Leasehold home ownership: exercising the right to manage

Summary
LEASEHOLD HOME OWNERSHIP: EXERCISING THE RIGHT TO MANAGE

INTRODUCTION

1.1 The right to manage ("RTM") was introduced in 2002 to give leaseholders the ability to take over the landlord’s management functions in respect of their building, without having to buy the freehold. It is a “no-fault” right, which leaseholders can exercise without the need to prove a complaint against their landlord or managing agent.

1.2 The relevant legislation is the Commonhold and Leasehold Reform Act 2002 ("the 2002 Act"). The 2002 Act sets out what was intended to be a simple process, beginning with the leaseholders setting up a dedicated “RTM company” of which the leaseholders are members. If the RTM is claimed successfully, the leaseholders, through the RTM company, take control of services, repairs, maintenance, improvements, and insurance in respect of their building.

1.3 However, stakeholders told us about numerous problems with the existing RTM regime, including:

(1) unpredictable and sometimes excessive costs of claiming the RTM, particularly as the RTM company is liable for the landlord’s costs as well as its own;

(2) restrictive qualifying criteria meaning it is not possible to claim the RTM in respect of multiple blocks on an estate, buildings with more than 25% non-residential space, or leasehold houses;

(3) information about the building and management functions being provided to the RTM company too late in the process, so that the leaseholders cannot always make informed decisions about claiming the RTM or prepare for an efficient handover of management functions; and

(4) uncertainty as to how the RTM applies to areas which are shared with other buildings, such as gardens and car parks.

1.4 Government asked us to review the existing legislation with a view to making the RTM procedure simpler, quicker and more flexible, particularly for leaseholders. We have now published our final Report setting out our recommendations for reform, available on our website at https://www.lawcom.gov.uk/project/right-to-manage/. This is a summary of that Report.

The consultation

1.5 We published a Consultation Paper in January 2019, describing the current law and the problems to which it can give rise. We also set out our provisional proposals for reform, and asked consultees for their views. We received 275 responses from a range of stakeholders including leaseholders, freeholders, social housing providers, lawyers, managing agents and other professionals.

1.6 We also published a short survey which invited individual leaseholders and RTM company directors to share with us their experiences of the RTM. We received 150 responses to this survey.
1.7 We are publishing the responses to the consultation in full, together with a separate summary of the responses to the leaseholder survey.

1.8 In framing our recommendations, we have considered all consultees’ comments carefully.

Our recommendations

1.9 We are confident that the recommendations we are making will bring about significant benefits. In particular, they will:

(1) reduce the costs of making an RTM claim, and give leaseholders more control over those costs;

(2) make the RTM available to more leaseholders in a wider variety of buildings; and

(3) make the process of claiming the RTM less complicated and less likely to be frustrated because of mistakes in the process.

1.10 In the remainder of this summary document, we explain the key recommendations in the Report. By “key recommendations”, we mean those which represent the most significant changes to the current law and those which we think will be of most interest to stakeholders. We include paragraph references to the main Report where all of our recommendations are set out in full.

QUALIFYING CRITERIA (CHAPTERS 3 AND 4)

1.11 The 2002 Act sets out criteria which must be satisfied in order for the RTM to be exercised. The criteria concern the nature of the premises, the lease(s), and the landlord(s).

Premises in which the RTM is available

Houses

1.12 Under the 2002 Act, the RTM applies only to flats; houses are excluded. This exclusion was introduced, in our view, not for any principled reason, but rather because many of the RTM criteria were transposed from the enfranchisement provisions in the Leasehold Reform, Housing and Urban Development Act 1993, which concerned only flats. We recommend that the RTM should be exercisable in respect of leasehold houses as well as flats: paragraphs 3.7 to 3.12.

1.13 In order to integrate houses into the RTM, we recommend that no distinction should be drawn in the legislation between a “flat” and a “house”. Instead, there should be a single concept of a dwelling, such as “residential unit”: paragraphs 3.20 to 3.37.

Restrictions on premises

1.14 Currently, the RTM can only be claimed in respect of premises which:

(1) constitute a self-contained building or self-contained part of a building;
have 25% or less of the total internal floor area occupied by non-residential parts; and

contain at least two flats held by qualifying tenants (broadly speaking, these are leaseholders with leases of more than 21 years).

