

INTERNAL AUDIT REPORT

FROM: Audit and Risk Manager
TO: Head of Housing Services
C.C. Chief Executive
Deputy Chief Executive (BH)
Head of Finance
Housing Strategy &
Development Manager
Business Administration
Manager
Portfolio Holder – Cllr. Phillips

SUBJECT: Leaseholder Service Charges
DATE: 17 September 2018

1 Introduction

- 1.1 As part of the 2018/2019 Audit Plan an audit has recently been completed on the systems and procedures in place to manage Leaseholder Service Charges (LSC).
- 1.2 This report outlines the approach to the audit and presents the findings and conclusions arising.

2 Background

- 2.1 Whenever a council property is sold under Right to Buy (RTB) legislation and the council retains the leasehold (usually due to the sale of a flat in a block) the leaseholder is liable for service charges. In the main these relate to routine, minor repairs to the building and maintenance charges in respect of communal areas and facilities e.g. cleaning, window cleaning, lighting, grounds maintenance etc.
- 2.2 The estimated income in 2018/2019 is £200,000. There are currently 601 leasehold properties and annual bills range between £37 and £1,400 depending on the nature of the block, the services provided and any charges for major repairs.
- 2.3 In addition a further £66,000 is collected at the same time for buildings insurance.

3 Scope and Objectives of the Audit

- 3.1 The audit was undertaken to test the management and financial controls in place.
- 3.2 In terms of scope, the audit covered the following areas:
- Identifying properties and liable persons
 - Identifying costs
 - Raising invoices

- Leaseholder information

3.3 The audit programme identified the expected controls. The control objectives examined were:

- All properties that are liable to service charges and recharges for major works are identified
- All applicable costs are identified
- All applicable costs are recovered
- Costs are appropriately apportioned
- Challenges by 'customers' to charges levied are dealt with appropriately and in a timely manner
- Leaseholders are aware of what they are actually paying for
- Leaseholders are made aware of, and have the opportunity to influence, major costs that they will be liable for.

4 Findings

4.1 Recommendations from previous report

4.1.1 The last report on LSC was issued on 9 February 2016 and it contained two recommendations. The responses at the time and the current position are detailed below.

Recommendation	Management response	Current Status
A formal process for regular monitoring and chasing of leaseholder service charge debts should be put in place.	Agreed. The Income Recovery Manager in the Sustaining Tenancies section will implement a process for dealing with these debts.	Process in place. Income Recovery Team take over debt recovery at 2 nd reminder stage before forwarding to debt collection agency where required.
The service charges spreadsheet should be reviewed to ensure that formulae have been correctly applied when calculating the charges for individual properties.	The Scheme Accounting module of the Active H system will be implemented to ensure that the service charge for each property is correct.	Scheme Accounting module not fully implemented as decision made to not, at this stage, identify service charges for tenants. Service Charge spreadsheet formulae reviewed and contingencies in operation.

4.2 Identifying properties and liable persons

4.2.1 A significant change took place a few years ago in the management of LSC in that Active H played a more prominent role. Specifically, leaseholder accounts were created in Active H and Housing Services took over the responsibility for issuing and monitoring the invoices for the annual charges that had previously been the responsibility of the FAST team in Finance.

- 4.2.2 A database of leasehold properties is maintained in Active H and a leaseholder account is automatically opened when a rent account is closed as a result of the completion of a Right to Buy (RTB). Details of all properties to be charged are maintained in a number of other documents with the key one being the master spreadsheet used to calculate the annual charges.
- 4.2.3 The main issue with keeping leaseholder information up to date concerns the sale of a property and maintaining details of the names and addresses of occupiers, owners and landlords. People involved do not always remember to inform the council which can result in correspondence regarding charges and payment being ignored or discarded.
- 4.2.4 It is important to record and action any changes resulting from an RTB so that the appropriate changes can be made. Historically this required the exchange of information between teams of officers in Housing Services. This is no longer the case and RTBs and LSC are administered by the same team removing the risk that any sales will not be dealt with appropriately. Details of all completed RTBs in 2017/2018 were obtained and checked against Active H records to ensure that charges were being made and no anomalies were discovered.
- 4.2.5 When a property is sold responsibility for any repairs that are not of a communal nature passes to the leaseholder. When the RTB is being processed only repairs of an essential or emergency nature are authorised. If a repair is requested when an RTB is being processed or has been completed the following warnings appear on screen – "RTB: Only raise emergency jobs!" or "This asset is not owned by WDC!"

4.3 **Identifying costs**

- 4.3.1 The key area in the whole LSC process is the calculation of the charges to ensure that all chargeable costs are identified, that they are accurate and up to date and that they are apportioned fairly. It is vital that the individual components of the charges can be justified for those leaseholders who regularly query the charges.
- 4.3.2 The figures for the calculation of the annual charges are gathered from a number of sources. Active H provides the annual costs for repairs to the communal areas of blocks, aspects such as caretaking and grounds maintenance will be identified from contract documents, costs such as electricity will be identified either from bills as they come in or from TOTAL and costs such as the administration charge are supplied by Finance.
- 4.3.3 As well as routine annual costs, leaseholders are liable for their share of any major repairs such as lifts, door entry systems or windows. The plans for these types of repairs are prepared by the Assets Team and so meetings are held with the Business Administration Team to make them aware of any schemes in the pipeline that will affect leaseholders.
- 4.3.4 Where improvement works are to be carried out, the relevant leaseholders are informed of the total cost and of their share and that it will be added to their account. If any additional charge is such that it will cause the leaseholder hardship by having to pay it over one year then arrangements can be made to stagger the payment.

