

Clive Betts MP
Housing, Communities and Local Government Committee
House of Commons
London
SW1A 0AA

10 December 2018

Dear Mr Betts

Leasehold Reform

I write in response to your letter of the 21st November. That letter concerns the recent Select Committee meeting at which I attended and provided evidence.

Question 1

You have asked about our ground rent levels over the past 30 years and what review mechanisms were applicable to them.

I have had our past ground rents reviewed and I have been able to identify plots from 2003 to 2004. The majority are in range between £25 and £150 but there are some in London which are between £150 and £250. There were various review mechanisms in place but they mostly related to 10 yearly RPI reviews.

Question 2

You ask what advice we received or acquired with regard to the definition of “onerous” (in the context of ground rents).

The key thing here is, as I informed the committee, that there is no legal definition of “onerous rent”. My personal view is a rent that renders a particular property commercially and practically unviable.

I come to this view as most of our customers will be buying with the assistance of a loan from a high street mortgage lender; without the availability of a loan generally our customers would not be able to buy and we would not be able to sell. Therefore if we were unable to sell homes because of unfair lease terms as a customer could not qualify for a mortgage, obviously this would have a serious impact on the business, so we have a mutual interest to ensure the lease is fundable.

The UK Finance (previously named the Council of Mortgage Lenders) has for many years issued a Handbook which governs what is and what isn't acceptable to them in terms of (amongst other things) lease terms. It is divided into sections; the first of these sets out general terms, applicable to all lenders, and the second set out the requirements of each particular lender. They have also published a guide for new-build homes (I attach a copy).

The requirements of the various lenders differ. At the recent meeting with James Brockenshire MP at the Home Office (8th November 2018) it was accepted by the lenders (that did attend) that they should work together to provide a unified set of requirements. Having a unified approach would be welcomed.

In conclusion we must have set out rents at such levels and terms which were acceptable to the various lenders, which did not materially affect the value of the house, otherwise the customers would not have been able to secure a mortgage under the Finance guidance.

You then ask for an estimate of how many leasehold homes sold by Persimmon currently have now or will (in the next ten years) have a rent that exceeds 0.1% of the property value.

The introduction of the 0.1% of value "limit" is relatively recent and is referred to in Part 2 of the UK Finance Lender's handbook but not all lenders stipulate this requirement. Moreover it is largely for the first sale of a new build property. Whilst a number of Persimmon leases, in the past, will have a ground rent that exceeds 0.1% value, the rents must have been (initially) at such a level as were acceptable to the various lenders. That is to say, the lenders (at the time) viewed the lease as being viable for lending purposes. It is very difficult to predict or estimate how many Persimmon properties have or will have a rent exceeding 0.1% of value, particularly looking 10 years into the future as we don't know the current or future house price of past sales as it is dependent upon the market.

However as a guide our average selling price is currently £238,773 (1 June 2018 figure), giving an average of £238. Given that most of our ground rents are between £150 – £250 levels it is unlikely many of our properties would be sold with a rent exceeding 0.1% value. However moving forward we have issued a Group policy to ensure that rents must never exceed the 0.1% of value figure.

Question 3

I now turn to the issue of customers' claims that *"they were verbally offered the right to purchase their freeholders at an agreed price, only to find that the freehold had subsequently been sold on to a private investor without their knowledge and that the freehold could now only be purchased at a significantly higher cost than initially offered at the point of sale"*. I answer the points you set out:

- **Whether the leaseholder is notified in advance that the freehold is being sold to a third party.**

Persimmon has in the past sold leasehold as Persimmon's core business is as a developer and not a manager of leasehold assets. However as explained to the committee, we have not entered into any new agreements since 2014, but prior to that period customers were not pre-notified of the sale to a third party.

It is important to understand that any new freehold owner would be bound by statutory guidance for the calculation of premiums for lease extensions, enfranchisement and collective enfranchisement. Residents would have statutory protection.

