

IT'S THE LAW: Residential Lease Extensions

Lease Sir, can I have some more?



Leases have been around since long before Charles Dickens penned his first novel. The concept of distinguishing between different degrees of title to property ownership was introduced to England in 1290 by the Statute Quia Emptores.

635 years later we got the Land Registration Act 1925. From then onwards the legal title you could own in a property was limited to two categories:

- Freehold (which, for practical purposes, is title forever); and
- Leasehold (which is title limited to a fixed period, known as 'the term').

Nowadays, we also have the concept of commonhold. But for the purposes of this edition of IT'S THE LAW we, like almost everybody else, will just ignore that.

In this edition we are looking at residential leases. Not short lets and not periodic tenancies, but the sort of lease someone who wants to own a flat might buy. Terms of 125 years are probably most common. 99 years is also an old favourite.

As time goes by

The term of such a lease is likely still to be running when the first owner moves to smaller accommodation six feet under. But the fact that the lease will come to an end eventually will impact its attractiveness – and so affect the ease of sale, and value, in future years. That impact will get progressively worse as time goes by. Main stream lenders have policies about the minimum term left to run that they will accept as security. That varies from lender to lender but commonly it's somewhere around 80 years.

So, whilst the buyer of a leasehold property may complete their purchase with Great Expectations, careful consideration should be given to the length of the lease left to run, to ensure that they are not left with a Bleak House (or, in this case, flat).

How to avoid Hard Times

Luckily, the Leasehold Reform, Housing and Urban Development Act 1993 (we'll call it **the Act** for short) comes to the rescue.

The Act provides a statutory right for the owner of a lease of a flat to buy an extension of the remaining term, provided that they satisfy certain criteria. If they do, then they are known as a 'Qualifying Tenant' and they may be entitled to get a new lease which has an additional 90 years added on top of their then remaining lease term.

Their annual ground rent will be reduced to a peppercorn (i.e. nothing) which is another win for them. Amendments, other than the term and rent, can be agreed if the lease requires updating to bring it into the 21st Century.

How to Qualify

In order to consider yourself a Qualifying Tenant the following criteria must be met:

- You must hold a long lease of your flat. The Act defines that as being a lease granted for a term of 21 years or more. It's the whole term initially granted that matters, not the length of term remaining at the time. Whilst it's drafted poorly, the relevant legislation implies that shared ownership tenants will need to have staircased to 100% before they can qualify;
- You must have been the registered owner of the long lease for at least two years prior to applying for an extension;
- You must be a residential tenant. The provisions of the Act do not extend to business tenants. They tend to be looked after by the Landlord and Tenant Act 1954, which is a whole different ball game.

However, a tenant whose immediate landlord is a Charitable Housing Trust will not be a Qualifying Tenant, where the property forms part of the accommodation that the Trust provides in pursuit of its charitable purposes.



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Most Housing Association tenants will not, therefore, benefit from the right, because their landlord will fall within the definition of a Charitable Housing Trust.

In the beginning

The first step that needs to be taken by a Qualifying Tenant intending to exercise their rights under the Act is to serve a notice of that intention. The notice must be in writing (which for these purposes rules out email). Although there is no prescribed form, the Act sets out certain information that needs to be included, such as the Qualifying Tenant's details and the premium that they are willing to offer in return for the extension. The notice must be served on the 'Competent Landlord' who may be the freeholder of the block or the owner of a headlease which is sufficiently long or, in some cases, both. If the notice is not completed and served correctly the landlord may have grounds to reject it. If they do, the tenant will have to go back to the beginning.

Bargain hunter

In order for the notice to be valid, the premium offered to the landlord must be 'reasonable'. A Qualifying Tenant would be well advised to appoint a valuer to advise them to make sure they get it right. Tenants will tend to want to offer a premium towards the lower-end of what can be considered 'reasonable', in the hope of getting a 'good deal'. But if they go too low they risk the notice being invalid.

It's good to talk

The landlord is entitled to make a counter-offer with a higher figure. There is no requirement for their counter-offer to be 'reasonable'. If a counter-notice is served by the landlord, a negotiation period commences which can last for at least two months. During that period the tenant's surveyor will discuss their calculations with the landlord's surveyor with a view to achieving a compromise and agreeing the premium. If no counter-notice is served by the landlord, the tenant will be entitled to apply to the County Court for a Vesting Order, meaning that the lease will be granted to them on the terms proposed in their initial offer. For this reason, it is crucial for landlords to respond to the tenant within the prescribed time period. Large organisations should ensure they have adequate systems in place to ensure that notices being received are dealt with promptly.

Costly business

As soon as the Qualifying Tenant serves the first notice on the landlord, they will become liable for the landlord's reasonable legal and valuation costs. Also, the tenant can be compelled to pay a deposit to the landlord of 10% of the premium offered or £250 (whichever is higher).

Off to court

If the respective surveyors are able to negotiate and agree the premium to be paid, and the terms of the new lease, the lease extension can be progressed. If not, both the Qualifying Tenant and Competent Landlord will have a further four months (six months from the date of the landlord's counter-notice) in which to apply to the First-Tier Tribunal for a determination of how much should be paid and what the terms of the new lease should be.

Home stretch

Once the negotiations have been finalised and the lease itself is agreed (or determined by the FTT) and completed, the lease extension will be registered at the Land Registry. The lease extension is itself a new lease and the original lease will be treated as having been surrendered. If the original lease was subject to a mortgage that mortgage will essentially transfer to the new lease.

That'll cost you

If the Qualifying Tenant doesn't proceed to complete the lease extension within the required timescales, or if they do not apply to the FTT in time, they will temporarily lose their rights under the Act. They can start the process again, but only after 12 months. They will still be liable to pay the landlord's costs.

Safe as houses

A tenant of a house (rather than a flat) may also be entitled to a lease extension. The law governing leasehold houses is different, and falls within the Landlord and Tenant Act 1967 (LTA1967). Unlike with flats, tenants of houses have two options: to extend their lease by an additional 50 years, or to enfranchise (which is a fancy word for purchasing the freehold). On a lease extension under the LTA1967 no premium will be payable, but the landlord is currently entitled to increase the annual ground rent to an open market rent subject to review after 25 years. On enfranchisement under the LTA1967, the premium payable to the landlord (the purchase price) will be the market value of the freehold of the property according to the landlord's independent valuation advice.

Similar to the process for lease extensions of flats, the starting point is the tenant serving formal notice on the landlord stating their intentions (though no premium needs to be included in the initial notice) and if the proposed premium or rental value cannot be agreed following negotiations, the matter can be referred to the First Tier Tribunal for a determination.

Current Affairs

The existing law and practice surrounding lease extensions and enfranchisement has fallen under heavy criticism in recent years, with the Government agreeing that the system does not represent a fair deal for tenants. Our Mutual Friend, the Law Commission, responded in July 2018 by issuing a consultation paper following a detailed review, with the intention of simplifying the process for both landlords and tenants. Responses are being analysed before further steps towards reform can be taken, but it seems inevitable that significant changes to the system will be forthcoming in the future.

The tiny print

This is one of a series of leaflets published by Devonshires' Real Estate & Projects Department aimed at our property owning and developing clients. No action should be taken on the matters covered by this leaflet without taking specific legal advice.

Find out more

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