Guidance

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Advising on leasehold provisions including ground rent clauses

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Status

This guidance is to help you understand your obligations and how to comply with them. We will have regard to it when exercising our regulatory functions.

Who is this guidance for?

All solicitors and all law firms, their managers and employees particularly those dealing with leasehold conveyancing.

This guidance may be relevant to members of the public who are considering buying or selling a leasehold property.

Purpose of this guidance

To help you understand what our Standards and Regulations require when acting for clients who are buying leasehold properties and to avoid possible breaches of our requirements.

Introduction

We are concerned that clients are not receiving appropriate advice on onerous clauses in leases.

We have seen this arise most frequently in the context of ground rent clauses for newbuild properties. Depending on their wording, such clauses can result in an increase in the ground rent payable by the lessee from a few hundred pounds a year to more than, for example, £70,000 a year, over the course of the first hundred years of a lease. Such clauses can have a significant impact on the lessee due to the unexpectedly high costs and impact on the future value and saleability of the leasehold.

The SRA Standards and Regulations

We expect you to act in accordance with your professional obligations and to provide a competent level of service when dealing with leasehold conveyancing.

Failure to provide competent and independent advice may put you in breach of one or more of the SRA Principles or Code provisions. Our Principles require you to:

Principle 2: Uphold public trust and confidence in the solicitors' profession and in legal services provided by authorised persons.

Principle 3: Act with independence.

Principle 5: Act with integrity.

Principle 7: Act in the best interests of each client.

- You ensure that the service you provide to clients is competent and delivered in a timely manner: Paragraph 3.2 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 4.2 of the Code of Conduct for Firms.
- You maintain your competence to carry out your role and keep your professional knowledge and skills up to date: Paragraph 3.3 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 4.3 of the Code of Conduct for Firms.
- You consider and take account of your client's attributes, needs and circumstances: Paragraph 3.4 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 4.2 of the Code of Conduct for Firms.
- Where you supervise or manage others providing legal services: a) you remain accountable for the work carried out through them; b) you effectively supervise work being done for clients: Paragraph 3.5 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 4.4. of the Code of Conduct for Firms.
- You ensure that the individuals you manage are competent to carry out their role, and keep their professional knowledge and skills, as well as understanding of their legal, ethical and regulatory obligations, up to date: Paragraph 3.6 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 4.3 of the Code of Conduct for Firms

Our Codes also set out specific requirements which must be followed in respect of any third party who introduces business to you / your firm or with whom you share your fees (Paragraph 5.1 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 7.1 of the Code of Conduct for Firms).

You should also be aware of the provisions preventing you from acting where there is a conflict of interest or a significant risk of such a conflict

in relation to a matter (Paragraphs 6.2 of the Code of Conduct for Solicitors, RELs and RFLs and Code of Conduct for Firms).

Further, if things do go wrong, we require you to be honest and open with your clients, and if they suffer loss or harm as a result, you should put matters right (if possible) and explain fully and promptly what has happened and the likely impact (paragraph 7.11 of the Code of Conduct for Solicitors, RELs and RFLs and paragraph 3.5 of the Code of Conduct for Firms).

Providing competent advice

Clients rely on your advice on legal documents to enter into legal transactions. This includes ensuring that they understand the meaning and effect of the clauses, and have any risks drawn to their attention. This includes risks of a kind which may be obvious to you but which the client may not appreciate.

You will need to make sure that your client is fully and competently advised that they are purchasing a leasehold interest in the property concerned, and that they understand the implications of this and any material clauses.

This includes explaining to your client the effect over time of clauses which increase the rents payable. Particular features clients may need to understand:

- the exponential effect of clauses which provide for rents to increase periodically by a fixed amount (e.g. doubling)
- where a review operates by reference to a valuation, if there are stated assumptions (which may not always be correct) built into the review mechanism, such as a specific unexpired lease period

We consider that your obligation to provide competent advice would not be discharged solely by:

- describing the "current" rent charges
- referring to the wording as being a "standard clause"
- telling clients to read the lease clauses

Depending on the terms of the lease, clients may also need to be advised of other risks, and the consequences to the client if these do materialise. This includes the risk that a particular ground rent provision is likely over time to cause the lease to be treated as an assured shorthold tenancy under the Housing Act 1988, by virtue of exceeding £250 per annum (£1,000 per annum in Greater London) or otherwise. If this occurs, it will change the nature of the relationship between the client and the freeholder, which could be particularly significant if rent falls into arrears.

