



London Leaseholders' Network

Incorporating the LONDON FORUM FOR COUNCIL LEASEHOLDERS' ASSOCIATIONS

Submission to the Office of Fair Trading Enquiry into Housebuilding 2007

Summary

As the provision of housing again rises to the top of the agenda of UK priorities we find that, despite some 35 attempts to reform the legislation controlling its operation since 1880, leasehold, for all that it remains an anachronistic remnant of the feudal system, it is daily put to use more now than at any time, not only in its complete form, but increasingly in its economy form, as 'shared ownership'.

A 21st century analysis of its workings shows it to amount to:-

- a **contract that is unfair** in that its terms are imposed by landlords as providers on leaseholders as consumers.
- A contract that when running optimises the **abuse** by landlords of leaseholders as a captive market for insurance, building works and other services.
- A product that is marketed as property but which, once purchased, provides only the **wasting asset** of a right to occupy for a limited term.
- A contract for which the resolution of its shortcomings, through translation of the right to occupy into an interest in the freehold - the property - finds the leaseholder **discriminated against**.

Contents

Summary	page 1
Contents	page 1
1. Background	page 2
2. Leasehold as an Unfair Contract	page 4
3. Running with Leasehold – Insurance	page 5
4. Running with Leasehold – Works	page 7
5. Running with Leasehold – Services	page 9
6. Undertaking Enfranchisement	page 10
7. London Leaseholders' Network - who we are	page 11

London Leaseholders' Network

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Background

1.1. Leasehold

- 1.1.1 More than 50% of us now live in cities where housebuilding typically amounts to the construction of flats. These flats are then either rented by the week, under long leases, or shared ownership schemes.
- 1.1.2. A long lease can be sold and it can be inherited. Consequently it is considered as equity, can be used as collateral for loans and operates in the economy in the same way as the ownership of freehold property.
- 1.1.2. Increased ownership of equity across the economy is valued by Government for its potential to fund later life.
- 1.1.3. Purchase of a lease confers exclusive vacant occupation of a property whilst ownership and control of the property remains with the freeholder.

1.2. Initially:-

- 1.2.1. The leaseholder's benefits of occupation simulate those of the full ownership enjoyed by a freeholder with vacant possession.
- 1.2.2. The leaseholder enjoys a honeymoon period during which the market value of the lease will typically increase along with other local property values and a wise investor in a rising market, such as has been experienced over the last few years, can often get out with substantial gains.

1.3. In the medium term:-

- 1.3.1. The freeholder retains the responsibility and controlling hand over expenditure on the maintenance and improvement of the property. When the freeholder or landlord exerts this control then it is usual that it is not the freeholder but the leaseholder who under the terms of his or her lease is required to pay.
- 1.3.2. Housing is currently generally built for a sixty year life with major refurbishment after thirty years and cyclical decoration and maintenance on three to seven year cycles.
- 1.3.3. **It is during this interim period that dissatisfaction tends to set in amongst purchasers of leases.**

1.4. In the long term:-

- 1.4.1. A lease confers vacant possession for a fixed term. On reaching the end of that term the lease becomes worthless. For this reason it is recognized as a *wasting asset* - its value wastes away to nothing.
- 1.4.2. That a lease is a wasting asset aspect is generally said to begin to take effect once the remaining years, or term, on a lease drops below as many as 80 (eighty) years. A lease becomes progressively more difficult to mortgage or sell on as its remaining term decreases below 80 years.

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Office of Fair Trading Enquiry into Housebuilding Background

- 1.4.3. The initial term of a lease is determined without reference to the expected life of the building. Tower blocks in Westminster have been stated to have been built in the 1960s to last for 30 years but 125 year leases on flats in the blocks have been sold since the 1980s when the right to buy was introduced.
- 1.4.4. There is a recognised but conditional, procedure for extending a lease for an additional 90 years.
- 1.4.5. If a lease expires with a leaseholder in occupation then they have certain rights to continue in occupation as weekly tenants but all equity that they had will have wasted away.
- 1.4.6. When a lease is extended it is done without necessarily making reference to the building's condition or expected life.
- 1.4.7. Vendors do not draw attention to the length of lease when advertising leasehold property and in consequence the affect remains obscured from public view.
- 1.4.8. In order to dispose of a short lease the leaseholder is forced to negotiate an extension to the lease and finds himself beholden to the whim of a freeholder who can in practice through non co-operation make this difficult.

