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Boodle Hatfield Property Insights

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King's speech outlines further plans for leasehold reform

Leasehold reform has been on the political agenda for several years and there was therefore considerable speculation as to what the King's Speech in November would bring, particularly in the areas of enfranchisement and residential development.

Leasehold and Freehold Reform Bill

Whilst the King's Speech itself was perhaps light in detail, we do now have a little more clarity, with key reforms set out in a Leasehold and Freehold Reform Bill promising 'decisive action' to 'address one of the longest-term challenges that the country faces: fairness in the housing market' 'making it cheaper and easier for more leaseholders to extend their lease, buy their freehold, and take over management of their building.' The headline reforms include:

- **Making it cheaper and easier for existing leaseholders in houses and flats to extend their lease or buy their freehold.**
- **Increasing the standard lease extension term from 90 years to 990 years for both houses and flats, with ground rent reduced to £0 and removing the requirement for a new leaseholder to have owned their house or flat for two years before they can benefit from these changes.** Both of these points had already been mooted and are not particularly controversial given the current ability to make back to back 90 year extension claims and the ability to assign the benefit of an extended lease claim. Whilst the reference to the reduction of ground rent may look generous those in the know will appreciate that simply reflects the current position.
- **Increasing the 25% 'non-residential' limit preventing leaseholders in buildings with a mixture of homes and other uses such as shop and offices, from buying their freehold or taking over management of their buildings.** Whilst not a new proposal, this had not been anticipated to form part of the current reforms. This is a significant change and will increase the number of properties that may be enfranchised. As such, this looks set to prove contentious amongst landlords.
- **Banning the creation of new leasehold houses.** The inference being that this provision will apply only to newly built houses, rather than all new leases of houses, but this is not expressly spelt out. The ban will not extend to new flat leases, which whilst attracting a surprising high level of support in some quarters was surely never going to form part of the reforms, given the lack of any viable alternative form of tenure to leasehold for flat ownership. Commonhold seemingly on the back burner for the time being.

Further details of the proposed reforms are set out in the 150-page Leasehold and Freehold Reform Bill, published this week. The Bill will need to progress through Parliament before coming law. Whilst those in government have stated a clear intention to see the Bill pass into law before the next general election, this will require significant engagement from all involved.

Consultation on capping ground rent in existing leases

The King's Speech also included the promise of a consultation on capping existing ground rents to ensure that all leaseholders are protected from making payments that require no service or benefit in return. Whilst not forming part of the Leasehold and Freehold Reform Bill, the promised consultation was published within days of the King's Speech with the consultation closing on 21 December.

The consultation sets out a series of options as to how the government could intervene to cap the ground rent existing leaseholders pay. This builds on the existing legislation that already restricts all new residential leases to a peppercorn ground rent.

The consultation outlines five options:

- Capping ground rents at a peppercorn.
- Setting maximum financial value for ground rent.
- Capping ground rents at a percentage of the property value.
- Limiting ground rent to the original value when the lease was agreed.
- Freezing ground rent at current levels.

Each of the above options would require some degree of reform to the current position, 'no change' not featuring in the five options for reform. Whilst the potential significant financial impact for freeholders is acknowledged in the consultation, the consultation does not include provision for freeholders to be compensated for any loss of revenue or the ability for freeholders to capitalise the lost income stream by other means. The consultation can be viewed here and looks likely to provoke some lively debate in the run up to Christmas.

Renters Reform Act and no-fault possession notices

The King's Speech included a further nod to the government desire to progress the Renters Reform Bill notably the intention to abolish the ability of residential landlords to serve s21 'no fault' possession notices. The progress of the Renters Reform Bill to date has been slow, and the government has seemingly now acknowledged that the current court system must be reformed before the Bill can progress.

Simon Kerrigan, Property Partner

Levelling up to require disclosure of land interests

The Levelling Up and Regeneration Act 2023 became law at the end of October. A substantial piece of legislation with a not terribly eye-catching title aimed at 'levelling up' and 'breathing new life into business and the regions across the UK'.