1.15 In the Consultation Paper, we explained that these criteria have been the focal points of much of the litigation and frustration surrounding many RTM claims. We identified three particular concerns:

(1) the focus on the physical structure of the building and issues such as “flying freeholds” is unsuited to the RTM, which is concerned with management functions (in contrast to leasehold enfranchisement, in which defining the physical boundaries of the property is of greater importance);

(2) the requirement for self-containment often generates legal disputes which require expensive expert evidence as to whether any attachment between the building or part of a building and another structure means it is not self-contained; and

(3) the limit on non-residential floor area excludes many newer mixed-use developments, a feature of which is a substantial amount of space for shops, gyms, etc. In some cases, landlords have demonstrated a willingness to alter construction of the premises with this non-residential limit in mind, such that the RTM would not be available.

1.16 Some of the solutions we recommend to the problems outlined above are as follows.

1.17 First, we recommend that premises can qualify for the RTM if they are a (part of a) building reasonably capable of being managed independently, even if they do not satisfy the requirements for self-containment: paragraph 3.38 to 3.93. In practice, this means that leaseholders in premises currently managed independently can simply point to that existing management arrangement as evidence that the premises qualify for the RTM.

1.18 Second, we recommend that the non-residential limit be increased to 50%. This means that only premises in which more than half of the total internal floor area is occupied by non-residential parts will be excluded from the RTM: paragraphs 3.94 to 3.126. We agreed with the arguments presented by consultees that a limit of 25% non-residential area represented too narrow a restriction on RTM claims, particularly in light of the contemporary trends in property development. We think leaseholders should be entitled to manage premises in which a majority of the space is for residential purposes.

1.19 Third, we recommend that the RTM be exercisable in respect of premises which comprise or contain at least one residential unit held by a qualifying tenant, rather than two as in the current law: paragraphs 3.127 to 3.139. This change is necessary to incorporate leasehold houses within the ambit of RTM. In premises with only two residential units, we recommend the removal of the existing rule that both leaseholders must participate in the RTM claim: paragraphs 3.157 to 3.183.
Leases capable of supporting an RTM claim

1.20 The RTM is exercisable only by “qualifying tenants”. A qualifying tenant is a person who holds a lease of a residential unit for a term of more than 21 years. Holders of business tenancies and leases out of which another long lease is granted (i.e., intermediate landlords in a chain of leases) are not qualifying tenants, irrespective of the term of their lease.

1.21 The RTM can only be claimed in respect of premises in which qualifying tenants hold at least two-thirds of the total number of flats in the building or part of the building, and we recommend that this requirement remain in place: paragraphs 3.140 to 3.154.

Shared ownership

1.22 Shared ownership leaseholders purchase a “share” of a house or flat (usually between 25% and 75%) and pay a normal rent on the remainder of the property. They can generally purchase additional shares in the property over time, usually up to 100%, a process known as “staircasing”. This mechanism provides an avenue to homeownership for those who may not have been able to finance a mortgage for the full value of the property.

1.23 There is currently uncertainty as to whether a shared ownership lease constitutes a “long lease” for the purposes of the 2002 Act.

1.24 To address this uncertainty and expand the availability of the RTM, we recommend that shared ownership leases granted for more than 21 years should be a long lease for the purpose of the RTM legislation, regardless of whether the particular leaseholder has staircased to 100%: paragraphs 4.8 to 4.21.

Business tenancies

1.25 Business tenancies do not qualify for the RTM under the 2002 Act. A tenancy is a “business tenancy” only if business is being carried on by the leaseholder (as opposed to anyone else). The exclusion can therefore be easily circumvented by subletting the property to a third party (who can be connected to the tenant) to carry on the business use.

1.26 We are of the view that holders of business tenancies should continue to be excluded from the RTM (focussed as it is on management of residential properties). However, that exclusion must be drafted to preclude simple workarounds, and flexible enough to include mixed-use properties with a genuine residential purpose (such as live/work units) in the RTM regime.

1.27 Determining whether a long leaseholder is a qualifying tenant should require consideration of the modes of occupancy (commercial or residential) that the lease may permit, and the manner in which a residential unit is in fact occupied.

1.28 We recommend (paragraphs 4.106 to 4.130) that:

(1) where a lease does not permit residential use, the leaseholder should not be a qualifying tenant for the purposes of the RTM;
where a lease permits only residential use, the leaseholder should be a qualifying tenant for the purposes of the RTM; and

(3) where a lease permits both residential and non-residential use, the leaseholder should be a qualifying tenant for the purposes of the RTM unless the premises are occupied solely for business purposes.

