

## W.8 COMMONHOLD

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### 8.1 Introduction

Commonhold is a new system of land-holding, which was introduced by Part 1 of the Commonhold and Leasehold Reform Act 2002 ('CLRA 2002'). It is governed by that Act and the Regulations made under it (The Commonhold Regulations 2004, SI 2004 No. 1829—'CR 2004'), both of which came into force on 27 September 2004.

Unless otherwise stated, references to statutory provisions in this web-entry are to sections of CLRA 2002.

#### 8.1.1 Why was commonhold introduced?

Commonhold was designed to meet the needs of flat owners and of those who own other types of property which are said to be 'interdependent', such as homes in a retirement village or units on an industrial estate or business park. Although these sound like very different types of property—some residential and some commercial—they have several similarities. For a start, there are likely to be 'common parts' in all these developments; that is, areas which do not belong to any individual unit but are used by all unit holders. In a block of urban flats, the common parts probably will consist of the entrance hall, stairs, passages, lifts, parking areas and perhaps a small communal garden, while in a more rural setting there may well be extensive grounds and areas for social and sporting activities. Any scheme of development for property of this sort will need to provide for the ownership and upkeep of these common parts.

The other similarity between all these forms of property is that, in the interests of all the owners, there needs to be a system of rules controlling the use of individual units, and requiring each to be kept in a proper state of repair. If a flat in a block is allowed to deteriorate it can have an adverse effect on those above and below it, and obviously excessive noise or other anti-social behaviour will be of immediate concern to the neighbours. What is needed is a web of mutually enforceable covenants under which each unit holder takes on certain duties with the understanding that he or she also has the right to enforce the same obligations against other owners in the development.

This could easily be achieved at the outset by requiring each purchaser to enter into a mix of positive and negative covenants, the positive ones requiring him or her to keep the unit in repair and perhaps to contribute to the cost of maintaining the common parts, and the negative ones restraining certain activities, such as the keeping of pets. However, over the years the units are likely to change hands, and it is essential that the original covenants should run to bind and benefit the new owners. The burden of restrictive covenants made between freehold owners can be made to run with the land (see Chapter 25 of the book), but unfortunately, the same is not true of positive covenants, and as a result, there is no easy way to provide for the enforcement of positive obligations against successors of the original freehold owners.

This is a major difficulty associated with freehold ownership. By contrast, when a leasehold estate is assigned, covenants in the lease will run to bind (and benefit) the new tenant, irrespective of whether they impose positive or negative obligations. For this reason, flats and other interdependent properties

are almost invariably sold on long leases, and the owner of a unit does not acquire the fee simple estate in his property, however much he or she may have paid for it.

### 8.1.2. Disadvantages of leasehold schemes

Using a leasehold scheme overcomes the problems about ownership of the common parts and the imposition of positive obligations on successive owners, but at the same time it raises a number of other problems.

- (i) *The lease is of limited duration* The leasehold estate is regarded as a 'wasting asset', which, unlike freehold property, becomes progressively less valuable as time goes by. In consequence, banks and building societies these days are often unwilling to lend money on the security of leases with less than 60 years left to run and, as a result, some leasehold properties become difficult to sell, because a prospective buyer cannot arrange to finance the purchase.
- (ii) *Problems with landlords* Not surprisingly, landlords often act in their own interests, rather than in those of their tenants. For example, they may either fail to do repairs for which they are responsible, or, where leaseholders are required to contribute to the cost of repairs, may insist on doing more than appears to be necessary. Another recent issue has been properties let on terms that make the ground rent for the property rise substantially over the years, which may make the lease very hard to sell.
- (iii) *Danger of forfeiture* There is always the risk that a relatively minor breach of covenant may lead to forfeiture of the lease, resulting in loss of home and capital investment for the leaseholder and in some cases considerable financial gain for the landlord (although on the possibility of the court granting relief in such circumstances, see *Van Haarlam v Kasner* (1992) 64 P&CR 214).

### 8.1.3. Proposals for reform that led to commonhold

Over the years, a number of statutory reforms improved the position of the long leaseholder of residential property, and these are covered later in this web-entry (8.7.3). However, these improvements were seen by some as only 'tinkering' with the problem, and, from 1984, there were proposals for a more thorough-going reform, which would allow freehold ownership of flats and other similar units. Developing these proposals proved to be a lengthy business, involving a number of reports, consultations and draft bills. All this is a matter of history now and need not concern you, except that you should be aware that some of the earlier literature on commonhold deals with proposals that differed quite significantly from the scheme that was eventually introduced.

