

Technical report

Commonhold Lender Guide

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Introduction

One of the Government's manifesto pledges is to make commonhold tenure the default for properties affected by interdependence instead of leasehold tenure. This paper is intended to serve as an informative guide for what commonhold is and what the implications may be for lenders. Please note this paper refers to England and Wales only, as the feudal system in Scotland was abolished in 2000.

Leasehold tenure

The law in England and Wales allows any landowner to create an interest in their land (less than the interest they own), subject to certain restrictions.

A freehold landowner could create a licence/lease for another to occupy their land for a short period of time:

Assured Shorthold Tenancy

The default legal category of residential tenancy in England and Wales, normally for a period of 6 or 12 months, subject to regular rent payments and can be renewed. If notice is not served at the end of the specified period, the tenancy becomes a periodic tenancy (often referred to as a 'rolling' tenancy).

An Indefinite Secure Tenancy

For an indefinite period and subject to regular rent payments.

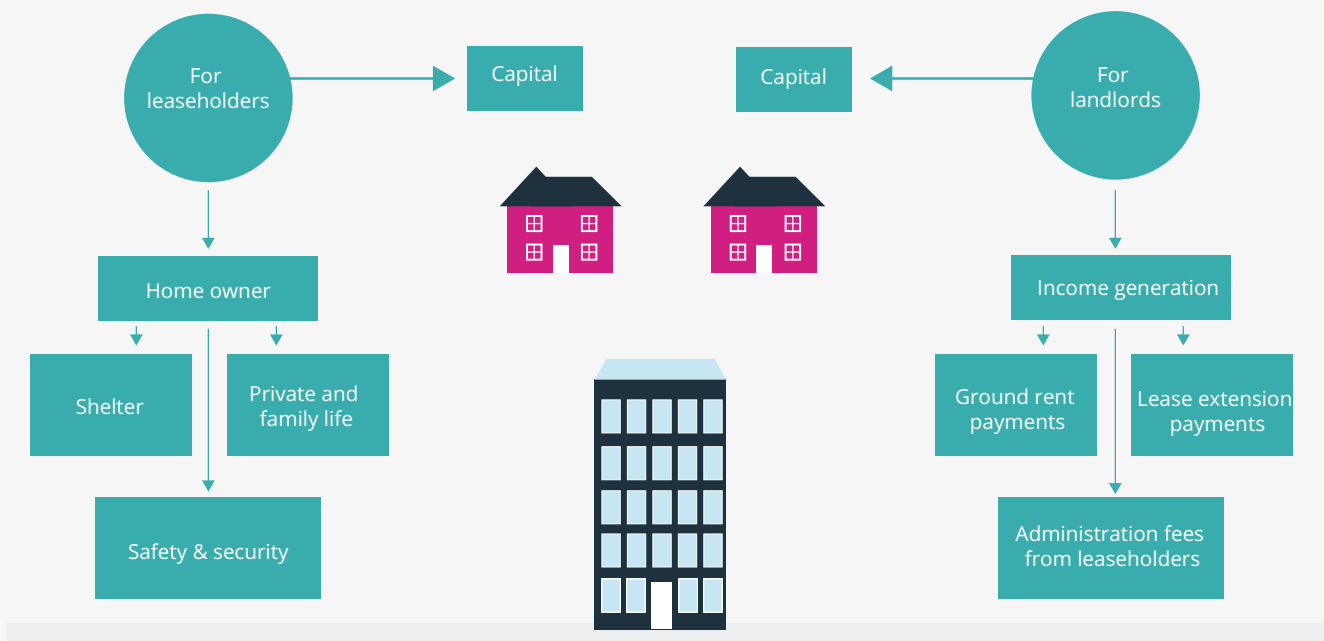
These occupations are considered inappropriate for secured lending.

Consider a potential tenant approaching a freehold owner and requesting a lease for a period of 100 years or more, subject to paying all the monthly rents upfront. The lessee agrees to maintain and insure the property, providing they can sell or bequeath their lease to another lessee, and agrees to hand the property back to the freeholder, in reasonable condition, at the end of the term.