Nature of the landlord

1.29 To expand the availability of the RTM and remove restrictions which we do not think are justified as a matter of policy or principle, we recommend the removal of two existing exceptions:

(1) the removal of the "resident landlord" exception which applies to premises containing fewer than five flats, so that leaseholders will be able to claim the RTM even where the landlord lives in the premises: paragraphs 4.26 to 4.52; and

(2) the removal of the rule that leaseholders cannot claim the RTM over a whole building if parts of a building are owned by different freeholders and one or more of the parts is self-contained: paragraphs 4.53 to 4.71.

THE RIGHT TO MANAGE MULTIPLE BUILDINGS (CHAPTER 5)

Multi-building RTM

1.30 The current law prevents leaseholders in multiple buildings acting together to take over management through a single RTM company in a single claim, even where they are on the same estate and share appurtenant property such as gardens or car parks.

1.31 It seems clear that, in some cases, multi-building RTM is the best way to facilitate giving leaseholders more control over the management of their homes, and we recommend a change in the law to make this possible: paragraphs 5.3 to 5.16. We do not recommend that there should need to be any particular link between buildings, such as a common service charge or shared appurtenant property, although we expect that leaseholders are unlikely to claim the RTM in respect of unconnected buildings: paragraphs 5.37 to 5.49.

1.32 We recognise that there are practical difficulties which might militate against multi-building RTM. There is the potential for conflicts of interest between buildings with different facilities or needs, or for the leaseholders of a larger block to “out-vote” the leaseholders of a smaller block and prioritise their own building. It may also be difficult to coordinate the participation of so many leaseholders. We therefore think that it should still be possible for leaseholders in individual buildings to acquire the RTM, even if they are located on an estate: paragraphs 5.17 to 5.27.

1.33 Our recommended model would allow any combination of buildings to progress an RTM claim through a single RTM company. The multi-building RTM would not necessarily need to cover all of the buildings on an estate.
1.34 Our recommendation, discussed above, to allow for the RTM to cover leasehold houses would mean that leasehold houses on an estate could also join a multi-building RTM.

Application of qualifying and participation criteria to multi-building RTM

1.35 We recommend that the qualifying and participation criteria should be met by each individual building which is to be included in the multi-building RTM claim: paragraphs 5.28 to 5.36. The RTM was introduced to give leaseholders more control over the management of their flats, not adjacent buildings which would not otherwise be able to acquire the RTM themselves or where the majority of qualifying tenants do not support the RTM.

Freedom to join or leave an RTM at a later date

1.36 We recommend that leaseholders in a building not originally included in a multi-building RTM claim, including a building which has previously been the subject of a separate RTM, should be able to join in the existing RTM arrangements at a later date: paragraphs 5.50 to 5.60. Both the RTM company and the leaseholders in the excluded building would need to agree to this.

1.37 We also consider that it should be possible for leaseholders to “break away” from an established multi-building RTM and claim the RTM in respect of their own building or a smaller number of buildings, subject to the expiry of a minimum period of time following the acquisition date of the original multi-building RTM: paragraphs 5.61 to 5.81.

THE RTM COMPANY (CHAPTER 6)

1.38 As mentioned above, before leaseholders can take any steps towards claiming the RTM, they must set up an RTM company. The legislation provides that this must be a company limited by guarantee, and must use specific articles of association (the “model articles”), which set out how the company is governed.

1.39 Every qualifying tenant is entitled to become a member of the RTM company at any time; whereas landlords are only entitled to become members after the acquisition of the RTM. The RTM company, and its directors, are bound by existing company law including directors’ duties.

1.40 Under the current law, only one RTM company can exist in relation to premises at any one time. There have been instances of landlords establishing RTM companies to try to prevent leaseholders from making a genuine RTM claim. Some managing agents establish companies to pressure leaseholders into acquiring the RTM, and appointing them as the managing agent for the premises.

1.41 Furthermore, leaseholder participation in RTM company decision-making is often curtailed, because there is no requirement for company directors to hold annual general meetings (“AGMs”).

1.42 We make the following recommendations to address these problems:
(1) to prevent the use of sham RTM companies, we recommend abolishing the rule that once an RTM company has been established for a set of premises, there can be no other RTM company for that premises: paragraph 6.37. Competing RTM claims will instead be prevented by provisions in the current law, the effect of which is that once an RTM company has served a claim notice in relation to premises, no other RTM company may do so until either: the claim has been withdrawn or rejected by the tribunal; or the RTM, having been acquired, has ceased (paragraph 6.34); and

(2) to ensure RTM company members can participate in company decision-making, we recommend that RTM company directors must hold an AGM: paragraph 6.102. RTM companies with only one member will be exempt from this requirement.

