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PHILIPS v FRANCIS AND DAEJAN - HOW ARE YOU MANAGING?

What a start to 2013!

- On the 8th January the following hit my inbox:

A recent decision in the High Court regarding consultation under Section 20 has left the management industry in "complete disarray". Managing agents are now required to consult with residential tenants in relation to ALL works, including routine repairs.

Where are we now?

- S.20 Consultation: Philips v Francis – overturned established S.20 practice in dealing with fragmentation
- Now required on all “qualifying works” above £250 threshold on a year by year basis
- Dispensation: 6th March 2013 - Daejan v Benson - Supreme Court reopened dispensation but on terms reflecting prejudice and with costs

The Challenge for Property Managers

- Unknown reactive repairs over the year can take you above threshold
- Cost and administration time of consultation on all minor repairs – cost implications
- Scale of administrative burden
- Complying without losing managements
- No definition of “qualifying works”

What are qualifying works?

Defined by Section 20 as "works on a building or to any other premises"

Little guidance from Tribunals

Paddington Walk Management v Peabody

Window cleaning was not qualifying work

"Qualifying work meant building works"

How should we consult?

- S.19 is the objective (not S.20) - Consultation provides "practical support" to S.19 (LTA 1985) – "Limitation of service charges: reasonableness"

- So that lessees do not:
  - i) pay for unnecessary or defective services
  - ii) pay more than they should
  - iii) pay for an unacceptable standard

- Advance consultation provides:
  - i) are works appropriate?
  - ii) more than one quotation
  - iii) consult on cost and quality of the works

- Failure may lead to Prejudice and a shortfall in recovery

What is prejudice?

- Contribution reduced to reflect the lessee's disadvantage suffered through consultation not being fully complied with

- Lessees in dispensation claims are now in a better position:
  i) benefit of hindsight
  ii) potential to recover reasonable professional costs

- Any departure from full compliance puts the landlord at risk of a shortfall and costs

- But, potential for a negotiated settlement with properly advised lessees

What are our options?

- The Tribunal approving a budget – later unforeseen qualifying works?
- Interpretations of the decision – risky?
- Long Term Agreements (i.e. over 12 months) – more simple process but can be very complex with schedules of rates
- Consultation and compliance with S.20

Manage qualifying works

Step 1 – Budget

- Inspect the building well ahead to identify qualifying works
- Look at your long-term maintenance plan and historical expenditure
- Prepare a summary of works (required or likely) with best guess at the gross costs and categorise into:

    1. Maintenance works (none building works – no element of repair)
    2. Qualifying building works (S.20) – known or likely/ anticipated repairs
    3. Qualifying Minor works provision “contingency” (S.20) – unknown repairs
    4. Qualifying works that can wait until the following year (start planning)

Manage qualifying works

- Compare qualifying works cost for that year against the S.20 limit to establish where the expenditure stands in relation to it
- Beware! Where you are well below the limit, you only need a major unexpected spend that cannot wait until the next financial year to tip you over the limit
- You need to cover yourself for this eventuality (i.e. with a view to prejudice)
- Along with your budget, serve a First “Notice of Intention to do Works” which very briefly sets out what works have been identified or are likely (i.e. 2 & 3 above)
- This includes a contractor nomination so you have a bank of them for when the works come up

Manage qualifying works

Step 2 - Tender

- Try and batch as many qualifying works as you can into a specification/tender exercise
- Serve Second “Notice about Estimates”
- Do the same for any sizeable additional works that arise through the year (assuming they were covered in a First Notice)

Manage qualifying works

Step 3 – minor repairs

- Always have S.19 in mind. Make sure you have evidence of:
  - i) The necessity for the repairs (condition report, photos etc)
  - ii) Competitive pricing (two or more comparable prices)
  - iii) The acceptable standard of the works (inspection notes/ photos)
- Keep the lessees informed/consulted
- Discuss and agree with the lessees if possible, how to liaise with or consult with them
- Maybe a quarterly repairs report on the contingency element
- Emergency repairs - dispensation in the established way

Manage financial years

- The S.20 limit is an annual contribution (with exceptions depending on the accounts period in the lease)
- Consider when the cost occurs and where it crosses financial years. The balance needs to be added to the following year's qualifying works total (having an impact on that year's works threshold)
- Try and get costs incurred in a single financial year

Manage financial years

- Where not possible then outstanding monies will need to be carried over into the following year's process/threshold:

- Stage 1 Notice has been done

- Stage 2 Notice stands (where no major variations)

- Send a fresh letter to tenants referring to previous notices, updating figures and showing any revisions to the contract sum with costs incurred and costs yet to be incurred (the carry-over figure)

Manage financial years

WARNING

- Make sure that any new leaseholder who has moved in during the intervening period have been provided with the previous notices

- Beware of major changes in contract – as before – serve fresh S.20 notices

Manage the client

- The risk of a shortfall in recovery and costs lies with the landlord
- Explain your policy/procedure and the risks of recovery and costs (depends on freeholder/RMC client, relationship with lessees and risk)
- It's a balance between risk, administrative burden/ costs, time delays etc
- Encourage long-term maintenance plans

Manage the client

- The situation may well change if ‘Francis’ is overturned
- ARMA, the RICS and the leasehold management industry have been lobbying for an appeal and or legislative changes
- Give your recommendation, for example
- Comply with S.20 consultation in a methodical structured manner; with proportionate administration costs to the service charge account; with dispensation only being used as a last resort or for emergency works

Not all bad news...

- The established approach worked well but Francis decision, whilst having unwelcome repercussions on the industry, has made us all think about some valid issues
- Highlighted the unwelcome practice of fragmentation
- The £250 threshold requires review although a recent motion in the House of Lords to define qualifying works and raise the threshold to £330 was unsuccessful
- Qualifying works requires proper definition

Not all bad news...

- Encourages property managers to think and plan works to their buildings more carefully with more pro-active property management
- Encourage/improves building focused knowledge and training for property managers
- Encourages long-term maintenance plans
- Encourages increased consultation with lessees over spending their money
- Dispensation is more focused and rather than being all or nothing (pre-Supreme Court), the terms awarded reflect the prejudice suffered by lessees
- Brought the industry (ARMA, RICS, BPF, LKP etc) together to lobby
- Francis leave to appeal - 18th/19th November hearing