

BSA response to DCLG consultation

Tackling unfair practices in the
leasehold market

Restricted
19 September 2017

Introduction

The Building Societies Association (BSA) represents all 44 UK building societies. Building societies have total assets of over £374 billion and, together with their subsidiaries, hold residential mortgages of over £292 billion, 22% of the total outstanding in the UK. They hold over £265 billion of retail deposits, accounting for 18% of all such deposits in the UK. Building societies account for 34% of all cash ISA balances. They employ approximately 40,000 full and part-time staff and operate through approximately 1,550 branches.

We have provided responses to only those questions that are directly relevant to our members.

General Comments

For both leasehold houses and leasehold flats there is scope to vastly improve the situation for existing and future leaseholders. Whilst leasehold in general has come under the spotlight several times before and subsequent improvements made, significant problems persist. In this response we have not commented on the suitability of leasehold as a tenure for property in the UK.

We are generally supportive of the Government's proposal to restrict the creation of new build leasehold houses, however Government should be mindful not to adversely impact the provision of affordable homes. In addition whilst there are improvements that desperately need to be made to the practical operation of the leasehold tenure and leasehold housing in-particular housing, it is important that any changes the Government makes do not blight existing leaseholders exacerbating the problem for them.

There is a lack of clarity and understanding amongst consumers of the practical workings of the leasehold tenure. We believe more should be done to improve consumer awareness of the complexities of leasehold properties. Firstly making it clear at the marketing stage of the homebuying process both the tenure and key details of the lease. Secondly, we propose that a model lease is developed. Whilst there will naturally need to be some tailoring of the lease we see no reason why the majority of the leasehold document cannot be standardised.

The UK Government should not support practices which are detrimental to UK consumers. We therefore strongly support the restriction of new build houses being created under leasehold for both Help to Buy Equity Loan and in general.

Information should be made easily available to assist leaseholders in understanding their options when dealing with onerous ground rent and other potentially unfair terms. There should be a clear pathway to challenging these terms and ensuring that consumers know their rights.

Leaseholders may find it difficult to prove that these terms are onerous or unfair. Government should seek to ensure that where terms are unfair they are unenforceable.

Several Building Societies have already taken steps to address leasehold issues by updating lending policies to restrict onerous ground rent and unfair lease terms, in a pragmatic and proportionate way.

Questions

Q5 What steps should the Government take to limit the sale of new build leasehold houses?

We are generally supportive of the Government's proposal to restrict the creation of new build leasehold houses. In a number of cases, it appears that this practice is designed solely to secure additional revenue for the developer or other third party with no benefit to the leaseholder. It could be construed as exploiting the asymmetry of information and lead to confusion and additional expense that the leaseholder did not fully understand at the point of purchase. Leasehold houses rarely benefit purchasers and it is right that Government is focusing on protecting consumers' interests in this area.

Q6 What reasons are there that houses should be sold as leasehold other than under the exceptions set out in paragraph 3.2?

- **within a cathedral precinct;**
- **on National Trust or Crown land;**
- **on land owned by local authorities and university bodies with the right for future development;**
- **in shared ownership with a 'restricted staircasing' lease;**
- **of special architectural or historic interest or adjoining properties where it is important in safeguarding them and their surroundings.**

Whilst in the vast majority of cases leasehold is not the appropriate tenure for houses, Government should be mindful not to adversely impact the provision of affordable homes. We agree that there are exceptions where leasehold housing may be appropriate, in addition to those listed in paragraph 3.2 it is often appropriate for Community Land Trusts, Co-housing and shared ownership to be on a leasehold basis.

The question that should be posed when permitting leasehold houses is whether it is to the benefit of consumers and those living in the local area. Where leasehold is permitted these should be subject to fair and transparent terms. Some lenders have already taken steps to prevent lending on properties with terms that they determine to be unfair or onerous, including a restriction in their lending policy on unreasonable escalating ground rent clauses and setting out minimum length of lease terms for new build properties.