In this situation, the property is held on a lease and lenders consider this defined term suitable for secured lending. This is what is referred to as leasehold. The property is mortgageable while the lease has a sufficient unexpired length to attract a buyer.

In summary, leasehold tenure is a time-limited interest in a property with control of the asset shared with a freeholder.

The below illustration demonstrates the purpose of the leasehold system as defined by the Law Commission's 'Reinvigorating Commonhold' paper. Under the current system, leaseholders are 'owners yet tenants' whose interests in the management of the block or estate may conflict with those of the freeholder or managing agent.



Commonhold tenure

Commonhold tenure was introduced in England and Wales in the Commonhold and Leasehold Reform Act 2002 (CLRA). This tenure is an alternative to the default leasehold tenure for properties affected by interdependence and was devised as a way of addressing key concerns of leasehold occupation including the lack of long-term ownership and unfair management practices.

It provides a legal framework allowing property owners (called 'unit holders') to have a freehold title (eliminating the diminishing asset that is a leasehold title) and that the use of, repair, and maintenance of both the individual units and the common parts are governed by a single document called the Commonhold Community Statement (CCS).

The commonhold system is a more democratic approach to the management of interdependent units and, in theory, allows greater control over expenditure as there are no additional costs borne by the presence of a landlord.

The below illustration from the Law Commission demonstrates how commonhold could simplify management over the current leasehold process through a unified contribution.

Please note the icons making commonhold contributions are the same as those in the Commonhold Association.

How does it work?

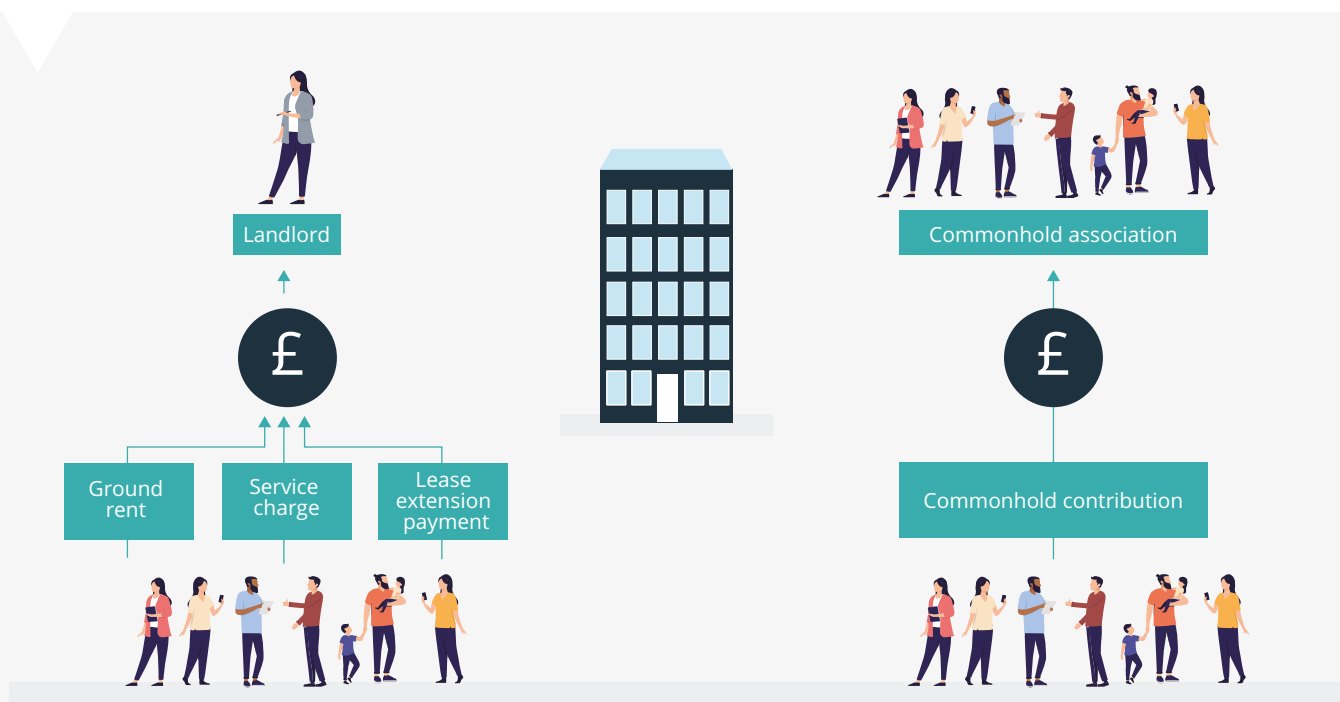
There must be a memorandum of association of a Commonhold Association (CA) alongside a CCS. Once a development is completed the initial title is divided into a community of freehold titles, with the title to the common parts held by the CA, of which only the individual unit holders can be members.

