Devonshires solicitors

Leasehold Management Brief

Issue 2

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Welcome

Welcome to the second edition of the Leasehold Management Brief.

This time around, we look at the Landlord and Tenant Act 1954 and 'Business Tenancies', which many Registered Providers may have experience of with their commercial units or even, as we have been dealing with recently, their own head offices! We cover the new Service Charge Cap and detail the limited circumstances in which it will apply.

We also look at compensation for disrepair in leasehold properties, a problem not just limited to tenancies, both from the landlord's and the leaseholder's perspective. Finally, two Ask the Expert questions and answers, from questions we have recently received.

Service Charge Cap

Under the Social Landlords Mandatory Reduction of Service Charges (England) Directions 2014, made pursuant to sections 219 and 220 of the Housing Act 1996 which were issued on 12 August 2014, a cap is imposed on the amount of service charge a social landlord can recover from a lessee in respect of the costs of works of repair, maintenance or improvement. Crucially though, the mandatory cap will only apply to the costs of repairs, maintenance or improvement where the cost of those works are funded wholly or partly by a grant or other financial assistance of any kind from the Decent Homes Backlog Funding, Secretary of State or HCA. In circumstances where the costs are capped because the works carried out were funded in the way mentioned, the cap imposed is £15,000 for a dwelling in London and £10,000 where it is not situated in London for works carried out in any 5 year period.

The mandatory cap will only apply in limited circumstances where the landlord has received financial assistance for carrying out such works. Therefore, the majority of service charges will be unaffected by the cap.

In addition to the mandatory cap, the Social Landlords Discretionary Reduction of Service Charges (England) Directions 2014, also made pursuant to sections 219 and 220 of the Housing Act 1996, allows social landlords to waive or reduce the service charge in respect of works of repair, maintenance or improvement payable by a lessee by an amount the landlord considers to be reasonable. The Directions set out criteria that the landlord should have regard to when considering whether to waive or reduce the service charges.

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Breach of access used to refuse a new business tenancy under Landlord and Tenant Act 1954.

Although Registered Providers (RPs) are obviously concerned with providing and managing residential accommodation, there are occasions when they must deal with commercial premises. Many RPs have portfolios of commercial property and their own offices will be commercial property. In these situations an RP may well be involved in a statutory lease renewal process under the Landlord and Tenant Act 1954 (the Act). That Act provides statutory protection for the tenants, allowing the tenant to request a new lease at the expiry of their existing lease but also provides for certain circumstances in which the request for a new lease by a tenant can be refused. This was recently considered in the case of *Youssefi v Mussellwhite* [2014] EWCA 885.

On appeal it was held that for the purposes of s30(1)(a) the neglect to repair had to be substantial. This would be a matter of fact for the judge to decide. However, the Court of Appeal concluded that the tenants' obligations in *[Youssefi]* did not extend to keeping the vegetation under control. Therefore, the landlord could not refuse the grant of a new lease on that basis. Despite this, the Court of Appeal was satisfied that the failure of the tenant to provide access and the fact that the tenant was not using the premises in accordance with the user clauses in the lease satisfied the statutory grounds for refusing a new tenancy.

The tenant argued that the breaches had not prejudiced the landlord to the extent that a new lease should not be granted.

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In this case, the tenant had leased a property described as 'a dwelling house, shop and premises' from the landlord. On the lease's expiry, the tenant sought a new lease under the statutory provisions. The landlord opposed the granting of a new lease due to:

1. alleged failure to repair and maintain as they had allowed extensive creeper growth around the building (s30(1)(a));
2. persistent delays in the paying of rent (s30(1)(b)); and
3. other substantial breaches by the tenant including the tenant failing to allow access and not using the property in a way that complied with the permitted uses under the lease (s30(1)(c)).

Crucially though, the Court of Appeal held that in demonstrating that the landlord's interests were prejudiced the landlord did not have to demonstrate a quantifiable loss and allowed the landlord's basis for refusal.

The decisions highlight the implications of breaching the terms of a lease by a commercial tenant. If the landlord is seeking to object to the renewal of a lease by its commercial tenant, then the landlord should consider how the tenant has acted and whether there have been any breaches of the tenancy that would allow refusal of a new lease.

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Can leaseholders claim compensation if the landlord has delayed or failed to carry out repairs?

If a leaseholder reports a repair, for example a problem with the roof, then the landlord will need to consider if it is responsible for the repair works to the building or internal repairs to the leaseholder's property and how it will be paid for. This will be dependent on the terms of the lease. The lease will typically require the landlord to keep the common parts, structure and exterior in repair. If a freeholder is in breach of the repair obligations set out in the lease and as a result the leaseholder has suffered loss, then the leaseholder is entitled to compensation in the form of damages, as well as the leaseholder having to carry out the repair.

Unlike disrepair claims in respect of an assured or secure tenancy, which only allow the tenants to make claims as far back as 6 years from when their claim is issued at court, a leaseholder can claim as far back as 12 years. This is because the lease is made by deed and as such has a longer limitation period.

When deciding how much compensation a leaseholder will be awarded where a landlord has failed to carry out their repair obligations under the lease, the court will attempt to place the leaseholder in the position he would have been in if the landlord carried out the repairing covenants properly.

Unfortunately, the assessment of general damages in a disrepair case is far from an exact science. General damages (namely compensation for loss of enjoyment and use of the property) are notoriously difficult to quantify but each case will turn on its own specific facts and the surrounding circumstances. The variation of any one of a number of factors can have a dramatic effect on the quantum awarded.