In paragraph 3.6 of the consultation it states *"Developers argue that the sale of new build leasehold houses in some areas of England is an accepted custom and practice, and that selling a freehold house could create a potential competitive disadvantage."*

We do not believe that this is generally accepted custom and practice, however there may be areas where pockets of leasehold housing exists where it has become the established practice, it would be worth examining these areas in greater detail . In some cases, a homebuyer will be unaware that they are buying a leasehold house until relatively late on in the process and even then, given the complexities of leasehold terms it is likely that they will be unclear as to exactly what this will mean for them.

This lack of clarity amongst consumers is the likely reason why, to our knowledge, there is often little or no discernible difference in price between leasehold and freehold properties. If consumers understood fully the potential difference it made to the long-term value of the asset that they were purchasing it is likely that given the choice they would opt for freehold.

We believe more should be done to improve consumer awareness of the complexities of leasehold properties. Firstly making it clear at the marketing stage of the homebuying process both the tenure and key details of the lease. Secondly, we propose that a model lease is developed. Whilst there will naturally need to be some tailoring of the lease there is no reason why the majority of the leasehold document cannot be standardised, much the same as the Homes and Communities Agency (HCA) sets out for shared ownership properties. This would improve transparency for homebuyers, lenders and conveyancers and enable fair comparison between lease terms and conditions.

At the moment leasehold agreements vary considerably, the important key facts are often very difficult to locate and decipher in long, and often unnecessarily complex documents. We are aware of some leases even including algebraic formula. We do not believe this is fair and transparent for a consumer, a model lease with standardised terms would improve the situation considerably.

Q8 Would limiting the sale of new build leasehold houses affect the supply of new build homes?

We have not seen any evidence that it would. Even in marginal housing developments, limiting leasehold does not appear to be the determining factor in making the site unviable.

We are aware of cases where, when challenged on the suitability of leasehold a developer has subsequently offered the property on a freehold basis, at an increased purchase price to reflect the difference in tenure and therefore the site remains viable.

Q9 Should the Government move towards removing support for the sale of new build leasehold houses through Help to Buy Equity Loan, unless leasehold can be justified and where ground rents are reasonable (which could be a nominal or peppercorn ground rent), and if not, why not?

Yes, the UK Government should not support practices which are detrimental to UK consumers. We strongly support the restriction of new build houses being created under leasehold for both Help to Buy Equity Loan and in general, subject to the exemptions detailed in our response to question 6.

In exempting leasehold housing from the Help to Buy Equity Loan scheme the Government will make a clear statement there onerous lease terms are unacceptable and should go a long way to ensuring that they cease.

Q10 In what circumstances do you consider that leasehold houses supported by Help to Buy Equity Loan could be justified?

Only under exceptional circumstances such as those detailed under Q6.

Q11 Is there anything further the Government could do through Help to Buy Equity Loan to discourage the sale of leasehold houses?

The Government could encourage builders to put right previous unfair leasehold terms by refusing to fund further projects by those builders that have previously sold properties under unfair lease terms and refused to revisit them. The Government should not be supporting firms that it believes are acting unreasonably and to the detriment of consumers.

A code of practice for developers and builders would be helpful which should set out very clearly expectations regarding acceptable and unacceptable practice, to give consumers and others confidence that they are treated fairly.

If developers and builders act in a way that contravenes this code, there should be an Ombudsman Service in place to offer recourse and redress for consumers. In much the same way as other sectors such as financial services providers are held accountable for unfair practices. The reputation of an industry can easily be tarnished by the actions of a minority; a code of practice is likely to improve overall consumer confidence in house builders and developers.

Q12 What measures, if any, should be considered to minimise the impact on the pipeline of existing developments?

The remaining houses on developments still under construction should be sold on a freehold basis, where this is feasible. Those properties on the site already sold as leasehold should be given the option to convert to freehold, which could be done through a deed of variation.

Limiting the reservation and increase of ground rents on all new residential leases over 21 years

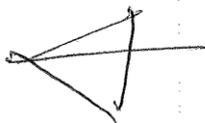
Q13 What information can you provide on the prevalence of onerous ground rents? We are keen to receive information on the number and type of onerous ground rents (i.e. doubling, or other methods) and whether new leases are still being sold with such terms.

The following was received by a Society as part of a mortgage application in June 2017.

