, a single flat owner could acquire the freehold and the other owner would be entitled to exercise the new right to participate in order to acquire a share of the freehold; and
  - (b) the abolition of the provision that where a leaseholder holds a long lease (or leases) of three or more flats in a building, there shall be taken to be no qualifying long leaseholder of those flats. The requirement is designed to prevent commercial investors participating in a collective enfranchisement claim, but it is ineffective at doing so.

1.63 We also explore whether the ability of commercial investors (as opposed to owner-occupier leaseholders) to benefit from enfranchisement rights ought to be restricted and, if so, how this might be achieved.

### **Exceptions from the enfranchisement regime**

1.64 In Chapter 9, we consider those cases in which particular leaseholders who would otherwise appear to qualify for enfranchisement rights in fact have more limited rights, or, in some cases, none at all. We consider the position of shared ownership leaseholders and leaseholders of the National Trust and of the Crown, amongst others.

1.65 In relation to shared ownership leases, our Terms of Reference are “To ensure that shared ownership leaseholders have the right to extend the lease of their house or flat, but not the right to acquire the freehold of their house or participate in a collective enfranchisement of their block of flats prior to having “staircased” their lease to 100%”. We ask questions to determine how to achieve this policy.

1.66 Enfranchisement legislation currently applies to the National Trust only to a limited extent in relation to land that is vested in the Trust inalienably. Leaseholders of houses on inalienable land of the National Trust may acquire a single lease extension, but not obtain the freehold. Leaseholders of flats on inalienable land do not enjoy any



enfranchisement rights, although we understand that the National Trust owns very few flats let on long leases. We ask whether the current situation should be retained.

## HOW SHOULD ENFRANCHISEMENT RIGHTS BE EXERCISED? (CHAPTERS 10 TO 13)

1.67 In Chapters 10 to 13 of the Consultation Paper, we consider the procedure by which enfranchisement rights are claimed, determined and put into effect under the current law, and set out our proposals for reform.

### Current law and criticisms

1.68 An enfranchisement claim begins by a leaseholder (or a group of leaseholders in the case of a collective enfranchisement claim) giving a notice to the landlord (a “notice of claim”). The landlord gives a notice in response (a “counter-notice”). The parties then negotiate the terms of the enfranchisement claim (usually through their professional advisers) and the claim will be completed by the grant of a lease extension or by the transfer of the freehold. Leaseholders are required to contribute to certain costs incurred by the landlord. Any dispute about the enfranchisement claim will (depending on the nature of the dispute) be referred to either the county court or to the Tribunal, or to both.

1.69 We identify a number of problems with the existing procedures. For example:

- (1) there are distinct procedural regimes for claims involving houses, and for claims involving flats. Inconsistencies between procedures create a risk that parties (or their advisers) will make mistakes by confusing one procedure with another. Those mistakes can lead to additional costs being incurred, or, in some cases, to the failure of a claim;
- (2) there is too much uncertainty over whether notices of claim are valid, or have been properly served. This problem is made worse in the case of claims concerning flats, because a landlord who does not serve a counter-notice must dispose of his or her interest on the terms set out in the leaseholder’s notice of claim;
- (3) the procedure for dealing with “missing landlords” is complex and almost impossible for leaseholders to follow. In some cases, the cost of trying to locate a landlord, and applying to the county court for a vesting order<sup>8</sup> if he or she cannot be found, can exceed the price to be paid for the interest claimed;
- (4) the legislation that applies to claims involving flats contains a series of deadlines by which steps in the procedure must be taken; any failure to meet those deadlines will lead to the claim being treated as having been withdrawn, the leaseholder(s) having to pay their landlord’s non-litigation costs, and a 12-month prohibition on the leaseholder(s) trying to undertake the process again;
- (5) the powers to deal with disputes or issues that arise during an enfranchisement claim are divided between the county court and the Tribunal. This division can be confusing for the parties, and can lead to a number of separate applications

