Law Commission
Reforming the law

LEASEHOLD HOME OWNERSHIP: EXERCISING THE RIGHT TO MANAGE

Summary of Consultation Paper

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RIGHT TO MANAGE CONSULTATION

INTRODUCTION

1.1 The right to manage ("RTM") was introduced in 2002[1] to give leaseholders the ability to take over the landlord's management functions in respect of their building. 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 sets out what was intended to be a simple process, beginning with the leaseholders setting up a dedicated "RTM company" to which the management functions will be transferred. However, the requirement for strict compliance with the statutory procedures can be unforgiving to leaseholders and has afforded landlords opportunities to frustrate or delay an otherwise valid claim.

1.3 We have been told by stakeholders about other problems with the existing RTM legislation, including:

(1) restrictive pre-conditions to exercising the right, such as the inability of an RTM company to manage multiple blocks on an estate, the ban on the RTM in buildings with more than 25% non-residential space, and the exclusion of leasehold houses;

(2) information about the building and management functions being provided to the RTM company too late in the process to allow them to manage effectively from the date the RTM is acquired;

(3) uncertainty as to the extent of the obligations that transfer to an RTM company, particularly in relation to property such as gardens and car parks shared with other buildings; and

(4) concerns about the adequacy and validity of the insurance taken out by RTM companies.

1.4 The Ministry of Housing, Communities and Local Government ("MHCLG") has asked the Law Commission to conduct a broad review of the existing RTM legislation with a view to improving it.

RESPONDING TO OUR CONSULTATION

1.5 This document summarises a longer consultation paper,[2] which sets out in detail the current law and our provisional proposals for reform designed to make the RTM procedure simpler, quicker and more flexible, particularly for leaseholders. References to chapters in this summary are to chapters of the consultation paper.

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[1] By the Commonhold and Leasehold Reform Act 2002.

[2] The consultation paper is available online at https://www.lawcom.gov.uk/project/right-to-manage/.

1.6 We invite responses to our consultation questions which are set out in full at the end of the consultation paper. They are also available in a separate document on our website. The deadline for responses is 30 April 2019.

1.7 We are keen to receive comments from as many stakeholders as possible, whether they agree or disagree with our provisional proposals. These views will be carefully considered and taken into account when forming our final recommendations, which will be published in a subsequent report.

1.8 You do not have to respond to every question.

1.9 Comments may be sent to us using the online response form, which can be accessed at https://www.lawcom.gov.uk/project/right-to-manage/. Where possible, it would be helpful if this form was used.

1.10 Alternatively, comments may be sent:

(1) by email to RTM@lawcommission.gov.uk; or

(2) by post to RTM Team, Law Commission, 1st Floor, Tower, 52 Queen Anne's Gate, London, SW1H 9AG.

1.11 Our website also includes a short survey which we invite individual leaseholders and RTM company directors to complete in order to share with us their experiences of the RTM process.

1.12 For further information about how the Law Commission conducts its consultations, and our policy on the confidentiality of consultees' responses, please see page iii of the Consultation Paper.

QUALIFYING CRITERIA FOR PREMISES (CHAPTER 2)

1.13 The RTM can only be claimed in respect of premises which satisfy certain criteria.[3] These consist of:

(1) a self-contained building or part of a building;

(2) which contains at least two flats held by "qualifying tenants" (broadly speaking, these are leaseholders with leases of more than 21 years); and

(3) where qualifying tenants hold at least two-thirds of the total number of flats in the building or part of the building.

Current law and criticisms

1.14 The current qualifying criteria for premises are problematic in the following ways:

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[3] Commonhold and Leasehold Reform Act 2002, s 72(1).

(1) the requirement for at least two flats to be held by qualifying tenants excludes leasehold houses, as well as mixed commercial-residential premises such as a building with a shop on the ground floor and a flat upstairs;

(2) they require premises to be a "self-contained" building, or part of a building. This has generated a great deal of litigation requiring expert evidence on whether any attachment between the building or part of a building and something else means it is not self-contained;

(3) the criteria were copied over from the collective enfranchisement legislation, despite the fact that different policy considerations apply to enfranchisement and the RTM. Some requirements, such as a "self-contained part" of a building needing to be a "vertical division" are used in collective enfranchisement to protect freehold title and avoid "flying freeholds". This is not a concern in RTM;

(4) leaseholders are unable to acquire the RTM where the majority, but less than two-thirds, of flats in the building are held by qualifying tenants; and

(5) premises with non-residential parts of more than 25% are excluded from the RTM. This leads to legal challenges over floor measurements, and arbitrarily excludes certain buildings from the RTM regime.

Proposals for reform

1.15 In response to these problems, we:

(1) Provisionally propose to extend the RTM to leasehold houses by adopting the concept of a "residential unit", as recommended in our enfranchisement consultation paper.[4]

(2) Ask consultees whether they prefer either:

(a) to expand the definition of "building" to include all structures with a degree of permanence, which form part of, and change the physical character of, the land; or

(b) to retain the existing requirements for a self-contained building or part of a building, but give the tribunal discretion to waive non-compliance where the acquisition of the RTM is not reasonably expected to cause particular practical problems for any interested party.

