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Landlords can avoid service charge consultation

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Landlords can still recover substantial service charges even if they fail to consult with tenants

Summary

By a small majority, the Supreme Court has ruled that if a landlord fails to consult with tenants concerning proposals for works in respect of residential property (as required by the Housing Act 1985) it will be able to recover service charges provided that any prejudice suffered by the tenants is taken into account.

Previously, if landlords failed to consult tenants as required under the Housing Act provisions (see below) then a landlord would be entitled to recover a maximum of £250 from each tenant even though the cost of works might be substantially more, even millions of pounds in case of major refurbishment.

This is likely to be extremely good news for London residential landlords dealing with expensive repairs to major blocks of flats and bad news for tenants. The Supreme Court issued guidance that the Leasehold Valuation Tribunal ("LVT") should use its authority to dispense with consultation requirements even if the landlord's non-compliance is significant.

How much will Tenants have to pay?

The LVT should consider what steps or action the tenants would have taken if consulted and in what way the tenants' position was prejudiced because of the failure to consult.

For example, where a landlord carries out works costing, say, £1 million but failed to comply with the statutory requirements to consult to a small extent, such as failing to have regard to an observation made by the tenants, then the tenants might establish that the works could have cost, at the most, £25,000 more as a result of the failure.

The Supreme Court explained that the result of this example is that it would be reasonable for the LVT to grant dispensation, but only if the landlord agrees to reduce the recoverable cost of works from £1 million to £975,000. The LVT also has the power to impose a further condition that the landlord pays

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the tenants' reasonable costs incurred in connection with the landlord's application for dispensation of the usual consultation rules and statutory cap consequences.

A Mockery of the Consultation Process?

This is an important decision for the residential property industry. There is likely to be criticism that the legislation was not intended to allow a landlord in default of the consultation requirements to recover the cost of works through service charges everywhere no prejudice has been caused to the tenant.

Two of the three Lords in the Supreme Court dissented arguing that the LVT should be able to refuse dispensation on the ground of a serious breach or departure from the consultation requirements. In the dissenting judgments it was felt unfair that the "factual" burden of proof now lies on a tenant to show that it has suffered prejudice.

The majority decision was, however, that this decision does not simply allow a landlord to buy its way out of having failed to comply with the consultation requirements. The landlord would have to:

- pay its own costs of making and pursuing an application for dispensation to the LVT; and
- pay the tenants' reasonable costs in connection of investigating and challenging that application; and
- give the tenants a reduction to compensate fully for any relevant prejudice on the basis that the LVT will adopt a sympathetic attitude to tenants on that issue.

Comment

It is now likely that a landlord's failure to adhere to the consultation requirements will not be fatal provided that the tenants are put back into the position that they would have been in had the requirements been complied with.

This is undoubtedly good news for landlords and bad news for tenants. There will be no automatic bar on landlords recovering the cost of works if the consultation process has been avoided even if the landlord has failed to consult wilfully and in a material way.

There is some comfort for tenants in that a landlord's claim for service charge to recover cost of works may be reduced if there has been non-compliance. However, the LVT will only award a reduction if the tenants are able (and take the time and trouble) to prove prejudice. Tenants will need to show that a reduction in the costs of works would have followed if the consultation process had been adhered to. This decision is likely to cause uncertainty and result in more disputes to be decided by the LVT.

The Law

This legal update follows the case of *Deajan Investments Limited–v- Benson & Others* decided by the Supreme Court [2013] UKSC14.

The consultation requirements are set out in Part 2 of Schedule 4 of the 2003 Regulations under the

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Landlord and Tenant Act 1985 (as amended). The consultation process comprises three stages:-

Stage 1:

Notification of intention to do the works must be given by the landlord to the tenant with a description and reasons for the works and inviting observations and nominations of contractors allowing at lease thirty days.

Stage 2:

The landlord must seek estimates for the works, including from any nominee identified by the tenants or any tenants' association.

Stage 3:

Information about the estimates must then be sent by the landlord in the form of a statement to the tenants containing two or more estimates and a summary of the observations and its responses. Any estimate from the contractor nominated by the tenants must be included. The statement must say where and when the estimates may be inspected and give details for inviting observations allowing thirty days at least and the landlord must then have regard to any such obligations.

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For further information, please contact Matthew Spring of the Property Disputes Team by email or on 020 7465 4300.

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