Real Estate:UK

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To whom it may concern

Real Estate:UK (**RE:UK**), the representative body for the UK real estate sector, writes in response to the Ministry's consultation: *Quid prio quo leases and the ground rent cap.* For the avoidance of doubt, this letter should be treated as RE:UK's formal response to the consultation.

RE:UK brings together global and domestic capital, world-leading expertise and forward-thinking policy to drive growth. With over 500 member organisations spanning investors, developers, advisers and operators, we represent the full breadth and diversity of the market, including those investing in and providing homes for leaseholders.

Formerly the British Property Federation, we have constructively engaged with successive governments on reforms to the leasehold sector for many years, and support many elements of the forthcoming Commonhold and Leasehold Reform Bill.

However, we consider that this consultation is predicated on fundamental misconceptions about ground rents – which we identified in our submission to the Housing, Communities, and Local Government Select Committee's pre-legislative scrutiny of the Draft Commonhold and Leasehold Reform Bill (**Draft Bill**) – with several significant consequences for the reforms and the sector. As such, we feel we cannot respond through the normal process to this consultation and instead set out our concerns through this letter.

The consultation mischaracterises ground rents

The central reason we do not believe we can respond through normal channels to the consultation is that it is based on a misconception about what a ground rent is. Ground rent is a contractual payment that is consideration for the lease as granted; it forms part of the value of the property. The consultation, and the Government's wider positioning on ground rents, suggests that ground rents are payments of some other, unspecified kind – neither forming part of the lease value, nor payment for a service. This is incorrect.

The consultation appears predicated on the Government's belief that, because it has not seen specific evidence of it occurring, that lower premiums are not paid as a result of a ground rent being agreed. This is not reflective of the reality of the sector; obligations to pay ground rents can be and are reflected in lower premiums. This consultation's position appears to rely on the Competition and Markets Authority's investigation into a small number of ground rents; this was not reflective of the entire sector and should not form the basis of a blanket policy. To do so would continue to base policy on wholly insubstantial evidence, as has been done regarding the proposed £250 ground rent cap in the Draft Bill.

The consultation's framing of ground rents is also counter to the Ministry's previous position. The Impact Assessment for the Leasehold Reform (Ground Rent) Act in 2022 found that the existence of ground rent may be reflected in an average reduction of c.3.3% of the purchase price.[1] At paragraph 4.3.3, the Ministry explicitly states:

> *The average price increase for the average new build leasehold flat is comfortably within our central estimate of the freehold premium of 7.1%, indicating that there is scope for the upfront price to fully reflect the present value of the ground rents without breaching the freehold equivalent price (with a certain amount of leeway remaining to allow for the value of those continuing leasehold costs to still be reflected).*

In essence, it accepts that all leases meet the proposed definition of a quid pro quo lease as set out in the consultation – i.e. that the premium lower, and the rent higher, than each would otherwise have been, and the value of paying the lower premium greater than the capitalised value of the extra rent.

This is even more substantial in the retirement housing sector, with the Impact Assessment predicting a £15,000-18,000 (c.5%) increase in purchase prices due to ground rent capitalisation – contradicting the assumption underlying current Government policy proposals (including the blanket £250 cap itself) that ground rents across all properties are equal. The residential property market is diverse, and the value that ground rents reflect will vary across individual properties and tenures. For example, in retirement housing and holiday parks, the ground rent forms part of consideration for more extensive shared spaces, hence larger impacts of capitalisation.

The proposed definition and evidentiary requirements are unworkable

The proposed definition and accompanying evidentiary requirements place the onus on a freeholder to provide specific, historic evidence that a leaseholder was offered "meaningful choice", without any real detail as to what this constitutes, or what evidence will meet the required threshold. There are a number of issues with this approach.

Firstly, it assumes that, where the freeholder is unable to provide evidence that a leaseholder was offered multiple choices of ground rent (which will often be impossible, especially for older leases), that the ground rent is therefore invalid. We reject this framing; it runs counter to longstanding and accepted contract law, where a signed contract is the evidence of a concluded negotiation – and in the case of a leasehold property, where legal and financial advice has been sought as standard practice by both parties. As we have repeatedly noted, where a leaseholder was ignorant of obligations in their lease, this does not make the lease invalid – rather, it highlights issues with the conveyancing process and underscores the need for better advice to be provided to leaseholders.

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[1] Ministry of Housing, Communities and Local Government "Leasehold Reform (Ground Rent) Bill: Impact assessment for the peppercorn ground rent policy" (2021) at 4.3.3.

Secondly, the evidentiary requirements are entirely unworkable in practice. Given evidence of the kind the Government proposes will, in many cases, not exist, each lease will have to be considered on an individual basis, requiring a huge amount of cost and resource, and resulting in largely subjective valuation opinions which will increase the likelihood of disputes. Requirements to provide this evidence regarding successors in title are even more impractical, and we question from whom the successor is to receive their "meaningful choice".

Thirdly, it assumes that all properties and ground rents are equal. As we note above, this mischaracterises a large and diverse market where ground rents can form consideration for many different elements of a property.

The proposal to cap exempt ground rents after 40 years is antithetical to the Government's overall position

The Government accepts, in the consultation, that ground rents provided through quid pro quo leases are valid, and proposes not to interfere with their price. It has long been the sector's position that, as the ground rent forms part of the consideration and therefore the value of the lease, all leases are 'quid pro quo', and we reject consultation's characterisation of ground rents.

However, despite the Government's acknowledgement that ground rents of quid pro quo leases (fitting within its definition) are valid, it nonetheless proposes to limit these to a peppercorn after 40 years. This is, in effect, an acceptance that it will interfere, in many cases retrospectively, in valid contractual obligations and investment into those income streams – something we maintain will occur irrespective, through the blanket £250 ground rent cap.

Taken together, the above render the proposed exemption not only inconsistent, but exceptionally narrow and unworkable for the majority of the market, particularly given interests in ground rent income are from long-term, institutional investors like pension funds.

We urge the Ministry to reconsider whether the proposed exemption reflects the sector's historical practice and its current diversity, or indeed the Ministry's recent positions on ground rents. We request publication of the Ministry's assessment of the relationship between ground rent and the premium paid for a lease.

We remain, as always, willing to speak further on the above and to engage constructively on pragmatic solutions as the Government progresses its reforms.

Yours sincerely,

Real Estate:UK

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