

# INTERNAL AUDIT REPORT

**FROM:** Audit and Risk Manager  
**TO:** Head of Housing Services  
**C.C.** Chief Executive  
Deputy Chief Executive  
Head of Finance  
Business Support Manager  
Housing Strategy & Development  
Manager  
Landlord Services Manager  
Landlord Operations Manager  
Portfolio Holder (Cllr Matecki )

**SUBJECT:** Leaseholder Service Charges  
**DATE:** 19 October 2021

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## 1 Introduction

- 1.1 In accordance with the Audit Plan for 2021/22, an examination of the above subject area has recently been completed by Jemma Butler, Internal Auditor, and this report presents the findings and conclusions for information and, where appropriate, action.
- 1.2 Wherever possible, findings have been discussed with the staff involved in the procedures examined and their views are incorporated, where appropriate, into the report. My thanks are extended to all concerned for the help and cooperation received during the audit.

## 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 for 2020-21 was circa. £196k. There are currently 616 leasehold properties with annual bills ranging between £33 and £3,147 depending on the nature of the block, the services provided and any charges for major repairs.
- 2.3 In addition, a further £66k is collected at the same time for buildings insurance.

### 3 **Objectives of the Audit and Coverage of Risks**

3.1 The audit was undertaken to test the management and financial controls in place. This was achieved through a 'risk-based audit' approach whereby key risks are identified and then processes are assessed to provide assurance that the risks are being managed effectively. This approach has been in place by WDC Internal Audit since only the start of this financial year following an external review of the function.

3.2 In terms of scope, the audit covered the following risks:

- Financial loss through under recovery of charges.
- Inability to make charges.
- Additional paragraphs where needed.
- Non-compliance with legislation esp. section 20.
- Incorrect charging – invoice error / admin.
- Leaseholder unaware of service charges / poor legal advice / Council not informed of sale of property.

3.3 These were drawn from a combination of risks identified in the Significant Business Risk Register, the departmental risk register, and discussion between the Internal Auditor and the Business Support Manager (auditee).

3.4 These risks, if realised, would be detrimental to the Council with regards to meeting the following corporate objectives, as set out in the Fit for the Future Strategy:

- To ensure that all people are treated fairly and equally and to manage the Council's resources effectively.

### 4 **Findings**

#### 4.1 **Recommendations from Previous Reports**

4.1.1 The current position in respect of the recommendations from the audit reported in September 2018 was also reviewed. The current position is as follows:

<b>Recommendation</b>	<b>Management Response</b>	<b>Current Status</b>
1 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.	Agreed –implement quarterly reminders for non-payment and actively pursue debt before end of financial year. (Target date December 2018)	This has not been fully implemented. Reminders are issued to the leaseholder, but leaseholder debt is not actively pursued.

## 4.2 **Financial Risks**

### 4.2.1 **Financial loss through under recovery of charges**

There are 616 properties on the leaseholder database mailing list, extracted from the housing system (ActiveH) which stores the details for Council housing and property assets including leaseholders.

When a 'Notice of Transfer' form is received from a solicitor, informing the Council of a change of ownership, the housing team are able to update the information held for that property. When a leasehold property is purchased under the Right to Buy scheme the same process is followed enabling the information held to be updated.

There were 31 changes made to leaseholder details in the last financial year. Seven of them were leasehold properties sold under the Right to Buy scheme, the remaining changes were leaseholder to leaseholder sales. A sample of the properties with changes made within the last financial year were reviewed. All of the sample had a copy of the Notice of Transfer form saved to the file and the relevant changes had been made on ActiveH. Right to buy leasehold properties are kept at an agreed maximum leasehold charge for the first five years after purchasing, this was also documented.

A random sample of leaseholder accounts were reviewed on ActiveH. All of the sample were clearly identified as leaseholders. This prevents some of the repairs which the leaseholder would be responsible for from being carried out and charged to the Council.

### 4.2.2 **Inability to make charges**

The Business Administration Officer calculates the charges for leasehold properties annually by dividing the costs incurred between the number of properties in the block or development. This could be charges for grounds maintenance within a development or specific block related costs such as lift maintenance, which would be split between the number of properties within that block. The charges are calculated annually using a spreadsheet which holds the information for all of the relevant charges incurred. The Business Administration team then manually transfer the charges to ActiveH. The spreadsheet also has a notes section where the officers can find information regarding significant changes to the charge for when potential enquiries may be received from leaseholders querying the change in amount.

A sample of invoices was reviewed and charges matched those calculated on the spreadsheet. When the invoices are run the number produced are checked to ensure they match the number of leasehold properties registered on the list.

In most cases invoices are set up to be paid by direct debit preventing unpaid sums. Accounts that are in debt are reviewed regularly by the Business Administration team who issue the leaseholder with reminders to pay. Other than the reminders there is currently no process in place for the recovery of charges. This was highlighted in the previous audit. Although the Council has

an income recovery team, they currently only recover income for rent. Leaseholder service charges are not actively recovered.