## 8.2 The commonhold scheme

### 8.2.1 Outline

Where the new commonhold system is to be used, the property concerned (for example, a block of flats or a business park) will be registered at the Land Registry as '*commonhold land*'. The owner of each individual unit (the '*unit holder*') will be registered as its freehold owner, and will be a member of the '*commonhold association*'. This association will be a company limited by guarantee, with membership limited to unit holders, and it will be registered as the freehold owner of the common parts. The rights and duties of all unit holders will be prescribed by the '*commonhold community statement*', and the Act ensures that these rights and duties will benefit and bind successive owners of the unit.

A commonhold scheme thus overcomes the difficulties noted above: it makes provision for the ownership and maintenance of the common parts; it allows each individual owner to own the freehold estate in his or her unit; and it enables positive and negative obligations to be enforced between successive unit holders.

Each element of the commonhold system is now considered in a little more detail.

### 8.2.2 Commonhold land (ss. 1–4)

The Act opens with a definition of commonhold land. Section 1 provides that land is commonhold land if three conditions are satisfied:

- the freehold estate must be registered as ‘a freehold estate in commonhold land’;
- the land must be specified in the memorandum of a commonhold association as land in relation to which the association is to exercise functions; and
- there must be a commonhold community statement which makes provisions for the rights and duties of the association and of the unit holders.

The application for registration as commonhold land must be made by the current freehold owner of the whole property (s. 2), and must be with the consent of those persons, if any, who hold certain lesser estates in the land. Thus s. 3 and reg. 3, taken together, require the freehold owner to obtain consent from mortgagees, tenants with leases for more than 21 years and tenants holding under shorter leases which are to be extinguished when the commonhold scheme comes into operation (see 8.3.3).

Section 4 and Sch. 2 provide that an application to register land as commonhold may not be made in respect of certain types of land. The only exclusion you need to note here is that contained in Sch. 2, para. 1, which provides that land above ground level cannot be registered as commonhold unless the property below it is part of the same scheme. In other words, it will not be possible to register the top floors of a block of flats unless the intervening floors down to ground level (including any basement) are similarly registered. There can be no ‘flying freeholds’ (see rubric to Sch. 2, para. 1).

### 8.2.3 Unit holders (s. 12)

A unit holder is the person who is registered, or entitled to be registered, as the proprietor of the freehold estate in a unit (s. 12).

Each unit holder is entitled, and indeed required, to be a member of the commonhold association (see below). The Explanatory Notes which accompanied the Act on its passage through Parliament commented that:

this means that all unit-holders will have two interests in the property of the commonhold: a direct interest in the unit they own and membership of the commonhold association which owns the common parts (Exp. Notes, para 8).

It also means that they will have a say in the management of the property.

### 8.2.4 Commonhold association (ss. 33–5)

Section 34 provides that the commonhold association will be incorporated as a private company limited by guarantee. Documents known as the memorandum and articles of association are required for the incorporation of companies registered under the Companies Act 1985, s. 1, and special forms of these documents for use in incorporating a commonhold association are prescribed by CR 2004 (regs. 13 and 14, Schs. 1 and 2). Using the device of a registered company in this way enables unit holders, as members of the company, to control the operation of the commonhold scheme, while at the same time it provides a separate legal entity, distinct from its members, which can be registered as owner of the common parts.

Membership of the association will be limited to the holders of commonhold units within the scheme (s. 34(2) and Sch. 3, paras. 7, 10 and 12). In the case of any company limited by guarantee, the liability of the members for the debts of the company is limited to the amount they are said to guarantee, and s. 34(1) provides that the memorandum of association for commonhold associations will specify £1 as the amount to be guaranteed by each unit holder.

The commonhold association will be registered as owner of the common parts of the property (defined in s. 25(1)), and will be responsible for all aspects of managing the property. In practice, the work of management will be carried on by the directors of the association (who may well appoint professional

managers to undertake the work). Funding for all necessary activities will be obtained from the unit holders, under arrangements to be specified in the commonhold community statement (see below).

### 8.2.5 Commonhold community statement (ss. 31–3)

The commonhold community statement ('CCS') defines the physical property subject to the scheme, and contains the rules by which it is to operate.

The Commonhold Regulations 2004 prescribe the form and content of the CCS by means of a model statement, set out in Sch. 3, which must be adopted by all commonhold schemes. Part 4 of the model document contains rules which para. 4.1.2 provides are to be:

for the benefit of, and bind, all unit-holders and the commonhold association. Where stated, rules also bind tenants [i.e., those holding under leases from unit holders].

The rules contained in the Statement thus create the web of rights and duties which are needed for property containing interdependent units.

The model CCS is a lengthy document, and for your purposes it is probably sufficient to note that the matters which it covers include:

- allocation of rights and duties to each individual unit, including permitted use;
- provision for the conduct of all financial affairs of the commonhold, including arrangements for raising income to meet the expenses of running the property and if necessary for creating a reserve fund;
- provisions for insurance, maintenance and repair of the common parts by the commonhold association; and
- arrangements for the resolution of disputes between individual unit holders and between unit holders and the commonhold association.

