

Leasehold and Freehold Property in England

A French Position

Under the co-ownership system the tenant becomes the owner of the flat and the co-owner of the fraction of the common parts attributable to the flat.

The building is usually managed by the co-ownership manager (syndic de copropriété) which is a private legal entity and generally a specialist real estate company appointed by the co-owners during the Annual General meeting (Assemblée générale des copropriétaires).

The co-owners designate some of their members to act as a governing board (Conseil Syndical). The Conseil Syndical¹ then directs the Syndicat des copropriétaires on the instructions of the co-owners. The Syndicat des copropriétaires acts directly on the instructions of the Conseil Syndical.

B Basic Leasehold (England)

A basic lease confers a contractual right on the tenant to use the property subject to the terms of the lease. Each tenant is responsible for the upkeep of the interior of his flat whilst the freeholder (still commonly referred to as the landlord) is responsible for insuring the block and maintaining the main structure and common areas. The freeholder charges the tenants a ground rent for their use of premises in which he had a technically “superior” interest, and levies a charge to cover the costs involved in managing the property. There are a number of ways provided for by statute for the tenants to acquire some of the rights and responsibilities of the freeholder and to enhance their own rights.

1. Service charge exclusions

All the expenses incurred by the freeholder are commonly apportioned each year between the tenants by way of service charge.

Legal expenses arising from litigation of disputes in England must normally be paid by the unsuccessful party. In “small” claims (now up to £10,000), however, litigants must normally bear their own legal costs regardless of the outcome. The freeholder may therefore incur legal expenses pursuing an individual tenant which it cannot recover from that tenant.

Whether or not the freeholder is entitled to recover from all the tenants legal expenses incurred in pursuing an action against an individual tenant will depend on how the Lease document and in particular the service charge clause is drafted. In *Plantation Wharf Management Limited v Jackson and Another*², the lease permitted the recovery of professional adviser fees relating to the enforcement of covenants. The Land Chamber Upper Tribunal held that this was sufficiently clear and unambiguous to mean that the tenants were liable, via the service charge, for the landlord's costs of suing tenants.

Ideally, the tenant will wish to explicitly exclude from the service charge, any costs incurred by the landlord as a result of bringing legal action against a tenant.

¹ Similar to a Commonhold Association provided for under Part 1 of the Commonhold and Leasehold Reform Act 2002: <http://www.legislation.gov.uk/ukpga/2002/15/part/1>

² [2011] UKUT 488 (LC)

Other covenants in the lease can also be qualified or excluded so as to reduce the burden falling upon the tenants.

2. Right to manage

The right is exercised by the service of a formal notice on the landlord. Management of the property then transfers to the *right to manage company* set up by the tenants.

The landlord's consent is not required and there is no requirement to prove mismanagement on the part of the landlord however the landlord is entitled to membership of the company from the date of the acquisition.

See Part 2 of the Commonhold and Leasehold Reform Act 2002³ for detailed requirements.

Potential benefits:

- Enables tenants to have more input in management decisions. The RTM Company acquire the management functions for the premises which are defined in s.96(5) as functions with respect to services, repairs, maintenance, improvements, insurance and management. The transferred functions also include enforcement of the covenants under the lease.

Potential drawbacks:

- Management Company becomes subject to onerous statutory duties and liabilities which extend to all decision making regarding the property. This will usually require appointment of a specialist management agency.
- Involves setting up and running a company which involves time and cost.

No change:

- Landlord continues to receive rent, take the reversion when the leases expire or are surrendered or forfeited, and own the common parts.

3. Right to extend

The conditions under the Leasehold Reform Housing and Urban Development Act 1993⁴ must be satisfied; it must be a long lease (over 21 years) and it must have been owned for at least 2 years at the date of application. If granted, the extension will be for a term which expires 90 years after the expiration of the current lease.

The premium payable by the tenant in respect of the grant of the new lease shall be the aggregate of:

- (a) the diminution in value of the landlord's interest in the tenant's flat (the difference between the value of the landlords interest in the flat before and after the grant of the new lease if sold on the open market);

³ <http://www.legislation.gov.uk/ukpga/2002/15/part/2>

⁴ <http://www.legislation.gov.uk/ukpga/1993/28/contents>

- (b) the landlord's share of the "marriage value" (if there is still 80 years or more left to run on the lease, then marriage value will not be payable); and
- (c) any amount of compensation payable to the landlord (compensation for any reduction in value of the landlord's property which is not the tenant's flat).