- 4.3.5 As well as paying service charges most leaseholders opt to pay their buildings insurance through the council. Historically this meant the issue of a separate invoice but now the cost is included on the same invoice as the service charge. The leaseholder will effectively have two accounts in Active H. Where payment is made through Direct Debit the two accounts are credited automatically each month or each quarter and where payment is irregular a manual transfer has to be made from the main account to the insurance account.
- 4.3.6 The charge to be made for insurance is supplied to Business Administration by the Insurance and Risk Officer.
- 4.3.7 All of the costs and calculations for all of the leasehold properties are entered into a large and very detailed spreadsheet where the make-up of all the individual charges is clearly evident. The spreadsheet includes the figures from previous years and also an explanation of any significant variations between years.

4.4 **Raising invoices**

- 4.4.1 As previously stated, the invoicing and overall management of accounts that was undertaken by the FAST team is now undertaken in Housing using Active H. Accounts are issued annually and leaseholders are given a number of options for payment including direct debit, the website and in person using a Pay Point outlet. Invoices are raised using the detail in the master spreadsheet.
- 4.4.2 The majority of leaseholders pay regularly and by direct debit so regular monitoring of payments is not seen as a priority and it would be a manual exercise as there is no automated monitoring feature in Active H. The view taken is that it is question of balancing the time involved against the amounts outstanding bearing in mind that the individual amounts involved are relatively small. Monitoring is undertaken and reminder letters are issued but it tends to be an annual event. A number of accounts have been referred to Legal and to the Income Recovery and Financial Inclusion Manager.
- 4.4.3 A number of leaseholders do not have a regular, formal payment arrangement and are classified as "unknown" as regard their payment frequency. There is nothing wrong with this as far as they are concerned as they are not required to take up a regular monthly or quarterly payment option.
- 4.4.4 The proforma lease used by the council refers to the payment of LSC and states that LSC should be paid quarterly in advance but this is not enforced.
- 4.4.5 Currently there are around 65 leaseholders who have paid nothing so far this year in respect of LSC where the 1 April 2018 balance was £24,500 in total. This figure will in some cases include LSC from previous years. There are around 60 leaseholders with no payments against their insurance account so far this year and the total balance outstanding at 1 April 2018 was £11,500.

Risk

Where amounts are outstanding, not pursued and allowed to increase, they may not be recovered.

Recommendation

A more regular debt monitoring and recovery regime should be introduced and, where possible, leaseholders should be required to pay regularly in advance in accordance with the lease.

- 4.4.6 Where leaseholders wish to challenge any aspect of the invoicing process or of the amounts included in the LSC they can do so by routine correspondence methods and without recourse to the Corporate Complaints Procedure. Details of all the queries raised and responded to are retained in a leaseholder disputes – queries folder.

4.5 Leaseholder information

- 4.5.1 Leaseholders are provided with a plethora of information at various stages about the lease, the costs of becoming a leaseholder and about their rights and responsibilities and those of the landlord.
- 4.5.2 At the application or enquiry stage potential leaseholders are supplied with a leaseholder statement so that they are aware of the ongoing costs of becoming a leaseholder.
- 4.5.3 Leaseholders are supplied with a statement annually in advance of the issue of the invoice. This includes a detailed breakdown of the charges, an explanation of the charges and contact numbers in the event of a query or a repair.
- 4.5.4 The invoice itself includes a detailed summary of the leaseholder's rights and responsibilities. These are also included in the Leaseholders' Handbook which has recently been revised and is awaiting final approval. Information is also available on the WDC website explaining the leaseholder statement. The website also includes a copy of the Leaseholder Bulletin.
- 4.5.5 Whenever major works are to be undertaken that will affect leaseholders they are consulted under what is referred to as Section 20 and invited to make written observations in relation to the proposed works.

5 Conclusion

- 5.1 Following our review, in overall terms we are able to give a SUBSTANTIAL degree of assurance that the systems and controls in place in respect of Leaseholder Service Charges are appropriate and are working effectively.
- 5.2 The assurance bands are shown overleaf:

Level of Assurance	Definition
Substantial Assurance	There is a sound system of control in place and compliance with the key controls.
Moderate Assurance	Whilst the system of control is broadly satisfactory, some controls are weak or non-existent and there is non-compliance with several controls.
Limited Assurance	The system of control is generally weak and there is non-compliance with controls that do exist.

6 **Management Action**

- 6.1 The recommendation arising above is reproduced in the attached Action Plan (Appendix A) for management attention.

Richard Barr
Audit and Risk Manager

Action Plan

Internal Audit of Leaseholder Service Charges – September 2018

Report Ref.	Recommendation	Risk	Risk Rating*	Responsible Officer(s)	Management Response	Target Date
4.4.5	A more regular debt monitoring and recovery regime should be introduced and, where possible, leaseholders should be required to pay regularly in advance in accordance with the lease.	Where amounts are outstanding, not pursued and allowed to increase, they may not be recovered.	Medium	Business Administration Manager.	Agreed –implement quarterly reminders for non-payment and actively pursue debt before end of financial year.	December 2018 (end of quarter 3)

* Risk Ratings are defined as follows:

High Risk:	Issue of significant importance requiring urgent attention.
Medium Risk	Issue of moderate importance requiring prompt attention.
Low Risk	Issue of minor importance requiring attention.