In addition to the very detailed provisions which must be included in every CCS, an individual statement may contain 'local rules' specifying additional requirements which are to apply to that particular commonhold scheme.

From a land law point of view, a particularly interesting provision relating to the CCS is to be found in s. 31(7):

A duty conferred by a commonhold community statement on a commonhold association or a unit holder shall not require any other formality.

Thus, there will be no need for the purchasers of units to enter into covenants in the deed of transfer, and it appears from the Explanatory Notes (para. 80) that inclusion in the statement will also be sufficient to create easements over both individual units and the common parts, which again, save for the commonhold scheme, would normally require formal grant or reservation by deed. Regulation 15(4) of CR 2004 provides that the CCS must be signed by the person applying for commonhold registration, but there is no requirement for the use of a deed. Thus it seems that s. 31(7) creates an exception to the general rule that the grant of a legal interest must be made by deed (LPA 1925, s. 52(1)).

### 8.2.6 The nature of commonhold

You have now seen the various elements in a commonhold scheme, and noted several statutory definitions. You may have noticed, however, that no definition of 'commonhold' itself has been given. That is because there is no definition to be found in the Act. Section 1(2) explains that:

a reference to a commonhold is a reference to land in relation to which a commonhold association exercises functions,

but this merely takes us back to commonhold land and does not help to define the concept of 'commonhold'. This point is of importance because some writers speak of commonhold as a new form of tenure, but this is not a notion which one finds in the Act itself, which bases the structure of commonhold schemes on the existing system of freehold tenure. Thus each unit holder will own the fee simple estate in his or her unit, while the commonhold association will hold a similar estate in the common parts. The rights and duties of the various parties will be regulated by terms imposed by the CCS and by the relevant provisions of company law, but the land itself, although registered as 'commonhold land', will still be held in fee simple on socage tenure from the Crown and it does not appear that any other tenurial relationship will be created. On this point, you may like to see a note by Riddall ([2003] 67 Conv 358), in which he records a statement by the Lord Chancellor's Department:

Commonhold is a new way of holding freehold land, not a new form of tenure.

### 8.3 Creating commonhold

A commonhold scheme may be created in respect of:

- a new development, when for example a block of flats is being built or an existing building is being remodelled and developed for a new use; or
- an existing block of flats, or any other property with interdependent units, which is currently operated on a leasehold basis but which everyone concerned agrees shall convert to commonhold.

#### 8.3.1 New development with no existing unit holders (ss. 7 and 8)

A developer would normally decide at an early stage whether to market the property as commonhold and, if the commonhold system is to apply to the development, will set up the scheme before selling off any of the units. To do this the developer will need to incorporate the commonhold association and prepare the commonhold community statement. The developer will then apply for registration of the land as commonhold, supporting the application with the documents needed for incorporation (i.e., memorandum and articles of association), and the CCS. The application can be made only by the registered proprietor of the freehold estate or, in the case of unregistered land, by the person entitled to be registered, but the developer will normally fall into one or other of these categories. If not, the application will, of course, have to be made by whoever is entitled to the freehold estate. The application must also be accompanied by any necessary consents (ss. 2 and 3).

Following registration of the development site as commonhold land, there will be a transitional period, during which the development is carried out. At this stage, the commonhold scheme is not yet functioning, and it is still possible for the developer to change his or her mind and seek cancellation of the registration (s. 8).

The scheme becomes operative with the sale of the first unit. The purchaser is entitled to be registered as proprietor of the freehold estate in the unit the purchaser has bought and automatically becomes a member of the commonhold association; the commonhold association will be registered as proprietor of the freehold estate in the common parts (this will be done by the Registrar automatically without the need for any application by the association); and the rights and duties created by the CCS come into operation (s. 7(3)). The developer continues as registered proprietor of the freehold estate in the remaining units until each is sold.

#### 8.3.2 Conversion of property with existing unit holders (s. 9)

Section 9 of the Act applies the registration procedure already described to property in which there are already existing unit holders, thus enabling property in which the units are already owned by long leaseholders to be converted to commonhold.

The application for registration will be made by the freeholder in accordance with the procedure outlined above, but in this case must be accompanied by a list of the commonhold units and the proposed initial unit holders. Where the property is already fully occupied, as for example where an established block of

leasehold flats is being converted to commonhold, the 'proposed initial unit holders' will be the current long leaseholders. However, in the case of a new development in which some units have been sold but others remain unsold, the developer, or the developer's nominees, would be named as the initial unit holder of any unsold units.