1.43 We also recommend some minor clarifications to the current voting rights as set out in the model articles (at paragraphs 6.84 and 6.85), and set out two methods for allocating votes in properties with non-residential parts up to 50% of the internal floor area (at paragraphs 6.61 to 6.83). These will ensure that landlords cannot routinely outvote leaseholder members of an RTM company in such properties.

ASSISTANCE AND SUPPORT FOR RTM COMPANIES (CHAPTER 7)

1.44 One of the most common refrains we heard from consultees of all kinds, including leaseholders, was that leaseholders often have insufficient knowledge about the rights and responsibilities that are acquired by an RTM claim. This is particularly the case for leaseholders acting as RTM company directors. The educational resources that currently exist are often cost-prohibitive or inadequately detailed. Landlords were concerned that their property could be managed by people ill-equipped to do so, and leaseholders were concerned that it was difficult to understand all the implications of acquiring the RTM.

1.45 In many cases, leaseholders who have acquired the RTM may choose (but will not be required) to engage a professional managing agent, particularly in large and complex buildings or on estates. However, even if they appoint a managing agent, the RTM company directors will remain ultimately responsible for management of the building and for compliance with company law requirements.

1.46 In order to address this significant issue, we recommend that Government make training for leaseholders acting as company directors available free of charge: paragraphs 7.40 to 7.44. We recommend that at least one director of an RTM company should be strongly encouraged to complete training: paragraphs 7.17 to 7.39. This should cover both the company law obligations of RTM company directors, and information in respect of building management. This recommendation should be kept under review depending on what action Government takes in response to the Regulation of Property Agents: Working Group Report.¹ That report recommends a system of minimum entry requirements and continuing professional development for

¹ Ministry of Housing, Communities and Local Government, Regulation of Property Agents: Working Group Report (July 2019).
property agents and contemplates that this regulation might in future be extended to other parties including RTM companies.

THE ACQUISITION PROCESS (CHAPTER 8)

1.47 Stated broadly, the existing procedure required for acquisition of the RTM is as follows.

(1) Once set up (as described above in the summary of Chapter 6), the RTM company must serve a notice inviting participation on all qualifying tenants who are not already members of the RTM company.

(2) The next step is for the RTM company to serve a claim notice on any landlords or other relevant parties (such as managers that may be party to a tripartite lease). On the date of service, qualifying tenants representing at least half of the flats in the premises must be members of the RTM company. A copy of the claim notice must also be served on all qualifying tenants.

(3) The landlord or any relevant third party may serve a counter-notice either affirming the basis of the claim (“positive counter-notice”) or disputing the claim (“negative counter-notice”). If the RTM company wishes to contest a negative counter-notice and persevere with the RTM claim, it must apply to the Tribunal for a determination.

(4) If no counter-notice is served, the RTM company acquires the RTM on the date specified as the proposed acquisition date in the claim notice.

1.48 Some details of this procedure are opaque even to well-advised leaseholders, and minor technical errors can be used (by some landlords) as an avenue for obfuscation and delay.

1.49 We recommend a number of changes to the acquisition process, including the following:

(1) the requirement to serve notices inviting participation should be abolished: paragraphs 8.4 to 8.26;

(2) all notices under the RTM legislation should be capable of being given by email, subject to some restrictions: paragraphs 8.63 to 8.85;

(3) there should be a requirement that claim notices are signed by or on behalf of an RTM company (the signature(s) may be affixed electronically): paragraphs 8.27 to 8.41;

(4) RTM companies should only be required to serve freeholders of the premises. The onus will be on freeholders to pass this notice on to any intermediate landlords: paragraphs 8.47 to 8.50;

(5) service at certain categories of address will be deemed to have been effective: paragraphs 8.86 to 8.102;
(6) landlords (and other relevant parties) should be required to state and explain all objections in the counter-notice and should not generally be permitted to raise new arguments at a later stage: paragraphs 8.158 to 8.172;

(7) in cases where no counter-notice is received, the RTM company will have the option of confirming the validity of its acquisition of the RTM in the Tribunal: paragraphs 8.173 to 8.194; and

(8) the validity of RTM notices may only be challenged if they fall short of prescribed requirements relevant to the underlying purposes of those notices: paragraphs 8.212 to 8.232.