The CA requires at least two directors. They do not need to be members of the CA, or unit holders, and therefore could be appointed property professionals with relevant expertise in estate management.

The CCS records the units within the commonhold and:

- Details the provisions for the use, insurance, repair and maintenance of each unit.
- Regulates the use of the common parts.
- Obliges the Commonhold Association to insure, repair and maintain the common parts.

Commonhold can only exist in relation to freehold land; possessory land cannot be commonhold. It is not possible for a block to be of mixed tenure as a commonhold can only be created from the ground upwards. For example, there cannot be leasehold commercial units at ground floor with commonhold residential flats above.





Advantages of commonhold

- The value of leasehold properties depreciates over time as the lease diminishes. The shorter the lease length, the greater the cost to extend/enfranchise. Short-leased properties are also of limited saleability and mortgageability. The commonhold structure provides permanent ownership.
- The need to pay a ground rent to the freeholder, which sometimes can be onerous and subject to escalation, is eliminated.
- Unit holders have greater autonomy over what repairs are carried out and by whom.
- Leaseholders can face unpredictable service charges. Financial management of commonhold is more transparent, with costs being agreed by the CA.
- Commonhold tenure is more democratic, with all unit holders benefiting from equal voting rights.
- If the terms of a lease are broken by a tenant, they face the risk of lease forfeiture from the freeholder/landlord. This threat does not exist in a commonhold arrangement.

Disadvantages of commonhold

- The CA requires members to cooperate and actively participate in the management of the block. For contentious issues or larger blocks where it is more difficult to discuss with all unit holders, the decision-making process could be protracted and any progressive defects will worsen until a collective decision is made.
- Directors must lead the CA however, particularly in smaller blocks, there may not be anyone willing to take a leading role. This will then require payment for third-party estate managers.
- The lack of the deterrent of forfeiture could result in non-payment of contributions or other infractions of obligations.
- There is a lack of familiarity with the process across the industry which has stifled adoption. From a development perspective, installing a leasehold structure can provide a further revenue stream which a commonhold structure would not allow for. There is no incentive for a developer to ignore the potential revenue stream of leasehold.
- The limited adoption of commonhold tenure has led to a smaller pool of lenders willing to accept commonhold properties.

Conversion from leasehold to commonhold

Under the provisions of the CLRA 2002, an existing leasehold block can be converted into commonhold. For this to occur, consent is required of all leaseholders holding a registered lease originally granted exceeding 21 years, the freeholder, and all mortgagees.

In practice, this is likely to block the conversion process in most instances due to the number of individuals and organisations involved in the decision-making process, as there must be unanimous agreement to convert.

The Government has proposed simplification of this process in the Commonhold White Paper. However no additional legislation has been produced yet. The Government's White Paper suggests the threshold for conversion should be set at 50% but does not detail how the remaining 50% will be impacted if they are unable or unwilling to participate.

Alternatives to commonhold

Critics have highlighted that leasehold properties already have mechanisms in place similar to what commonhold can achieve – right to manage and collective enfranchisement.

