Setting service charges and maximising income

Jackie Dickins

Programme for the day

- Definition of a service charge
- Fixed v variable
- Pooled/de-pooled
- What service costs can be re-charged to leaseholders
- What service costs can be re-charged to tenants
- Elements in some detail – leaseholders
    - Management fees
    - Major works management fees
    - Sinking/reserve funds
    - Costs of improvement
- Managing agents

Programme for the day ...(cont'd)

- What costs cannot be re-charged as a service charge
- Effective service charge accounting
- Payability
- Major works costs

Service charges

- A landlord who provides a service for the benefit of tenants, and in doing so incurs reasonable expenses, should be entitled to recover those expenses from the tenant

  OR

- The service charge is designed to allow the landlord to collect funds for the payment of those services the landlord must provide to the lessee in the lease

Day-to-day services – service charges

Definition in respect of leaseholders and for tenants paying a <u>variable</u> service charge

- 'Service charge' [s18 LTA85] means an amount payable by a tenant of a dwelling as part of or in addition to the rent:
  - Which is payable, directly or indirectly, for services, repairs, maintenance, improvements or insurance or the landlord's costs of management, and
  - The whole or part of which varies or **may** vary according to the relevant costs
- The relevant costs are the costs or estimated costs incurred or to be incurred by or on behalf of the landlord in connection with the matters for which the service charge is payable:
  - 'Costs' **includes** overheads

Day-to-day services – service charges ...(cont'd)

- Relevant costs shall be taken into account in determining the amount of a service charge payable for a period:
  - Only to the extent that they are **reasonably** incurred, and
  - Where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a **reasonable standard**
- And the amount payable shall be limited accordingly
- Where a service charge is payable before the relevant costs are incurred, no greater amount than is **reasonable** is payable, and after the relevant costs have been incurred any necessary adjustment shall be made by repayment, reduction or subsequent charges or otherwise

Pooling/de-pooling the costs of services

- Pooled – the costs of the services are included in the rent
- 1% reduction of rent over previous few years (ended 2019/20)
  - Recovery of costs reduced year on year
  - Insufficient income to meet cost of providing services
  - Other services suffered
  - Not maximising revenue
- Even though no reduction, pooled service costs still bring issues, new Rent Standard 04/20:
  - Still under recovering as you must 'endeavour' to limit to CPI + 1%.

Fixed v variable

- Variable – enables surplus's or deficits to be carried forward to the next accounting period
- S18 LTA 1985 – definition of variable. No definition exists for fixed
- Fixed
  - If over spent – tough! You can't recover overspend.
  - If under spent – don't have to give money back
- Why adopt variable?
  - Can recover charges in full even where (with net rent) this exceeds target rents
  - Landlords more willing and able to vary services
  - More involvement by tenants
- S20 consultation necessary where variable regime in place – for periodic tenancies, for qualifying long term agreements for services, not structural/fabric repairs

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Fixed v variable ...(cont'd)

- Leases usually provide for a variable service charge
- Tenancy agreements: Variable term will include:
  - Frequency of variation
  - Basis for calculating the s/c
  - Method of apportioning any variation
  - Method of dealing with surpluses and deficits

What are providers doing in light of this?

- Many, but not all introducing TA's with a variable s/c
- Most shifting to de-pooling of service costs.
  - Argument strengthened when presented with cost of under-recovery
- However, more still to do!
  - Are there limitations of the lease/TA?
- Requires a review of TA's

Varying the TA

- Varying TA's:
  - What circumstances – management requirements/demands of tenants for additional services or stopping some services
  - Consider/look to terms and conditions of TA – outlines how and if can be changed; TA is a legally binding contract
  - By Unilateral variation provision (UVP) in the TA
  - Is there a mechanism to vary the services provided
  - Is there a mechanism for changing the service charge
    - If variable this will/should be included
  - Secure tenancies – HA '85 S102 and 103: Consultation and notice of variation, does not require consent
  - Assured tenancies – by agreement of both parties – note changes in writing and evidence by variation agreement

One final alert

- Consider Curo Places Ltd v Pimlett (UKUT) 2019
  - Weekly assured tenancy
  - TA did not include grounds maintenance (GM) in list of services that L/L provides
  - Service charge did not include an amount for GM
  - L/L provided GM
  - Decision:
    - Just because TA did not mention it could not say it was an additional service as it was a service that was provided
    - Can't be an 'extra' service if delivered for years
    - Cannot therefore rely on the UVP, and even if could use it to introduce the service the TA did not say the L/L was required to provide the service
    - Remember – for service charge provisions to be enforceable there must be an obligation to provide the service – S19 LTA '85

Introducing a service charge for service you are already providing

Local Authorities and Registered Providers:

- Check your Tenancy Agreement – have you included the service in the list of services provided?
- If yes, you can simply add the charge
- If no, you will need to add to the list of services i.e. vary the tenancy

Introducing a service charge for service you are already providing
...(cont'd)

Local Authorities:

- Statutory Variation Powers – S103 Housing Act 1985
  - LA serves notice informing tenant of the intention to vary the tenancy
  - Specifies the proposed variation and it's effect
  - Invites tenants to comment on proposal within 'reasonable' period of time
- Having considered the responses, LA is able to serve Notice of Variation specifying:
  - The variation
  - The date on which it take effect.