1.50 We also make recommendations to clarify how the acquisition date – the date on which the RTM company legally acquires management functions – is determined: paragraphs 8.265 to 8.324.

INFORMATION RIGHTS AND MANAGEMENT CONTRACTS (CHAPTER 9)

Rights to obtain information

1.51 Consultees consistently told us that leaseholders lack sufficient information about the premises to make an informed decision about whether to acquire the RTM. An RTM company can request information from any person which it reasonably requires to complete the claim notice. However, the information that can be requested under this right is limited and is unlikely to provide RTM companies with a full picture of the management functions that it would acquire.

1.52 An RTM company can also request information that it reasonably requires in connection with the RTM. However, the landlord is not obliged to provide this information until after the RTM is acquired, meaning that information is delivered too late to ensure a smooth handover of management functions. This right is also dependent on RTM companies asking for specific documents. However, RTM companies are often uncertain about what types of information they need, such as an insurance claims history.

1.53 Therefore, we recommend the following changes:

(1) in addition to information reasonably required to complete the claim form, RTM companies should be entitled to inspect or obtain a copy of any information that they reasonably require to decide whether to claim the RTM: paragraph 9.32;

(2) RTM companies should have a right to obtain any information they reasonably require to decide whether to apply to the Tribunal for a determination that they are entitled to the RTM: paragraph 9.35;

(3) Government should provide model forms which RTM companies can choose to use when exercising the right to obtain information: paragraph 9.54;

(4) the landlord should have a duty to notify RTM companies of material changes to information they have provided: paragraph 9.121; and
costs of complying with requests for information will depend on when that request is made: the RTM company should bear the landlord's costs of responding to a request for information before the claim notice is served. However, after the service of the claim notice, the landlord or other relevant parties (but not the RTM company) should bear their own costs of complying with their duties to provide information: paras 9.124 to 9.148.

1.54 Some consultees expressed concern that requirements to provide information could be difficult or impossible to fulfil in compliance with the requirements of the General Data Protection Regulation ("GDPR"). We are confident, however, that generally the provision of information to the RTM company would comply with the GDPR on the basis that it is necessary for compliance with a legal obligation: paragraph 9.151.

**Notices relating to management contracts**

1.55 The acquisition of the RTM will affect existing arrangements that the landlord has in place with third parties such as managing agents, cleaning contractors and garden maintenance contractors. The 2002 Act prescribes a procedure by which the landlord must both notify the RTM company of such management contracts, and notify the contractors of the impending RTM acquisition.

1.56 The 2002 Act does not make provision for the termination of existing management contracts, and we understand that management contracts often do not contain provisions as to termination on acquisition of the RTM. An RTM company will not be party to, and therefore not be bound by, any contracts entered into by the landlord prior to the acquisition of the RTM.

1.57 In practice, the relevant communications about the management contracts are often provided by the landlord very late in the process, sometimes even after the acquisition date. This gives the RTM company and contractors little or no time to put in place new contractual arrangements.

1.58 To address these issues, we recommend strengthened notice requirements:

1. for management contracts entered into prior to the determination date, the landlord must notify the contractor of the RTM claim and the RTM company of the new management contract as soon as possible after the claim is determined, and no later than 14 days afterwards: paragraph 9.176; and

2. for management contracts entered into after the determination date, we recommend that the landlord must provide the relevant notifications on the date the contract is entered into, or as soon as possible afterwards if not reasonably practicable on the date. In any event, the notification must occur before the acquisition date: paragraph 9.177.

1.59 We also clarify our view that in general, the acquisition of the RTM will cause existing management contracts to be considered frustrated: paragraph 9.173. Exceptions to this general position might be when the landlord is aware of the possibility of an imminent RTM claim before entering into the management contract, or if the management contract explicitly contemplates an RTM claim as a future possibility.
MANAGEMENT FUNCTIONS (CHAPTER 10)

1.60 The RTM company acquires the "management functions" under the relevant leases, being functions relating to services, repairs, maintenance, improvements, insurance and management. After acquisition, the landlord cannot undertake any management functions which the RTM company is "empowered or required" to undertake, unless this has been agreed with the RTM company.

Regulated activities

1.61 In relation to retirement or other specialist accommodation, it is possible that an RTM company may become responsible for providing "regulated activities" to leaseholders, such as health and social care. These services are governed by the Care Quality Commission, with which the services provider (in this case, the RTM company) must be registered. Failure to register is a criminal offence.

