

BRODIES LLP

WRITTEN SUBMISSION

We welcome the opportunity to respond to the Call for Views on the Housing (Scotland) Bill. We do not have comments to make on the Bill as currently drafted but would suggest that the opportunity should be taken to revisit the 20 year restriction on leases of dwelling houses which currently applies in Scotland.

We appreciate that others before us have petitioned for the removal of student accommodation from the properties affected by the 20 year lease restriction but felt compelled to raise the issue once more. With the welcome upturn in the property market and the increased demand for student accommodation, we are increasingly finding that the 20 year restriction on leases of residential property is causing difficulties in connection with the investment in and funding of such accommodation.

The Private Rented Housing (Scotland) Act 2011 provided the Scottish Ministers with the power to prescribe other bodies or types of body who would be free to enter a lease of residential property for more than 20 years. We would suggest that, when the Ministers consider the terms of the Housing (Scotland) Bill, they should at the same time exercise the power provided by the 2011 Act and remove providers of student accommodation from the 20 year restriction.

Background

Section 8 of the Land Tenure Reform (Scotland) Act 1974 restricts the length of any lease of property used as a private dwelling house to 20 years. Section 138 of the Housing (Scotland) Act 2010 removed the 20 year restriction for leases granted after 1 March 2011 to social landlords, bodies connected to social landlords, rural housing bodies and to lessees who are “a body prescribed, or of a type prescribed, by the Scottish Ministers by order made by statutory instrument.”

Should student accommodation be treated as private dwelling houses?

We have canvassed some opinions and the consensus has been that, whilst it may not have been the intention of the legislators, certain types of student accommodation are affected by Section 8 of the 1974 Act.

Student accommodation comes in different forms. In the case of buildings with a number of rooms which share kitchen, bath and living facilities, we would strongly

argue that such buildings should be treated as institutions and should not be treated as residential dwelling houses. However, there is no definitive commentary or guidance to say that this should be the case for the purposes of the 1974 Act.

It is harder to argue that buildings containing self-contained student apartments / bedsits should not be treated as buildings containing residential dwelling houses. Indeed, for VAT purposes, HMRC confirms in their VAT Information Sheet 02/14, that 'cluster flats' which have their own front door and en suite facilities but share kitchen and living facilities will be treated as dwellings.

The potential for the restriction in the 1974 Act to apply is therefore clear and therein lies the problem for long term investment in such an asset class.

Funding the development of student accommodation

There are several transactional structures for the development, funding and leasing of student accommodation. One example would be where a developer constructs student accommodation and then leases it on a long lease to a university which will enter short term letting arrangements with the students. Another would be where the university grants a long lease to the developer, the developer then constructs the accommodation and either undertakes the management of the short term lettings itself or, employs another company to do so.

Whatever transactional structure is chosen, the common denominator in most is the long lease which is an asset which can be sold for investment purposes. The long lease is employed to ensure that control over the use and maintenance of the property is retained and the investment is protected. It is also favoured by the student accommodation operators such as the university or the developer referred to in the examples above.

The basic funding model for investment in student accommodation will involve a lender providing the funding for the lease of the building as a whole in return for a standard security over that lease. For it to be possible to grant such a standard security over a lease, the lease must last for at least 20 years and one day (a "long lease"). In terms of Section 8 of the 1974 Act, there is an implied condition that no part of a property subject to a long lease may be used as a private dwelling house.

The effect of breaching Section 8 of the Land Tenure (Reform) (Scotland) Act 1974

Section 9 of the 1974 Act provides that if the condition prohibiting the use of the property or part as a private dwelling-house is breached (the condition implied by Section 8), the lease will not become void or unenforceable. However, the landlord is then entitled to serve notice asking the tenant to cease the use of the property for residential purposes. If the tenant fails to do so, the landlord may take action to remove the tenant. If during that action it is proved that the landlord approved of the residential use, the court will limit the remaining term of the lease to 20 years or the remainder, whatever is the shorter.

Notwithstanding Sections 8 and 9 of the 1974 Act, long leases of student accommodation most certainly have been granted. However, various agreements such as purchase options and buy backs are often entered into between parties to mitigate the effects of the 1974 Act. None of these additional agreements is entirely satisfactory as they are binding on the parties to them and are not binding on successors. This leaves tenants exposed in situations where the property is sold by the original landlord to a third party who is not party to the agreements which were put in place to protect a tenant from the effects of the 1974 Act.

The threat of Section 9 of the 1974 Act being invoked by a landlord, such as the university or the developer mentioned in the examples above or, more likely, a successor purchaser of the university or the developer, is a threat which makes long term investment in student accommodation less attractive and more complicated than it need be. This in turn can also severely limit the ability to invest capital in the development of the necessary infrastructure at a point when such investment is so badly needed.

Conclusion

Student accommodation is a popular and in demand form of investment across the UK. The Scottish Government has expressed its desire to lift barriers on residential leasing in order to make this a more attractive option and encourage institutional and larger-scale investment. In the interests of removing one such barrier, we would urge the Scottish Ministers to exercise their power under Section 8 3(A)(d) and prescribe student accommodation providers as bodies which will be permitted to take long leases of accommodation to be occupied by students. Should the Ministers decide to proceed with the necessary statutory instrument, we would be happy to assist and

share our experience of advising clients in connection with the developing, funding and leasing of student accommodation.

Brodies LLP
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