1.5. The root problem is that:-

- 1.5.1. The leaseholder buys into circumstances over which he or she subsequently has no control and whilst legislation was enacted in the form of the Commonhold and Leasehold Reform Act 2002 (CLARA) that was intended to replace leasehold with commonhold under which tenants would share between them the ownership of the freehold and with it joint responsibility for the control of expenditure on the property's repair and maintenance along with the burden of its cost.
- 1.5.2. CLARA failed to have the desired effect for newly constructed properties because it left leasehold in existence as an option alongside of commonhold. Given the choice landlords have stuck with leasehold that favours them with a continuing interest in the properties.
- 1.5.3. CLARA failed to have the desired effect for existing properties because the hurdles to be negotiated to carry out the process of *enfranchisement*, to commonhold are too many and too difficult to be surmounted.
- 1.5.4. Following 5 years of the operation of CLARA at 19th July 2007 there were 13 registered commonholds comprising 129 units (Lords answer by The Parliamentary Under-Secretary of State, Minister of Justice Lord Hunt of Kings Heath 26th July 2007 leaving some 3 million leasehold units with the potential shortcomings as outlined in this report.

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Leasehold as an Unfair Contract

2.0.0. The dissatisfaction felt by leaseholders in the medium and long term is attributable to a lack of fairness in, firstly the way that leasehold is entered into and secondarily to the way in which it is subsequently operated by landlords. *These faults are inherent in the leasehold system as currently framed in law.*

2.1. Entering into a lease

2.1.1. When entering into a lease, purchasers usually engage several professionals, ostensibly to safeguard their interests but in practice leases are offered on a take it or leave it basis and the only alterations that the professionals can bring about are the correction of outright errors and advice to pull out of the deal. *As such the lease is an unfair contract.*

2.1.2. The lease is a contract that is drawn up by the freeholder's legal advisors to serve the medium and long-term interest of the landlord. The conveyancing process includes a stage during which the terms of the lease are examined and agreed. Whilst it is not impossible for an individual lease to be altered to suit the purchaser of a lease and there may be isolated examples where this has been achieved, the general case is that the lease is presented on a take it or leave it basis. *As such the lease is an unfair contract.*

2.1.3. Leases have value as equity because they can be transferred in ownership through inheritance or sale but the purchaser of a lease that is not a new lease has absolutely no right to agree the terms. If he or she wants them altered he or she can try by approaching the landlord and subsequently the regional Leasehold Valuation Tribunal but effectively he or she is bound to operate under terms that were laid down and nominally agreed between two parties other than himself some years earlier. *As such the lease is an unfair contract.*

2.1.4. The process can, in theory, work in the case of a single building that is to be leased to a single leaseholder with a new and individual lease but in these circumstances freehold would be sought and expected from the outset.

2.1.5. Likelihood of a lease being varied during the conveyancing process diminishes rapidly in inverse proportion as their numbers increase within one building.

2.1.5. Likelihood of a lease being varied during the conveyancing process diminishes further in inverse proportion to the amount of leasehold properties a landlord has because a landlord will naturally want to limit the number of lease types.

2.1.6. If lease purchasers were able to work together they could perhaps exert their collective interest but the landlord has the upper hand because he or she takes them as individuals as they come and then enforces his need for a common approach against them.

2.1.7. Leaseholders subsequently have a right to apply to their landlord for the names and addresses of their fellow leaseholders under Section 11 of the Leasehold Reform, Housing and Urban Development Act 1993 (ch 28) but by they acquire this right by virtue of their leases and by the time that they have these the terms of the leases have been set.

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Running with leasehold ~ Insurance

3.0.0. The lease will normally require the landlord to take out adequate insurance for the building and the common parts, and will give him the right to recover the cost of the premium through the service charges. This policy will not normally cover the possessions of individual leaseholders.

3.1. In the landlords' interest

3.1.1. The lease is an instrument devised by the landlord who owns the building but it is the leaseholders who pay for the insurance of his asset.

3.1.2. The landlord or the managing agents make the choice as to which insurers are used, which policy is taken and which clauses are included.

3.1.3. So long as the insurance clauses meet the landlord's basic requirements the landlord gets no direct benefit of a competitive deal because all the costs are to be passed on to the leaseholders.

