McCarthy & Stone

Ground rents

And their role in creating retirement communities

On 21 December 2017, the Government announced that it was considering removing ground rents on all future new-build properties.

Since the announcement, companies building c.90% of owner-occupied retirement developments in England have requested an exemption from this change to recognise the fact that retirement communities do not use ground rents in the same way as mainstream housebuilders. We use them to help fund the **construction costs** of the large shared spaces that are integral to our developments. Without this additional income, we could not afford to provide these communal areas.

In October 2018, we were pleased that the Government proposed that the retirement communities sector would be granted an exemption to these changes. This briefing note explains why fair and stable ground rents are so important to our sector.

Our ground rent terms*

- Average £466 per year
- On fair and stable terms
- Fixed for 15 years, longer than the average stay of our homeowners
- Increases linked to inflation or two per cent per annum if higher, and compounded yearly
- McCarthy & Stone remains as the landlord

We support Government reforms on unfair and aggressive leasehold practices

We believe aggressive ground rent practices should be stopped. However, retirement developers have been caught up in these proposed reforms unintentionally. This is because Government's main aim is stopping the sale of leasehold houses, which we do not build, and banning aggressive ground rent terms, such as those which double every few years, which ours do not.

How ground rents help pay for the construction of shared areas in our retirement communities

Shared areas in retirement communities account for

c.30%

of total floorspace, much more than mainstream flats

Shared spaces include communal lounges, restaurants, mobility scooter rooms, well-being suites, guest suites and staff accommodation.

These areas are essential to the lifestyle that retirement communities provides and are the equivalent of 3-8 otherwise sellable apartments.

c.£1 million

– the **cost of building shared areas** in **Retirement Living** developments

c.£2 million

– the **cost of building shared areas in Extra Care** developments (Retirement Living Plus)

We therefore use ground rents differently to mainstream housebuilders as **they underpin the viability of retirement developments**. Ground rents are not a windfall profit for us but an essential part of development viability as they help pay for the construction of these shared areas.

* Further information is available in the frequently asked questions section on our website, www.mccarthyandstone.co.uk/faq

Retaining all management and landlord responsibilities

Our fair and stable ground rents provide a one-off contribution of c.£600,000 on average per development. This is because the right to receive the ground rent is sold to investors when a development opens.

Importantly, while we sell the freehold to an investor, we retain the head lease in all managed developments, and therefore remain as the landlord, unlike in mainstream housing.

- Accordingly, **all management responsibilities stay with McCarthy & Stone**.
- This means the freeholder has no contact with our homeowners and **cannot change any of the terms of the lease**. All they have is the right to receive the ground rent.

What would happen without ground rents

Removing ground rent income from retirement communities will hit the sector hard. The proposed reforms in December 2017 had an immediate impact on our business and reduced our ability to compete for new land. Without this income stream, we are not able to buy as many sites as we would like at a time when the sector should be expanding quickly to meet increasing demand. This will limit the growth plans of the industry. In FY18 we exchanged on 54 new sites, compared to 75 in FY17 due to this uncertainty.

We believe there is a strong case for retirement communities to be exempt from the proposed reforms and to continue to charge fair and stable ground rents. We remain engaged in discussions with Government and will respond in full to their latest consultation.

Offering consumers a choice

As part of the exemption, the Government is proposing to provide older people with a choice of how to pay for their retirement property. Purchasers will be provided with a choice of either paying a higher sale price at a ground rent of £10 per annum or a lower sale price with a specified economic ground rent. This will be subject to various controls, including full explanations, no charges, independent legal advice and a complaint or redress mechanism. We are happy to agree to this proposal as it puts the consumer in full control of how they wish to pay.

The alternatives to ground rents are not in the consumers' interests

Why can't you increase your sale prices?

We would need to raise prices by c.£15,000 to c.£18,000 per apartment to cover the costs of building the communal areas without ground rents. This would severely impact affordability for our customers and result in the cost of our products being out of kilter with other properties, thereby significantly reducing our market. Our customers would rather pay a small yearly charge in ground rent, rather than a much larger cash payment up front.

83%

of over 65s would rather pay a ground rent of c.£500 a year to a higher purchase price of c.£15,000 to c.£18,000

(Populus survey, 2018)

Why can't you add the lost income to your service charge?

Ground rents are not the same as service charges. Service charges cover the day-to-day costs of **management and maintenance** within our developments, such as the heating and cleaning of communal areas, buildings insurance and redecoration. They are tightly regulated by national legislation and must relate to the management services provided within the development, not the building costs.

Why can't you charge an exit fee?

Some other retirement village operators charge customers large exit fees, sometimes worth up to 30% of the property's value. This helps pay for the building of their communal areas. We do not think this is in the consumers' interests, as customers could end up paying much more overall.

This note provides a summary of our position.

For further information, please contact:

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