Introducing a service charge for service you are already providing ...(cont'd)

Registered Providers:

- Is there a contractual ability to vary the services? –UVP
- Peabody Trust v Reeves [2008] EWHC 1999 – UVP deemed unfair terms (Consumer Contracts Regulations).
- This will depend on the specific wording of your Tenancy Agreement, examples where it may be possible include:
  - a stock transfer association may have made promises at the time of transfer such as 'no service charges introduced for 10 years', after 10 years a charge can be introduced
  - and a service that had previously been funded by an alternative source (such as supporting people), then a charge may be able to be introduced if the options are stop providing the service or introduce the charge

Introducing a service charge for a new service

Local Authorities: follow Section 103 procedure

Registered Providers:

- Does your Tenancy Agreement contain a clause allowing you to vary the services?
- If yes, you will need to do a housing management consultation:
  - Write to the affected tenants advising what it is you are going to do and how much it will cost them
  - Give them an opportunity to provide feedback on what you are proposing
  - Introduce the charge

Introducing a service charge for a new service ...(cont'd)

- If no, then the only way the tenancy can be varied is if both parties agree (turkeys voting for Christmas?)
  - e.g. CCTV to combat a rise in ASB
  - Seeking to persuade the residents of the desirability of the new service
  - Explain costs (and eligibility for benefits)
  - Residents will need to sign an Addendum to vary the Tenancy Agreement
- What if you do not get 100% approval?
  - A housing management decision as to whether you introduce the service or not.

Depooling

- Mapping what services are provided where?
- How are services delivered?
- What level are services provided at?
- How much does it cost you to provide services?
- IT
- Financial modelling
- Developing policies, systems and procedures
- Consultation
- Resourcing and managing the process

Switching from fixed to variable and vice versa

Local Authorities follow the Section 103 procedure.

Registered Providers:

- Cannot be achieved without all of the tenants agreeing
- Variable to fixed can be difficult to sell
- Fixed to variable should be easier to achieve
- Potential to be running both systems concurrently

Varying Services
Wilcock v The Guinness Partnership Ltd [2019] UKUT 146 LC

- Mr W had an AST of a flat which provided in respect of the service charge:-
- *"be variable and reviewed annually when the net rent is reviewed. At that time the service charge may be increased or decreased. This will be done according to the costs incurred in the service charge period. Annually the Association will consult with tenants regarding the services provided"*
- The specified services were: Garden Maintenance, Lighting (Stairways), Landlords Lighting (External)
- Guinness charged for bulk refuse removal and Mr W challenged the charge to FTT

Varying Services
Wilcock v The Guinness Partnership Ltd [2019] UKUT 146 LC ...(cont'd)

- FTT held charge payable as tenancy agreement provided for a variable service charge and so Guinness "*entitled to charge for services in addition to those specified in the original tenancy agreement*"
- Appeal to UT limited to recovery of Bulk Refuse Removal
- The question was whether the provisions of the tenancy agreement permitted Guinness to charge for services other than those set out in the schedule
- UT held that conclusions of FTT were wrong, the service charge being 'variable' only referenced the amounts to be charged, it did not entitle Guinness to add to the services

What might be included in a service charge? – leaseholders

- Consider the lease – schedule
- LTA 1985/87
- Case law

And:

- The lease will specify what the service charge liability is and how it is apportioned. This could be as varied as ‘a reasonable percentage’ or a specified percentage
- The lessee has no obligation to pay anything other than what is provided for in the lease,therefore:
- Whatever the justification of the action, you cannot recover the costs unless the lease entitles you to do so.
- You can only successfully pursue a lessee for arrears of service charges if you have successfully cleared all of the ‘payability’ hurdles

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What is included in a service charge? – leaseholders

- Determined by lease– lease plan, definition of demised premises
- Provision of all equipment/services/ maintenance
- Costs of improvements – if lease allows
- Management fee
- Sinking/reserve fund – if lease allows
- 'Major works' costs, including professional fees
- 'Major works' management fees
- Managing agents fees/invoiced sums – to be discussed later

Not an exhaustive list – only if lease allows for recovery

What might be included in a service charge? – leaseholders

- Repairs and maintenance
- Cleaning
- Grounds maintenance
- Buildings Insurance
- Lift – contract/repairs
- Door entry systems – contract/repairs
- Security/car parking gates – contract/repairs
- TV aerials – contract/repairs
- Fire safety – including smoke detectors/extinguishers/dry risers
- Health and safety – inspections and resultant upgrades
- Refuse disposal – paladin hire

Not an exhaustive list

What might be included in a service charge? – leaseholders ...(cont'd)

- Surrounding estate (defined in the lease, not in tenancy agreements!)
  - Parking spaces/garages including locking posts, door frames
  - External communal areas, trees/lawns/walls/fences/paths/roadways/lighting

What can be included in a service charge – leaseholders only?