Where property with existing unit holders is registered as commonhold land, the scheme will come into operation immediately. The Registrar will, without requiring separate applications, register the various unit holders as proprietors of the freehold estates in their respective units and the commonhold association as freehold owner of the common parts.

Although the desirability of converting properties with long leasehold units into commonhold was a driving force behind the introduction of the new system, it appears unlikely that such conversions are straightforward and do not seem to have been common occurrences. The difficulty arises from the requirement for consents set out in s. 3 of the Act.

Under s. 3 (supplemented by reg. 3), an application for registration as commonhold land can be made only with the consent of a number of people who may have interests in the property. These include the freehold owner (who as you have seen has to make the application) and owners of leases granted for more than 21 years (for the position of tenants under shorter leases, see 8.3.3). This means that a block of flats cannot convert to commonhold without the agreement of the freeholder and of all long leaseholders. In the course of the Bill's passage through Parliament repeated efforts were made to amend this provision, so as to enable conversions to be made with the consent of a smaller proportion of leaseholders (80 per cent being suggested as a suitable figure). In the view of the Government, however, this would lead to an undesirable mix of commonhold and leasehold units in the same property (because the unwilling leaseholders could not be compelled to convert their interests into commonhold and so would continue as leaseholders, with the commonhold association as their landlord), and it was therefore essential to insist on the requirement that all should consent. Opponents of this requirement considered that it ruled out all possibility of conversion of existing properties, and this may well go some way to explaining the very slow take-up for the new system.

### 8.3.3 Extinction of existing leases

One final point which we must note is that the Act provides that when a commonhold scheme comes into operation:

any lease of the whole or part of the commonhold land shall be extinguished by virtue of this section (ss. 7(3)(d) and 9(3)(f)).

The Act thus creates a new way in which leases may come to an end: extinction on conversion to commonhold. This should cause no difficulty where the lease is for more than 21 years, since the consent of the leaseholder will have been required under s. 3. Presumably the leaseholder would not consent unless either he or she was to be bought out by the developer or was becoming a unit holder under the new scheme. However, the consent of tenants holding under shorter leases (for not more than 21 years) was not required under s. 3 itself, and as a result their leases could be ended against their will. Section 10 provides for payment of compensation by the freeholder to those whose leases are extinguished without consent.

Although contained within the Act when enacted, the provisions for extinguishing leases without consent were regarded as unsatisfactory (and, indeed, likely to raise human rights issues), and changes to them were made by CR 2004. Regulation 3(1) adds holders of leases granted for not more than 21 years to the list of those whose consent is required for commonhold registration, *unless* they are entitled to the grant of a replacement lease. Regulation 10(2) authorises the grant of such a lease for not more than 21 years, provided that it is of the same premises, on the same terms, at the same rent, and for a term equivalent to the unexpired term of the extinguished lease (or for 21 years, where that lease had more than 21 years

left to run). These new provisions thus give shorter leaseholders some bargaining power, and provide the developer with an extra inducement to offer longer leaseholders.

### 8.3.3.1 Subleases

The provisions requiring consents and authorising the creation of replacement leases apply only to leases held from the freeholder. They do not apply to subleases, however long they may be, although such a sublease will of course come to an end with the extinction of the head lease from which it is derived. Thus the subtenant can rely only on the s. 10 provisions for compensation (in this case payable by the sublandlord), unless the sublandlord has acquired a replacement lease, in which case it would be possible to negotiate with him or her for a new sublease.

## 8.4 Managing a commonhold property

The commonhold association is the registered proprietor of the common parts of the property, and has overall responsibility for all aspects of managing the development, including an ability to bring the whole scheme to an end through the process of voluntary winding-up (see 8.6.1). Since only unit holders are permitted to be members of the association this means that they are in effect solely responsible for the conduct of commonhold affairs, and through their votes can control the operation of the scheme.

For practical reasons, however, it is necessary for day-to-day management to be carried on by a few individuals, and the Act gives responsibility for this to the directors of the association. In addition to the general duties to which they are subject as directors of a company limited by guarantee, the directors of a commonhold association will have specific duties imposed on them under the Act and by the provisions of the CCS.

One of the most important of the directors' responsibilities is for the financial management of the commonhold. They are required to make an annual estimate of the income needed to meet running costs and other expenses, and to assess the contribution to be made by each unit holder. They may also raise additional sums of money when required, for example to fund major building work or to meet some emergency.

Under s. 35 the directors are charged with the general duty of using their powers to facilitate the unit holders' enjoyment of their rights and property. They are also responsible for ensuring that individual unit holders act in compliance with commonhold rules, and are required to use all available means for this purpose. In doing so, however, they are to be mindful of the desirability of using alternative dispute resolution methods wherever possible, and the Act provides (s. 35(3)(a)) that the directors:

need not take action if they reasonably think that inaction is in the best interests of establishing or maintaining harmonious relationships between all the unit-holders, and that it will not cause any unit-holder (other than the defaulter) significant loss or ....disadvantage.