Right to manage gives leaseholders the right to take over responsibility for management of a block/estate should at least 50% of the leaseholders agree. The freeholder does not need to provide consent and once the legal process has concluded a right to manage company will be incorporated, with participating leaseholders added as members or shareholders. Whilst owners will be able to exercise greater control, the property remains a leasehold asset with a freeholder interest who retains ownership of the fabric of the building, grounds and airspace.

Collective enfranchisement refers to the right of leaseholders under the Leasehold Reform, Housing and Urban Development Act 1993 to take ownership and management of a block from the freeholder, giving each unit a share of the freehold. This is an expensive process, as alongside payment of the share of the premium to purchase the freehold, fees for both the leaseholder and the freeholder must be paid too. Not all blocks will meet the qualifying criteria and fees will likely be due in determining whether a block is viable before the process begins irrespective of whether the enfranchisement is successful.



The future of commonhold

Adoption of commonhold tenure has been low since inception, with a reputed uptake of around 15 blocks including Spire View (Pickering, 2008) which was repossessed after failing to sell enough completed units due to the limited lender acceptance of commonhold and the concurrent economic downturn.

The Leasehold and Freehold Reform Act 2024, passed under the previous Conservative Government, amongst other changes, banned the sale of new leasehold houses, removed the requirement for a leaseholder to have owned their property for two years before purchasing or extending their lease, and requires greater transparency over service charges.

The incoming Labour Government has pledged to take these changes further, and it is anticipated the draft Leasehold and Commonhold Reform Bill will be published in H2 2025 for pre-legislative review. The expectation is that new leasehold flats will be banned and commonhold will become the default tenure in its place.

When the Feudal system was abolished in Scotland, some blocks owned collectively as freeholds fell into disrepair without the appropriate legal structure to enforce maintenance. It is anticipated that upcoming legislation

will view the Scottish experience as a cautionary tale and seek to ensure changes to commonhold tenure do not lead to the same outcome. Additional legislation was eventually introduced in Scotland demonstrating the existence of a functional process that commonhold could model itself upon.

For commonhold to succeed as a replacement for leasehold, the following will need to be addressed:

- The comfort of familiarity with leasehold tenure for developers and legal professionals.
- The lack of incentivisation for developers to implement commonholds.
- The opportunity developers currently have in selling the freehold interest to increase revenue for the development.
- The hesitancy from mortgage lenders to accept commonhold properties.
- Potential resistance from the market, as commonhold will not succeed without the participation of purchasers.

Impact on value

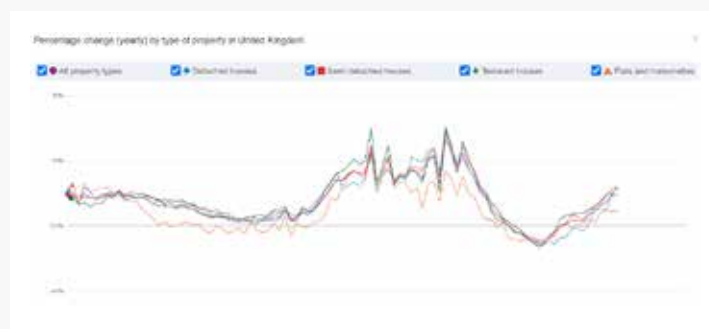
The impact of commonhold tenure on value is currently unquantifiable and the effect of the White Paper's intended direction on saleability is dependent on the detail of the associated legislation that is yet to be published.

Flats are likely to be the dominant property type affected by commonhold. Since the Grenfell fire, the price performance of flats has lagged below that of houses since late 2017/early 2018 (source: HMLR).

Recent history has demonstrated greater volatility of the price of flats. The implementation of the Medium Rise Scheme (later renamed the Cladding Safety Scheme) in late 2022 coincided with the market turmoil following the mini budget, making it impossible to determine if this slowed the widening of the performance gap.

The data shows that, despite fluctuations, the prices of flats are beginning to perform more closely with houses.

If the implementation of commonhold does not satisfy the concerns of stakeholders and creates a two-tier market, it is possible this gap will begin to widen again.



Newbuild

The proposed expansion of commonhold tenure in England and Wales could significantly reshape the new-build flat market, where leasehold has long been the norm.