(3) Ask whether the requirement for at least two-thirds of the flats in the premises to be held by qualifying tenants should be reduced to 50%. This would bring more buildings within the scope of the RTM. It would remain the case that the number of qualifying tenants who become members of the RTM company must be equal to at least half of all the flats in the premises.[5]

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[4] Leasehold home ownership: buying your freehold or extending your lease (2018) Law Commission Consultation Paper No 238, para 8.41.

[5] Commonhold and Leasehold Reform Act 2002, s 79(5).

(4) Provisionally propose to abolish the requirement for a minimum of two residential units held by qualifying tenants. This will allow qualifying tenants to acquire the RTM by themselves in a building where there are no other residential premises or one other flat which does not qualify for the RTM.

(5) Provisionally propose that the exemption for properties with non-residential premises of 25% or more should be removed, replacing it with a requirement that RTM companies must instruct professional managing agents where there are commercial premises of 25% or more of the internal floor area.

QUALIFYING CRITERIA FOR LEASES (CHAPTER 3)

1.16 The legislation sets out certain criteria which must be satisfied in order for the RTM to be exercised. The criteria concern the nature of the leaseholder's lease, the nature of the landlord, and the use of the premises.

Nature of the lease

1.17 The RTM can only be claimed by a "qualifying tenant", being a leaseholder under a long lease.[6] Broadly speaking, this is a lease granted for more than 21 years.

Shared ownership

1.18 The only element of the definition of "long lease" that we provisionally propose should be amended is how it applies in the context of shared ownership leases.

1.19 Shared ownership leases are defined in the Commonhold and Leasehold Reform Act 2002 ("2002 Act").[7] Shared ownership leaseholders usually purchase a minimum stake of 25% of the value of the leasehold property and can subsequently purchase further shares of a set percentage up to 100%, a process known as "staircasing".

1.20 The implication under the 2002 Act[8] is that a shared ownership lease of a flat where the leaseholder has not staircased to 100% is not a long lease and thus would not qualify for the RTM. However, conflicting decisions in the High Court and the Upper Tribunal have led to significant confusion on this point.

1.21 We understand from stakeholders that, in practice, shared ownership leaseholders are perceived to be qualifying tenants for the RTM by all parties involved. Stakeholders have reported extensive examples of shared ownership leaseholders who have not staircased to 100% participating in the RTM. We are not aware of any issues which have arisen in RTM as a consequence of their shared ownership status.

1.22 Furthermore, shared ownership leaseholders are responsible for 100% of the service charges for the property and common parts, despite "owning" only a share, so we think that they should have the right to participate in the RTM.

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6 Commonhold and Leasehold Reform Act 2002, s 75.

7 Commonhold and Leasehold Reform Act 2002, s 76.

8 Commonhold and Leasehold Reform Act 2002, s 76(2)(e).

1.23 For these reasons, we propose that shared ownership leaseholders who have long residential leases should be qualifying tenants for the purposes of the RTM, whether or not they have staircased to 100%.

Types of landlord

1.24 Resident landlord: In some circumstances, the fact that the landlord is living in the building prevents the leaseholders from exercising the RTM. A few stakeholders told us that it is unfair for leaseholders to be deprived of the right to have a say in the management of the building for which they pay service charges just because the landlord also lives there. We provisionally propose that the "resident landlord" exemption be removed.

1.25 Multiple freeholders: Where parts of a building are owned by different freeholders and one of the parts is self-contained, then the building as a whole cannot currently be subject to the RTM.[9] However, leaseholders can still apply for the RTM of the self-contained part or parts of the building.[10] We provisionally propose that this restriction should be removed, so that the entire building could be managed together, by one RTM company. We also propose that the tribunal[11] should have a power to reconcile any conflicting or diverging provisions in the different leases.

1.26 National Trust: National Trust property is not exempted from the RTM under the 2002 Act. We have been told by the National Trust that, in practice, the flats they let on long leases form part of buildings which do not qualify for the RTM. However, National Trust leasehold houses are likely to qualify if the RTM were to be extended to houses. The National Trust was concerned that the RTM could allow leaseholders to become responsible for shared appurtenant property such as listed parks and conservation areas, which they would not be in a position to maintain. We therefore provisionally propose that National Trust properties should be exempted from the RTM.

Use of premises

Business tenancies

1.27 Business tenancies such as work/live units do not qualify for the RTM under the 2002 Act. However, the exclusion is not tightly drafted and is defined as per the Landlord and Tenant Act 1954. There, a tenancy is a "business tenancy" only if business is being carried on by the tenant (as opposed to anyone else). It is quite easy to circumvent the exclusion by subletting the property on a short lease to a third party (who can be connected to the tenant) to carry on the business use. We propose removing this exclusion, to be replaced with an exclusion for leases which prohibit residential use.

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9 Commonhold and Leasehold Reform Act 2002, sch 6, para 2.

10 Tanfield Chambers, *Service Charges and Management* (4th ed 2018) para 25-12.

11 By which we mean the First-Tier Tribunal (Property Chamber) in England, and the Residential Property Tribunal Wales in Wales.

RTM ON ESTATES (CHAPTER 4)

Multi-building RTM

1.28 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 pay into the same service charge fund or share appurtenant property such as gardens or car parks.[12]

1.29 We have been told by stakeholders that an estate could be more effectively managed as a whole, rather than as separate buildings or parts of buildings.