The "marriage value" is the difference between:

- (a) the aggregate of:
 - (i) the value of the interest of the tenant under his existing lease,
 - (ii) the value of the landlord's interest in the tenant's flat prior to the grant of the new lease, and
 - (iii) the values prior to the grant of that lease of all intermediate leasehold interests (if any); and
- (b) the aggregate of:
 - (i) the value of the interest to be held by the tenant under the new lease,
 - (ii) the value of the landlord's interest in the tenant's flat once the new lease is granted, and
 - (iii) the values of all intermediate leasehold interests (if any) once that lease is granted.)

The Landlord's share of the marriage value is 50%.

C Acquiring Freehold (Leasehold with a share of Freehold)

There are also circumstances where tenants can acquire the freehold outright. These may be where the freeholder gives them an option to buy the freehold, or where they qualify for the right under statute. The following statutes are relevant.

1. Right of First Refusal

Tenants have the option to buy the freehold should the landlord choose to sell his interest in the property or should the option to purchase be included in the lease subject to certain conditions being satisfied under Part 1 of the Landlord and Tenant Act 1987⁵.

2. Collective Enfranchisement

The Leasehold Reform, Housing and Urban Development Act 1993⁶ enables tenants to acquire the freehold of premises at a price determined in accordance with schedule 6 of the statute.

⁵ <http://www.legislation.gov.uk/ukpga/1987/31/contents>

⁶ <http://www.legislation.gov.uk/ukpga/1993/28/contents>

There are various requirements contained within the statute in relation to qualifying premises and qualifying tenants.

The premises extend to acquisition of the common parts:

Section 1(2)(a) provides that when exercising the right to collective enfranchisement, the qualifying tenants are entitled to acquire the freehold of any property which the qualifying tenant is by his lease, entitled to use in common with the occupiers of other premises. Technically known as “appurtenant property”, this includes such things as garages, outhouses, gardens, and parking areas.

D Your Neighbours’ Landlord and their Tenant

Unlike the co-ownership system in France, a tenant in England who acquires a share of the freehold does not become the sole owner of his or her flat and the co-owner of the fraction of the common parts attributable to the flat (although the new commonhold⁷ tenure has some parallels with the French system).

The tenant now owns two separate interests:

- 1) a leasehold interest in a specific flat; and
- 2) a share of the freehold interest in the whole of the building.

In other words, he owns the freehold of his own flat jointly with his neighbours, and also owns a share of the freehold of their flats – he becomes his own landlord and theirs collectively with his neighbours.

There are nevertheless potential benefits for the tenants from this arrangement:

- Tenants who own the freehold have greater control over the running of the building such as the repair and maintenance of the building, granting of lease extensions, sale of leasehold and insurance.
- A share of the freehold may potentially make a property more saleable due to increased control and protection. It may add value as an additional interest in the property but generally only in cases where the lease has less than 80 years left to run. If the tenant already holds a 999-year lease, then the addition of a share of the freehold interest per se adds no real value.
- There is the ability to granting a lease extension with less cost – this is particularly important where a lease has less than 80 years to run. The lease can be extended for little or no additional payment. If the lease can be extended at the same time as

⁷Defined as “a system of freehold tenure of a unit within a multi-occupancy building, but with shared responsibility for common services”. The form of tenure was only introduced to England in the Commonhold and Leasehold Reform Act 2002. It remains very rare in practice: “In the years since the 2002 Act became law, only a handful of commonholds have been registered whilst hundreds of thousands of long leases have been granted during the same period. As of 3 June 2009, there were 12 commonhold residential developments comprising 97 units in England and one commonhold residential development, comprising 30 units, in Wales.”

the freehold is purchased, the consideration paid for the freehold can be deemed payment for the lease extension also.

There are of course also some potential drawbacks:

- There is no guarantee that all the freeholders will agree on any decision. This can be a particular problem with regards to lease extension. If a lease extension is not granted this can impact on the saleability of the property.
- Where many tenants hold a share of the freehold interest it may be difficult to contact the other owners. Some tenants may live elsewhere and have sub-tenants in occupation. Or they may simply ignore communications.
- The responsibility for the maintenance, repair and insurance of the building and for providing various functions to tenants, and the collecting of service charges and ground rent to pay for all this, requires significant time input.

The following steps are often taken to address these drawbacks:

1) Setting up a company

- If the tenants set up a company to own the freehold, the company structure can help the decision-making process
- On the sale of the freehold interest, an individual owner would sell its share in the management company which avoids obtaining each shareholder's signature.
- The articles of association of the company can set out the circumstances in which leases will be extended or other predictable requests dealt with.

2) Use of a legally binding agreement between tenant shareholders

The agreement can be included in the articles of association or be entered into separately and drafted to include:

- an obligation on all parties to approve extension of a lease upon request at no premium; and
- provision for resolving disputes such as referring matters of disagreement to a third party surveyor or arbitrator.

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