Disclosure of land interests

The Act includes the outline detail of new 'Part 11 provisions' aimed at providing a 'clear line of sight' across a piece of land, allowing public bodies, including the Land Registry, access to information (including transactional documents) setting out who owns, controls or has an interest in land.

The information that may be requested within these provisions may be used for a range of purposes including, but not limited to:

- **Beneficial ownership purpose:** Identifying attempts to evade or avoid the disclosure requirements set out in the Economic Crime (Transparency and Enforcement) Act 2022 including the requirements for overseas entities owning UK land to register at Companies House.
- **Contractual control purpose:** Promoting greater land transparency by the publication of data such as conditional contracts, pre-emptions and options that may be used by developers to control land.
- **National security purpose:** Other uses described as 'wider national security and macro-economic purposes'.

The requirement to provide information will be enforced by measures that will prevent landowners from registering changes to the Land Registry title registers where required information has not been provided. Failure to provide required information will be a criminal offence.

Further information will be provided in the form of as yet unpublished regulations. It is likely that these measures will impact significantly on the ability of land owners and contracting parties to keep transactional information confidential including by means of current well established practices such as the use of Land Registry exempt information documents and unilateral notices.

Andrew Wilmot-Smith , Partner and Head of Property

Pending changes to energy performance certificates

Landlords of residential properties have become familiar with the requirement to provide their tenants with an Energy Performance Certificate of band E or better before letting or continuing to let a residential property in order to comply with the Minimum Energy Efficiency Standards (MEES). It had been anticipated following government consultation that the MEES requirements for residential properties would be tightened to Band C or above from April 2025 for new lettings and April 2028 for existing residential tenancies.

Whilst many had anticipated a delay in implementing the proposed change, it was a surprise to most when the government announced in September that the MEES requirements for residential properties will now remain at Band E. Whilst this may come as a relief to landlords faced with the increased costs associated with improving an EPC rating or claiming and registering an exemption, many residential landlords will have already started the process of reviewing and upgrading their properties.

There is no indication that the MEES requirements for commercial properties will benefit from a similar change of policy and, at present, the government remains on track to increase the MEES requirement for commercial properties to Band B or above by 2030 with Band C by 2027 as an interim standard.

Kate Symons, Property Senior Associate

Key measures of relevance to entrepreneurs include:

- The "full expensing" regime has been made permanent (i.e., businesses can continue to claim back certain investments in full against corporation tax).
- Extension to the 75% discount on business rates up to £110,000 discount for retail hospitality and leisure businesses for another year as well.
- £500m of funding for UK artificial intelligence over the next two years to fund more 'innovation centres' to help make the UK an 'AI powerhouse'.
- The promise of a new £150m Investment Opportunity Fund.
- An additional £4.5bn of support is promised between 2025 and 2030 for our fastest-growing innovation sectors.

More detail, on all of the above measures is likely to follow in due course.

Charlie Hewlett, Corporate Senior Associate

Autumn statement brings support for entrepreneurs

Despite speculation from various sources in the run up to the Autumn Statement, the Chancellor of the Exchequer, Jeremy Hunt, did not cut stamp duty rates, or introduce the mooted 'rebate to renovate' to reduce stamp duty for householders undertaking energy efficiency upgrades.

The Autumn Statement did however include reference to the need to 'support entrepreneurs in raising capital' and the importance of supporting 'universities, scientists and start-ups' announcing the need to back 'the entrepreneur taking risk in a modern dynamic economy' and the announcement that business rates relief will be extended for another year seeing the government freeze the small business multiplier.

Updates on the Building Safety Act

Second staircase timescale for implementation

The Government confirmed in July that new guidance would be introduced requiring second staircases in residential buildings above 18m in height. We now have more of an idea as to the timing of the new provisions with the announcement from Michael Gove in late October that developers will have 30 months from the date that the changes to Approved Document B are formally published during which new building regulations applications can conform to either the guidance as it stands today or to the new guidance requiring a second staircase. After the 30 months all applications must adhere to the new guidance and a second staircase will be required.