- **Whether the leaseholder is first offered the chance to purchase the freehold on the same terms and at the same value as are offered to third-party purchasers (including either when you sell to an associated company or when you sell the associated company to a third party).**

At present we have no intention of disposing of the leaseholds to a third party but if we did we would offer first refusal to all of our customers.

- **What constraints, if any, are placed on the third party offering the freehold to the leaseholder at a higher cost.**

In the past there were none but as the new owner is bound by statutory formulae if the extension or collective enfranchisement was being conducted through the relevant Tribunal.

- **What changes, if any there have been on such policies over the past 30 years.**

There has been very little change until recently, as the Industry has listened to various stakeholders over leasehold.

- **What changes, if any, are being proposed by your company on the sale of freehold interests to third parties.**

We have not entered into any sales agreements to dispose of our freehold interests since 2014. At present we do not intend to dispose of any but if we did, we would inform the customers so they would have the opportunity to use the right to buy.

- **What information is made available in writing to purchasers of properties at the time of initial sale on the cost of the leasehold compared to the cost of freehold.**

Persimmon did not separately market leasehold and freehold properties on a site where estates were being sold as leasehold so the comment was not discussed as all the houses were leasehold. The only exception to this is once we decided to stop selling leasehold houses, we looked for an appropriate phase to change the freehold and put the price up to reflect the change of status depending upon market conditions. Nevertheless reservation contracts would clearly state the tenure of the home along with details of ground rent and estate service charges. Each customer would have been advised financially and legally by (respectively) an independent mortgage broker/advisor and solicitor.

- **What information is provided in writing to purchasers of leasehold properties on the costs of purchasing the freehold in the future and whether there is a guaranteed price for such a purchase.**

Persimmon provides a letter shortly after reservation of a leasehold house confirming that the freehold can be acquired at the lesser of 25 x the ground rent or a professional valuation (based on the statutory formula). This is also indicated in the contract. In addition they would receive advice from their legal adviser.

Question 4

As regards your question: "could [you] confirm whether any members of the Board or other directors or senior managers of your company own or control shares in companies which have purchased freehold interests from you, including any 'associated companies', or have personally benefitted from the sale of freeholds to third party investors where that opportunity was not first offered to an affected leaseholder."

We are not aware that a current or previous Persimmon plc director has, or had, an interest in:

- the ground rent companies that the Group sold between 2011-2014 following their sale; nor
- the purchasers of those ground rent companies.

Question 5

You directed us to your website to view the various complaints made against this Company and other house builders. It seems that the complaints largely fall into three categories upon which I now comment:

Mis-selling a house as leasehold

I do not believe there has been any mis-selling by this Company. A customer purchasing a new build Persimmon property will be represented by financial and legal professionals. As I said at the Committee there are a number of instances during the conveyancing process by which the customer will be explicitly advised of the tenure. There is the reservation agreement on which the tenure is marked; the checking on and reporting on the legal documents (the contract and transfer) by a lawyer on behalf of the customer; the customer being financially advised by a mortgage broker; and the mortgage and valuation process. As explained I find it hard to understand that a customer would not know the property was leasehold.

Onerous ground rents

I am not aware of a case where a Persimmon customer has been unable to fund a purchase or dispose of their home with a loan on the basis of ground rent levels set by Persimmon and as stated to the committee I would be happy to investigate any that you believe to be the case.

A developer changing its sales on an estate from leasehold to freehold

As explained Persimmon have only changed a 'Leasehold' estates to 'Freehold' estates recently, once we decided to stop selling leasehold at an appropriate phase of the development. The customers who purchased a leasehold property in these circumstances have complained, but as stated, the price was increased to reflect this change depending upon market conditions.

