



Enfranchisement Guide

September
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The ***Leasehold Reform, Housing and Urban Development Act 1993*** (the 1993 Act) introduced the right for flat owners with qualifying leases to collectively acquire the freehold of the block in which they were residing. This right is known as **collective enfranchisement**. (The right for house owners to acquire their freehold, was introduced by the Leasehold Reform Act 1967)

The 1993 Act also introduced a right for an individual to obtain a lease extension, which is an additional 90 years plus the residue of the lease term at a peppercorn rent. This right is further detailed in a short guide to individual lease extensions produced by Dawsons.

Due to the complexities and cost of implementing a collective enfranchisement claim in practice, the individual right to a lease extension has proven more popular.

As a result of these complexities the Government passed the Commonhold and Leasehold Reform Act 2002 (the 2002 Act) which simplified the qualification rules and valuation principles. We predict that more and more flat owners who are disgruntled by the current leasehold system will want to take advantage of collective enfranchisement to gain control of what is usually their most significant investment.

We can help you because we have been in practice for over 275 years and have an established reputation in this area of the law, independently verified by the two leading legal directories:- the Legal 500 and Chambers. We have a team of experts who specialise in this complicated area of law and regularly appear in the **Leasehold Valuation Tribunal**.

This guide provides advice on the law as at 1 July 2007. It is intended as a general guide only and is not a substitute for detailed advice as circumstances differ from one block to another. Dawsons is happy to provide the first initial interview for free and thereafter will provide fee estimates for each stage of the process.

Dissatisfaction with your landlord

If you are reading this, then we assume you wish to have greater control over what is probably the single biggest investment you have made - your home or if you are non-resident your likely position. Your lease may be getting shorter and you may be worried about the prospect of selling your flat in the future. Will you get proper value for it, if your lease has less than 70 years to run? Are you facing high levels of service charge with apparently very little to show for it? Are you continually in

dispute with your landlord? Is your lease defective thereby affecting its marketability?

There are many reasons why you may wish to exercise the right to collective enfranchisement. However, there may be other suitable options, such as an individual lease extension or to exercise the right to manage. These are the subjects of other guidance notes produced by Dawsons or which can be found on our website: www.dawsonslp.com.

So you want to apply for collective enfranchisement?

Assuming you want to apply for collective enfranchisement there are five matters to consider before you bring a claim. In outline, these are:

- Checking that the building qualifies under the 1993 Act
- Identifying who will be the participating tenants
- Ensuring you can afford to bring a claim
- Establishing a nominee company to acquire the freehold
- Creating and executing a participation agreement.

Taking these in turn...
please refer to
Diagrams 1 and 2

Qualifying tenants

Qualifying tenants are tenants who own a lease originally granted for a term of more than 21 years. If a flat has more than one lease granted for at least this length then it is the person at the bottom of the chain who is the qualifying tenant.

Due to changes introduced by the 2002 Act it is no longer necessary to prove residence, so anybody can now participate as a qualifying tenant, including companies. Unlike an individual lease extension there is no need to prove that you have owned the lease for at least two years. Any length of ownership will suffice.

Usually, it is possible to establish the number and identity of the qualifying tenants by undertaking a search at the Land Registry. Failing this, if parts of the title are unregistered it is possible to serve an information notice on the landlord or his managing agents requiring details of the various leasehold interests in the block. This notice places no commitment on the flat owner but the response to the notice should provide sufficient information to ascertain whether the building contains a sufficient number of qualifying tenants for it to qualify.

If any tenant in the building owns three or more flats then they are debarred from being qualifying tenants.

What is the purchase price?

What is it going to cost? In broad terms, the purchase price to be paid by the participating tenants to purchase the freehold of the building is the aggregate of:

- the building's investment value to the freeholder
- one half of the marriage value - this is the increased value attributable to the freehold by virtue of the participating tenants being able to grant themselves

extended leases at a nil premium and at a peppercorn rent.

- compensation for loss in value of other property owned by the freeholder, including development value resulting from the severance of the building from that other property.