3.1.3. The landlord or the managing agents can, and often does, charge a management, arrangement or administration fee on top of the insurance premium. ("Landlords' £1bn insurance sting" Jo Thornhill, Mail on Sunday 30 May 2006 at:-

http://www.thisismoney.co.uk/mortgages/buy-to-let/article.html?in_article_id=409465&in_PAGE_ID=56)

3.1.5. The landlord or the managing agents may earn substantial commission on the insurance. In the instance cited above it amounted to 100% of the premium.

3.2. The requirements.

3.2.1. Under the terms of the lease it is to be expected that the landlord will be legally required to insure the building against fire and any other perils.

3.2.2. If the building is damaged the landlord has to claim on this insurance and the insurance payout has to be spent on reinstating the landlord's building.

3.2.3. In theory it should not be possible to get a mortgage on a property that does not have buildings insurance.

3.2.4. Many mortgage companies are prepared for single flats to be insured as individual properties but this brings the risk that all the common areas, the roof and even subsidence are not covered – without which the flat would be unviable. Also if each flat has a separate insurance then the administrative process of dealing with all the claims following an incident will be significantly increased. If flats are insured separately and one of these insurances is allowed to lapse then this would threaten the entire rebuilding project in the event of a major loss.

3.2.5. The provision of alternative accommodation for all the occupants ought to be covered.

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Running with leasehold ~ Insurance

3.3. The leaseholders' concern.

- 3.3.1. The landlord is bound by the lease to ensure that any damage caused by an insurable event is made good by the landlord and it is the landlord's responsibility under the terms of the lease to ensure that he has adequate insurance to cover this.
- 3.3.2. The insurance that the leaseholder has an interest in is that he or she wants to know that if in the event of being displaced during repairs or rebuilding he or she will be provided with equivalent temporary accommodation. This risk ought to be included in the landlord's insurance.
- 3.3.2. The leaseholder does not get any choice over any aspect of the insurance but is simply given the bill without seeing anything that could be described as a competition.
- 3.3.3. Leaseholders frequently complain that they could have made substantial savings had they be able to shop around for insurance. The spread of prices between the lowest and the highest can be as much as five times.
- 3.3.4. Deals such as discounts offered where an occupier signs up for contents insurance along with their building insurance are not available to leaseholders.
- 3.3.5. It is in the landlords interest to have the premium reduced by significantly increasing the excess on the policy. Subsequently if a claim is made, the leaseholder may find that no benefit is gained from the insurance because the amount that would have been claimed is less than the excess. In these circumstance the leaseholders get bills for the repairs that they thought should have been covered by the building insurance that they have been paying for.
- 3.3.6. A landlord dealing with a large number of properties will see every single block as a statistic. If subsequently a property has subsidence there have been instances where it has been found that the subsidence was known about by the landlord's or managing agents' organisations before the current insurance was taken out. In these cases the insurers will, like as not, refuse to pay out and landlord will attempt to pass the cost of underpinning to the leaseholders. This is what happened initially on Highbury Quadrant Estate N5, the landlord being the London Borough of Islington.

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Running with leasehold ~ Works

4.1.2. Overview of Repairs.

- 4.1.2. The property only naturally deteriorates with time and maintenance is then required.
- 4.1.2. Although maintenance of the property benefits the freeholder in the long run, the leases normally require that the leaseholders pay for this between them.
- 4.1.2. Historically, both commercial as well as residential leases, were generally 'repairing leases' that required that leaseholders hand back property in the same condition as that in which they found it by repairing at their expense
- 4.1.3. The FAQ on Bedford Estates web site has the question:-
- "Q. *I have a full repairing lease. Why does the Estate carry out external decorations and then re-charge the cost to me?"*
- "A. *Almost all of our commercial leases reserve this right to the Estate, with a three yearly redecoration cycle. The reasons for this are to ensure that Estate properties are maintained in good decorative order and repair. Where possible we try to redecorate blocks of property in the same year to maintain consistency of appearance. There can also be economies of scale arising from this, which are passed on to tenants. Many tenants do not have the expertise or the time to get involved with organising and supervising external decorations and welcome having this done for them.*"
- 4.1.4. The landlord, or the managing agent, decide upon the works to be carried out. The decisions made can have far reaching effect on both the amount to be paid by the leaseholders and the extent of their disruption during the works but they are a captive market and the landlord's **dominant position** in supplying these services leaves to what amounts to a **captive market** and the leaseholders wide open for **abuse**.