I have attached a copy of Clause 8 of the Lease and the reason for this is the rent review has the £"150.00 ground rent doubling every ten years up until the 50th anniversary where the rent becomes capped.

The effect of this is as follows:

Rent 2008: £150
Rent 2018: £300
Rent 2028: £600
Rent 2048: £1200
Rent 2058: £2400
Rent 2068: £4800



The term of the mortgage is 35 years and assuming completion is this year the rent in the final year of the mortgage (2052) would be £1200

8.1 On each Review Date the rent is to be increased to double the Rent reserved before the relevant Review Date and the reviewed Rent will be payable from and including the relevant Review Date

DCLG acknowledges in its consultation that in 2016 10,000 leasehold houses were sold and in total approximately 1.2million leasehold houses are currently in existence. Typically lenders will only capture and store a limited amount of data regarding the lease such as the length of the term, initial ground rent and the fact that the property is leasehold. Copies of the legal documentation are only likely to be held by the conveyancer if anywhere, it is therefore difficult to quantify the extent of the issue, particularly as homeowners will only become aware upon a rent review or sale of the property.

Q14 What would a reasonable ground rent look like, in terms of i) the initial annual ground rent, ii) the maximum rate of increase in annual ground rent, and iii) how often the rate of increase could be applied to an annual ground rent? Please explain your reasons.

What is considered reasonable may well differ from region to region and is open to interpretation. Terms which affect the future saleability of the property and impact the affordability of a homeowner will clearly fall under the category of unreasonable.

The Building Society sector is supportive of the stance Nationwide building society and others have taken restricting its lending on onerous ground rent in a pragmatic and proportionate way. We would like to see leasehold properties adhere to key principles which are fair and transparent for consumers. At no point do we believe that doubling of ground rent is fair or appropriate, this should be linked to an appropriate index and not reviewed too often.

Q16 Would restrictions on ground rent levels affect the supply of new build homes? Please explain.

No, we do not believe that is would.

Q17 How could the Government support existing leaseholders with onerous ground rents?

Information should be made easily available to assist leaseholders in understanding their options when dealing with onerous ground rent and other unfair terms. There should be a clear pathway to challenging these terms and ensuring that consumers know their rights. Government should seek to understand whether these contracts meet unfair consumer contract terms definitions and whether these terms can and should be considered void and therefore unenforceable.

From our understanding even if a lease is in scope of unfair contract terms, the mere fact that a term seems to be unfair (eg ground rent increasing at an exponential rate) it does not mean that a court would necessarily deem it an unfair term.

Exempting leaseholders potentially subject to 'Ground 8' possession orders due to their level of ground rent

Q19 Should the Government amend the Housing Act 1988 (as amended by the Housing Act 1996) to ensure a leaseholder paying annual ground rent over £1,000 in London or over £250 in the rest of England is not classed as an assured tenant, and therefore cannot be issued with a Ground 8 mandatory possession order for ground rent arrears? If not, why not?

Yes, we would be supportive of the proposed amendment.

Service charges for maintaining communal areas and facilities on freehold and mixed tenure estates

Q20 Should the Government promote solutions to provide freeholders equivalent rights to leaseholders to challenge the reasonableness of service charges for the maintenance of communal areas and facilities on a private estate? If not, what management arrangements on private estates should not apply?

Yes, we believe freeholders should have equivalent rights.

Future issues

Q21 The Housing White Paper highlights that the Government will consult on a range of measures to tackle abuse of leasehold. What further areas of leasehold reform should be prioritised and why?

For both leasehold houses and leasehold flats there is scope to vastly improve the situation for existing and future leaseholders. As mentioned in our responses to earlier questions there is a need for a model lease with standardised terminology. Earlier disclosure of the details of the lease would also help prospective homeowners in reaching informed decisions. These issues should be examined as part of the Government review into the Homebuying process.

Whilst there are improvements that desperately need to be made to leasehold and in-particular leasehold housing, it is important that any changes the Government makes do not blight existing leaseholders exacerbating the problem for them. There is a danger of creating a two-tier market which would be unhelpful.

The BSA would be happy to continue its engagement with Government as it progresses policy in relation to leasehold reform.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £345 billion, and account for approximately 20% of both the UK mortgage and savings markets