1.62 We recommend that RTM companies should not take over regulated health and social care because of the uniquely serious consequences for vulnerable leaseholders if these services are not performed correctly, and for the RTM company in terms of action for regulatory breaches: paragraphs 10.38 to 10.43.

Insurance

1.63 On acquisition of the RTM, the RTM company becomes obliged to insure the premises. The landlord retains the right to continue insuring the premises at its own expense.

1.64 We identified the following issues with the current position:

(1) RTM companies sometimes struggle to obtain insurance due to not having sufficient and timely information about the premises' insurance history; and

(2) uncertainty as to an RTM company’s ability to claim on the insurance in the event of the building’s complete destruction, because responsibility for reinstatement is not one of the management functions transferred to the RTM company.

1.65 We have concluded that it is not appropriate for reinstatement obligations to be acquired by the RTM company. This would create significant financial risks for the RTM company, leaseholders and landlords. We are of the view that joint procurement by the RTM company and landlord is the easiest way to secure a policy with good prospects of paying out in the event of a reinstatement claim being made.

1.66 We make the following recommendations to address the issues above (paragraphs 10.77 to 10.80):

(1) the RTM company should use our recommended right to request early information, discussed above and in Chapter 9 of the Report, to obtain information about current insurance arrangements and claims history;

(2) landlords and RTM companies should seek to work together to procure suitable insurance cover in joint names. In the absence of agreement being reached, the
Tribunal should have jurisdiction to make a determination as to the insurance policy to be procured in the names of both the landlord and the RTM company. In the interim period pending the implementation of a determination, the landlord would continue to insure the premises; and

(3) the landlord should have rights to request a written summary of insurance cover placed in relation to the premises and to inspect or be sent a copy of the policy and associated documents.

Shared appurtenant property

1.67 The courts have held that an RTM company takes over the management of appurtenant property such as gardens and car parks automatically, even where the use of that appurtenant property is shared with owners or occupiers of other buildings that are not included within the RTM claim.

1.68 This causes problems from a practical perspective, including:

1.69 We have concluded that RTM companies should not automatically acquire management functions over appurtenant property shared with other buildings which are not part of the RTM claim. We recommend (paragraphs 10.130 to 10.146) that an RTM company should be able to acquire management functions over such property if the property has been specified in the claim notice, and either:

1.70 Where the Tribunal determines that the RTM company is to acquire management functions in respect of non-exclusive appurtenant property, the Tribunal may make directions as to how that property should be managed.

Lease variations

1.71 The management functions acquired by the RTM company are those in the relevant leases, and what the RTM company can do is both enabled and limited by the leases. When the RTM is acquired, the RTM company may have difficulty exercising its management functions because of the terms of the leases. For example:

(1) where service charge provisions for leases are interlinked on an estate where not all buildings are part of the RTM, this may cause problems regarding the liability for and apportionment of service charges; and
(2) where the RTM company acquires management of non-exclusive appurtenant property, lease variations may be required to set out the management and payment arrangements (alternatively, this may be done through a management agreement).

1.72 We recommend that the Tribunal should have the power to order a variation to a lease if the acquisition of the RTM makes management of premises in accordance with the leases unworkable: paragraphs 10.151 to 10.154. This applies to premises affected by the RTM, regardless of whether they are subject to the RTM or not. The variation would last only for the duration of the RTM and any party with an interest in affected premises will be able to apply to the Tribunal. We envisage that the option representing the least interference with parties’ rights and obligations should be adopted in any given case.

Uncommitted service charges

1.73 Currently, on the acquisition date, or as soon as possible afterwards, landlords are obliged to transfer to the RTM company any accrued uncommitted service charges they hold. We identified the following issues with this process:

(1) delays in RTM companies receiving the funds as there is no deadline by which they must be transferred; and

(2) shortfalls in the service charge account, caused by leaseholders being in arrears and the landlord having no obligation to recover them for the benefit of the RTM company.

1.74 We recommend that landlords should be required to transfer any uncommitted service charges to the RTM company on the acquisition date: paragraphs 10.187 to 10.203. Landlords may retain a sum required to discharge any service costs incurred up to the acquisition date which have not yet been paid. Landlords will need to evidence the costs that are outstanding to retain monies for this purpose.