Finally you invited me to write to you "on a number of other issues" which the Committee was not able to deal with due to time constraints. As I understood it the three main topics for discussion were to be:

- A. Reforming or replace leasehold
- B. Improvements to dispute mechanism systems
- C. Voluntary steps to ensure leaseholders are fairly treated

I would firstly say that Persimmon has listened to various stakeholders on this matter and have taken a lot of comments on board. For example: We have phased out leasehold houses for new estates and new phases; we have ensured that leases are granted at low rents with RPI reviews; we have policies to ensure that permission fees are fair and reasonable and are binding on successors; we have a clear policy to enable customers to acquire freehold reversions to houses at a fixed cost.

However we support the Government's proposals for further reform of the sector and have responded to the consultations on Leasehold Reform and Leasehold Enfranchisement. We make the following comments:

Reform or replace leasehold

Leasehold is the traditional means by which flats are sold in England and Wales. The criticisms include the requirement to pay ground rent and unreasonable costs charged by landlords and their managing agents to the maintenance of common areas and facilities. We support the Government's proposal to limit ground rents. In terms of unscrupulous landlords charging for maintenance etc, Persimmon uses a "Residents Management Company" structure under which control of directing maintenance (and the costs of it) will ultimately be governed by the leaseholders themselves. In terms of maintenance etc this is somewhat akin to a Commonhold structure. We would have no objection to a Commonhold structure so long as the procedure for its establishment is reasonably practical and cost-effective and lenders "get on board" with this form of tenure. A Scottish system using "factors" (essentially professional management companies) also seems workable as long as the residents are protected in the event of the factor's insolvency.

Dispute resolution etc

The industry must already adhere to the Consumer Code and there are of course proposals to develop an Ombudsman system. In terms of tribunal claims (for example for reversion cost disputes and service charge disputes) Persimmon supports the simplification of this recourse, with the customer being protected in respect of fees by a fixed-fee code or similar.

Extending statutory service charge protection mechanisms to freehold houses.

Whilst not directly affecting Persimmon's business model (as Persimmon uses residents management companies) Persimmon supports extending rights already given to leaseholders of flats and leasehold houses to the owners of freehold houses on an estate (for example consultation obligations).

Enfranchisement

Persimmon supports reducing (or removing) the 2 year period for a leaseholder to qualify for reversion purchase. We also support simplifying the process for calculating the price to a fixed multiple or a % of value.

I hope this provides a comprehensive response to the issues that you raised.

Yours sincerely

A handwritten signature in black ink, appearing to be 'D Jenkinson', written in a cursive style.

D Jenkinson
Group Managing Director

New build leasehold properties



Background

This document provides information on the issues relevant for lenders and their advisers concerning lease terms for **new build leasehold properties** in England and Wales, which may have a particular implication for the value of the property and for affordability of the mortgage loan.

This document is for information only. It does not form part of, or override any CML member's lending policies or guidance to their professional advisers such as valuers or conveyancers. Nor does it take precedence over relevant clauses of the CML Lenders' Handbook, such as s 5.14.1 and 5.14.9.

The document does not address all lease terms. It is the responsibility of the legal adviser to advise the lender client on the lease, in accordance with the CML Lenders' Handbook, and any special instructions. **It remains the responsibility of the prospective purchaser to undertake their own investigations into the property they wish to purchase.**

*NB: It is important to note that the considerations and policies of individual lenders for lending on **existing leasehold property** and **shared ownership property** may differ, particularly around acceptable lease length, although the overarching considerations will be the same.*

Overarching considerations for lenders

Affordability

Lenders need to establish if the lease will have any impact on the borrower's affordability. It is a regulatory requirement for lenders to take account of all known future changes to a borrower's income and expenditure that could affect the affordability of their mortgage. As such, understanding the level of ground rents, how they increase over the mortgage term and other known charges due under a leasehold agreement, are relevant to lenders' assessments of affordability.

A lender's risk might also be increased if ground rent, or other charges are disputed by the leaseholder borrower in the future and the borrower does not pay while in dispute, as in such situations the lease could potentially be forfeited and the lender's security put at risk.