Repairs and maintenance

- To structure of the building
  - Of all walls and floors forming the external boundary of the dwelling
  - The foundations
  - Whole roof structure – including chimneys
  - Door and window frames in the external walls – Sheffield City Council v Oliver
  - Balconies
  - Walls/fences/gates to the building
  - To common parts
    - Staircases, passages, landings
    - Internal parts of the building including fixtures and fittings
    - Internal and external decoration

What can be included in a service charge- leaseholders only? ...(cont'd)

Repairs and maintenance

- Services to the building
  - Communal pipes/wiring/conduits supplying utilities
  - Communal tanks/cisterns
  - Rain water pipes/guttering/main drains
  - Refuse chutes

Service charges and leaseholders

But note:

- Can only charge for:
  - Areas that are the landlords responsibility under terms of the lease agreement, eg, common areas
  - Lease provides the leaseholder rights to benefit/use
  - Lease obligates leaseholder to make payment for the right/use
  - Improvements – if the lease allows
- There's **no** legal definition of 'common areas' but in England they usually mean all areas that the individual leaseholders do **not** own, ie, the structure, roof, guttering, water tanks, stairs, walkways, gardens, etc
  - What have you demised – common areas of challenge, ie, window frames, flat doors
  - What does lease say about contribution towards use of premises, eg, lifts,
  - Lease plan is important

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Service charges and leaseholders – interesting cases/determinations

- Retirement Lease HA v Schellerup [2020] UKUT 232 (LC)
  - Not allowed to recover notional costs of providing accommodation for a resident warden – 'costs foregone' e.g the rent they could have received/derived.
  - Lease terms – l/l can recover 'costs' e.g actual expenditure.

What is included in a service charge? – tenants

- Determined by the tenancy agreement – schedule attached
  - Possibly an estate plan?
- Provision of all mechanical and electrical equipment/services/ maintenance, eg, lifts/door entry
- Costs of improvements
- Administration fee – of administering services, and only on eligible (under HB/UC) service charges
- Provision of equipment/usage – formerly depreciation
- Managing agents fees/invoiced sums but not for maintenance of block- to be discussed later

Not an exhaustive list – only if schedule with tenancy agreement allows for recovery

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What might be included in a service charge? – tenants

- Cleaning
- Grounds maintenance
- Lift – contract/repairs
- Door entry systems – contract/repairs
- Security/car parking gates – contract/repairs
- TV aerials – contract/repairs
- Fire safety – including smoke detectors/extinguishers/dry risers
- Health and safety – inspections and resultant upgrades
- Refuse disposal – paladin hire
- Surrounding estate (defined in the lease, not in tenancy agreements!)
  - Parking spaces/garages including locking posts, door frames
  - External communal areas – trees/grass cutting

See handout

What can be re-charged to tenants

- Social tenants; what does the TA say/schedule – remember eligible and ineligible service charge costs
- Intermediate rent (assured shorthold tenancies) – above social rent up to 80% of market rent – S/c might or might not be included in rent
- Affordable rent – 80% of market rent inclusive of service charges
- Secure – rent officers may restrict s/c as a % of rent. Look what TA says?
- Supported – most service costs re-charged via the s/c except for personal services/care/emergency alarm systems, etc
- Market rent – assessed against local levels of rent. S/C is usually fixed within the rent
- Note: rent regime from 04/20 will limit rents (inclusive of service charges) to no more than CPI+ 1%

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Welfare Benefits – Ineligible/eligible service charge costs

- Housing benefit: Ineligible personal services, eg
  - Non communal daily living expenses e.g fuel
  - Personal services e.g. Cleaning of rooms/window cleaning
  - Hard wired emergency alarm systems

  And many more....

Welfare Benefits – Ineligible/eligible service charge costs ...(cont'd)

- Universal credit:
  - Tenant must have an obligation to pay for the service
  - Particular service must be deemed eligible
  - Encouraged not to use term 'intensive housing management'
  - Ineligible service costs:
    - Provision of recreational facilities in communal rooms – TV's, computers, TV licences, internet
    - Costs associated with leisure, eg, hairdresser

When considering charging, ask the questions?

1. Is the service eligible to be charged as a service charge?
2. Is the service eligible for HB/UC?

Estate service costs payable by freeholders /tenants of houses

- Estate service costs – policy may dictate that costs met by public purse i.e council tax
- Sales under RTB by LA's – therefore
  - no service charge payable by tenants and leaseholders of houses
  - No service charge payable by leaseholders for estate service costs
- S106 arrangements = no public purse revenue, usually !!
  - Tenants of houses/flats should meet costs via a service charge
  - Freeholders of houses should meet costs via an estate charge
    - Not a service charge
    - Transfer document = contractual requirement for payment
  - Leaseholders – estate service costs included in the service charges
- Stock transfer HA's/organisations
  - May have hybrid arrangements e.g some former RTB sales no requirement to pay (see main 2nd bullet above), and since transfer introduced a requirement to contribute.