If an application is made within the 30 months that does not follow the new guidance the developer will have 18 months for construction to get underway in earnest (i.e. the pouring of concrete for either the permanent placement of trench, pad or raft foundations or for the permanent placement of piling). If it does not, they will have to resubmit under the new guidance.

Accordingly, if a project has already obtained planning permission with one staircase it has some time to get construction underway and the development will not need to immediately be redesigned and resubmitted.

Qualifying leasehold loophole addressed

A significant loophole in the Building Safety Act 2022 (BSA) that had the potential to adversely impact on leaseholders has now been addressed giving certainty to both landlords and leaseholders when renewing a qualifying lease.

To benefit from the BSA leaseholder protection provisions available to leaseholders in high rise blocks, the tenant must hold a 'qualifying lease' granted before 14 February 2022. As originally drafted, the qualifying lease status would be lost if the lease was extended after this date as the extension of the lease effects a surrender of the original lease and the grant of the new extended lease. This has now been addressed by new provisions added to the BSA at the end of October which provide that a 'connected replacement lease' (that is a new lease replacing another that was a qualifying lease) will be a qualifying lease where all other criteria are satisfied. The new provisions will take effect retrospectively and will therefore apply to extended leases granted during the period since the leaseholder provisions came into force.

Registration of high-rise buildings

The provisions of the BSA requiring the mandatory registration of all residential buildings that are over 18 metres high or have more than 7 floors came into force on 30 September 2023. New buildings completed after 1 October 2023 must have a relevant completion certificate or final notice and must be registered before residents can occupy them. The register is not yet open for public view and evidence of registration must therefore be requested as part of the due diligence exercise where dealing with a property.

Sarah Rock, Construction Partner

Real Estate funding

Traditionally, banks and institutional lenders have held sway in providing financing for property ventures. However, in recent years, the emergence of private debt funds and alternative lenders has injected a new dimension into real estate financing. So, what are the factors propelling this surge in private debt within the UK's real estate sector, how is its profound impact being felt, and how is this not all bad news for traditional lenders?

A shift in real estate financing

The real estate sector, long reliant on conventional banking channels, has experienced a notable disruption with the surge of private debt. Multiple factors have converged to drive the surge of private debt in the UK's real estate domain. Following the global financial crisis of 2008, Trussonomics and the high inflation-high interest rate environment in which we now live, banks have become more risk-averse and stringent in their lending practices. Private debt funds have capitalised on this demand by offering real estate developers and investors access to alternative financing sources with competitive returns. On the one hand, investors are seeking higher yields beyond those offered by traditional investment avenues. The typically floating-rate nature of real estate debt makes it attractive to investors, resulting in significant capital inflows.

On the other hand, banks are tightening lending criteria and withdrawing from certain types of riskier lending all together. This has paved the way for non-traditional lenders to step in and fill the void. The evolution of technology has also played a pivotal role. Fintech platforms have streamlined the lending process, facilitating faster loan approvals and enabling alternative lenders to effectively assess property risks. This has democratised access to capital, allowing a broader range of players to participate in real estate ventures. It's also been beneficial on the investor side; platforms have enabled a much wider variety of investors (and a larger number on each transaction) to participate in loans. Previously, the costs of managing these investors would not have been worthwhile for private debt originators.

How developers can reap the rewards

Private debt has increased the availability of tailored financing options. Unlike traditional banks, private debt funds often specialise in specific property types or niches, enabling developers to secure loans that are closely aligned with the unique attributes of their projects without the multiple rounds of credit committees. This is what gives private debt the edge; bespoke financing combined with swift execution. Furthermore, private debt has proven particularly beneficial for smaller developers and property investors. These stakeholders often face challenges accessing funding through traditional avenues due to their size or limited credit history. Private debt's flexibility and less rigid underwriting criteria provide them with a lifeline to finance projects that might otherwise have remained unrealised.