In leasehold cases, the amount of compensation will be based on the notional open market rent obtainable for a private tenancy of the property although working out the notional market rent can itself lead to disputes between the parties. In addition to that figure, there may well be a 10% uplift in the compensation following the Court of Appeal decision of *Simmons v Castle* [2012] EWCA Civ 1288.

Therefore, where a landlord has not carried out its repair obligations under a lease, that landlord could be liable to pay the leaseholder compensation for loss of comfort and convenience, which can be determined by a notional reduction in rent. A 10% uplift may also need to be applied to the compensation awarded. In addition to this, the leaseholder may also be entitled to special damages including the second-hand replacement value of damaged items.

It is important to note that if a leaseholder has raised concerns about repairs being outstanding, the first things for the landlord to consider are the repair obligations under the lease and whether the landlord is responsible for the repair at issue.

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"General damages (namely compensation for loss of enjoyment and use of the property) are notoriously difficult to quantify."

Q: We are a Registered Provider and we leased a house from a private landlord which we then sub-let to our tenant on an AST. We have since obtained possession and we have just handed the empty house back to the owner. The owner has now raised concerns about the condition of the house and is asking for compensation. What can we do?

A: When a property is leased, the lease itself will set out the obligations owed by the landlord and the obligations owed by the tenant. The lease should set out who is responsible for repairs during the lease.

Leases for the type of arrangement mentioned are drafted in different forms but they are often drafted so as to make the landlord responsible for the more substantial repairs, such has keeping the structure and exterior of the property in repair. There may also be provisions for the leaseholder/RP to carry out the repairs themselves and then to recover the cost of those repairs from the landlord. On other occasions, the lease may be drafted so as to provide for the leaseholder to carry out repairs and to hand the property back to the landlord in no worse condition that it was when originally let.

If the landlord was required to carry out repairs but failed to do so and that is the reason for the property being in a poor condition at hand-back, then that could be an argument as to why the landlord is not entitled to any compensation. That will need to be raised with the landlord.

However, if the RP was required to carry out the repairs and to hand the property back in no worse condition than when originally let, then you need to consider whether that was the case and if so how you can evidence that. There is often a schedule of condition that is prepared at the start of the lease for this very reason. A schedule of condition is then prepared at the end of the lease and the two schedules compared with one another to determine the extent of any deterioration. If there has been a deterioration and that was because the leaseholder/RP had not carried out the repairs that it should have done, then the general position is that the landlord will be entitled to compensation for the cost of the repair work that the leaseholder/RP should have carried out.

Therefore, the first step to take is to consider the lease and, in particular, consider the repair obligations owed by you, the RP. This will have a significant impact on how you respond to the landlord. You will also want to make arrangements for obtaining evidence of the condition of the property when it was handed back to the landlord. Legal advice should be obtained where the sums in question are significant as there may be issues of interpretation of the lease to consider as well as evidence and statutory limits on compensation.

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Q: We are a Registered Provider and want to introduce a sinking fund for our leaseholders on one of our schemes to help the leaseholders pay their service charges. Can we do this?

A: Sinking funds can help leaseholders budget for the costs of services provided by their landlord, for example where the landlord has to carry out major repairs such as replacing a roof and then seeks to recover the cost of those works from the leaseholders via the service charge. The sinking fund provides for regular contributions to be made into the fund by the leaseholders. The amount in the fund is built up over time and the sums in that fund can be used towards the costs of any major works. This means the leaseholders avoid having to pay a large lump sum contribution toward the cost of the works.

However, in order for the leaseholders to contribute towards the fund, there must first be a provision in the lease for there to be such a fund. If no such provision exists then there is no right to demand sums for a sinking fund. Some leases will make express reference to contributions being made to a sinking fund. Others may make indirect reference to such a fund but still allow the landlord to set up such a fund. Some leases, in contrast, will have no provision whatsoever for a sinking fund. If there is no provision for such a fund in the leases and you still want to introduce a sinking fund, then you will need to agree this with the leaseholders first and then vary their leases to reflect this. It will be up to each leaseholder whether they want to agree to this and if a leaseholder does not want to, then you cannot force them to agree. Without any provision in the lease and without any such agreement with the leaseholders, the landlord will have no entitlement to establish a sinking fund.

Sinking funds must also comply with the overriding statutory provisions, for example section 19 of the Landlord and Tenant Act 1985. Under section 19 service charges must be reasonable. The amount to be paid into the sinking fund by the leaseholders will, therefore, be subject to what is deemed to be reasonable. If a sinking fund has been built up to become a significant amount that is more than ample to cover any major works then it may not be reasonable to continue to make demands for the same contributions from the residents.

Therefore, the first step to take when considering introducing a sinking fund is to review the lease(s) in question to determine whether or not there is provision to allow for the establishment of a sinking fund in the first place. This is not always clear so you may want to obtain advice on the interpretation of the lease to see if it allows the establishment of a sinking fund. If the lease does not allow for the establishment of a sinking fund then you will not be able to establish such a fund unless you can get express agreement from the leaseholders to do so.

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"Leaseholders avoid having to pay a large lump sum contribution toward the cost of the works"

Leasehold Management Training Programme

2014/15

Devonshires' Leasehold Management Team is pleased to present the 2014/15 Leasehold Management training programme.

Invitations outlining programme and speaker details will be issued for each event.

Seminar Programme

Leasehold Management for Beginners

7 October 2014

Leases: Dealing with Breaches

4 November 2014

Leases: Dealing with Dilapidations

13 January 2015

Commercial Lease Management for Beginners

31 March 2015

Service Charges and Consultation

28 April 2015

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