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<sup>8</sup> An order under which the court completes the transaction in place of the landlord.

having to be made during the course of a claim, causing the parties to incur further unnecessary costs and delays;

- (6) the Tribunal has the power to determine any disputes between the parties as to the terms on which any claimed interest is to be acquired; but once heads of terms have been agreed, any dispute about how those terms are put into effect is dealt with by the county court. This distinction can lead to further costs and delay;
- (7) the powers of the county court and of the Tribunal to make an order that one party should pay the other party's litigation costs are very different. As such, the determination of certain disputes or issues carries a greater risk that such an order will be made than others. The different powers as to costs can make it more difficult for parties to assess in advance the potential costs of bringing an enfranchisement claim;
- (8) there is plenty of scope for parties to disagree, or to argue different positions. The threat of litigation about those points, and the time it can take to resolve disputes, can be used tactically against a party who is seeking to complete the process speedily and at minimal cost. This consequence can be an incentive for leaseholders to agree to voluntary transactions (that is, outside the statutory enfranchisement regime) which can expose them to significant risks, such as (in the case of a lease extension) onerous terms in the new, extended lease;
- (9) few can operate the procedure without professional assistance, which can be costly. Both legal and valuation costs can be significant, and can be disproportionate to the property value. In some cases, the costs involved actually exceed the premium payable. These costs are borne by both leaseholders and landlords, though leaseholders are required to pay their landlords' reasonable "non-litigation costs" so will often feel the burden of costs more acutely;<sup>9</sup>
- (10) many leaseholders object in principle to their obligation to pay their landlord's reasonable non-litigation costs. They also criticise the level of non-litigation costs claimed by some landlords, and the expense of contesting the sums claimed. Leaseholders can find themselves stuck between a rock and a hard place. If leaseholders or their solicitors think that the costs claimed by a landlord are unreasonable, leaseholders must make a claim to the Tribunal, wait for the outcome of that claim (which they may win or lose), and pay their own solicitors' costs. It will often be quicker and easier simply to pay the costs claimed by the landlord, even if they are unreasonable;
- (11) in contrast, some landlords have criticised their inability to recover the full costs incurred in dealing with enfranchisement claims, and the lack of any provision to require leaseholders to provide proper security for their costs; and

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<sup>9</sup> Bringing an enfranchisement claim will lead both parties to incur legal and other costs even if there is no dispute that needs to be resolved by a court or Tribunal. For example, the parties might incur legal costs when serving notices on the other, and in completing and registering the grant of a new extended lease or the transfer of the freehold to the leaseholder. The parties might also incur professional valuation costs. We refer to these costs as "non-litigation" costs.

- (12) a leaseholder who wishes to sell his or her premises with the benefit of a notice of claim which has already been served must assign the notice and the lease together. If that is not done successfully, the purchaser will have to serve a fresh notice of claim, but in some cases can only do so after he or she has owned the property for two years. This has been widely criticised.

### **Proposals for reform**

1.70 We provisionally propose introducing a single procedure that would apply regardless of the enfranchisement right being claimed. This proposed procedure would provide for:

- (1) standard forms to be prescribed, which would make claims easier, simpler and cheaper to commence and respond to, and reduce the risk of notices being invalid;
- (2) an enfranchisement claim to be started either by leaseholders serving a notice (a "Claim Notice") on their landlord or, where that is not possible, by applying to the Tribunal for an order allowing the claim to proceed in the absence of the landlord;
- (3) a Claim Notice to be deemed to have been served on a landlord if posted to an address falling within specified categories of address, making it easier for leaseholders to serve notices. Leaseholders will not have to take time-consuming and costly steps to locate their landlord where they have not been provided with up-to-date contact details. And nor will leaseholders be faced with assertions that landlords have not been properly served;
- (4) a landlord's notice (a "Response Notice") to be accompanied by a draft contract (if any) as well as a draft transfer or lease. Later stages of the enfranchisement process would therefore be frontloaded, and areas of potential dispute can be identified at an earlier stage;
- (5) challenges to the validity of notices to be permitted only on a limited number of defined grounds. Arid, costly and time-consuming debates about whether a notice complies with the numerous technical requirements would therefore be avoided;
- (6) leaseholders to be able to apply to the Tribunal for a determination of their claim where:
  - (a) their landlord has given a Response Notice, but issues remain in dispute after a prescribed period;
  - (b) a Claim Notice has been properly served, but no Response Notice has been given within a prescribed period; or
  - (c) the Tribunal has granted an order permitted the claim to proceed (as set out at paragraph 1.70(2) above);
- (7) in each case referred to at paragraph 1.70(6) above, the Tribunal to determine the claim based on the evidence provided, and its own expertise. It will not be required to allow the leaseholders to acquire the interest on the terms proposed