With an experienced business client, it may not be necessary to provide the same level of detail as would be required by an inexperienced or vulnerable purchaser, although we would expect that anything unusual or potentially onerous would still be drawn to the client's attention. Where clients specifically request advice to enable them to understand aspects of the lease, you must provide the advice requested.

It may not be within the scope of an ordinary legal retainer to advise on the marketability of a lease in future. However, if you do purport to advise on this, you should ensure that such advice takes into account the effect of any such clauses. Where a valuation on the lease is provided to you, and relies on any incorrect assumptions (for instance, about rents being fixed over time), you should act in the best interests of your client by advising accordingly and correcting the valuer.

Where we receive complaints about a failure to advise appropriately on lease clauses, we apply our Enforcement Strategy [https://beta.sra.org.uk/sra/corporate-strategy/sra-enforcement-strategy/] in deciding what action to take. Generally, we will not penalise a single negligent act or an omission and will focus on cases where there is evidence of seriously or persistently poor levels of competence demonstrating a pattern of behaviour; an example of which might be an overly mechanical "copy-and-paste" approach to advising. Patterns of concerning behaviour can indicate a failure in systems and controls, poor levels of competence, or an unwillingness or inability to learn lessons.

However, a single case is capable of demonstrating behaviour falling well below the standards we require. We are likely to consider matters as more serious where a firm or an individual has knowingly acted outside their competence or has failed to take reasonable steps to update their knowledge and skills, or those of their employees. We will also take into account the harm caused by the individual or firm's actions and the impact this has had on the victim(s).

Leasehold Reform (Ground Rent) Act 2022

The Leasehold Reform (Ground Rent) Act 2022 has introduced changes which affect property purchases involving leasehold dwellings.

The Act came into force at the end of June 2022 for most types of properties, and if you represent buyers, developers or landlords, you should be aware of these changes. These include:

- If any ground rent is demanded as part of a regulated new residential long lease, it cannot be for more than one peppercorn per year. In effect, most residential leaseholders will not face financial demands for ground rent.
- Landlords are banned from charging administration fees for collecting a peppercorn rent.

- Landlords who require a payment of ground rent in contravention of the Act face penalties of between £500 and £30,000, enforced by way of a civil penalty regime, and they can also be required to refund any prohibited rents collected.
- For existing leaseholders entering into voluntary lease extensions after commencement, the extended portion of their lease will be reduced to a peppercorn.

There are only selected exceptions from this Act. These are tightly defined and include applicable community-led housing, certain financial products, and business leases which are defined by the Act as leases of commercial premises which include a dwelling, use of which substantially contributes to the business purposes.

Statutory lease extensions for both houses and flats remain unchanged and are therefore exempt from the provisions of the Act.

Read the full Leasehold Reform (Ground Rent) Act 2022 [https://www.legislation.gov.uk/ukpga/2022/1/contents/enacted] for further information.

Referrals and conflicts of interest

It is acceptable for your firm to be on "recommended" lists of housing developers. Such lists can be mutually beneficial for the client, the developer, and your firm.

You should however have regard to the core requirement to act with independence and not to allow your advice to be influenced by commercial interests arising from any arrangement or relationship that you may have with the developer.

We do not place any restriction on you being instructed by developers that provide incentives to their customers to use recommended firms. However, you should take into account your obligations under Rule 5.1 of the Code of Conduct for Solicitors, RELs and RFLs, and our guidance on conflicts of interest, and:

- if the developer has any financial or other interest in referring the client to you, clients must be clearly informed of this before you accept instructions.
- you must not offer any improper incentive, either monetary or otherwise, to a housing developer to include you on a recommended list.
- clients should not be obliged to use a specific firm – if it becomes apparent they were told that they were, we expect you to raise the issue with the developer and to advise your client that there is no restriction and that they are free to instruct legal advisors of their own choosing.

We expect you to be especially careful in cases where the developer has imposed a short deadline on a client to exchange contracts, after which the client would lose some benefit or entitlement (such as a contribution to stamp duty, or fittings for the house). You should recognise that this may cause your client to become vulnerable to exchanging on a transaction without fully understanding it (including seeking further advice if desired) and you should take steps to mitigate any such risks. These could include providing early clear advice about the necessary steps in the process, and how long these can take, and making sure that advice on material risks is provided without delay. When deciding what regulatory action to take, we will consider whether you took advantage of your client's vulnerability.

Further help

If you require any further assistance, please contact the Professional Ethics helpline [https://beta.sra.org.uk/home/contact-us/] .