Other elements in more detail

- Management fees
- Administration fees
- Major works admin fees
- Sinking / reserve funds
- Costs of improvement

Management fees v administration fees

- Tenancy agreements – may be silent/list to include it/reference
- Leases – can confuse/be silent – Nellie Hamilton v L B Of Brent
- Historical background to administration fee
  - Pre-owner occupied portfolio
  - Management and maintenance allowance in rent for back office/overheads
- Administration – to administer the service excluding overheads
- Management fee for leaseholders – all costs of management, including costs of managing the services

Management fees

- Usually only charged to leaseholders
- Management fees can be a contentious area
- Covers the offices, salaries, national insurance, pensions and staff training of the landlord. They also pay for everything else associated with running an office
- **No** statutory guidelines when it comes to what landlords can charge for their services – S19 LTA '85 – reasonable
- Fees charged should depend on not just the size and type of property but the range of services that the landlord is required to provide
- Percentage add-on – not favoured by RICS,ARHM, FtT
- Leaseholders can challenge the 'reasonableness' and payability of the fee (s27A LTA85) at a tribunal

Management fees – tribunal decisions

- City of Westminster v Mr Palley LON/00BK/LSC/2006/0383
  - Detailed presentation by CoW
  - Burden of proof upon Mr Palley to demonstrate why the fee was unreasonable
  - Considered functions of a large local authority versus that of a private managing agent
- Dominion Housing Association v various leaseholders LON/00AJ/LSC/20008/0015
  - Consideration of management charges of third party managing agents + those of the RP = Very high
  - Detailed presentation by RP
  - Contribution towards costs by RP
  - Considered what services RP provides

Fees for major works – leaseholders only

- Normal practice that along with the standard fees, additional fees will be charged for the handling of major works and long-term agreements, including the sending of the required consultation notices (s20 LTA85)
- % of costs not favoured – by RICS, ARHM, first tier tribunal
- Discrete exercises on specific projects – calculation should be straight forward

Sinking funds v depreciation (provision of equipment/usage)

- Sinking funds (replacement provision) – are a pool of money collected to build up sums for expenditure incurred only once or twice during the course of a lease as the building ages, such as replacing windows, roofs, lifts or central heating systems
- Depreciation – covering the cost of an asset by writing off its cost of provision over its estimated life
- Difference – depreciation is to collect for replacement of capital spent on equipment, sinking fund collects in advance to avoid large demands from leaseholders in any one year when equipment or fabric of the building is replaced
- In reality – same approach, same calculation, ie cost of installation divided by its estimated life
- Sinking v Reserve funds – terms have become interchangeable over the years – used to be SF for capital items and RF for non-capital items

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Sinking funds/reserve funds

- If the lease says the Lessor 'must' collect funds for future/long term costs then a fund must collected and held
- Standard HE(former Housing Corporation) leases include a provision, other leases vague:
  - 'To pay…costs…of any services incurred or to be incurred by the Lessor'
- Local authorities – some provide, some don't. Perceived as administratively cumbersome/difficult
- Advantages – equalises costs over a period of time
- Disadvantages – cumbersome to manage particularly RTB funds and require review
- Periodic review – materials/life cycles change

Sinking/reserve fund accounts

- The monies should be kept in a separate bank account and held on trust: S42 LTA 1987 if you are an 'agent' of the freeholder
- Social landlords not bound by S42 LTA 1987
- Placing the reserve fund in trust is also to avoid the consequences of an insolvent freeholder when the liquidator may try to seize the money if it is not clearly designated as such
- The freeholder or managing agent is not allowed to draw on the fund for any other purpose although if the lease allows it, the fund can be used on a temporary basis to finance the cost of routine services, thereby avoiding the need to borrow money

Improvements

- Tenants – yes unless associated with the fabric and structure of the building – then not recoverable (S11 LTA'85 – in with the rent)
- Tenants – for mechanical/electrical and other costs associated with chargeable services, then they are recoverable – usually as a depreciated sum
- Leaseholders - What does the lease say about recoverability?
  - There must be an express term/clause: 'to improve', 'improvements'

Improvements ...(cont'd)

- Improvement v repair?
  - Some case law
  - No definition
  - Replacement with current day materials
  - To provide a facility/feature that did not exist previously
  - Must be able to demonstrate cost saving over the life of improved replacement
- Subject to S20 where applicable
- If unsure – ask the FTT to decide

Repair v Improvement ...(cont'd)

- *"Is the repair so radical and extravagant as to amount to creating a new thing in place of what was there and not a mere replacement"*
- The replacement of a door or window which complies with modern materials and with current standards; and also complies with Fire Regulations/buildings insurance requirements would not constitute an improvement

Apportioning costs of services

Common methods of apportionment

- Fixed percentage for each property
- ‘Fair proportion’ or ‘reasonable proportion’
- Floor space – not advisable
- Local authorities – usually equal split or by rateable value

<u>Changing apportionment calculation?</u>

- With consent of each tenant
- Application to court (if cannot reach agreement)

Apportionment of costs

- Check what the Lease/TA says
- What benefits/use of facilities? – might require different schedules to reflect this
- Mixed tenure blocks – be consistent
- Cannot change the apportionment calculation unless the Lease allows this

"Even if it is fair and reasonable to do so"

Kelsall v London Borough of Islington (2006)

Working with managing agents

Working with managing agents/ management companies

- Working with managing agents:
  - Different financial years; cumbersome to manage, requires accruals/prepayments, however HE S/O lease states:

'Definition of account year as 'means a year ending on [31 March]'