in their claim notice if the landlord could not be served, or has not responded, so unfair windfall gains for leaseholders would be removed;

- (8) in each case referred to at paragraph 1.70(6) above, the Tribunal to determine the leaseholders' entitlement to bring a claim, and the terms of acquisition, to include the terms of any contract, transfer or lease extension and a date for completion;
  - (9) either party to be able to apply to the Tribunal for an order giving effect to the transaction if it is not completed by the date agreed or set by the Tribunal;
  - (10) landlords who failed to serve a Response Notice to be entitled to apply to the Tribunal to take part in a claim, and to set aside any determination made, in limited circumstances;
  - (11) leaseholders to be entitled to withdraw their claim at any stage prior to completion of the transaction, with a requirement that they pay some of their landlord's costs if they do so;
  - (12) claims not to be deemed withdrawn, but landlords to be empowered to apply to strike out a claim on notice. Traps for the unwary, which can currently result in claims failing and leaseholders having to pay their landlord's costs, would therefore be removed; and
  - (13) the benefit of a leaseholder's notice to be automatically assigned on any sale of the lease to a third party. Inadvertent errors in properly assigning a notice to a third-party purchaser would no longer result in claims failing and leaseholders having to pay their landlord's costs.
- 1.71 We also propose that all disputes and issues that arise during an enfranchisement claim should be dealt with by the Tribunal. Leaseholders would no longer have to navigate the complex division of responsibility between the court and the Tribunal, and disputes will be resolved more quickly, and in one go. We believe that the Tribunal's existing limited powers to make an order that one party pay the other party's costs should apply to all cases. In addition, we propose the introduction of a new dispute resolution procedure for low value claims.
- 1.72 We also invite the views of consultees as to whether leaseholders should be required to contribute to their landlord's non-litigation costs. If that requirement is retained, we set out options for reforming the way in which any contributions are set, and outline a potential fixed-costs regime. A fixed-costs regime would allow leaseholders to know at the outset the amount of costs that the landlord will be entitled to claim, and will prevent leaseholders from feeling compelled to accept having to pay unreasonable costs.

## **WHAT SHOULD IT COST TO ENFRANCHISE? (CHAPTERS 14 AND 15)**

### **Valuation and our Terms of Reference**

- 1.73 When a leaseholder exercises the right to enfranchise, the total cost to the leaseholder is comprised of two distinct components:
- (1) professional costs, namely fees paid to lawyers and valuers; and

- (2) the “premium” – the price the leaseholder needs to pay the landlord for the extended lease or the freehold.
- 1.74 Calculating the premium is known as “valuation” as it involves putting a financial value on the interest being obtained by the leaseholder(s) from the landlord. Valuation therefore refers to calculating the price to be paid, separate from any professional costs incurred. Lower premiums are beneficial to leaseholders, at the expense of the landlord who receives less money for the lease extension or the freehold. We consider valuation in Chapters 14 and 15 of the Consultation Paper.
- 1.75 Our Terms of Reference (see paragraph 1.26 above) include specific provisions in respect of premiums. They require us to:
- (1) set out the options for reducing the premium payable by existing and future leaseholders to enfranchise, whilst ensuring sufficient compensation is paid to landlords to reflect their legitimate property interests;
  - (2) produce options for a simpler, clearer and consistent valuation methodology; and
  - (3) make enfranchisement easier, quicker and more cost effective (by reducing the professional costs), particularly for leaseholders, including by introducing a clear prescribed methodology for calculating the premium.
- 1.76 The question whether premiums should be reduced is not solely a question of law: it involves considerations of law, valuation and, ultimately, political judgement. There is no suggestion that existing leaseholders should be able to obtain a freehold or lease extension without paying the landlord an appropriate price. Our task is to set out the options for reducing premiums that are payable by leaseholders while ensuring sufficient compensation is paid to landlords. It will then be for Government to decide whether, and if so how, to reduce premiums.