These provisions form part of the process for dispute resolution set out at length in the model CCS.

When considering the enforcement of unit holders' duties, you should note that one sanction for breach which is available to landlords of leasehold properties is specifically excluded from commonhold schemes. Section 31(8) provides that:

a commonhold community statement may not provide for the transfer or loss of an interest in land on the occurrence or non-occurrence of a specified event.

In other words, there can be no provision for a unit holder to forfeit his or her estate, however serious or repeated the breaches of duty may be. This may be problematic if a unit holder proves to be a very bad neighbour and may be another reason why commonhold is not being widely used.

## 8.5 Nature of a unit holder's interest

You have seen that unit holders will be registered as the freehold owners of their units, and this is, of course, the principal advantage of a commonhold scheme. In addition, unit holders have the right to use the common parts of the development, although a CCS may provide that certain common parts may be reserved for the use of specified unit holders (s. 25(2)) (as for example if separate parking areas are designated for use by particular units).

Unit holders also have the benefit and burden of the various obligations imposed by the CCS: they will have to contribute their prescribed share to the annual budget and meet any additional financial demands; they will almost certainly have some obligations about the repair and maintenance of their individual properties; and they will be subject to restrictions on the use of their units and their behaviour in them. But all their neighbours will be subject to similar obligations, and unit holders who are affected by breaches of duty, whether by another unit holder or by the commonhold association, should be able to take appropriate action under the dispute resolution process set out in the model CCS.

When a unit is transferred to another holder (as for example when a current owner sells a flat), s. 16 provides that the new owner takes subject to all existing rights and duties, and that the previous owner shall not incur any liabilities or acquire any rights in respect of the property after the transfer. This latter provision cannot be disapplied or varied by agreement, so there should be no way of providing for any continuing liability on the part of the out-going owner—nor indeed any way in which he or she could stipulate for some continuing right under the scheme.

### 8.5.1 Restrictions on dealing with the freehold estate

While in general a unit holder has the usual powers of a freehold owner, it is important to note that there are some unusual restrictions on what the unit holder may do with the property. It is a long-established principle that the estate owner should have a free and unfettered power to alienate his or her property; thus, for example, tenants of leasehold property can assign or sublet the property with legal effect even though in breach of covenant. Section 15(2) maintains this principle in so far as a complete transfer of the property is concerned:

a commonhold community statement may not prevent or restrict the transfer of a commonhold unit

but ss. 17–20 impose considerable restrictions on other dealings with the freehold estate.

#### 8.5.1.1 Restrictions on leasing

(1) *Residential commonhold* A major restriction relating to residential commonhold is to be found in s. 17(1), which provides:

It shall not be possible to create a term of years absolute in a residential commonhold unit unless the term satisfies certain prescribed conditions.

These conditions are now set out in reg. 11(1), which provides that:

- the term must not exceed seven years (with the exception of replacement leases for up to 21 years—see 8.3.3);
- no premium should be payable; and
- there should be no option for renewal that would take the total term to more than seven years.

Section 17(3) provides that an attempt to create a term which contravenes the prescribed conditions will be 'of no effect'. Under s. 17(4) a party to such a void transaction may seek appropriate relief from the court, which may include an order that the transaction shall take effect as if 'it provided for the creation of a term of years of a specified length' (presumably a term complying with the required conditions).



The reason for this limitation on the unit holder's freedom to deal with his or her own property is to be found in the government's policy that:

residential commonhold units should not be let for long unbroken periods . . . to avoid the possibility of repeating the difficulties which exist in leasehold blocks now. (Exp. Notes, para. 65).

Thus, the provision is designed to guard against the situation in which flats are held by non-resident owners who regard the property as an investment but have no direct personal interest in it, while the actual occupiers, who are immediately affected by the condition of the development, have no say in its management (tenants will not be members of the commonhold association and under the model CCS have duties but no rights).

(2) *Non-residential commonholds* Leases of units in a non-residential commonhold scheme are to take effect subject to any provisions of the CCS (s. 18), and at present it seems that the imposition of any restrictions on leasing is regulated only by the needs of individual schemes.

### 8.5.1.2 Restrictions on other transactions

Section 20 regulates the creation of other interests by the freehold owner. The section opens with the very general provision that:

A commonhold community statement may not prevent or restrict the creation, grant or transfer by a unit-holder of—

- (a) an interest in the whole or part of his unit;
- (b) a charge over his unit.