  - Preferred wording

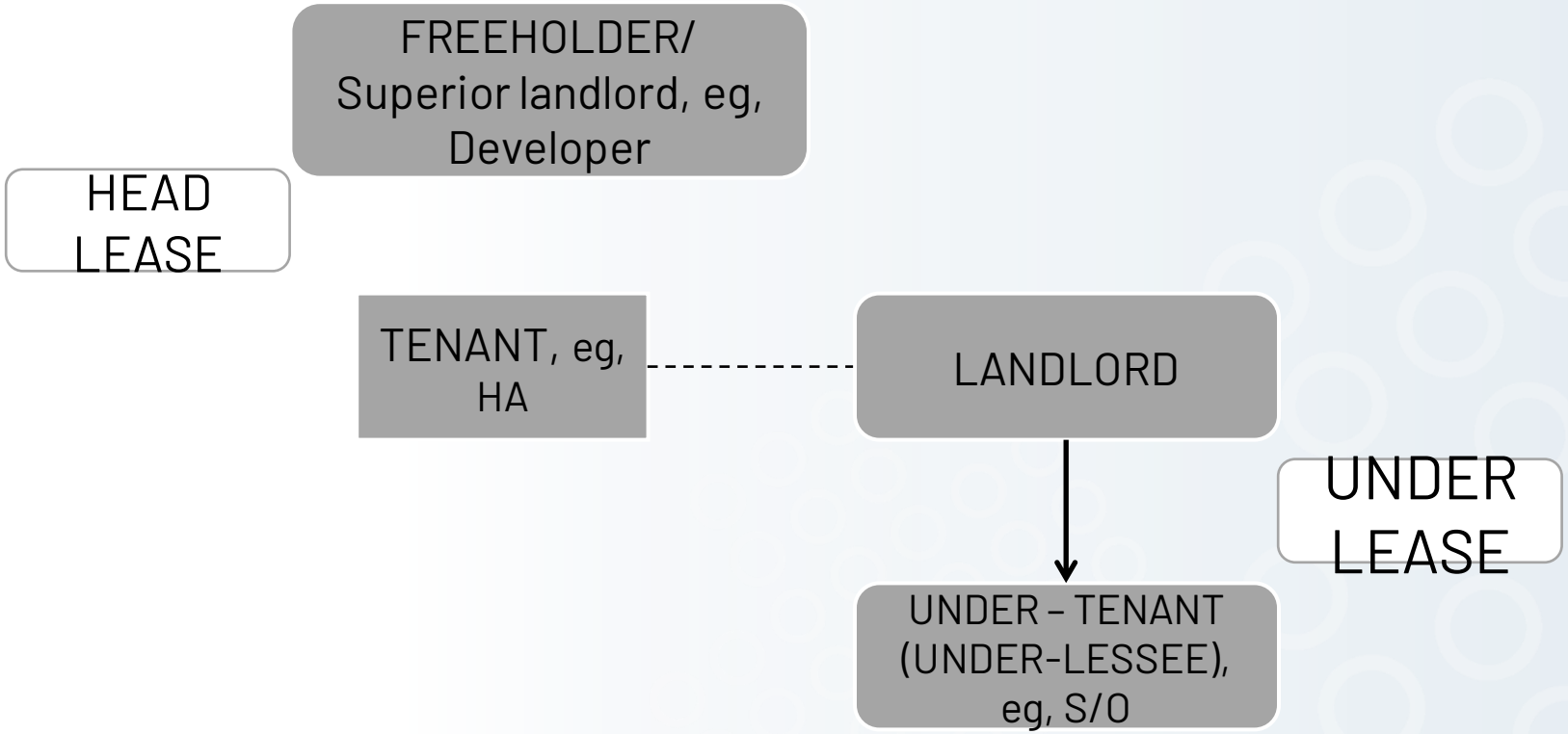
'means 1 April in each year of the Term or such other date or dates in each year of the Term as we may by written notice to you, stipulate'

Working with managing agents/ management companies ...(cont'd)

- High management fees: So what impact does this have on the fee you charge? – remember Dominion HA case
- Little accountability
- Bias against social tenants
- Differing level/access of/to services, eg, separate entrances, use of gym/swimming pool!

- Important to understand what the provisions of the head lease contain
  - Who is responsible for what?
  - Avoid duplication

S106 arrangements – typical structure



Managing the managers – private managing agents

- Usually mixed tenure (tenants and shared owners)
- Housing providers' required to make payment of service charge under terms of head lease
- Housing provider is the (head) leaseholder
- Housing provider has same rights of challenge of service charge costs as under-lessees
- Necessary to establish working relations with managing agent
- Board membership until shared owners own 100%
  - Tempting to retain some control but think of the consequences!

Non-rechargeable services

Items that are not service charges

- For assured and secure tenants and other periodic tenancies(leases less than seven years):
  - Repairs and maintenance – S11 LTA 1985, net rent
  - Building insurance
- For all tenures:
  - White goods to individual properties –gifted or included in sale

Items that are not service charges – leaseholders

Administration charges

- The consideration and granting of **approvals** for structural alterations, sub-letting or selling
- **Late service charge payment**
- Providing information, eg pre-contract enquiries during sales
- Charges that may arise from a breach or alleged breach of covenant
- Supply and/or administration of a deed of covenant
- Providing certified copies of a share certificate or a member certificate
- A breach (or alleged) breach of the lease terms

Items that are not service charges – leaseholders ...(cont'd)

Remortgage notice of charge.