Following the 2002 Act, there is now no marriage value attributed to a lease which has more than 80 years unexpired on the relevant date. This represents a real saving to tenants.

The 2002 Act has also changed the valuation date which is now the date when the **initial notice** is given. Under the 1993 Act, the date used to be when everything was agreed, which in practice could be up to two years from when a claim was first made. Such delays in a rising market only benefited landlords.

For the purpose of calculating the price, tenants must take advice from a properly qualified surveyor or valuer. Dawsons has close links with various firms throughout London and can recommend several who will be suitable.

In addition to the price and the participating tenants' own legal costs and valuation fees, you will be required to reimburse the freeholder for his legal costs and valuation fees.

Legal Costs - Depending on the circumstances, it could cost from several thousand to several hundreds of thousands of pounds to acquire the freehold. The larger the block the more expensive it is likely to be, if only because the logistics of dealing with everyone in a larger block creates more costs than dealing with smaller blocks. Dawsons has sufficient experience to be able to estimate the likely cost to each participating tenant.

Finance and tax advice - There are different ways to consider how to finance the acquisition. In most cases the finance will have to be obtained from the participating tenants themselves, either from savings or from borrowings secured against their flat. It may be possible to secure borrowing against the freehold being acquired, although in our experience this is difficult since the participating tenants will want to extend their leases at a peppercorn rent and this therefore robs the freehold of its value.

However, if the block has redevelopment potential, then it may be possible for a developer to provide finance if it later receives a leaseback of that area, for example the airspace of the roof. Any arrangements with a third party to finance the acquisition may have to be disclosed to the freeholder and this may affect the price which is paid to acquire the freehold.

In some cases there are tax implications to consider, both in relation to the participating tenants' individual positions and also in relation to the Nominee Company set up to purchase the freehold. Dawsons's tax department can provide advice.

Ultimately, the burden of financing the acquisition will fall on the participating tenants. They will have to effectively fund not only their own share, but also any non-participating tenant's share. There are various ways to achieve this:

- The participating tenants share can be pro rata based on their service charge proportions
- Each flat could have a fixed share and the participating tenants will be required to pay for their own flat and a proportion of the non-participants
- The participating tenants could receive an overriding lease over each of the non-participants flats,

although in our experience such arrangements create their own problems regarding managing the building in the future.

- The Nominee Company can issue unsecured loan stock in respect of the non-participating tenants' shares which can be redeemed once the Nominee Company receives income, generated from future lease extensions of non-participating tenants' flats.

Creation of a Nominee Company

In our experience there is no need to establish a Nominee Company if there are four or less flats in the building. For these smaller buildings it is possible to acquire the freehold through all four tenants under a trust arrangement. Although there is an initial cost in establishing a trust it removes the need for on-going costs which a company has to incur.

For larger buildings all claims will need to establish a private limited company. Some thought will need to be given to who will act as the directors of that company and who will be the secretary. The company will have to submit annual returns to Companies House and produce accounts, so will have an on-going cost. Failure to file accounts/returns will cause the Company to be struck off the register of companies, resulting in the freehold being returned to the Crown under the "Bona Vacantia" rule.

There is no legal requirement requiring all qualifying tenants to become members of the company and initially, membership should be restricted just to the participating tenants. Although the 2002 Act contains rules requiring the creation of a "Right to Enfranchise Company" together with an automatic right for every tenant to participate these are not in force and are expected never to be implemented. If you are left out of

a claim your only right will be to seek an individual extension. For more information, see our guide on Lease Extension.

The participation agreement

It is advisable in all but the simplest of cases for an agreement to be drawn up between the participants and the Nominee Company to provide a framework of the way in which the participating tenants should work together to acquire the freehold. The participating tenants will be heavily reliant on each other staying together as a group and the agreement set out when payments will be required to fund the acquisition and the consequences of any failure to comply with its terms.

The initial notice

The claim is triggered by the service of the initial notice. This must be personally signed by the participating tenants and served on the landlord. It is often difficult to serve the landlord, especially if he is already aware that you intend to bring a claim, and a professional process server may be required.