1.30 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 a larger block to "out-vote" a smaller block and prioritise its own building.[13] 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.

1.31 However, 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. We provisionally propose that the law should allow for the RTM to be acquired over two or more buildings where the leaseholders in those buildings:

(1) contribute to a common service charge; and/or

(2) share the use of the same appurtenant property such as gardens or car parks.

1.32 We make provisional proposals for a "flexible model", allowing any combination of such 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 the estate.

1.33 Our provisional proposal, 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

1.34 There is a question of how the qualifying and participation criteria should apply in the context of multi-building RTM: should the criteria have to be satisfied by each building included in the claim, or should it be applied as a whole across all of the buildings? We propose that both the qualifying criteria and the participation criteria should be met by each individual building. 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.

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12 This is the result of a 2015 Court of Appeal decision, *Ninety Broomfield Road RTM Co Ltd v Triplerose Ltd* [2015] EWCA Civ 282, [2016] 1 WLR 275.

13 *Ninety Broomfield Road RTM Co Ltd v Triplerose Ltd* [2015] EWCA Civ 282, [2016] 1 WLR 275 at [52] to [54].

Freedom to join or leave an RTM at a later date

1.35 We have considered whether the leaseholders in a building not originally included in a multi-building RTM claim should be able to join in the existing RTM arrangements at a later date. While we see no issue with this where the RTM company and the leaseholders in an excluded building both agree to the addition, we do not think the leaseholders in an excluded building should have a right to join if the RTM company does not agree.

1.36 We also consider the opposite question: should it 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? We provisionally propose that it should be possible to break away in this way, subject to the expiry of a minimum period of time following the acquisition date of the original multi-building RTM.

Voting rights

1.37 There is a question about whether voting rights in a multi-building RTM company should operate in the same way as for single buildings. As mentioned above, there is some concern that larger blocks could dominate decisions to the detriment of any smaller blocks. However, we consider that any variable or weighted votes for multi-building RTMs would lead to unjustified additional complexity and cost, and do not make any proposals for special voting arrangements.

Shared appurtenant property

1.38 Under the current law, an RTM company takes over the management of appurtenant property automatically, even where that appurtenant property is shared with other buildings that are not included within the RTM claim.[14]

1.39 This causes problems from a practical perspective.

(1) Multiple parties may be responsible for management of the shared appurtenant property, which can lead to duplication of effort and potentially higher costs for leaseholders. It could also result in under-management or non-management of the appurtenant property.

(2) Because the management of appurtenant property transfers automatically, RTM companies may not know what appurtenant property there is, or that they are responsible for managing it. The issue of who is responsible for the appurtenant property may not even be considered until an issue arises years into the future.

1.40 We think that management of appurtenant property which is exclusive to the building or buildings claiming the RTM should always be transferred to the RTM company when the RTM is acquired.

1.41 In relation to appurtenant property shared with other buildings which are not part of the RTM claim, we do not think that it should transfer automatically. We think management of that shared appurtenant property should remain with the landlord

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[14] See *Gala Unity Ltd v Ariadne Road RTM Co Ltd* [2012] EWCA Civ 1372, [2013] 1 WLR 988 and subsequent cases.

unless the parties agree an alternative arrangement, or the tribunal makes a determination that some other arrangement should apply (on application by the RTM company).

THE RTM COMPANY (CHAPTER 5)

1.42 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 (which set out how the company is governed).

1.43 Every qualifying tenant is entitled to become a member of the RTM company. The company will also require directors, who may be qualifying tenants or third parties. The RTM company, and its directors, are subject to existing company law including directors' duties.

Current law and criticisms

1.44 We have identified the following issues with the current law:

(1) the incorporation process is sometimes abused by third parties, such as some landlords and managing agents, who set up "bogus" RTM companies for their own purposes. Some landlords establish RTM companies to try to prevent leaseholders from doing so. Some managing agents establish companies to pressure leaseholders into acquiring the RTM, and then appointing them as the managing agent for the premises;

(2) RTM company members often struggle to participate in company decision-making, because there is no requirement for company directors to hold annual general meetings ("AGMs");

(3) RTM directors often have insufficient knowledge about their responsibilities. The educational resources that currently exist are often cost-prohibitive or inadequately detailed. The lack of knowledge of directors is most apparent in relation to large blocks; and

(4) 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.

Proposals for reform

1.45 We address these problems by making the following provisional proposals:

(1) preventing "bogus" RTM companies by 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. Instead, once an RTM company has served a claim notice for a set of premises, no other RTM company could do so until the claim has been withdrawn or rejected by the tribunal or the RTM, having been acquired, has ceased;

(2) ensuring RTM company members can participate in company decision-making by introducing a rule that company directors must hold AGMs;

(3) encouraging prospective RTM company directors to undertake free training on the RTM regime and their obligations under it; and

(4) allowing RTM companies to recover their reasonable management costs from leaseholders as part of the service charge, as if the lease expressly allowed for this.

1.46 MHCLG is currently undertaking work to set professional standards for managing agents.[15] In this context, we also seek consultees' views on whether it should ever be mandatory for RTM companies to use a managing agent which meets the regulatory standards to be set by MHCLG. Possible circumstances that we suggest could trigger such a requirement are: the proportion of commercial property within the premises, the size of the premises, and the premises having special characteristics, such as being a listed building.

