

Regulatory Appraisal

1. Title The Service Charge (Consultation Requirements) (Wales) Regulations 2004

Revised procedures for consulting service charge payers about service charges.

2. Purpose and Intended Effect

i) The issue and objective

Currently, service charge payers must be consulted on works where the cost exceeds £1,000, or £50 multiplied by the number of dwellings let to leaseholders who pay a variable service charge, whichever is the greater. This formula means that some service charge payers must be consulted on works for which their personal liability is very small. In small buildings, however, service charge payers may have to pay bills for hundreds of pounds without being consulted first.

Another problem is that the existing requirements do not catch contracts for the provision of ongoing services. Landlords are currently free to enter into long term contracts for the provision of services which could cost service charge payers considerably more than the prescribed amount over a period of time, without giving the service charge payers any opportunity to comment on the matter.

Our objective is to ensure that, before significant sums of service charge payers' money are committed to works or services, service charge payers are given the opportunity to comment on the landlord's intention to carry out works or the landlord's intention to enter a long term agreement.

ii) Risk assessment

Without change, landlords would sometimes be required to consult where it makes little sense to do so, or else face the possibility that they would be unable to recover the full costs of the works concerned.

Service charge payers, on the other hand, might find that their landlords had entered into large contracts without their knowledge. Whilst they could still dispute the reasonableness of the charges, they will be in a better position to challenge the landlord's decision, if flawed, where they have been consulted at the outset. Where the issue is not cost but quality or the need to carry out work at all, this may be particularly important. It can be very difficult, after the event, to establish precisely what has or has not been done. In the most serious cases, defective works may even cause damage to the building, which may only become apparent years later.

3. Options

(i) Options identified:

The following options have been identified:

Option 1: Do nothing.

Option 2: Change the threshold so that consultation only has to take place where the amount payable by any service charge payer exceeds a certain amount.

Option 3: Require the manager to give a written explanation of the reasons for the choice of contractor.

Option 4: Require managers to consult on any contract - including those for services rather than works - that was let for a period of more than 12 months where the amount payable by any service charge payer exceeds a certain amount in any 12 month period of the contract. As with the existing major works provisions, landlords will have to obtain two quotations, at least one of which will have to be from a wholly unconnected contractor. Managers will also be required to consult on the need for individual items of work under the contract where these exceed the individual limit. However, they will not need to obtain two quotations where the work is part of a long-term contract.

ii) Issues of equity or fairness

These changes should increase fairness, by providing a more consistent and sensible set of rules to govern when service charge payers should or should not be consulted. It will also make landlords more accountable on how they spend service charge payers money.

4. Benefits

Option 1: None.

Option 2: This will provide a more logical basis for deciding whether or not consultation is necessary. Managers will be spared the need to consult where individual liability is very small. Service charge payers will always be consulted where their personal liability exceeds a certain sum. In addition, effective consultation should make it less likely that managers will be challenged over the cost of work later in proceedings.

One of the key benefits of consultation for service charge payers is that it notifies them of the landlords' intentions at an early stage. If necessary, they can challenge the reasonableness of the proposed works or seek an injunction. It also makes it easier for them to monitor works and, where

appropriate, to gather evidence of any shortcomings in the contractors' performance.

Option 3: Landlords will not be able to dismiss service charge payers' comments out of hand. Where an explanation is not given, or where the explanation is inadequate, service charge payers would be alerted at an early stage and will then have to consider the best course of action, as above. This will increase pressure on landlords to provide good value for money.

Option 4: Landlords will not be able to evade the existing requirements by separating large jobs into a series of smaller items of work, all let under a single contract. At the same time, it will enable them to gain the benefits of a long-term contract, without needing to later seek alternative quotations for individual items despite being contractually bound to a single provider.

This option will also extend the consultation requirements to cover services as well as works. This will place landlords under greater pressure to obtain value for money when contracting for long term services as well as for major works.

5. Compliance Costs & business sectors affected

The controls will potentially affect the landlords of the million or so leasehold flats in England and Wales, a small number of other properties subject to variable service charges, and the agents that are employed to manage certain of those properties. Leaseholder-managers would also be affected. This includes both private and public sector landlords.

Option 1: None.

