

COMMONHOLD AND LEASEHOLD REFORM ACT 2002

EXPLANATORY NOTES

COMMENTARY ON THE SECTIONS: PART 1

Absent Landlords

Chapter 5: Other provisions about leases

Service charges, administration charges etc.

Section 150: Extending meaning of service charge and management etc

246. *Section 150* gives effect to Schedule 9 which makes a number of changes to existing provisions relating to the management of, and service charges in respect of, leasehold properties. In short the changes apply the provisions to, or in relation to, improvements and, with the exception of loans to local authority or registered social landlord leaseholders, any other matters which may be specified by order. The changes are described in detail in the notes on Schedule 9 below.

Section 151: Consultation about service charges

247. *Section 151* substitutes two new sections (20 and 20ZA) for section 20 of the 1985 Act (which requires landlords to consult tenants before carrying out works to which a tenant is obliged to contribute through a service charge, and restricts their right to recover the cost if they fail to do so).

248. The new sections provide a power to prescribe, through regulations, the consultation requirements that landlords must comply with before carrying out any qualifying works or entering into a qualifying long term agreement. A qualifying long term agreement is an agreement entered into by or on behalf of the landlord or a superior landlord for a term of more than twelve months. The consultation requirements will apply where, in the case of works, the costs exceed a specified amount and, in the case of a long term agreement, the costs payable under the agreement as a whole or the costs incurred during a specified period exceed a specified amount. The specified amount, or period, will in each case, be set by regulations and may be set by reference to the amount which will be payable by any one or more tenants as service charges.

249. If landlords do not comply with the consultation requirements the amount that they will be able to recover will be limited to an amount specified in regulations. Landlords will be able to apply to a LVT for a determination to dispense with all or any of the prescribed consultation requirements. Regulations may provide that agreements which would otherwise be qualifying long term agreements may be exempt from the consultation requirements in prescribed circumstances or if they are agreements of a particular description.

Section 152: Statements of account

250. *Section 152* substitutes a new section for section 21 of the 1985 Act (which gives tenants the right to request a summary of the costs on which their service charge is based).
251. The new section 21 will instead require landlords to provide annual accounting statements. The statements will include information about monies paid into a service charge fund, or standing to the credit of the service charge fund, as well as costs incurred by the landlord. Statements will have to be certified by a qualified accountant, except where exempted by regulations. This is similar to the existing requirement to have summaries certified, except where they relate to a service charge paid by the tenants of four or fewer dwellings. Landlords will also have to provide leaseholders with a summary of their rights and obligations in relation to service charges.
252. The form and content of statements, accountants' certificates and summaries of rights and obligations will be prescribed by regulations. Different provision could be made for different cases - for example, special provision could be made for landlords of smaller properties. The regulations will be subject to annulment by either House.
253. Statements of account will have to be provided no later than six months after the end of an accounting period. The first accounting period will begin on the day on which the new section 152 comes into force or, if later, on the first day on which service charges become payable by a tenant under a lease of any of the dwellings. The landlord will choose the last day of the accounting period, subject to the requirement that no accounting period should be more than 12 months long. Subsequent accounting periods will be consecutive.
254. This section also introduces a new section 21A. This will allow tenants to withhold payments where landlords fail to provide documents which exactly or substantially meet the relevant requirements. The sum that they will be able to withhold will be equal to the sum standing to their credit at the beginning of the accounting period in question, plus any charges that they had paid during that particular accounting period. However, the right to withhold will not apply where a LVT determines that the landlord has a reasonable excuse for his failure. The right to withhold ceases once satisfactory documents are provided, even if these are provided after the relevant deadline.
255. In interpreting the new sections 21 and 21A, it should be noted that section 30 of the 1985 Act defines a "landlord" as including any person who has a right to enforce payment of a service charge.

Section 153: Notice to accompany demands for service charges

256. *Section 153* requires landlords to include with service charge demands a summary of leaseholders' rights and obligations in relation to service charges. It inserts a new section 21B into the 1985 Act. Subsection (2) of that new section provides a power to prescribe the form and content of such summaries by regulations.
257. Subsections (3) and (4) of the new section 21B give leaseholders a specific right to withhold payment of service charges if the required information is not provided.

Section 154: Inspection etc. of documents

258. *Section 154* substitutes a new section for section 22 of the 1985 Act (which allows tenants to inspect documentation which supports a summary of costs). The new section 22 will give tenants the right to inspect documentation relevant to their accounting statements within 21 days of their request. They will also be able to take copies of that information, or have copies provided to them, on payment of a reasonable fee. The right to inspect documents ends six months after they are provided with the corresponding statement of accounts or, if later, six months after the deadline for providing that statement.