- Remortgage notice of charge (receipting only)
- All of the above can be challenged at the FTT who can also vary a lease to deal with charges or unreasonable formulas and therefore preventing future disputes arising on the same issues

Can be re-charged to leaseholders as an administration fee – remember to include S158 Notice with invoice

Ground rent – leaseholders only

- Leaseholder only liable to pay when receives:
  - Formal demand – S166 CLRA 2002
  - In writing
  - ‘Notes for leaseholder’
  - 30/60 days time scale – date for payment given in the notice cannot be earlier than 30 days from the date notice is given, and not more than 60 days after that date. And the date for payment cannot be earlier than the date set out in the lease itself
  - Period to which it relates
  - Name and address of landlord

Recovery of ground rent

- Determination of debt owed:
  - By admission
  - Small claims
- Ultimate sanction – forfeiture

Leasehold v freehold charges

- Leasehold = service charge
  - Lease specifies what is included
  - Landlord and Tenant Acts apply
  - FTT – jurisdiction
  - Covenant to pay continues on assignment
- Freehold = estate charge
  - Transfer document specifies what is included
  - Landlord and Tenant Acts do not apply
  - FTT – no jurisdiction
  - Covenant to pay continues on assignment – if solicitor is 'on the ball'!
- Enter into contract if no arrangements within transfer document

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Exercise – Setting a service charge

Effective service charge accounting

Day-to-day services – service charge

- **Setting service charge budgets (new developments):**
- Will require calculations in order to market scheme for sale/letting – six months before handover
  - Obtain copy of head lease/proposed underlease
  - Familiarise yourself with the location
  - Obtain copies of the proposed scheme layout to consider:
    - No. of units/who has benefit of what facilities?
    - Parking arrangements- space per unit, or first come first served?
    - Estate facilities: play areas/community rooms
    - Landscaped areas
    - Access roads: will they be adopted
  - Obtain copies of the proposed block design
  - Obtain a schedule of the proposed M&E installations

Day-to-day services – service charge ...(cont'd)

Setting service charge budgets(new developments) ...(cont'd):

- Attend or obtain copies of the meetings between the employers agent, the developer and your organisation:
  - Invite asset management and housing management representatives.
  - Design out the need for services or the cost of the service, eg, Landscaped areas. But:
  - Require robust M&E components and building materials with long life-span – reduces impact on asset management budget/reduces housing management problems/reduces call on reserve fund for leaseholders
  - Ensure fit for purpose
  - Designs/plans change
- As soon as the final block/scheme design and M&E considerations agreed

Day-to-day services – service charge ...(cont'd)

Setting service charge budgets (new developments) ...(cont'd):

- Obtain quotes for proposed services based on design/layout using plans:
  - Cleaning/gardening/windows – from existing contractors.
  - Existing similar size scheme and similar features – for electricity use
  - Employers agent to provide costs of and lifespan of M&E components to calculate reserve fund and to include other building components, eg, roof replacement/windows, etc
  - Contracts: A number of the M&E installations may be under contract. What does it cover? – servicing only, and repairs and emergencies. Contingency may be required
  - Consider additional features – refuse disposal, security

Day-to-day services – service charge ...(cont'd)

Setting service charge budgets(new developments) ...(cont'd):

- Create a mechanism for holding the values for calculating the service charge – usually an excel spreadsheet!!
  - Will hold a list of services – with accompanying values provided
  - Will identify which tenures benefit from what services for contribution purposes however although tenants do not contribute to building insurance or day to day repairs to the fabric of the building this does not mean that the cost is spread over the remaining units
  - Benefit means use of, eg, play areas/gardens/parking
  - You may end up with Schedules representing benefit of services
  - How do you want the costs to be split (within Schedules if they are in place)- equally/by no. of bedrooms/square meterage?
  - Be generous in your calculations

Day-to-day services – service charge ...(cont'd)

- See handout – example calculation.

Day-to-day services – service charge ...(cont'd)

Setting service charge budgets(new developments) ...(cont'd):

- Ensure that the lease/TA terms correspond to what you want to achieve:
  - Are the services identified in the lease/tenancy agreement explicit enough ?– no grey areas
  - Have you retained responsibility for repairs and maintenance(L/H) on, eg, window frames/flat front doors
  - What does it say about parking? – a common problem. Who is responsible for maintenance of the car parking space if the leaseholder has sole use?
  - The terms for how the property is used and the conduct should also be explicitly outlined/stated – assists with user/conduct management issues

Day-to-day services – service charge calculation ...(cont'd)

- Common problems for new developments:
  - Marketing process/advice to tenants/leaseholders
  - Lease demise, eg, balconies/use of facilities
  - Electricity – meters not catalogued, how will you apportion costs?
  - Parking – arrangements unclear
  - Water meters – accessibility, how to apportion costs
  - Is the design fit for purpose?

Day-to-day services – service charges

- Setting service charge budgets (pepper-potted, eg, RTB/A):
  - Prior to making offer
  - Consider proposed lease plan – boundaries, what services do you want the leaseholder to contribute towards- block services only? Or to include services for the estate?
  - Visit scheme
  - Use costs of existing owner-occupied flats in same block/development,- if the lease in question includes all of the costs you want to recover
  - If first sale in the block
    - Consider outturn costs for previous three years for all services – **NB**: some services may not be re-charged to tenants, eg, grounds maintenance; some may not be easy to obtain in the format required, eg, area-/borough-wide, not to block level
  - Apply lease apportionment – RV/no. of bedrooms/equal split/be consistent
- Sinking fund/depreciation calculation:
  - Technical services for lifecycle costs for all M&E
  - Regular review – materials change, therefore so does the lifecycle

Effective service charge management and accounting

- Getting it right from the outset:
  - Conflict of interests: sales/finance/development

or,

- For existing portfolio:
  - Capture-map lease/tenancy obligations and restrictions
- Agreeing roles and responsibilities:
  - Who monitors the service?
  - Who is responsible for the budget?
  - Is this the same person responsible for payment?
- Regular monitoring

Effective service charge management and accounting ...(cont'd)

- Purchase ledger arrangements;
  - Coding to
    - Estate
    - Block – remember Schedules
    - Unit
  - Codes for;
    - R&M to structure
    - R&M to M&E installations
    - Codes for each
- Responsibilities for placing/ordering repairs
  - Training – Why important?