### **Sufficient compensation and human rights**

- 1.77 Our Terms of Reference require us to consider valuation options that ensure “sufficient compensation is paid to landlords to reflect their legitimate property interests”.
- 1.78 Views will invariably differ on what constitutes “sufficient compensation”. In legal terms, however, one aspect of sufficient compensation is the right to peaceful enjoyment of property contained in Article 1 of the First Protocol to the European Convention of Human Rights (“A1P1”), which is incorporated into English law by the Human Rights Act 1998. In *James v United Kingdom*,<sup>10</sup> the European Court of Human Rights held that enfranchisement was a deprivation of the landlord’s property and so A1P1 was engaged. However, the rights conferred by A1P1 are qualified, which means that an interference with peaceful enjoyment, including the deprivation, of property can be justified in certain circumstances. It must be shown that the interference complies with the principle of lawfulness and pursues a legitimate aim by means that are reasonably proportionate to the aim sought to be achieved. This final question focuses upon whether a fair balance has been struck between the demands of the general interest of the community and the requirements of the protection of the individual’s fundamental

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<sup>10</sup> (1986) 8 EHRR 123.

rights. In that regard, the court accepts that a margin of appreciation must be left to the national authorities. The compensation paid to the landlord is a key aspect of determining whether an interference with his or her rights is proportionate. In *James*, the court held that the UK was acting within its margin of appreciation and so the enfranchisement regime was compatible with A1P1.

1.79 We will be developing our human rights analysis of the valuation options available to Government over the course of the project. In addition, the human rights implications of reducing premiums cannot be considered in isolation and will depend on other aspects of the reformed regime. Part of the aim of our consultation is to inform our views on what is, and what is not, sufficient compensation in accordance with the Terms of Reference, having regard to human rights considerations.

### **Competing interests**

1.80 The interests of landlords and leaseholders are diametrically opposed, and establishing consensus between the two interest groups – in relation to valuation but also in relation to many of the other issues we are considering – will be impossible.

(1) Landlords come in all shapes and sizes: private family estates (for example, the Grosvenor Estate and Cadogan Estate); charities (for example, the National Trust); developers; pension and other funds; private individuals; investors; and leaseholder-owned companies. From their point of view, they have investments which are being expropriated from them compulsorily. They are likely to object to any reduction in the premium, and if anything are more likely to argue that the current basis for assessing premiums is “unfair” because the resulting premiums are too low.

(2) Leaseholders are also varied: ordinary home-owners (ranging from those with limited means through to very wealthy owners); non-resident owners (such as buy-to-let landlords, those with a second home, those who have invested in property); and some speculative investors and developers who purchase flats with a view to exercising enfranchisement rights and profiting from selling on an enhanced interest. From their point of view, they have properties which are held on a leasehold basis for one of two reasons. That is, because that is the standard method by which flats can be owned in England and Wales, and because developers are insisting on selling houses on a leasehold basis. They will object to any increase in the premium, and are likely to argue that the current basis for assessing premiums is “unfair” because the resulting premiums are too high.

1.81 Government’s desire to reform the enfranchisement regime in order to provide a better deal for leaseholders as consumers is, of course, directed at individual home owners rather than investors.