However, s. 20(3) then cuts this freedom down by providing that:

It shall not be possible to create an interest of a prescribed kind in a commonhold unit unless the commonhold association—

- (a) is a party to the creation of the interest, or
- (b) consents in writing to the creation of the interest.

Any attempt to create an interest in contravention of this requirement shall be 'of no effect'. At first glance, you might think, therefore, that a unit holder cannot even mortgage his or her property without securing a resolution of the commonhold association, but at the very end of the section (s. 20(6)), we are told that the 'interest' referred to throughout does not include a charge—so at the end of the day, it appears that the unit holder may mortgage a unit without having to ask for the neighbours' permission.

It was thought that Regulations to be made under the Act would prescribe the interests which could not be created without the participation or consent of the commonhold association (see Clarke [2002] 66 Conv 349 at 375–6 and n. 10, which suggested that such interests were likely to include easements and profits). However, there is no reference to prescribed interests in CR 2004, and provisions in the model CCS about dealings with the land (para. 4.7) relate only to the transfer and leasing of units.

## 8.6 Ending commonhold

The Act provides for the commonhold scheme to be brought to an end either voluntarily, with the consent of the unit holders, or compulsorily in the event of the association's being unable to meet its debts.

### 8.6.1 Termination by voluntary winding-up (ss. 43–9)

In certain circumstances, the unit holders may agree that it is desirable to bring the commonhold to an end. It could be, for example, that the members wish to sell out to a developer and divide the proceeds between themselves.

In order to do this, the consent of at least 80 per cent of the members of the association is required (s. 43(1)(c)), voting in favour of resolutions to wind-up the association and appoint a liquidator. They must also agree the terms of a statement (the 'termination statement'), which sets out the association's proposals for dealing with the land and for distributing the association's assets (which, of course, would include the purchase money to be obtained on the sale of the property).

Section 44 provides that where 100 per cent of the members vote in favour, the liquidator may make an application for the land to cease to be commonhold land (a 'termination application') directly to the registrar. If the vote is not unanimous but does satisfy the minimum requirement of 80 per cent, s. 45 requires that the liquidator must apply to the court to determine the terms on which a termination application may be made and the content of the termination statement. This process is, of course, designed to protect the interests of the dissenting minority.

Once the necessary procedures have been followed, the association is entitled to be registered as the proprietor of the freehold estate in each commonhold unit (i.e., the individual unit holders are divested of their titles), and the property can then be dealt with as proposed in the termination statement.

### **8.6.2 Termination by winding-up by the court (ss. 50–4)**

This method is used where the association is unable to meet its debts and a creditor presents a petition for winding-up under the Insolvency Act 1986, s. 124. This is obviously a very serious matter for the unit holders, since the role of the commonhold association in owning the common parts and managing the whole property is crucial to the operation of any commonhold scheme.

#### **8.6.2.1 Succession orders**

Accordingly, where the court makes a winding-up order, s. 51 empowers it to make a further order as well, a 'succession order', which gives recognition to a new association ('the successor commonhold association') which will take over responsibility for running the commonhold and will be registered as proprietor of the common parts. The circumstances in which this will be done are not specified, the Act merely providing in s. 51(4) that:

The court shall grant an application [for a succession order] unless it thinks that the circumstances of the insolvent commonhold association make a succession order inappropriate.

It seems likely that an order would be granted in circumstances in which the debts of the association can be met, presumably from the reserve fund (see s. 39) with, if necessary, additional funds raised by the members. The Explanatory Notes to the Act describe the arrangements for a successor commonhold association as being designed to ensure that:

those members of the association who have paid all their liabilities to the creditors of the insolvent association may continue to live in a stable commonhold development (para. 102).

#### **8.6.2.2 No succession order**

If a succession order is not made, the winding up goes ahead and s. 54(4) provides that once it is completed the registrar is required to take such action as will result in the land no longer being registered as commonhold land and to give effect to the liquidator's determination.

Such an outcome would of course cause great difficulty for the unit holders, who would be left with freehold title to their individual units, but with uncertainty about the future ownership of the common parts and with no one to manage the property as a whole or enforce obligations between units.

### **8.6.2.3 Consequences for the unit-holder if the commonhold association is unable to pay its debts**

A company is a separate legal person distinct from its members. The commonhold unit holder, as a member of a company limited by guarantee, would be liable to contribute only £1 to the debts of the association in the event of its being wound up (see 8.2.4). However, any comfort this might seem to give to a unit holder is really illusory, for two reasons.

#### **(i) Unit holder's liability to pay assessments and levies**

In addition to the annual assessment to meet estimated outgoings, the commonhold association is entitled to raise further sums to maintain a reserve fund and to meet emergencies (ss. 38–9). It is likely that the debts which the association cannot pay would have been incurred by providing services to the unit holders (for example, by repairing and improving the property) and the company itself, or possibly the liquidator, would most probably raise money to meet such debts by requiring extra contributions from the unit holders (see Crabb (2004) 25 Comp. Law 213 at 215–6).