ACQUIRING THE RTM – NOTICES (CHAPTER 6)

1.47 To acquire the RTM a number of steps must be taken:

(1) The leaseholders must set up an RTM company.

(2) The RTM company must then:

(a) serve a notice inviting participation on the qualifying tenants who are not already members of the RTM company;[16] and then

(b) serve a claim notice on any landlords or other relevant third parties, provided that it has the requisite level of membership.[17] 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 disputing the claim. If this occurs, the RTM company must apply to the tribunal to acquire the RTM. 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.[18]

Notice inviting participation

1.48 The notice inviting participation is intended to ensure that qualifying tenants are given the opportunity to join the RTM company before the start of the RTM process. We understand that many RTM companies make efforts to identify qualifying tenants and persuade them to join the company and that they would do this in any case. Qualifying

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15 Ministry of Housing, Communities & Local Government, *Protecting consumers in the letting and managing agent market* (April 2018) p 7. Available at: https://www.gov.uk/government/consultations/protecting-consumers-in-the-letting-and-managing-agent-market-call-for-evidence.

16 Commonhold and Leasehold Reform Act 2002, s 78(1).

17 Commonhold and Leasehold Reform Act 2002, s 79.

18 Commonhold and Leasehold Reform Act 2002, s 90(2).

tenants already have an unfettered right to join the RTM company at any time. The notice inviting participation may therefore be of limited use to leaseholders – but any mistakes made by the RTM company may be used by landlords to challenge the RTM claim.

1.49 We therefore provisionally propose to abolish the requirement to serve a notice of invitation to participate. To ensure that qualifying tenants are aware of their right to join the RTM company, we propose that the prescribed notes accompanying the claim notice should include a statement to this effect.

Counter-notice

1.50 The RTM company must serve a claim notice, asserting its intention to acquire the RTM. Where the landlord (or relevant third party) does not serve a counter-notice, there is deemed to be no dispute about the entitlement of the RTM company to acquire the RTM.[19] The RTM company acquires the RTM on the date specified in the claim notice. However, there is then no obvious venue for determining whether a claim is valid, and no protection from challenges to the RTM made in the future. We therefore provisionally propose that where no counter-notice has been served, the RTM company may apply to the tribunal asking it to determine:

(1) that the RTM is capable of being acquired;

(2) the date on which the RTM will be, or was, acquired; and

(3) any special arrangements for the management of non-exclusive appurtenant property.

Simplifying the notices

1.51 The form and content of claim notices are set out in regulations.[20] We have been told by stakeholders that some landlords seize on small and relatively insignificant errors made in notices by RTM companies to attempt to defeat RTM claims. We consider that the following changes to the law would help to deal with this:

(1) giving a discretion to the tribunal to waive any requirement or allow a notice to be amended to fix an error;

(2) reducing the grounds on which a notice can be challenged;

(3) providing that a signature from a single officer of the RTM company will be sufficient for the signature of notices;

(4) allowing the prescribed notices to be given by email, to certain categories of email address;

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[19] Commonhold and Leasehold Reform Act 2002, s 90(3).

[20] Commonhold and Leasehold Reform Act 2002, ss 80(8) and (9); Right to Manage (Prescribed Particulars and Forms) (England) Regulations 2010/825; Right to Manage (Prescribed Particulars and Forms) (Wales) Regulations 2011/2684.

(5) deeming a claim notice to have been validly served on the landlord if it is sent or delivered to:

    (a) an address specifically provided for the service of RTM notices, or the landlord's current address; or

    (b) the landlord's last known address, an address given under sections 47 and 48 of the Landlord and Tenant Act 1987 or the latest email address given for serving notices generally, plus the landlord's address for service listed at HM Land Registry; and

(6) reducing the circumstances in which a claim notice is deemed to be withdrawn, instead empowering landlords to apply to strike out a claim notice where the RTM company has not initiated the next step in the process.

Pre-service checks

1.52 Under our proposals, an RTM claim notice served at a designated address will be deemed to have been validly served, whether or not it is actually received. Consequently, we suggest that RTM companies should be required to undertake pre-service checks (including searching HM Land Registry) to ascertain the most appropriate address at which to serve the claim notice. We made the same proposals in our enfranchisement consultation paper.

Missing landlords

1.53 Where the identity of the landlord is known, but no address can be found at which to serve an RTM claim notice, or where the landlord is unknown, we provisionally propose that the RTM company should conduct certain pre-service checks. As in enfranchisement, we also provisionally propose that they should place an advertisement in the London Gazette before applying to the tribunal for a determination as to whether the RTM can be acquired.

THE ACQUISITION DATE AND INFORMATION (CHAPTER 7)

The acquisition date

1.54 Ideally, the RTM company would acquire the RTM at a convenient point in the annual service charge cycle to promote good management. That is likely to be either:

(1) at the end of a service charge year – so as to align a transfer of management functions with the end of an accounting period; or

(2) if the RTM is to be acquired during a service charge year, shortly before a service charge payment falls due under the leases – so as to ensure that the RTM company receives money to fund its management.