Impact of sales process

- RTB/A
  - S125 offer notice – limits for first five years other than inflation
  - Lease – what does it say the landlord is responsible for and does it require payment from the lessee for those obligations?
  - Lease plan – dictates boundaries for charging purposes
- Second generation
  - Pre-sale enquiries
  - Public relations
  - Management issues
  - Affordability
- New first sales – marketing literature is key:
  - Consumer Protection Act (previously Property Misdescriptions Act)
  - Public relations
  - Management issues
  - Affordability
  - DLP policy and procedure

Impact of the letting process

- Calculating the cost of providing the service as accurately as possible
- Affordability
- Public relations
- Minimise complaints
- Transparency
- Management issues
- Equivalent lease plan

Difficulties with leases/existing management arrangements

- Different leases:
  - % contribution do not meet 100% of costs
  - Clauses inconsistent with tenancy conditions: different rights and obligations
  - Map out the key lease terms
  - Created at different times within same building/estate – different obligations/responsibilities
- Mixed tenure – S106 agreements, differing use of premises, eg, gym, play areas – 'poor doors'
- Conflict – lease v tenancy agreement, eg, pets
- Secure v assured tenancies – some services not allowable by rent officer as service charges
- What does the tenancy agreement schedule of services include?

Monitoring the service charge budget – leaseholders and tenants where a variable service charge applies

For it to work effectively:

- Clear contract arrangements for all services – accessible
- Quality standards are maintained
- Robust purchase ledger systems – also provides transparent audit trail if needed
- Regular review of spend v budget – variances visible: quarterly/six monthly

Simply put:

- Know what the costs of the services are: relies on a sound purchase ledger process in place
- Know where (what buildings/properties/estates) are receiving the service – who receives the service
- Know to what extent the service is being delivered
  - No. of hours, eg caretaking
  - Sq meterage – grounds maintenance
  - Contract arrangements – servicing only, includes R&M, emergency call-outs?
- Know that the service charge accounting system (Excel??) reflects all of the above, that the 'rules' correspond

Monitoring the service charge budget ...(cont'd)

- Scrutiny of communal repairs costs – common errors:
  - Repairs to tenants/leaseholder properties
  - Insurance claims
  - Incorrect building estate – miscoded
- Internal communication for:
  - Alert to breaches in service
  - Alert to exceptional spend

Monitoring the service charge budget – good practice where a variable service charge exists

- Communication with customer:
  - When there is a significant breach of service – prompt
  - Alert to significant variances when they take place explaining why –
    - Can be S20B equivalent
    - Future proof for when the consultation limits increase
- Good use of information technology (Ensemble/Qube?):
  - Records S125 limitations
  - Records lease apportionments for individual properties
  - Provides audit trail of costs incurred
  - Can easily retrieve supporting information – S22 requests
  - Can produce user friendly monitoring budgets for officers

Monitoring the service charge budget – good practice ...(cont'd)

- Can produce schedules of repairs for customers to accompany accounts
- Ownership is still an issue!
  - Who should monitor the budget?
    - Neighbourhood/estate /tenancy services officer
    - Home ownership officer
    - Asset management
    - Finance officer/manager

Payability

Payability

- Payable under-lease/TA?
- Apportionments:
  - Governed by terms of lease
- Typical lease:
  - Floor area
  - Rateable value
  - Fixed proportions
  - Duty to pay a ‘fair and proportion’ or words to that effect

Payability ...(cont'd)

- Demands for service charges:
  - Demanded in correct name and in accordance with lease dates
- S48 Landlord and Tenant Act 1987
  - No rent or service charge will be due unless the Landlord has served upon the Tenant a written notice giving an address in England and Wales at which notices can be served by the Tenant upon the Landlord
- S47 LTA '87
  - No service charge will be due unless the demand includes the name and address of the Landlord. And if the address is not in England and Wales to also provide an address in England and Wales where notices can be served upon the landlord

Payability ...(cont'd)

Section 21B Landlord and Tenant Act 1985

- The service charges (summary of Rights and Obligations, and Transition Provisions) England) Regulations 2007
  - Form of summary has been prescribed by statute
  - Printed or typewritten
  - No smaller than point 10 font
  - Applicable to Wales
- Failure to comply = tenant is not liable to pay service charge

Payability ...(cont'd)

S20B

- Demanded within 18 months of being incurred or
- Tenant notified in writing that costs have been incurred he will be required to contribute towards them
- Costs are incurred when become payable by landlord – OM V Burr May 2013
- Failure to comply = tenant is not liable to pay service charge

Payability – Section 20B Landlord and Tenant Act 1985 ...(cont'd)

(2) Subsection (1) **will not apply if**, within the period of 18 months, beginning with the date when the relevant costs were incurred, the **tenant was notified** in writing that the costs had been incurred and he would subsequently be required to pay

- Southwark V Woelke – what does your lease say about invoicing/billing for major works costs?