At the end of the financial year (March 2021) there were 80 leaseholder accounts in arrears of £10 or over. The total debt of these accounts at that time was £37,996.

## **Recommendation**

**An income recovery process should be established and followed.**

### **4.3 Legal and Regulatory Risks**

#### **4.3.1 Non-compliance with legislation esp. section 20**

The main legislation in place is the Section 20 Consultation legislation which manages one-off costs. The consultations must happen where leaseholder contributions are expected to be over £250 per leasehold property; VAT must be included within the estimated cost. There is information about the Section 20 Consultation legislation available at The Leaseholder Advisory Service website. This provides in-depth details of what landlords need to consult with leaseholders about and what works qualify for consultation. Non-compliance with the legislation limits the ability to recover costs from the leaseholders towards the cost of the works or service.

The legislation has three stages: Pre-tender, Tender and Award of Contract. These stages provide leaseholders with the details of the work or service required and the opportunity to comment on the proposal at every stage. The Leaseholder Advisory Service website provides letter templates to ensure all notices and proposals contain the legally required information.

A sample of leaseholder consultation documents was reviewed. The pre-tender letters issued included the required information and stated a consultation timeframe. Tender and award of contract letters also included estimated / confirmed costs and the repayment period. All letters viewed quoted the legislation and relevant contact details for queries.

There is a leaseholder handbook available which documents the relevant legislation and processes for leaseholders and the Council. It also provides additional information and contact details for the leaseholders should they require it.

### **4.4 Reputational Risks**

#### **4.4.1 Incorrect charging – invoice error / admin**

Once the charges have been calculated for the leasehold properties and input onto ActiveH the invoices can be issued to the leaseholders. Invoices are produced through an automatic mail merge function and a copy is saved in a file for the relevant year. Samples were reviewed and properties were invoiced the correct amount according to the calculated sum on the spreadsheet.

The complaints procedure is set out within the leaseholder handbook, should there be an issue with the invoice or service provided. The complaints process followed is the standard Council complaints procedure. Only one complaint from a leaseholder could be identified, as this was more than 2 years old and regarding a repair issue it was not felt to be relevant for the audit.

#### 4.5 **Other Risks**

##### 4.5.1 **Leaseholder unaware of service charges / poor legal advice / Council not informed of sale of property**

There are a number of opportunities to make sure a leaseholder is made aware of any charges. This includes information from their solicitor when they initially look at purchasing the property, when the annual invoice and statement regarding fees are issued and, when invoices are unpaid, the reminders of which are sent out. In addition to these there is also information available on the Council's website.

When a property is sold, either through the Right to Buy scheme or leaseholder to leaseholder sales, the solicitor should get in touch with the housing team to inform them of the potential sale of the property so the team can pass on all relevant charges and information including any proposed work and the related charges. This ensures that the buyer will have all of the relevant information regarding the true costs before purchasing the property.

The Housing Services Risk Register recognises that there are risks involved with leasehold properties and has some controls in place to help manage them. The main risk is identified as "Failure to adequately manage leaseholders"; controls include working with the tenants and complying with the Section 20 legislation. There is no risk identified for the loss of income through non-payment of leaseholder invoices.

There is a large amount of information and guidance available for leaseholders on the Council's website. This includes information of what the service charge might cover and an example statement showing the breakdown of the charges. The website provides a facility for leaseholders to pay their charges securely using an online link.

The information available also includes the Section 20 Consultation legislation and sets out the Council's duty to follow it when charges / contributions towards works will be more than £250. There are a number of other relevant pages with information for leaseholders including: repairs and alterations, selling your home and insurance.

The guidance available informs the leaseholders that they must seek permission from the Council before selling their home and properties purchased after 18th January 2005 through the Right to Buy scheme must be offered to the Council first. A link to the current leaseholder handbook (2018) is also provided.

## 5 **Conclusions**

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 to help mitigate and control the identified risks.

5.2 The assurance bands are shown below:

<b>Level of Assurance</b>	<b>Definition</b>
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.

5.3 An issue regarding the collection of debt was identified which requires further action.

## 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 - October 2021

Report Ref.	Risk Area	Recommendation	Rating*	Responsible Officer(s)	Management Response	Target Date
4.2.2	Financial Risk	An income recovery process should be established and followed.	Medium	Landlord Services Manager and Landlord Operations Manager	To create & implement procedure for management and recovery of leaseholder debt.	31 March 2022

\* The ratings refers to how the recommendation affects the overall risk and are defined as follows:

High: Issue of significant importance requiring urgent attention.

Medium: Issue of moderate importance requiring prompt attention.

Low: Issue of minor importance requiring attention.