Property value and saleability

If ground rents and other charges appear to have an impact on the value and saleability of the property, lenders may, together with other matters, take this into consideration in deciding whether, and how much, to lend. **Lenders will rely on the advice of professional advisers, particularly the mortgage valuer, here.**

The length of the lease term also has relevance to the value of the property, as at a certain point, it may be necessary to negotiate and pay for an extension of the lease to preserve the property's value for the future.

General points

- Given that lenders must consider both affordability of the borrower, and the sustainability of the value of the property, lease terms which involve obligations for future payment, such as ground rents, are more likely to be considered acceptable for lending purposes if they are set at levels that will not materially change mortgage affordability in the future, or impact on the value of the property; and that the lease length is suitably long (i.e. is granted for hundreds, rather than tens of years).
- Lenders may query why a property is offered as leasehold. This is particularly so for leasehold houses.
- It is important that lease information for new homes is made available as early in the home buying process as possible, so that conveyancers and valuers can provide advice and lenders can make appropriate lending decisions.

- In relation to ground rents, lenders would expect to see nominal ground rents, reflecting the origins of the ground rent being 'peppercorn' in nature.
- Under current leasehold legislation, there are certain provisions which present a risk that the lease may be terminated or forfeited by the landlord (freeholder), leaving the property owner without a leasehold interest, and the lender mortgagee without a security. Therefore, lenders will expect that a conveyancer acting on their behalf advises on such risks and how they might be mitigated. An example is the relevant provisions of the Housing Act 1988 in relation to the creation of an Assured Tenancy where the ground rent exceeds £250 per annum or £1000 in Greater London.

Specific considerations

Lenders will expect professional advisers such as conveyancers and valuers to consider:

- The length of the initial lease term granted. As a general principle, longer lease terms will help sustain the property's value for longer, as there should not be a need to seek an extension of the lease in the medium term (i.e. over the term of the mortgage). Lenders using the CML Lenders' Handbook already stipulate a **minimum lease residue requirement** (see s 5.14.1 of the CML Lenders' Handbook).
 - Lenders recognise that there may be different lease lengths for houses and flats.
- The mortgage term in relation to the lease term, with particular regard to a likely review of the lease once 80 years or less are remaining.
- The initial annual ground rent figure. Professional advisers should take into consideration:
 - the level of the ground rent in relation to the property's market value,
 - the type of property (e.g. a flat or a house)
 - whether the ground rent is fixed or rises periodically,
 - If the ground rent does rise periodically, the formula by which it rises.
 - Where the property value is below £100,000, some lenders may wish to see a de minimis maximum initial ground rent figure (e.g. £100) is applied.
 - Whether the ground rent figure is at a level which triggers legislative provisions (such as under Part 1 of the Housing Act 1988), potentially creating a risk for the lender's security.
- The ground rent review formula (if not a fixed figure). Professional advisers should take into consideration:
 - The CML Lenders' Handbook at s 5.14.9, which provides that lenders will accept a periodic increase in ground rent, provided that the amount of the increased ground rent is fixed or can be readily established and is reasonable.
 - Where the formula is one which uses increases in line with an index, whether the index is a recognised UK index and is appropriate and/or acceptable to them. Some lenders may also expect a cap on the maximum ground rent amount, to guard against the ground rent reaching an unreasonably high sum, which could impact on the property's value, the continued affordability of the mortgage and the future saleability of the property.
 - Some lenders may be concerned to see the use of compounding formulas, or the use of minimum increases, in conjunction with an index-linked formula.
 - Where the formula does not link with a recognised index, and instead uses a multiplier (e.g. doubles) at set intervals, the frequency of the rent review intervals. There is no single industry view on a minimum acceptable frequency, as it may depend on other factors such as the initial amount of the ground rent, and whether there is a cap on the number of times the rent is reviewed.
- Other fees charged under the lease
 - Where other fees are charged under the lease (for example, on a transfer of equity) lenders will expect that these are set at reasonable levels. Where the fees follow the ground rent formula (for example, if they are set at 50% of the prevailing ground rent), lenders will have similar expectations as set out above for ground rent formulas.