#### **(ii) Loss of commonhold status**

It seems probable that the court would make a succession order only if the debts of the original company could be cleared, or at any rate substantially reduced. If no successor association is appointed, the property may lose its registration as commonhold land with the undesirable consequences for the unit holders that we have already noted. With such a possibility hanging over them, it is likely that unit holders will try to mount a rescue operation by raising money to meet the association's debts, even if they are not legally obliged to do so.

## **8.7 Evaluation of commonhold**

### **8.7.1 Advantages of commonhold**

You have already seen the principal advantages of the new system. The unit holder is enabled to hold the freehold title to the property and can benefit from the positive and negative obligations which bind neighbours in the scheme. The problem of ownership of the common parts is solved by vesting it in the commonhold association, and management of the property and enforcement of obligations can be undertaken by the association on behalf of its members instead of by a landlord acting in the landlord's own interests.

Another advantage is that the form and content of commonhold community statements are required to follow a standard pattern, and it was thought that this would simplify the process of dealing with individual units, both on their original purchase and on subsequent sale. By contrast, there is no common form for the grant of a lease, and a good deal of time can be spent on negotiating terms at the outset and then scrutinising them when the property comes to be sold.

### **8.7.2 Disadvantages of commonhold**

There are several aspects of the new scheme which may well have proved unattractive to purchasers and, in some cases, to the professional lenders who would fund their purchases.

#### **8.7.2.1 Restrictions on the power of the unit holder to deal with his freehold estate**

These restrictions are mentioned at 8.5.1. The most serious one appears to be the limitation on the length of leases which may be created in respect of a residential commonhold unit. This restriction was intended, for understandable reasons, to prevent the use of residential commonholds as long-term investments. Deterring investors, however, inevitably limits the pool of potential buyers, which in turn may make commonhold schemes appear less attractive to developers. The more restricted market might also be of concern to mortgagees who may have to sell the property if the borrower defaults.

#### **8.7.2.2 No provisions for forfeiture for breach of obligations**

One would not expect there to be provisions for forfeiture of a freehold estate, and indeed many will see the absence of forfeiture as giving commonhold a positive advantage over long leaseholds. Nevertheless,

it does mean that there is no ultimate sanction for persistent breach of obligation, and no simple way in which unit holders of the association can rid themselves of 'nuisance' neighbours.

### 8.7.2.3 *Problem of insolvency*

Because commonhold has been used so infrequently, it is difficult to assess the effect of the Act's provisions on winding-up without knowing the circumstances in which the court would recognise a successor association. Obviously there would be major difficulties for unit holders if the original association were to be wound-up without a replacement.

Earlier proposals for the introduction of commonhold contained very detailed provisions about what would happen in cases of insolvency. By contrast, the Act goes to the opposite extreme and really tells us very little about what will happen if the association cannot meet its debts. The possibility of insolvency is of concern not only to prospective purchasers but also to their lenders, and it must be remembered that if commonhold were to succeed it had to be attractive to the lending institutions.

It has been suggested that the possible danger to commonhold owners (and their mortgagees) may, however, be more apparent than real, since it seems that 'experience in other countries, including the United States, suggests that it is very rare for a commonhold association to be wound up on the grounds of insolvency' (Driscoll [2000] *Solicitors Journal* 849 at p. 852). Other writers, however, take a more pessimistic view of the matter, one in particular drawing attention to the problems that could arise from inadequate or even non-existent insurance against injury resulting from failure to maintain the property (see Wong [2006] 70 *Conv* 14 at 22–4).

### 8.7.2.4 *Lack of any regulatory body or specialist tribunal*

The process of setting up a commonhold scheme depends solely on producing the right documents to the Land Registry and securing registration of the property as commonhold land. There is no process for scrutinising the original proposals nor for monitoring the management process when the scheme is in operation. Further, if the alternative dispute resolution process prescribed in the model CCS does not succeed, disputes between unit holders or with the association will be dealt with through the existing court system. Experience in other jurisdictions with similar schemes suggests that it would be better for such matters to come before a separate body or tribunal which could build up specialist expertise.

The draft Commonhold Regulations provided that a commonhold association must be a member of an approved ombudsman scheme. The final version of the Regulations does not contain any compulsory provision, and the model CCS merely provides that disputes between unit holders and the commonhold association may be referred to the ombudsman 'if the commonhold association is a member of an approved ombudsman scheme' (CR 2004, Sch.3, Part 4, para. 4.11).