Option 2: Minimal. This will result in an increase in the number of premises that will be caught by the consultation requirements; under the previous requirements, small blocks of flats would not have been caught.

Option 3: Minimal to Moderate. The landlord will have to spend time considering how to set out his reasons for accepting the tender. We anticipate the costs of producing the letter to be minimal for the majority of landlords.

Option 4: Moderate. There will be a larger number of additional cases caught by this option and as noted in option 3 in some cases this will increase administration costs.

6. Consultation

Consultation on these proposals was undertaken in November 2002. Even though the consultation was also put on the Assembly's website, only two responses were received. One of these was concerned about "too much

unnecessary consultation with tenants and the costs to their service charge payers”, whilst the other welcomed the change.

The draft Bill and consultation paper were also widely circulated. The Assembly undertook this consultation in Wales on behalf of the Secretary of State and the responses were passed to the Department of the Environment, Transport and the Regions to be taken into account with the others received. Over a thousand responses were received in all, 44 of which came from landlords, managing agents or management companies responsible for 20 or fewer leasehold units (i.e. flats or houses).

We are satisfied that these reforms will not have a disproportionate effect on small businesses.

7. Other Costs

We would ordinarily expect any additional costs to managers to be passed onto service charge payers through management fees and service charges contributions.

Landlords will be unable to enforce full payment of service charges where the consultation requirements are not met – except in cases where the landlord has good reason to ignore them (e.g. in the event of an emergency, where there is no time to consult). Leasehold Valuation Tribunals (LVT) will have jurisdiction over such matters as they relate to liability. LVTs are designed to be a cheaper equivalent to the Courts, so the cost to the parties will be lower than under the existing arrangements.

LVTs in Wales are set up by the Rent Assessment Panel for Wales, which is funded by the Assembly. Any additional cases involving failure to consult on long term contracts will be absorbed from within existing provision as other areas of work on regulatory tenancies is now decreasing. Funding from the Assembly for salaries and fees and general expenses for the Rent Assessment Panel for 2003-04 is £137,000

8. Results of consultations

The responses to the consultation on an England and Wales basis indicated general support for all these reforms. Nearly all respondents (99%) agreed that the threshold for consultation on major works should be changed so that consultation only has to take place where the amount payable by any service charge payer exceeds a certain amount. This included 92% of landlords, agents and management companies responsible for 20 or less units.

There was also widespread support (95%) for the proposal that landlords should be required to give a written explanation of the reasons for their choice of contractor. This included 72% of landlords, agents and management companies responsible for 20 or less units.

Finally, 91% of respondents agreed that the consultation requirements should be extended to cover contracts, including 72% of landlords and agents who owned and/or managed 20 or less units. However, some concern was expressed regarding any requirement to consult on contracts of employment. Certain local authorities in England were also concerned that the proposals for dealing with long term contracts might not be adequate to deal with Private Finance Initiatives, however, these do not apply in Wales.

During the passage of the Bill through Parliament, views were also sought on the consultation requirements. As a result, the Bill was amended to introduce a de minimis threshold for consultation on long term contracts. The Assembly supported the Bill at all stages.

As a result of representations made following the consultation in England, the trigger for consultation on long term agreements has been increased from £25 to £100. We consider this to be a more sensible level which will mean that landlords will not have to consult service charge payers on as many contracts. We have also introduced new requirements for public sector landlords so that the consultation provisions do not conflict with EU Procurement Rules. Furthermore, we have limited the circumstances in which a landlord has to write to service charge payers after the award of a contract thus making the requirements less burdensome than expected.

9. Summary

Four options were under consideration. Option 2 could produce net savings for landlords; options 3 and 4 would result in additional costs. However, we do not expect the overall cost to be significant and service charge payers are entitled to information about – and a say in – the way that their money is spent. The reforms have widespread UK support, and will increase the pressure on managers of leasehold property to provide good value for money. We believe that leaseholders in Wales should benefit from the reforms. The Regulations will therefore implement options 2, 3 and 4.

10. Enforcement, Sanctions, Monitoring and Review

The Welsh Assembly Government would be able to monitor the new system by examination of LVT decisions and by using the feedback provided in correspondence from the public.