1.75 To address the issues created by service charge arrears we recommend that the landlord should undertake a reconciliation of each leaseholder’s service charge contribution. The landlord would then transfer the sums that should be in the service charge pot on the assumption that the landlord has collected sufficient sums from each leaseholder to cover their share of the actual service charge expenditure incurred. The sum transferred would therefore also include any sums by which a leaseholder’s actual service charge contributions exceed their share of actual expenditure.

Management costs

1.76 RTM companies have no legal means of recovering their management costs from leaseholders. This puts them in a worse position than landlords, who are often entitled to recover such costs through the service charge. It also leaves them at risk of challenge if, as most RTM companies do currently, they recover these costs through the service charge without being entitled to do so.
1.77 We recommend that RTM companies should be permitted to recover certain prescribed costs of management as an additional service charge in circumstances where the lease does not make provision for this: paragraphs 10.204 to 10.224.

POST-ACQUISITION RIGHTS AND OBLIGATIONS (CHAPTER 11)

1.78 On the acquisition date, certain statutory rights and obligations are transferred to the RTM company, either exclusively or to be shared with the landlord. The landlord retains all other lease obligations and gains various new rights against the RTM company. The leaseholders retain all existing rights and obligations save where these relate to a management function, in which case they will be enforceable by, or against, the RTM company in place of the landlord.

1.79 Some of the issues we identified relating to obligations which transfer exclusively to the RTM company will be addressed by the training and guidance for RTM directors, which we discuss above. We also make various recommendations as summarised below.

Lease consents

1.80 Leases will invariably contain restrictions on what leaseholders can do with their premises. Some of these restrictions will amount to an outright prohibition (known as an “absolute” covenant), where leaseholders are entirely prohibited from doing something. More commonly, the lease will contain “qualified” covenants which provide that something cannot be done without the landlord’s consent.

1.81 The RTM company and the landlord both retain rights and obligations relating to lease consents for actions which require consent (for example, consent to carry out structural alterations to the premises). This shared responsibility gives rise to practical problems:

(1) leaseholders request consent from the RTM company, which should notify the landlord. If the RTM company delays notifying the landlord, this can have timing implications for the consent request;

(2) the RTM company may also not realise it is required to notify the landlord and give consent without the landlord having the opportunity to object;

(3) landlords may be served with the notice directly and give consent themselves without the RTM company being involved; and

(4) both the RTM company and the landlord may be entitled to charge a reasonable fee for granting consent to the applicant leaseholder, meaning the leaseholder may have to pay twice for the same consent.

1.82 We recommend that landlords should only have the right to receive notice of, and to object to, approvals relating to assignment, underletting, charging, parting with possession, the making of structural alterations or improvements or alterations of use. RTM companies should be under a duty to either notify the landlord of such an application (if it is minded to approve it) or refuse the application within a reasonable time and in any event within 30 days after receipt of the application. Landlords may object to such approvals being granted by the RTM company by applying to the
Tribunal for a determination within 30 days of receiving notification of the request for approval from the RTM company: paragraphs 11.3 to 11.54.

1.83 We also suggest that Government should consider clarifying that:

(1) landlords cannot charge administration fees for lease consents after the RTM has been acquired: paragraphs 11.55 to 11.63; and

(2) RTM companies are not entitled to give retrospective consents or consents in respect of absolute covenants, as these are not consents given “under” the lease: paragraphs 11.64 to 11.76.

Inclusion of landlord’s details in demands for payment

1.84 Landlords have a duty under section 47 of the Landlord and Tenant Act 1987 to provide their name and an address for service in England and Wales in any written demand for sums payable under a lease including rent, a service charge or administration charge.

1.85 There is some ambiguity as to whether section 47 also requires RTM companies to include the name and address of the landlord when giving a written demand of this kind. We recommend that RTM companies should not be required to include the landlord’s name and address in any demand for sums payable under the lease: paragraphs 11.77 to 11.91 of the Report.

COSTS AND DISPUTE RESOLUTION (CHAPTER 12)

Allocation of costs

1.86 An RTM claim necessarily involves costs for both the RTM company and the landlord (we refer to these as “non-litigation costs”). If the RTM claim is disputed by the landlord, there will also be litigation costs. Indeed, disputes subsequent to the RTM acquisition may result in litigation, and bring with them inevitable costs for both sides.