## 8.7.3 **How does commonhold compare with long leaseholds?**

In considering this question, it is necessary to bear in mind that the position of long leaseholders of residential property has been very considerably improved in recent years. In 8.1.2, the disadvantages of leasehold ownership are outlined: the nature of the lease as a 'wasting asset' and the fact that landlords, naturally enough, tend to manage property in their own interests, rather than in those of their tenants. The details of the statutory protection of long leaseholders is outside the scope of this text, but you should be aware that their position has been significantly improved by a series of reforms which began in 1967 with the Leasehold Reform Act. Thus individual leaseholders now have the right to require the grant of new leases when their old ones expire and, through a process known as 'leasehold enfranchisement', also have the right to buy out their landlord, thus acquiring the freehold estate in the property. In the case of flats, the difficulties already noted about the running of covenants and the ownership of the common parts prevent owners acquiring the freehold of individual flats, but the leaseholders as a group may buy the freehold of the whole property, vesting it in a company formed for the purpose. This has become a common practice and it is normal to use a guarantee company for this purpose.

Part 2 of the CLRA 2002 made improvements to the position of long leaseholders of residential property. It imposes restrictions on the use of forfeiture, facilitates both the acquisition of a new lease and the purchase of the reversion, and gives leaseholders a new right to take over the management of the property without having to show fault on the part of the landlord.

These statutory reforms go a long way towards making leasehold property a more attractive option than it was in the past, and it may well be that purchasers and lenders consider that leasehold property offers more security than is to be found in the untried system of commonhold.

#### 8.7.4 A slow start for commonhold

So far there has been little enthusiasm for the new system. A survey carried out as the Act came into force found that developers were cautious about promoting commonhold, regarding it as ‘untried and untested’ and having concerns about the attitude of lenders. It appeared that some developers abandoned proposals for commonhold schemes because of ‘the perceived reluctance on the part of major banks and building societies to lend against commonhold tenure’ (see Dankin [2005] EG—18 June 2005 (No. 0524) 171).

A few months later a slightly more hopeful note was struck with a report that the first two registrations of property as commonhold land had been completed and that there were three more applications in the pipeline (see Fetherstonehaugh [2005] EG—3 September 2005 (No. 0535) 104), and in 2006 there came the news that a commonhold structure had been chosen for a major new development at Milton Keynes. It is planned that the Milton Keynes Oakgrove Millenium Community Scheme will provide up to 2,300 new homes, two new schools, a landscaped wildlife area, a health centre, shops and business premises. The development of an integrated new community of this type means that there will be a need to manage the neighbourhood as a whole, with residents and business users all contributing to the cost of services and ‘having a say’ in what is to be done, and the developers consider this can best be achieved through a commonhold scheme (see Baker [2007] EG—4 March 2006 (No. 0609) 173). As yet, however, there has been no sign of other major developers following this lead.

#### 8.7.5 Law Commission proposals

Linked to concerns about the increase in sales of properties leasehold, rather than freehold, there have also been concerns expressed by the government as to why commonhold is not being used more widely. Thus far fewer than 20 commonholds have been registered. In July 2020, The Law Commission published a report examining the reasons why commonhold has not been popular and making recommendations to increase its uptake, partly by making it easier for existing leaseholders to convert to commonhold without the consent of the freeholder and mortgage lender and without unanimous consent of all leaseholders affected. You can find the report online at <https://www.lawcom.gov.uk/project/commonhold/>

#### FURTHER READING

Aldridge Report—‘*Commonhold: Freehold Flats and Freehold Ownership of Other Interdependent Buildings*’, 1987 Cm 179 Part 1—Introduction.

Clarke, ‘The Enactment of Commonhold—Problems, Principles and Perspectives’ [2002] 66 Conv 349.

Kenny, ‘Commonhold—At Last?’ [2001] 65 Conv 1.

Smith, ‘The Purity of Commonhold’ [2004] Conv 194.

#### Slow start for commonhold

Dankin, ‘Lenders have fears’ [2005] EG 18 June 2005 (No. 0524) 171.

Fetherstonehaugh, ‘Slow on the uptake’ [2005] EG 3 September 2005 (No. 0535) 104.

Baker, ‘A better system of land tenure’ [2006] EG (No. 0609) 173 (the development at Milton Keynes).

#### Concerns about insolvency

Driscoll, 'Leasehold Reform and Commonhold' (2000) 144 Sol Journal 22 September 2002 849.

Crabb, 'The Commonhold and Leasehold Reform Act 2002: a company law perspective' (2004) 25 Comp.Law 213 at 215–6.

Wong, 'Potential Pitfalls in the Commonhold Community Statement and the Corporate Mechanisms of the Commonhold Association' [2006] 70 Conv 14 at 22–24 and 33–36.

### **Reform**