1.55 Where the date specified in the claim notice is not one of the two dates identified above, the RTM company is likely to require an advance from its members to fund initial expenditure. We consider that this is undesirable, but do not propose to enshrine mandatory dates in statute as they may not be the best dates in every case.

1.56 We do however make some proposals for reform. Currently, where a negative counter-notice is served but it is subsequently agreed or determined that the RTM company is entitled to acquire the RTM, the acquisition date is three months after:

(1) the day the counter-notice was replaced by the acceptance; or

(2) the date on which the determination becomes final.[21]

1.57 We provisionally propose to change these set three-month periods into minimum three-month periods. We think that the RTM company should have the right to apply to the tribunal to vary the original acquisition date specified in the claim if it subsequently proves inadequate.

1.58 Under the current law, a failure to include the acquisition date in the claim notice renders the claim notice invalid. Our above proposals to limit the grounds on which a claim notice can be challenged would change this. We therefore provisionally propose that, if the RTM company failed to specify the acquisition date, either party could apply to the tribunal for a determination of the acquisition date.

Right to information

1.59 Before it serves a claim notice, an RTM company is entitled to request from any person any information which it needs to be able to complete the claim notice, which is a fairly limited category.[22] The RTM company also has a broader right to request from the landlord any information which it might reasonably require in connection with exercising the RTM. Although the RTM company can make the request at any time, the landlord is not obliged to provide the information until the acquisition date.[23]

1.60 We have identified several problems with the provision of information.

(1) Information about the management functions is not shared early enough in the RTM process to be of any use. RTM companies often do not have information which they require to carry out their management functions properly, or even to decide whether they want to exercise the RTM in the first place.

(2) The right to information is 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.

(3) The information provided often does not deal properly with shared appurtenant property and services.

Our proposed reform: a new “information notice”

1.61 We provisionally propose that a new “information notice” be introduced. It would be a prescribed form, listing certain types of information, such as the insurance claims history, which the RTM company requests from the landlord.

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21 Commonhold and Leasehold Reform Act 2002, ss 90(5) and (4).

22 Commonhold and Leasehold Reform Act 2002, s 82.

23 Commonhold and Leasehold Reform Act 2002, s 93(3).

1.62 We also propose that the information notice should request information about the management functions actually carried out at the premises. Management functions can be divided into three categories:

(1) Category 1 – Functions which relate to the premises over which RTM is claimed and any appurtenant property exclusive to the premises. These transfer to the RTM company automatically when the RTM is acquired.

(2) Category 2 – Functions which relate to non-qualifying premises, such as short let flats retained by the landlord. These remain with the landlord.

(3) Category 3 – Functions which relate to non-exclusive appurtenant property such as a garden shared by two blocks. Under our proposals discussed above, these functions would be presumed to remain with the landlord unless there is an agreement or tribunal order to the contrary.

1.63 We envisage the information notice asking for information about each category.

1.64 We ask consultees whether the RTM company should be entitled to receive the management information before it is determined that the RTM company is entitled to acquire the RTM. While it would be useful in many cases, we also note that, if the RTM is not ultimately acquired, then either or both parties may have incurred wasted costs in the provision of information. We consider which party should cover the landlord's costs in Chapter 10.

1.65 If consultees wish the provision of information to be brought to an earlier point, we ask how this should work. We consider but reject the idea of a mandatory information notice, served before the claim notice. This would add time and cost to the process, and in cases of fairly straightforward premises where the RTM company is well-informed, it may be an unnecessary step. Although we think that, in the majority of cases, RTM companies would benefit from receiving management information from the landlord, we do not consider that they should be required by law to ask for it.

1.66 We outline two possible processes for optional information notices:

(1) Option 1: the RTM company could elect to serve an information notice along with the claim notice. The landlord would be required to provide the information notice along with the counter-notice (whether or not the landlord accepted the RTM company's right to acquire the RTM). However, the RTM company would not have had the benefit of the information before serving the claim notice. This would mean that the RTM company had not had the option of receiving the category 3 information about non-exclusive appurtenant property in advance of making the claim. It may not therefore be in a position to make a request for the management of that non-exclusive appurtenant property in the claim notice (although it could do so at a later point).

(2) Option 2: the RTM company could elect to serve an early information notice in advance of the claim notice, and the landlord would be required to provide the information within a set period of time. This could assist RTM companies seeking to exercise the RTM over more complex properties where there is more likely to be, for example, shared appurtenant property. If the RTM company did

not choose to serve an early information notice, it could still request the information along with the claim notice, as in option 1.

1.67 We propose that there be either a 28-day limit for landlords to provide the required information, with an extension possible in exceptional circumstances, or a 60-day limit with no possibility of extension. The landlord could be fined for failing to provide the information.

1.68 It is possible that the date the information is provided and the acquisition date will be months apart. The information provided may have become outdated in the meantime. We therefore propose that the landlord be under a duty to:

(1) notify the RTM company of any material changes to the information previously provided; and

(2) confirm, on the acquisition date, that there are no material changes which have not been notified.

Notices relating to management contracts

1.69 The 2002 Act prescribes a procedure for the landlord to notify both the RTM company of the existing management contracts and the contractors to be notified of the impending RTM acquisition.[24]

1.70 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. This is a particular issue where there are fixed-term contracts or contracts with long notice periods in place. It may not be clear whether the contract has been terminated automatically or not, or what compensation may be payable to the contractor.[25]

1.71 As a matter of law, an RTM company is not liable under, or bound by, any contracts made by the landlord prior to the acquisition of the RTM.