4.2. Improvements and other alterations.

- 4.2.1. Leases often allow for leaseholders to also be charge for improvements. For example such items as a double glazing replacement where painting the existing windows would have sufficient for maintenance alone.
- 4.2.2. In practice legislation aimed at providing consultation for leaseholders over both maintenance and improvements amount to no more than giving leaseholders a right to be heard and their comments "taken into consideration".

4.3. The landlords' economies of scale.

- 4.3.1. The increasing use, by local authority landlords, of innovative ways of engaging large contractors militate against the leaseholders putting forward local small jobbing builders with lower overheads to tender for works.
- 4.3.2. A landlord will naturally apply economies of scale where they are available.
- 4.3.3. It is in the landlord's interest to have all bills for individual repairs dealt with on an aggregated basis through a relatively large contractor.
- 4.3.4. The landlord merely passes the costs on and consequently does not share his leaseholders' interest in keeping their size down.

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Running with leasehold ~ Works

- 4.3.5. When a public sector landlord contemplates major repairs across all its properties it now frequently chooses to aggregate all the work into one vast project and enters into a *framework agreement*.
- 4.3.6. Each leaseholder is given the chance to express their concern and can contact their own international contractor to ensure that they see the advert in the Official Journal of the European Union (OJEU) but their local builders will not be able to handle either the size of the contract nor the process of bidding.
- 4.3.7. Matters are generally made worse by the fact that the exact nature, timing and certainty of the works to be carried out are not generally known when the framework agreement is being set up.

4.4 Strategic Alliancing Agreements

- 4.4.1. Strategic Alliancing Agreements that are now being set up along with Framework Agreements would be worthy of examination as contrary to fair trading practice in their own regard.
- 4.4.2. Under these agreements the framework contractors agree to share details of their supply chains with a view to enabling all the less competitive contractors to adopt the supply chain of the most competitive in each field.
- 4.4.3. Whilst this will drive down costs for that particular landlord it amounts to the formation of a *cartel* and will give those contractors engaged within framework contractors for any one landlord an unfair advantage when tendering for work with any other landlord. Any new contractor trying to enter the market will have no hope of competing.
- 4.4.4. One such Strategic Alliancing Agreements could involve as many as a dozen contractors and two or three such agreements operating say in various London boroughs could effectively pull the vast majority of contractors operating on refurbishment works in the Region into one massive *cartel*.

4.5. How can leaseholders be expected to Pay?

- 4.5.2. Where the works undertaken result in a bill to the leaseholder in excess of £350 he or she may be subject to forfeiture and effectively be made homeless if he or she can't pay but it is always argued that leaseholders can always borrow against the equity that they have in their leases.
- 4.5.4. Borrowing against the equity in a lease will not work for those who are too elderly to be able to get a mortgage, or those who have insufficient credit rating for instance due to already having borrowed excessively. (Average consumer debt June 2007 was £8,841 and including mortgages £55,567)
- 4.5.5. Borrowing against the equity in a lease will only work in a rising market but not when property prices are falling or even if they are stable.
- 4.5.6. The rising market that has prevailed for the last few years has masked the essential faults outlined here.

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Running with leasehold ~ Services

- 5.0.1. Landlords increasingly offer other services to leaseholders that are not essential to keeping a roof over their heads find that they have no choice.
- 5.0.2. If leaseholders have outstanding bills for ground rent or service charges in excess of £350 then they can be subject to *forfeiture* and become homeless.

5.1. Concierge services –

- 5.1.1. Concierge services are frequently sub contracted to companies that do not aim to do more than ensure that someone is present for the contracted hours.
- 5.1.2. The service frequently is found to be provided by an ever-changing staff who consequently do not get to know the buildings or occupants that they are there to serve.
- 5.1.3. The service is often found not to cover sufficient hours not sufficient entrances and other aspects of a building to amount to a worthwhile security asset and generally not to provide value for money that could not be bettered through exposure to open competition.

5.2. Cleaning services

- 5.2.1. Cleaning services are frequently sub contracted.
- 5.2.2. The service frequently is found to be provided by an ever-changing staff who consequently do not get to know the buildings or occupants that they are there to serve.
- 5.2.3. The service is often found to be generally poor and not to provide value for money that could not be bettered through exposure to open competition that could bring in a local individual who could enjoy a higher personal take home pay for a smaller outlay by cutting out irrelevant office staff.