The landlord's costs will start to run against you from the time the initial notice is served.

This notice must (among other things) specify:

- The extent of the property to be acquired - supported by a plan
- Full particulars of all qualifying tenants in the building - not just the participating tenants
- The price being offered for the freehold. This must be genuine and realistic - too low and it will invalidate the notice.
- The date by which the freeholder must give his counter-notice, being a date not less than two months from the date of service of the notice.

The landlord's response

On receiving the initial notice the landlord is likely to respond by:

- Asking the participating tenants to deduce title (this can easily be done by producing entries from the Land Registry)
- Inspecting the building for the purpose of carrying out a valuation.

The landlord's counter-notice

Within the period specified in the initial notice the freeholder must serve his counter-notice. If he does not, the price will be fixed at the price in the initial notice and an application to the court is required to enforce it.

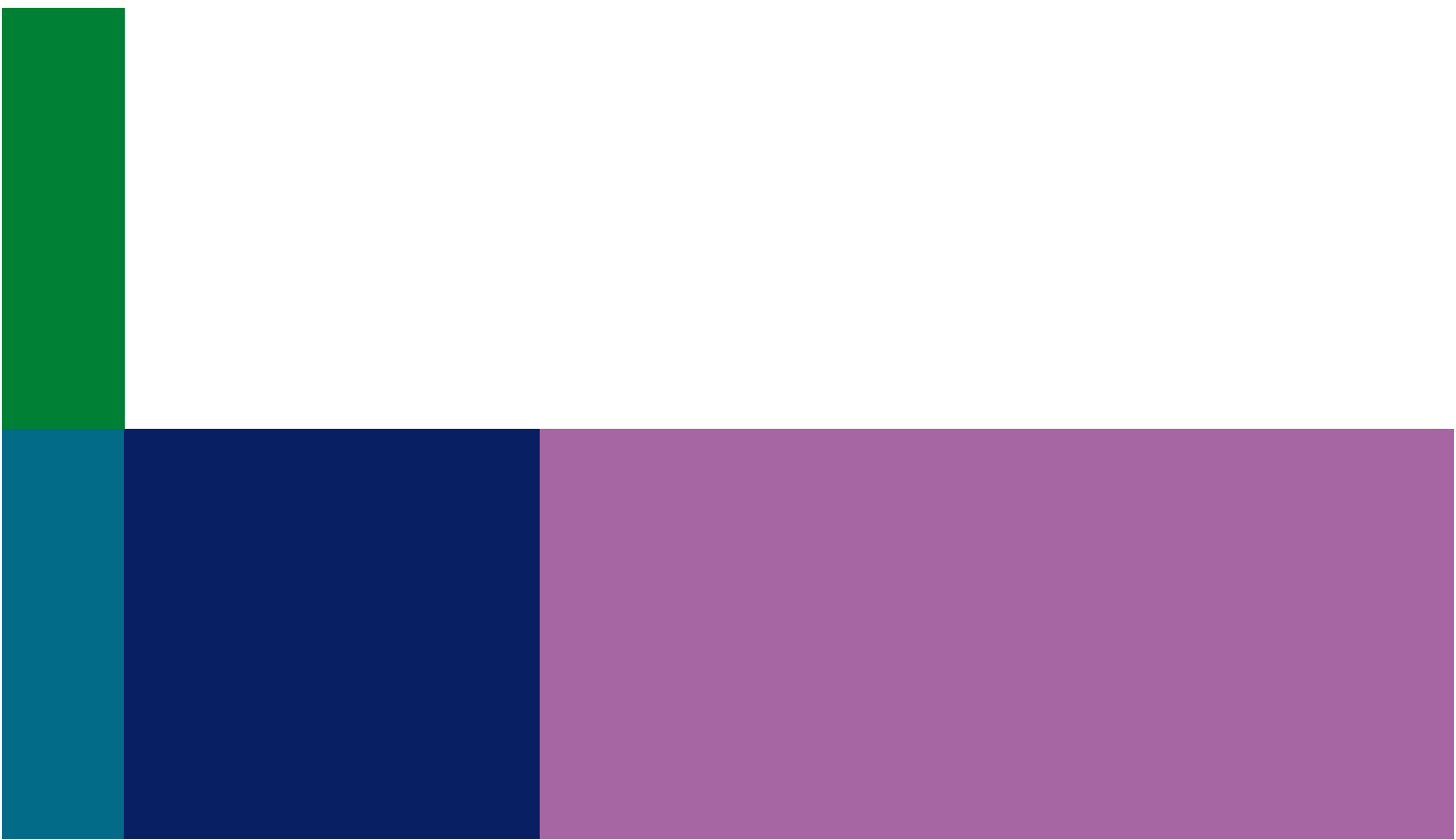
Assuming that the freeholder responds in time (and it will be a very rare occasion when he does not!) then he must state whether or not the claim is admitted. If it is denied then the participating tenants must decide whether to apply to the courts if they wish to dispute the denial.