1.72 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 time to consider their options.

1.73 To address these issues, we propose a more transparent and timely system for dealing with management contracts, with each stage to be completed within prescribed periods before the acquisition date.

(1) The landlord should send the following prescribed information as part of the information notice:

(a) a list of all the management contracts and contractors, with contact details; and

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[24] Commonhold and Leasehold Reform Act 2002, ss 91 and 92.

[25] As we discuss in Chapter 7 of the consultation paper, this in part depends on whether the contract would be “breached” or “frustrated” in law.

(b) a copy of the contracts or details (including terms) of the management contracts, the cost and the notice period, if any.

(2) At the same time, the landlord should serve notice on contractors, in line with the current process, except that the notice should also state that the contract will terminate on the acquisition date unless the RTM company and contractor agree otherwise.

(3) The RTM company should then commence negotiations either with existing contractors for new contracts or with other contractors to ensure continuity of service.

(4) The RTM company should respond to the landlord identifying which contractors it does not wish to maintain a contractual relationship with.

(5) The landlord should then notify:

(a) those contractors which the RTM company does not wish to maintain a relationship with that their services shall not be required from the acquisition date; and

(b) the remaining contractors that the RTM company has indicated a preference to maintain a contractual relationship with them, but that the contract as between the landlord and the contractor shall terminate from the acquisition date.

Management contracts and employment rights

1.74 The Transfer of Undertakings (Protection of Employment) Regulations 2006[26] ("TUPE") may apply to contractors who are directly employed by the landlord, such as resident caretakers. TUPE sets out rules for preserving the rights of employees on the transfer of an undertaking by which they are employed, so that the employees may be transferred to the new undertaking if TUPE applies. The application of TUPE would have various implications for both the acquisition process and the ability of the RTM company to terminate or vary the terms of the employment following the acquisition date.

1.75 We invite consultees to share their experiences of TUPE and landlord's employees' rights in the context of the RTM with us, to help determine whether this is a prevalent issue and whether we could or should offer further guidance. We also ask whether consultees have experience of a caretaker or other employee of the landlord having a right to occupy a flat in the building.

MANAGEMENT FUNCTIONS (CHAPTER 8)

1.76 The RTM company acquires the "management functions" under the relevant leases, being functions relating to services, repairs, maintenance, improvements, insurance and management.[27] Importantly, the RTM company can only acquire functions which

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26 SI 2006 No 246.

27 Commonhold and Leasehold Reform Act 2002, s 96(5).

the lease permits the landlord to undertake. For example, if the lease does not contain an express power for the landlord to carry out improvement works, the RTM company cannot do so as a matter of law.

1.77 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.[28]

Regulated activities

1.78 In relation to retirement accommodation, it is possible that an RTM company may become responsible for providing "regulated activities" to leaseholders, such as personal care or transport services. These services are governed by the Care Quality Commission, with which the services provider (ie the RTM company) must be registered. Failure to register is a criminal offence.

1.79 There is a risk that RTM companies will not have the knowledge or resources to provide these services adequately. As well as the RTM company facing action for regulatory breaches, the potential consequences to vulnerable leaseholders of sub-standard provision are serious, and could be fatal.

1.80 We ask whether such regulated activities, such as the provision of care or any other services, ought to be excluded from the definition of "management functions", so that they do not transfer to the RTM company. Any exclusion would only relate to the regulated activity and not otherwise to general management of the building.

Insurance

1.81 Currently, 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.

1.82 We have identified the following issues with the current law:

(1) RTM companies struggle to obtain insurance because they have no credit history to enable them to get a competitive deal, and do not acquire sufficient and timely information about the premises' insurance history.

(2) Landlords often cancel the existing insurance policy as soon as the RTM is acquired, leaving the RTM company to obtain expensive insurance at the last minute, without possessing the service charge funds to cover the cost.

(3) Some RTM companies under-insure the premises, either in an attempt to lower the service charge, or because they have failed to undertake regular insurance valuations to ensure coverage is sufficient.

(4) It is not clear that the RTM company is obliged to rebuild the premises in the event it is destroyed rather than merely damaged. This could lead to technical arguments under insurance law about the right of the RTM company to claim on the insurance in the event of the building's destruction, because of the

[28] Commonhold and Leasehold Reform Act 2002, s 97(2).

requirement for the policyholder to have an "insurable interest" and to be able to demonstrate actual loss.

1.83 We make the following provisional proposals:

(1) The RTM company should be given the current insurance policy, the insurance claims history and a copy of the last reinstatement valuation as part of the documentation provided by the landlord to the RTM company before acquisition of the RTM.

(2) The landlord should be entitled to request a copy of any insurance contract entered into by the RTM company in respect of the premises, to be provided within 21 days of the request.

(3) The legislation should be clarified so that the management functions transferred to the RTM company include reinstatement, provided that the landlord is so obliged under the lease.

(4) The landlord should be able to apply to the tribunal for a determination that the RTM company has under-insured, and the tribunal should have the power to:

(a) direct that top-up insurance costs be recoverable from the RTM company/leaseholders as a service charge; and/or

(b) make directions that the RTM company, in future, must procure insurance that satisfies particular criteria.