5.3. Ground maintenance services.

- 5.3.1. Ground maintenance services are frequently sub contracted.
- 5.3.2. The service frequently is found to be provided by an ever-changing staff who do not get to know the buildings or occupants that they are there to serve.
- 5.3.3. The service is often found to be generally poor with grass left longer than agreed, refuse left scattered throughout the grounds and generally not to provide value for money that could not be bettered through exposure to open competition that could bring in a local individual who could enjoy a higher personal take home pay for a smaller outlay by cutting out administrative staff.

5.4. Television and other communication services.

- 5.4.1. If every occupant were to seek provision of communication services separately, it would lead to an unsightly and deleterious proliferation of cables and dishes but their provision by the landlord exposes the leaseholders to exploitation with the provision of poor services whilst adding on their own commission without any real incentive to seek out the best deal because that the leaseholders are a captive market.

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Undertaking Enfranchisement

- 6.0.1. The leaseholder can attempt to gain control over his or her situation by exercising their right by *enfranchisement* to collectively take over the freehold.
- 6.1.1. Anyone could buy a freehold were it to be offered on the open market but for the leaseholders to obtain it by enfranchisement they are placed at a disadvantage. Effectively they are *discriminated against*.
- 6.2. Discrimination against a leaseholder purchasing the freehold through enfranchisement**
- 6.2.1. Residential Leaseholders are prohibited from exercising their right to enfranchise where 25% or more of the whole premises are non-residential. Thus these leaseholders are *discriminated against*. (Section 115 Commonhold & Leasehold Reform Act 2002 (Ch 15))
- 6.2.3. Residential Leaseholders are prohibited from exercising their right to enfranchise where they cannot gain the co-operation of one half of the qualifying tenants and thus they are *discriminated against*. (Section 13 Leasehold Reform, Housing and Urban Development Act 1993 (Ch 28) as amended by Sections 119 & 120 Commonhold & Leasehold Reform Act 2002 (Ch 15))
- 6.2.4. Leaseholders only qualify for enfranchisement once they have been leaseholders for a minimum of 2 years and thus they are *discriminated against*. (Sections 127, 130 & 139 Commonhold & Leasehold Reform Act 2002 (Ch 15))
- 6.2.5. Leaseholders holding a lease where the un-expired term is less than 80 years have to make an additional payment against 'marriage value' despite the fact that they pay an open market value when purchasing the lease initially. This marriage value is not brought into purchases of freeholds sold on the open market nor where enfranchisement involves a lease with more than 80 years on the term. Thus the leaseholder with a lease shorter than 80 years is *discriminated against*. (Section 146 Commonhold & Leasehold Reform Act 2002 (Ch 15))
- 6.2.6. Where the marriage value is brought into play it is calculated against a sliding scale and the interest in it is apportioned by a fixed 50 / 50 % split with the landlord. This amounts to *price fixing*. (Section 145 Commonhold & Leasehold Reform Act 2002 (Ch 15))
- 6.2.7. Further classes of leaseholder are defined as selected for the application of marriage value according to the relationship between their ground rent and rateable value. Thus they are *discriminated against*. (Section 1 Leasehold Reform Act 1967 (Ch 88))
- 6.2.8. The Commonhold & Leasehold Reform Act, in so far as it ensures the discrimination against leaseholders purchasing their freehold compared with individuals purchasing it on the open market amounts to a *breach of European Community Law*.

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Office of Fair Trading Enquiry into Housebuilding
The London Leaseholders' Network

- 7.1. London Leaseholders' Network is the umbrella group for borough wide leaseholders' associations across London.**
- 7.2. The Network holds regular meetings bringing together representatives of organisations from over a dozen of the 33 London Boroughs
- 7.3. The Network is recognised as representative of London's social leaseholders by Communities and Local Government, The Mayor's office of the Greater London Authority, The Leasehold Advisory Service and the London Tenant Federation. In consequence the Network sends delegates to the Social Sector Working Party (Leasehold) and the London Mayor's Housing Forum Consultation Sub-Group

This submission is made in response to the Office of Fair Trading's
Investigation into:-
Housebuilding in the UK – Housebuilding Market Study August 2007

Any enquiries regarding this response should be made to:-

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