### **Current law and criticisms (Chapter 14)**

1.82 The current law does not set out a single method of valuation.

(1) The 1967 Act deals with valuation in relation to houses. It provides various methods of valuation in relation to acquiring the freehold of a house. Which method applies is dependent on a number of factors. No premium is payable for extending the lease of a house. But the absence of a premium does not mean

that a lease extension is necessarily an attractive option. As we note above, the rent payable under the extended lease is a “modern ground rent”. As a result, what the leaseholder saves by not paying a premium, he or she pays by way of rent over the 50-year extended term of the lease.

- (2) The Leasehold Reform, Housing and Urban Development Act 1993 (“the 1993 Act”) governs valuation in relation to flats. The Act contains separate provisions on valuation for collective enfranchisement claims and lease extension claims.

1.83 Despite the myriad of provisions, the approach to calculating the premium is broadly the same in all cases, save for those claims to acquire the freehold of a house to which the valuation method laid down by section 9(1) of the 1967 Act applies. The general approach to valuation is designed to ascertain the market value of the landlord’s interest in the property. By contrast, the valuation method in section 9(1) of the 1967 Act, which is intended to apply to certain “low value” houses, is considerably more favourable to leaseholders, though also more complicated and difficult to operate.

1.84 There are four main criticisms of the current approach to valuation.

- (1) An appropriate balance is not necessarily drawn between the competing interests of landlords and leaseholders. The 1967 Act was passed primarily to meet the anxieties of ordinary householders in areas where long leases of houses were widespread, but those who derived most benefit from the Act in financial terms were relatively wealthy leaseholders of houses in expensive areas of London. The various amendments to the 1967 Act, and the introduction of the 1993 Act, have shifted the balance between landlord and leaseholder, so that the subsequently introduced bases of valuation seek to compensate the landlord in full at a market value. But leaseholders may argue that the premium is too high and does not reflect the fact that the asset they are buying is their home. The discontent amongst leaseholders has been fuelled by the practice of some developers of selling leasehold properties with rent review clauses leading to very high ground rents. Such rent reviews make the need to enfranchise and buy out the ground rent more imperative, whilst significantly increasing the premium payable to do so.
- (2) Valuation is complicated and expensive. The valuation provisions and methodology are not readily understandable to the lay person and are difficult to apply without specialist advice. Where the capital value of the property is low, the professional fees may be disproportionate to the price payable. One of the reasons for complexity is that there is a wide valuation margin and a lack of standardisation, which gives scope for disputes and a lack of certainty as to the price that will be payable.
- (3) The valuation methodology is both artificial and circular. Both of these criticisms stem from the fact that, in calculating the market value, various statutory assumptions must be made. In particular, it must be assumed that there are no statutory enfranchisement rights attached to the interest; that is, that the leaseholder has no right to buy the freehold or to a lease extension. But in reality, nearly all leasehold properties benefit from statutory enfranchisement rights and therefore the “market value” being calculated is, to an extent, artificial. It is circular because the price of a short lease in the market is the value of a long

lease/freehold less the cost of extending the lease or acquiring the freehold. As a result, while the market value determines the price payable under the statutory regime, the price payable under the statutory regime determines the market value.

- (4) There are also numerous technical problems with the valuation methodology.

