

The Investor's Guide to Leasehold and Freehold Property



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So you are a property investor thinking of investing in property in the UK?

Then, alongside some of the other differences in rules on purchasing property, you may have come across the terms 'leasehold' and 'freehold'. If you are not sure what they mean, this guide will explain each of these terms, as well as the advantages and disadvantages of each.

What Does Freehold Mean?

Freehold means that you are the **sole owner of a property**.

Houses or buildings: Freehold ownership means that you own the entirety of the building and, usually, the land it stands on.

Apartments: If you own the freehold for an apartment, then this will only include the 'internal' parts relating to your ownership; the common parts (such as the entrance, gardens, grounds, stairs and lifts, roof, loft and cellars) will be shared between all other apartment owners in a block.

If you own the freehold on a property, you can own it for as long as you wish and then hand it down to friends or relatives who may inherit the property in the future, without interference.

The property will appear in your name on the land registry and this will be a major selling point in the future when you can transfer it to others.

Most *houses* in the UK are sold as freehold, unlike *apartments and flats* which are normally sold with short or long leasehold agreements.



Advantages of Freehold

- You will not be asked to pay ground rent.
- You have full control on the maintaining of the property
- You won't be required by a landlord to contribute to potentially costly building repairs, maintenance and service charges
- Sales with freehold are generally less complicated and involve less paperwork than complex leasehold agreements that may contain hidden restrictions.

Disadvantages of Freehold

- You will have full responsibility for maintenance of the property and any repairs
- It may take up more of your time to manage a freehold property
- If repairs are expensive, then these will need to be paid for out of your own pocket rather than with the help of property occupiers
- Buying the freehold on a leasehold property can be expensive.





What Does Leasehold Mean?

Leasehold means that you own a lease on a property rather than own the property outright. A lease is, in effect, a licence which permits you to use the building for a period of time. Like renting a property, you will need to follow certain rules and make regular payments to a landlord.

These payments are often called ground rents; they may also include service charges, depending on how a building is managed.

Investing in a leasehold property typically means that you are buying a lease which may last from 90 years to 999 years.

Some properties are sold with leases far shorter than this, so it is worth checking how long your lease is before buying, for two very important reasons:

1. The longer your lease, the more valuable your property is
2. If you want your children to inherit your property, then it is much better to own a lease which lasts for several hundred years.

Before purchasing a leasehold property, it is also important to check the conditions of the lease carefully.

Service charges can increase significantly over time on some leasehold properties and contributions to 'sinking funds' (funds to cover repairs and maintenance) can become points of conflict between landlords and residents.

If you own a leasehold apartment in a block, then the leaseholders may claim their rights to manage (RTM). This means they will take responsibility for the building management and appoint directors to oversee activities. In this instance, all the leaseholders (usually, but not always) automatically belong to the management company which is responsible for the building. Any important decisions concerning the building as a whole, contribution to 'sinking funds' and service charges will be decided by a vote among residents rather than by a separate external management company or landlord which may not have the same interests in the residents. However, ownership of the property will still remain with the original owner or landlord.



Advantages of Leasehold

- You can often share responsibility for maintenance and costs of repairs
- Insurance and responsibility for the building ultimately falls upon the landlord
- Leasehold properties are typically part of a larger block of properties where day-to-day management is taken care of. This can save time.

Disadvantages of Leasehold

- You never fully own the property or have full control over it
- There are many restrictions on your lease and rules likely to be set about pet ownership in the building, smoking and so on.
- You may have little to no control of costs such as service charges and ground rents
- Short leasehold properties are worth less than equivalent freehold properties
- Short leasehold properties will, ultimately, be handed back to the landowner when the lease expires.





Freehold or Leasehold – Which Is Better for Investors?

From an investment point of view, a lot depends on the length of your lease. The longer the lease, the more the property will be worth.

For example, if Mr Jones puts his apartment up for sale with a 50-year lease and Mrs Smith puts her identical apartment for sale with a 99-year lease. Mr Jones will only sell his apartment for 70% of the value Mrs Smith will get on her sale.

Longer-term leases, such as the popular 999-year leasehold period, will see little difference in resale value in the foreseeable future - for example, the price for which you could sell next year will be very similar to the price if you sold in 20 years (disregarding inflation, etc). In theory there will be a problem for your distant ancestors in the next millennium but there will be little to be concerned about in your lifetime.

From an investment point of view, blocks of apartments in the UK will generally have some form of leasehold agreement attached to them so, aside from future value, it is always worth checking restrictions on what you can and cannot do without the permission of the landlord.

As long as you look carefully at the costs, responsibilities and obligations involved with your leasehold and include them in your return-on-investment calculations, there is no reason not to consider a leasehold property — unless the costs of ownership outweigh your returns.

Extending Your Lease

It is sometimes possible to extend your lease, even at the point of sale. However, this can be expensive and requires legal advice from an expert in this area.

Buying the Freehold on Your Leasehold Property

If you think that freehold sounds better than leasehold, you *may* have the right to purchase the freehold. This is known as 'enfranchisement'. Again, specialist legal advice is required to explore your options in this area.



Summary

The differences between leasehold and freehold will affect your likely future return-on-investment. It is important, therefore, to consider how purchasing freehold or leasehold fits with your current investment strategy:

- A leasehold property is by its nature a diminishing asset; but the longer your lease is, the more value it will hold in the longer term.
- If you are an investor who likes to be in full control of your assets, then freehold can often be the better option.





Contact Us

The good news is that the Colordarcy Team are all experienced property investors who have built up their own property portfolios from scratch. We are 100% certain that you will gain valuable information and advice from our team and, as such, you will be in a stronger position to make an informed choice.

We look forward to hearing from you and would like to take this opportunity to welcome you to the Colordarcy family.

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