Section 155: Liability to pay service charges: jurisdiction

259. *Subsection (1)* inserts new section 27A into the 1985 Act. *Subsection (1)* of the new section provides that landlords or tenants may apply to a LVT for a determination as to whether service charges are payable and, if they are payable, by whom they are payable, to whom they are payable, the amount which is payable, the date they are payable and the manner in which they are payable. *Subsection (2)* of the new section makes it clear that an application may be made even if a payment has already been made. *Subsection (3)* of the new section enables landlords or tenants to apply for such a determination before relevant costs are incurred.
260. *Subsection (4)* of the new section provides that an application cannot be made to a tribunal under this section if the matter in question has been agreed or admitted, if it has already been determined elsewhere, or if it is subject to a 'post-dispute arbitration agreement' (see below). *Subsection (5)* of the new section makes clear that a matter has not been agreed or admitted for these purposes by virtue of a person having paid all or part of the sum in question.
261. These provisions replace and extend the existing provisions under section 19(2A) to (3) of the 1985 Act (which enable LVTs to determine the reasonableness of service charges) which are repealed by Schedule 14. *Subsection (6)* of new section 27A now provides that arbitration agreements are void unless arbitration is agreed to after a particular dispute has arisen. Previously LVTs were unable to hear disputes where leases contained a section requiring the use of arbitration. *Subsection (7)* of that new section provides that this new jurisdiction for LVTs is in addition to any existing jurisdiction of the courts.
262. *Subsections (2) and (3)* of this section define 'post-dispute arbitration agreement' for the purposes of the 1985 Act.

Section 156: Service charge contributions to be held in separate account

263. *Section 156* amends the 1987 Act. It introduces a new section 42A which will require payees to hold service charge funds from separate groups of service charge payer in separate accounts. Payees are defined in section 42 of the 1987 Act as "the landlord or other person to whom any such charges are payable under the terms of their leases". Certain classes of landlord are exempt from section 42 – these exemptions also apply to new section 42A.
264. The new section 42A will also require payees to notify the relevant financial institution, in writing, that sums standing to the credit of a trust fund are to be (or are) held in it. Regulations under section 42A(2) and 42A(11) will prescribe the type of account in which service charge funds can be kept (for example, this might include an interest-bearing account) and the sort of financial institution that can be used (for example, these might include recognised banks and building societies). The regulations will be subject to annulment by either House. Section 42A(10) provides a power to make regulations exempting managers from the requirement to use separate bank accounts for separate groups of service charge payers.
265. Tenants will have the right to ask for proof that the relevant requirements have been complied with. Payees will have 21 days in which to provide such proof. In addition, tenants will be able to withhold service charges where they have reasonable grounds for believing that section 42A has not been complied with.
266. *Section 157* also inserts a new section 42B into the 1987 Act. This makes it an offence for any person to fail to comply with section 42A without reasonable excuse. On conviction, they would be liable to a fine not exceeding level 4 on the standard scale (currently £2,500).

Section 157: Service charges: minor and consequential amendments

267. *Section 158* gives effect to Schedule 10 to the Act, which makes a number of minor, consequential amendments. The changes are described in detail in the notes on Schedule 10 below.

Section 158: Administration charges

268. *Section 158* gives effect to Schedule 11. The changes are described in detail in the notes on Schedule 11 below.

Section 159: Charges under estate management schemes

269. *Section 159* provides that charges levied by landlords under estate management schemes shall be subject to a test of reasonableness to be determined by the LVT.
270. *Subsection (1)* defines the schemes that are covered by the section. They are schemes made under section 19 of the 1967 Act or under Chapter 4 or section 93 of the 1993 Act. *Subsection (2)* defines 'variable estate charge' and provides that a variable estate charge is only payable to the extent that it is reasonable.
271. *Subsection (3)* provides a right for any person subject to an estate charge to apply to a LVT for the variation of the estate management scheme. Such an application can be made on the grounds that either the estate charge specified in the scheme is unreasonable or that any formula for the calculation of estate charges is unreasonable. *Subsections (4) and (5)* provide that where a tribunal agrees that an estate charge is unreasonable, it can order the scheme to be changed accordingly.
272. *Subsection (6)* provides that an application may be made to a LVT for a determination whether or not an estate charge is payable and, if so, by whom it is payable, to whom it is payable, the amount which is payable, the date on which it is payable or the manner in which it is payable. *Subsection (8)* provides that the jurisdiction of the LVT in such matters is in addition to any jurisdiction of a court. *Subsection (9)* provides that no application may be made in respect of a matter which has been agreed or admitted by a leaseholder or which has been determined by a court or arbitral tribunal. *Subsection (10)* provides that payment of all or part of a charge does not constitute admitting or agreeing it. *Subsection (11)* provides that certain agreements providing for questions about estate charges to be determined in a particular manner are void.

Manager appointed by leasehold valuation tribunal

Section 160: Third parties with management responsibilities

273. *Section 160* corrects a defect in the appointment of a manager procedures under Part 2 of the 1987 Act. By virtue of the amendments made by this section leaseholders will be able to apply to a LVT for the appointment of a new manager where a lease provides for management functions to be carried out by a third party manager rather than the landlord. At present, leaseholders with such leases do not have the same rights as other leaseholders to apply for a new manager where the existing one is failing to manage the building properly. The grounds for appointment are extended by this section to cover acts or omissions by a third party manager as well as a landlord.

Section 161: Restriction of resident landlord exception

274. *Section 161* restricts the current exemption from the provisions of Part 2 of the 1987 Act for resident landlords in converted houses. The exemption will not apply if at least half of the flats in the building are held on long leases which are not business tenancies under Part 2 of the Landlord and Tenant Act 1954.