Although commonhold was introduced in 2002, adoption has been negligible due to legal inflexibility and lack of developer incentives. Proposed reforms (Law Commission, 2020; Leasehold and Freehold Reform Bill, 2024) aim to change this by making commonhold viable for complex, high-density, and mixed-use developments.

For developers, commonhold presents a loss of recurring income streams from ground rents and freehold sales. This change necessitates increased need to front-load profitability within their business models. However, the transparency and fairness of commonhold may appeal to ethically conscious buyers, offering a potential marketing advantage.

Developers may also face higher administrative complexity during the initial setup of Commonhold Associations.



Considerations for lenders

The current process of leasehold to commonhold conversion is convoluted and unless a more robust process for conversion is introduced once new leasehold flats are banned, existing leasehold blocks may perform worse than newer commonhold blocks as there may be a stigma. Conversely the public may be cautious of commonhold, and the inverse may occur. There is no guarantee commonhold will be accepted by the public and there is a risk of creating a two-tier market.

Lenders are required to give their consent for leasehold to commonhold conversion. Lenders will therefore need to consider the implications of consent if changes are made to the current process (particularly if there is evidence of the emergence of a two-tier market), and ensure they are appropriately resourced with the relevant knowledge to process requests.

Whilst service charges will continue to be due in the form of commonhold contributions, forfeiture of the lease is no longer a deterrent to non-payment. Current provisions for debt recovery are limited and would likely require a lengthy and costly court process to recover the debt if the basic steps (such as charging interest) are ineffective.

The Law Commission has indicated that CAs should be able to apply to the court for an expedited order to sell a unit if bills are unpaid. The White Paper proposes that a lender would be notified once the debt has crossed a currently unspecified level, allowing them to 'step in' to potentially avoid possession proceedings and add the costs onto the outstanding loan. This will require additional legislation to be passed before this proposal can be implemented.

Public liability insurance is recommended by The Law Commission as essential to protect the CA from insolvency. If this is not mandated by legislation, unprotected blocks may

suffer limited mortgagability as lenders may choose not to lend where there is no insolvency protection.

Blocks and estates will still be subject to deterioration however if there is a lack of professional involvement within the CA, residents may not have the skills or awareness to commission appropriate maintenance nor seek out the most appropriate contractors to carry out works.

As there will no longer be a landlord and tenant relationship, Landlord and Tenant Act 1985 S.20 notices for major works will not be applicable for raising funds for repairs. CAs will instead be able to take out loans either as a fixed charge using some or all the building as collateral, or a floating charge against future payments made by unit holders however this will need to be managed by the CA and may be beyond the capability of non-professional directors.

There may be challenges in finding suitable CA directors in smaller blocks and it could be expensive to appoint a third party. The costs of third-party directorship would be reflected in the commonhold contributions which could affect saleability if they are high.

The removal of leasehold tenure will not guarantee lower financial contributions. Whilst it will give owners greater control over the block and the CA may be able to appoint contractors or pay for works deemed more financially palatable than previously, this comes with a greater liability to comply with what can be complex legislative obligations. The CA will be the principle accountable person under the Building Safety Act 2022 - if they fail to meet their obligations saleability and mortgageability may be impacted and legal action can be taken against the CA and potentially individuals within it. It is possible that upcoming legislation will mandate professional involvement for higher-risk blocks in mitigation.

Conclusion

The Government's White Paper has made its position clear – commonhold is due to replace leasehold as the default tenure for interdependent properties.

Whilst this may improve public perception of flats and provide occupants with greater control over management, there are risks associated with this change including that of creating a two-tier market and the complexity in converting existing leaseholds into commonholds.

The detail of the associated upcoming legislation is paramount in providing further clarity to the key issues currently associated with commonhold tenure. This is expected later in 2025.

Resources

[Commonhold White Paper](#)

[Commonhold and Leasehold Reform Act 2002](#)

[Law Commission Commonhold Summary](#)

[Law Commission Commonhold Review](#)

[HMLR House Price Statistics](#)

[Propertymark Commentary](#)

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