Uncommitted service charges

1.84 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 have 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 the arrears and pass them on to the RTM company.

1.85 We provisionally propose the following solutions:

(1) obliging the landlord to pay the RTM company 50% of the estimated accrued uncommitted service charges by the acquisition date, with the remainder payable within six months of the acquisition date; and

(2) requiring the landlord to use reasonable endeavours to pursue service charge arrears accrued prior to the acquisition date, and to pay any funds recovered to the RTM company.

POST-ACQUISITION RIGHTS AND OBLIGATIONS (CHAPTER 9)

1.86 On the acquisition date, certain statutory landlord rights and obligations are transferred to the RTM company, either exclusively or to be shared with the landlord.[29] These include, for example, the obligation to hold service charge funds on trust, and obligations to repair defective premises. The landlord retains all other lease obligations and gains various new rights against the RTM company.[30] 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.

1.87 Some of the issues we identify relating to obligations which transfer exclusively to the RTM company we hope will be addressed by the improved training and education for RTM directors, which we discuss above.

1.88 We make a proposal to clarify a current uncertainty in the law, to ensure that the RTM company is only required to provide its own contact address on a service charge demand, and not that of the landlord.

Lease consents

1.89 A particularly problematic issue we have identified is that the RTM company and the landlord both retain rights and obligations relating to lease consents (for example, consent to carry out structural alterations to the premises, keep a pet or sublet the premises). This shared responsibility gives rise to practical problems:

(1) At present, leaseholders request consent from the RTM company, which has to notify the landlord of the request and allow prescribed periods of time for landlord objections. 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) Equally, landlords may be served with the notice directly and give consent themselves without the RTM company being involved.

(4) Both the RTM company and the landlord may be entitled to charge a reasonable fee for granting consent to the applicant leaseholder,[31] meaning the leaseholder may have to pay twice for the same consent.

1.90 We ask whether some of the delays and confusion could be minimised and set out two possible options. The RTM company and landlord could instruct a joint adviser to reduce the costs. Alternatively, the current procedure could be reformed to make it more efficient, either by the leaseholder serving the application for consent on both

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29 Commonhold and Leasehold Reform Act 2002, ss 98 to 103; sch 7.

30 Commonhold and Leasehold Reform Act 2002, sch 7.

31 Commonhold and Leasehold Reform Act 2002, s 158 and sch 11, para 2; and sch 7, para 16.

the RTM company and the landlord, or the RTM company being obliged to pass the application to the landlord within a set time.

DISPUTE RESOLUTION AND COSTS (CHAPTER 10)

1.91 The exercise of the RTM necessarily incurs up-front costs for the RTM company and, in many cases, the landlord. Where the RTM claim is contested by the landlord, there may also be litigation costs. Once the RTM has been acquired, the RTM company, landlord and leaseholders have reciprocal rights and obligations owed by and to each other. If things go wrong, this can lead to disputes.

1.92 Currently, disputes concerning the RTM company are allocated to the tribunal, the county court or the High Court, depending on subject matter, value, complexity and the remedy sought. Partly as a result of this fragmented allocation of jurisdictions, there is no consistency as to the rights and liabilities of the RTM company as regards legal costs.

1.93 The current law is problematic in the following ways:

(1) There is a divided jurisdiction over disputes, with responsibility for different issues split between the tribunal and the courts. This creates complexity for the parties and is likely to increase costs.

(2) Landlords have a general right to recover all reasonable costs arising out of an RTM claim notice. This may encourage them to conduct a forensic analysis of the claim to find minor defects, as they know the cost of the process is always recoverable from the RTM company.

(3) Landlords currently benefit from qualified one-way costs shifting. This means that, 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.[32] By contrast, the landlord is not required to pay the RTM company's costs where the landlord unsuccessfully challenges the claim. This is unusual in civil litigation, particularly given that in this situation it operates in favour of the party which is generally more powerful and better resourced.

(4) To prevent landlords from recovering their litigation costs through the service charge, leaseholders must apply for an order under section 20C of the Landlord and Tenant Act 1985. This relies on leaseholders being aware of the need to make an application, which is often not the case.

Proposals for reform

1.94 We explore possible options for change.

(1) We provisionally propose giving the tribunal exclusive jurisdiction over disputes arising from the RTM provisions, and in respect of the enforcement of such decisions.

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[32] Commonhold and Leasehold Reform Act 2002, s 88(3).

(2) We ask consultees whether mediation or arbitration might be helpful at any stage of the RTM process in relation to any issue, pre- or post-acquisition of the RTM (for example, to agree the division of management of shared appurtenant property), in order to avoid disputes in the court or tribunal.

(3) We ask whether the RTM company should continue to make any contribution at all to the landlord's costs and, if so, how this could be limited (for example, by fixed or capped contributions). We give the example of a fixed sum for each residential unit over which the RTM is being exercised. Such a regime could operate so that, as the number of residential units increased, the fixed sum per unit would decrease (for example, £50 per unit for the first 10 units, and £30 for the next 10 units). This would recognise that landlords incur legitimate costs in providing information to RTM companies and otherwise dealing with an RTM claim, but would prevent them taking advantage by inflating their expenses.