There is no prescribed S20B Notice, however...refer to LB Brent v Shulem B

Payability – limitation

- Limitation of service charges:
- No statutory time limit for a tenant to bring an action – Cain v Islington 2015 UT, might assist
- Landlord bringing an action:
  - Recovery of rent or 'service charge reserved as rent': six years from date when payment first becomes due
  - Service charge not reserved as rent: 12 years from date when payment first becomes due

NB. Fact that tenant has paid does not amount to admission S27 A(5) LTA'85,

Payability – reasonableness

- Reasonableness
- Common Law
  - Unclear
- Section 19 Landlord and Tenant 1985:
  - Payable to the extent that:
    - Reasonably incurred
    - Reasonable standard

Payability

- General principles of reasonableness:
  - Contemplated under lease does not make it automatically reasonable to incur costs – Garside v RFYC 2011 UT –affordability must be taken account of, and Waaler v Hounslow
  - Fact that it is reasonable to have a service does not automatically mean that the costs associated with the service will be reasonable
  - Doesn't have to be the cheapest but can't be grossly out of line with market norms
  - Would landlord have chosen method of repair if he was paying for repair himself

Notices of rights and obligations

- Service charges – S153 CLRA: (S21B LTA)
  - New format since July 13
  - No smaller than font size 10
  - Must be sent with all demands for payment
  - Tingdeng Holiday Parks Ltd v Cox 2011 UT
- Administration costs – S158, can now be challenged at first tier tribunal:
  - New format since July 13
  - No smaller than font size 10
  - Must be sent with all demands for payment
- Ground rent – S166, does not apply to shared owners:
  - Prescribed format

Failure to comply = tenant is not liable to pay

Scrutiny of costs

- S22 LTA 85 request:
  - Request within six months of receiving summary – in writing
  - Reasonable facilities to inspect, copy receipts/accounts
  - Or to be sent to tenant
  - Must be provided within one month of the request
  - No direct charge can be made for providing the information – additional costs to be included in management fee
  - Charge can be made for copying/being sent a copy

Section 27A Landlord and Tenant Act 1985

- FtT (PC) has jurisdiction to determine:
  - Who has to pay?
  - Who is to receive payment?
  - How much?
  - When is payment to be made?
  - How is it to be paid?
- Can be requested in **advance** of demands

First Tier Tribunal (Property Chamber) consideration

- When determining the above it can consider:
  - Test of reasonableness
  - Terms of the lease
  - Other statutory limitations
- This does not allow the FtT (Property Chamber) to change the dates for payment as set in the lease

No application can be made which

- The tenant has agreed or **admitted** (paying the demands is not admitting) S27A(5)
- Has, or will be **referred to Arbitration** following agreement after the dispute arose
- Has been decided by a **court**
- Has been **decided by Arbitration** mentioned above

FtT

- Consideration of cases:
  - Transferred from County Court
  - Hearing
  - Without a hearing (on papers)
  - Preliminary hearing
  - Fast track – (aim to deal ten weeks)
  - Standard track
  - Emergency hearings

Major works costs

Major works

- Legislative procedure – Section 20 consultation
- Other consultation – newsletters, website, surgeries prior to S20
- Tease out pre-determination applications
- Interim certificate payments – S20B notices
- Variations identified – further consultation required with leaseholders
- Final payments as soon as possible after practical completion
- Invoice – since Southwark v Woelke, in line with lease and as for other items of repair
- Use of resident liaison officers/satisfaction surveys
- Storage of associated documents/handover on staff changes
- Major works debt – offer repayment options

S20 consultation

- What is it about? Consultation with people who are required to meet the costs of the works via a variable service charge
- Why consult?
  - Put tenants on more equal footing
  - Section 20 Landlord and Tenant Act 1985
  - Significant reforms in the Commonhold and Reform Act 2002
- Objective of consultation – allowing tenants to comment on landlord's proposals for works and/or services

What are you consulting on?

- Qualifying works:
  - 'Works on a building or any other premises', the costs of which will be recovered from the tenant through the service charge bill
- Qualifying Long Term Agreements:
  - Agreement made on behalf of the landlord for a period of over 12 months – this applies equally to tenants with variable service charges, eg, cleaning/gardening

Cost threshold

- Qualifying works:
  - Relevant contribution of any tenant – more than £250
- Qualifying Long Term Agreements:
  - Relevant contribution of any tenant – more than £100 in any accounting period

More detailed information/copy Notices can be found at:
www.lease-advice.org

When do the regulations apply -Consultation – five sets

- Enter into a Qualifying long term agreements where no public notice is required.
  - Schedule 1
- Enter a QLTA, where public notice (now Find a Tender) is required, - Schedule 2
  1. Works more than £4+M
  2. Services more than £189KQualifying works under qualifying long term agreements
- Works carried out under a QLTA - Schedule 3
- Qualifying works not under a qualifying long term agreement:
  - Schedule 4 (1) – works for which a public notice is required
  - Schedule 4 (2) – works for which a public notice is not required

Any questions?