1.87 At present, the RTM company (and therefore the leaseholders) pays a significant proportion of those costs, meaning that the costs of an RTM claim can be extensive and unpredictable. Some of the shortcomings of the current law include:

(1) RTM companies currently have to pay the landlord’s reasonable costs arising out of an RTM claim notice. This may encourage landlords to conduct an overly forensic analysis of the claim to find minor defects, as they know the cost of the process is always recoverable from the RTM company;

(2) in disputes, if the Tribunal decides that the RTM company is not entitled to acquire the RTM, the RTM company is liable to pay the landlord’s reasonable costs. By contrast, the landlord is not required to pay the RTM company’s costs if the landlord unsuccessfully challenges the claim; and

(3) where a landlord is left to pay litigation costs, they can often charge them back to the leaseholders through the service charge or as an administration charge under the leases, so that the leaseholders end up paying even if they are
successful in the Tribunal. This means that leaseholders may in effect be paying to litigate against their own interests.

1.88 We recommend significant changes to the allocation of costs incurred during acquisition of the RTM and disputes:

(1) RTM companies should no longer be required to pay landlords’ non-litigation costs: paragraphs 12.72 to 12.145. This means that leaseholders will not face the uncertain prospect of covering the costs incurred by the landlord in evaluating and responding to the RTM claim. The exception to this rule is the case in which an RTM claim fails and the RTM company has acted unreasonably in proceeding with the claim; in such circumstances, the landlord will be able to recover its reasonably incurred non-litigation costs;

(2) In relation to the costs of disputes, each party should bear their own costs in any Tribunal proceeding relating to the acquisition or exercise of the RTM, subject to the Tribunal’s existing powers to alter costs awards on the basis of a party’s conduct or wasted costs: paragraphs 12.146 to 12.169. The Tribunal should also have the power to issue a restraint order in respect of RTM claims if a number of such claims are made, without any merit, in relation to the same premises: paragraphs 12.174 to 12.175; and

(3) Any term of a lease which purports to enable a landlord or manager party to the lease to recover costs incurred in litigation or otherwise as a result of the acquisition of the RTM should be unenforceable: paragraphs 12.176 to 12.188. This recommendation will not prevent RTM companies from recovering management costs or RTM-related litigation costs through the service charge.

Who decides disputes?

1.89 Currently, disputes concerning the RTM company are allocated, depending on subject matter, value, complexity and the remedy sought, to either the Tribunal, the county court, or the High Court. These different jurisdictions have different procedural and costs rules. The legal costs incurred by parties to RTM disputes may vary greatly, therefore, depending on which jurisdiction is engaged.

1.90 In order to resolve this fragmentation problem, we recommend that the Tribunal:

(1) should continue to have jurisdiction over disputes arising in the course of an RTM claim: paragraphs 12.6 to 12.23; and

(2) should be given exclusive jurisdiction to determine whether a requirement of the RTM provisions has been satisfied, whether in the course of a claim, or the exercise of management functions after a successful claim: paragraphs 12.24 to 12.38.

TERMINATION OF THE RTM (CHAPTER 13)

1.91 Over time, it may become either impossible or undesirable for the RTM company to continue to manage. Leaseholders may wish to terminate the RTM or the RTM company may become insolvent.
1.92 Key criticisms of the termination provisions that we have been told about include:

(1) there is no general right for RTM companies to apply to the Tribunal to give up management;

(2) it is unclear whether the Tribunal has jurisdiction to declare that the RTM has re-commenced where a struck off RTM company is restored to the Register of Companies;

(3) where the RTM automatically ceases under the current law, it is not always clear to whom the management reverts; and

(4) the four-year ban on further RTM claims following cessation of the RTM is excessive.

1.93 Our recommendations to address these issues include:

(1) the RTM company should be able to apply to the Tribunal if it wishes to give up the RTM, including in relation to one or more buildings in a multi-building RTM. Landlords should be able to participate in such proceedings: paragraphs 13.119 to 13.144;

(2) management functions should generally revert to whoever is responsible for exercising those functions under any leases of the premises when the RTM terminates. If that party no longer exists, management functions should transfer to the landlord: paragraphs 13.152 to 13.173;

(3) the person taking over management functions should have 90 days from the RTM ending to apply for the appointment of a manager: paragraphs 13.178 to 13.194; and

(4) landlords should have a defence to an RTM claim where the premises have been the subject of a previous RTM which terminated in the preceding two years. If the defence is raised, the RTM company could apply to the Tribunal for an order that the RTM claim should proceed in any event: paragraphs 13.216 to 13.242.