If the claim is admitted, the landlord's counter-notice must state:

- Which of the tenant's proposals contained in the initial notice are acceptable
- Which of the proposals are not acceptable and the freeholder's counter-proposals.
- Whether the freeholder wants a leaseback on any unit in the building not held by a qualifying tenant (this will include any flat occupied by a regulated tenant or commercial tenant).

Application to the Leasehold Valuation Tribunal

If any of the terms of the acquisition (including the price) remain in dispute after two months from the landlord's counter-notice then either party can apply to the Leasehold Valuation



Tribunal for the matters in dispute to be determined. There are five LVTs in the country. The one for London is at 10 Alfred Place, London WC1E 7LR. Telephone Number 020 7446 7700, Fax Number 020 7446 7897.

An application to the LVT must be made within six months following the landlord's counter-notice. If not, then the claim is lost and you will have to wait at least 12 months before re-applying. In addition, you will be liable for the landlord's costs.

The hearing before the LVT is usually informal, although it is conducted like a court with both sides being given an opportunity to put forward their case. The LVT panel generally consists of two professionals and one lay person. Usually both parties are represented by barristers, who are experts on cross-examination and by their valuers.

Under the 2002 Act the LVT has the power to award costs up to a maximum of £500 or such greater amount as shall be prescribed by the Government where a person has acted "frivolously, vexatiously, abusively, disruptively or otherwise unreasonably in connection with the proceedings".

Determination of price and other terms

Once the terms of acquisition have been agreed or determined by the LVT the matter reverts to a straightforward conveyancing transaction with the parties entering into a contract and thereafter completion (usually 28 days later). In most transactions a contract is dispensed with and the parties proceed direct to completion.

Completion

On exchange (if there is one) a 10 per cent deposit will need to be paid and on completion the balance of the price becomes payable together with the freeholder's costs and arrears of ground rent/service charge. It is therefore vital that all arrears of rent and service charge owed by the tenants in the building are paid up to date, otherwise these sums will need to be financed by the participating tenants.

Once completion has taken place the purchase is registered at the Land Registry and through the Nominee Company the participating tenants will become the freeholder of the building, subject to their existing flat leases. The participants will (through the Nominee Company) be able to grant

themselves extended leases and if necessary, will be able to affect any desirable variations to their leases, for example by amending deficient service charge provisions.

The Nominee Company will assume the landlord's responsibilities for the management of the building and the administration of the service charge account in accordance with the terms of the flat leases and statute. For all but the smallest building, such responsibilities will be devolved to professional managing agents. Dawsons has links with various managing agents in London and is happy to recommend several whom other clients have found satisfactory.

The process of bringing a claim for collective enfranchisement can be costly and time-consuming. It will require persistence and patience by (usually) a small group of dedicated flat owners to drive the process forward. However, with proper advice and guidance it is possible to be successful and to see the fruits of success in a well-managed block and an enhancement in your flat's value.

For further assistance, please contact
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