Borrower due diligence

Although whether borrowing from a bank or private lender might appear to give rise to the same considerations, there are certain idiosyncrasies specific to private lenders which could have disastrous consequences for a borrower. The two most important are:

- **The ability to fund.** There are typically very few concerns about whether a bank is able to fund future drawdowns; they are typically well capitalised. Private lenders will rarely have equivalent balance sheets but will they be likely to continue to fund loans? Have they used a special purpose vehicle for a loan which has very little assets? Inability to fund could lead to borrowers having to refinance the debt in full which is expensive and time consuming.
- **Managing a default.** Particularly after the bad publicity achieved by RBS' GRG team following the global financial crisis, banks tend to be reluctant to enforce. Private lenders don't have the same regulatory considerations and could therefore be more aggressive when the going gets tough.

So how can a borrower mitigate these risks? Due diligence is key; picking private lenders that are well-capitalised or have access to significant capital. Many will also work harder than banks to ensure they are repaid in full without resorting to enforcement if nothing else to ensure that their loan is protected. Checking their track record is vital.

Challenges on the horizon

The lack of standardised reporting and transparency in the private debt market also poses risks. Investors may struggle to accurately assess the risk associated with various loans, potentially leading to misinformed investment decisions. Ensuring adequate disclosure and reporting mechanisms are in place will be pivotal in maintaining market integrity.

There is also an increase in the leverage offered by private debt. Some private funders are requiring very little equity to be injected by the borrower and whilst this enables a wider variety of borrowers to access projects, it also comes with risks. Having little skin in the game means when the going gets tough a borrower might not be willing to invest the time to resolve issues, as they stand to gain very little, if anything, if a solution is achieved. It's critical for private lenders and their investors to understand these risks and balance them with the rewards available.

As private debt gains prominence in the UK's real estate sector, regulatory oversight has become a priority. As things stand, lending against commercial real estate is entirely unregulated. Although borrowers in this space are typically very sophisticated, striking the right balance between fostering innovation and protecting stakeholders is paramount. Regulatory bodies are increasingly focused on creating a framework that ensures responsible lending practices, risk mitigation, and adequate investor protection.

Can private debt and bank debt co-exist?

It's not all bad news for banks and other traditional lenders. Investors in private lenders are typically less interested in the low leverage-low return tranche of a piece of debt – a space banks are very happy to operate in. This is presenting both banks and private lenders an opportunity to co-exist.

Those banks who are ahead of the game are partnering up with private lenders and offering them leverage. The bank takes the low loan to value tranche leaving the private fund to take the riskier first loss tranche. Given the low risk profile for the bank, they are getting increasingly comfortable with allowing the private debt provider to originate transactions and manage the relationship with the borrower. This is potentially a win-win for all parties. The borrower only deals with one counterparty but with more leverage than it could get from a bank,

the private debt provider can do bigger ticket sizes and offer higher returns to its investors and the bank is able to fund transactions on a last-loss basis without having to originate or manage the loan. The difficulty of course is that it takes time to build relationships between banks and private lenders and it's not always the case that each of them will be a perfect fit for each other.

Harnessing regulation to unlock transformative potential

The surge of private debt in the UK's real estate sector has ushered in a new era of financing possibilities. As alternative lenders and private debt funds carve out a significant role, developers and investors are gaining access to innovative financing solutions that cater to their unique needs. While the advantages are evident, regulatory vigilance is necessary to ensure that the sector remains resilient and transparent. By addressing challenges related to risk assessment, transparency, and market stability, the UK can harness the transformative potential of private debt to reshape its real estate landscape for the better. If banks and debt funds can work together to get the formula right, there are potentially benefits to be reaped for the industry as a whole.

Partners, Rahul Thakrar and Jonny Hyndman

This document is intended to provide a first point of reference for current developments in aspects of the law. It should not be relied on as a substitute for professional advice. If advice on a particular circumstance is required please contact your Boodle Hatfield lawyer.

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