(4) We propose that each party should bear their own costs of litigation, unless there has been unreasonable behaviour or wasted costs on either side. This would give the parties the power to determine how much they are willing to spend on the claim and any disputes arising from it. It would also lessen the impact on RTM companies of landlords choosing expensive lawyers and making technical objections.

(5) We propose that there should be a presumption in favour of an order under section 20C of the Landlord and Tenant Act 1985 to prevent landlords recovering their litigation costs from leaseholders through the service charge.

TERMINATION OF THE RTM (CHAPTER 11)

1.95 Over time, it may become either impossible or undesirable for the RTM company to continue to manage. The RTM may wish to terminate because, for example, leaseholders' successors in title do not have the same level of enthusiasm for the RTM and the responsibilities it entails, or because the RTM company becomes insolvent.

Current law and criticisms

1.96 Much of the publicity and criticism of the RTM relates to the acquisition process, and there has typically been less of a focus on the current termination provisions. We have been told about the following criticisms of the termination provisions:

(1) Some stakeholders representing landlord or managing agent interests have suggested that the RTM should terminate where membership of the RTM company falls below 50% of the qualifying tenants.

(2) Others told us that there are not enough rights for a landlord to step in to remove an RTM company where it is failing. A landlord can apply to the tribunal for a manager to be appointed under the Part 2 of the Landlord and Tenant Act 1987, but have no standalone right to apply to take management back themselves.

(3) RTM companies have limited options as to how they can give up management if the landlord does not agree to take it back. There is no general right for RTM companies to apply to the tribunal to give up management.

(4) There is some doubt as to whether the tribunal has the jurisdiction to declare that the RTM has re-commenced where an RTM company which had been struck off the Register of Companies is restored to the register.

(5) There are certain circumstances in which the RTM will automatically cease under the current law. It is not always clear to whom the management reverts on the occurrence of one of these events.

(6) Where the RTM has ceased to be exercisable by the RTM company, there can be no further RTM claim over those premises for a period of four years. The tribunal has jurisdiction to determine that the four-year ban does not apply where it considers it would be unreasonable for it to apply.[33] Some leaseholder stakeholders have told us that four years is too long. While the tribunal can disapply the four-year ban in some circumstances, leaseholders see this process as unnecessarily expensive and burdensome.

Proposals for reform

1.97 On balance, we do not consider that the RTM company should have to prove periodically that it meets a set threshold for leaseholder membership. However, we provisionally propose that, if the landlord or any leaseholder makes an application to appoint a manager due to poor management by the RTM company,[34] the tribunal should take into account whether or not the RTM company remains supported by a majority of leaseholders as members.

1.98 In any case of termination, we believe that there should be express provision as to who becomes responsible for management post-termination. We think that, unless the issue is agreed between the parties or determined by tribunal, the default position should be that management reverts to the party who is responsible for management functions under the lease. If that person no longer exists, the management functions should generally revert to the landlord.

1.99 We propose some amendments to the detail of some of the existing grounds for termination of the RTM. The main amendments are:

(1) Where an agreement between the RTM company and the landlord to terminate the RTM does not have the support of all the qualifying tenants, the agreement should have to be approved by the tribunal. This is to protect the interests of minority leaseholders. The tribunal should approve the agreement if it is satisfied that leaseholders will be able to enforce performance of the management functions in the leases against the party proposed to be responsible for management functions.

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[33] Commonhold and Leasehold Reform Act 2002, sch 6, paras 5(1)(b) and 5(3).

[34] Under Part 2 of the Landlord and Tenant Act 1987.

(2) Where an application for restoration to the Register of Companies is made within 30 days of a strike off taking effect, the RTM company, once restored, should be able to apply to the tribunal to have the management functions restored to it.

(3) The regime regarding the appointment of a manager does not currently apply to leasehold houses or buildings containing just one flat. We think that the regime for the appointment of a manager should be extended to apply to any premises subject to an RTM.

1.100 We propose the following in relation to the transfer of management:

(1) The RTM company should be able to apply to the tribunal:

(a) to give up the RTM; and

(b) for either:

(i) the management functions to be transferred back to the default party under the lease (or, failing that, the landlord); or

(ii) a manager to be appointed. We envisage that the tribunal would only make this order where the landlord or third party no longer exists, has managed poorly or has clearly expressed a resolve not to manage the building once the RTM ceases.

(2) The landlord should, while the RTM is continuing, have the right to apply to the tribunal for either:

(a) the management functions to be transferred back to the default party under the lease (or, failing that, the landlord); or

(b) a manager to be appointed.

(3) Within the period of 30 days following an RTM ceasing, the landlord should be able to apply to have a manager appointed rather than the management functions reverting automatically back to the default party under the lease (or, failing that, the landlord).

1.101 We also propose that, where the RTM ceases but the RTM company still exists and is not subject to any insolvency regime, the RTM company should be obliged to account for and pay over the uncommitted service charge funds to the person who takes over the management functions.

1.102 There should be a statutory assignment of the right to pursue outstanding service charge contributions owed to the RTM company by leaseholders or the landlord to the party who takes over the management functions.

1.103 The time restriction on the ability of leaseholders to make a new RTM claim following the failure of an RTM should be reduced. We ask for consultees views as to what an appropriate time restriction would be.