### **Options for reform (Chapter 15)**

1.85 In the Consultation Paper, we identify some overarching considerations for reform.

- (1) We consider that the legislation could be simplified by adopting a consistent valuation methodology. We acknowledge, however, that the most favourable method of valuation contained in section 9(1) of the 1967 Act for the freehold acquisition of a house would need to be maintained (or an equivalent provision introduced) to ensure that the premium is not increased for those who currently benefit from it.
- (2) While a consistent regime has the advantage of simplicity, there are difficulties in a “one size fits all” approach. In particular, it means that in some cases the professional costs incurred in enfranchisement may exceed the premium. We therefore consider whether a separate regime should be created for low value claims.
- (3) Currently, the same premium is payable regardless of whether an enfranchisement right is being exercised by (for example) a homeowner in respect of his or her home, or an investor. We note that the identity of the leaseholder exercising the right might be significant in respect of A1P1, as it may be possible to justify a lower premium being paid by a homeowner purchasing his or her home than by an investor. Therefore we note that differentiating between leaseholders might be considered, if the Government wishes to lower the premium payable by homeowners to a level that would not be justified for any other type of purchaser.
- (4) Valuation often involves the use of rates to determine certain aspects of the valuation formula. Identifying these rates can be contentious and can make a significant difference to the premium that will be paid. Any option for reform that continues the need for these rates could be combined with putting in place a procedure for prescribing the rates to be used. To reduce the premium payable, the rates could be prescribed at a level that benefits leaseholders. Prescribing rates would also save both landlords and leaseholders professional costs, and would remove uncertainty about how the premium will be calculated.

1.86 We then set out options for reform, which we divide into two categories.

- (1) The adoption of a simple formula. These options move away from attempting to identify a market value. Examining market value inevitably involves variables, and therefore uncertainties, and associated professional fees. These difficulties are removed by adopting a simple formula. A simple formula (depending on how it is set) would reduce premiums, although there is a risk that the level of the premiums would be arbitrary. We identify two possible formulae:



- (a) a ground rent multiplier, whereby the premium paid is a multiple of the ground rent. This approach has been highlighted in a Private Member's Bill introduced by Justin Madders MP; and
    - (b) a percentage of the capital value of the property.
  - (2) Options based on current valuation methodology. These options to reduce premiums involve components of the existing valuation methodology. These different components can be combined in different ways. It will ultimately be a matter for Government to make the political determination of what those components will be as their inclusion or non-inclusion will affect how premiums are calculated. As noted above, they could be combined with prescribing rates in a way that is favourable to leaseholders.
- 1.87 We include various worked examples in the Consultation Paper to indicate, in simple terms, the effect on enfranchisement premiums of the different options for reform. We ask for consultees' views on the advantages and disadvantages, and practical workability, of these different options for reform.
- 1.88 Finally, we consider how an online calculator could be used to support valuation. We note that depending on the valuation methodology adopted, an online calculator could limit or even remove the need for expert assistance. In particular, an online calculator could most fully be utilised alongside prescribed rates.
- 1.89 The human rights implications of each of these options will need to be examined. A simple formula may be difficult to justify under A1P1 in all cases, as the resulting premium may be very low relative to the value of the interest of the landlord being acquired. It may, however, be possible to identify a category of properties in respect of which a simple formula would be appropriate. Moreover, the bounds of acceptability under A1P1 will need to be examined to ensure that a methodology involving prescribed rates is human rights compliant. The body or organisation responsible for setting these rates will be judicially reviewable and the substance of its decisions subject to scrutiny by reference to A1P1. This conclusion will depend not just on the premium payable, but also on who is asked to pay that price, the qualification criteria that apply to the property, the existence of alternative valuation bases and the social policy objectives being pursued.

## **OTHER LEASEHOLD INTERESTS (CHAPTER 16)**

- 1.90 In Chapter 16, we address particular procedural and valuation issues that arise where there are intermediate leases sitting between a leaseholder's lease and the freehold.

## **CONCLUSION**

- 1.91 We have made detailed provisional proposals for a new enfranchisement regime in the Consultation Paper, which we think have the potential to improve the existing enfranchisement rights and improve the current enfranchisement process for both leaseholders and landlords. The options for valuation reform, as required by our Terms of Reference, would benefit leaseholders at the expense of landlords.

- 1.92 We seek the views of all stakeholders with an interest in enfranchisement reform on the proposals and questions in our Consultation Paper, including landlords, individual leaseholders, professional advisers, and representative groups.
- 1.93 After the close of our public consultation, we will review our proposals and options for reform in the light of consultees' comments on them. We will then publish a final report setting out our recommendations for reform, and – in relation to valuation reform – setting out the options that are available to Government.