Event Fees

—— analysing the Law Commission consultation paper

A briefing note for retirement community operators

In October, the Law Commission published its "Consultation on Residential Leases: Fees on Transfer of Title, Change of Occupancy and Other Events".

The consultation paper and supporting documents provide a useful insight into the market for older people's housing, including international comparators. The Commission highlights historic issues with "event fees", particularly the subset of these known as "transfer fees", drawing from the OFT investigation results published in 2013. However, it has determined that "this form of housing brings benefits to both residents and to society – and we wish to encourage it... We do not think that there is anything wrong with deferred fees as such. However, it is essential to make these fees transparent".

As a Corporate Supporter of ARCO, we have prepared this briefing paper for providers of retirement communities to provide a summary of the proposals for modifying the law as it applies to "event fees".

What is an event fee?

The suggested definition of an event fee is a fee which the tenant is obliged to pay under a term in a residential lease, where:

1. the term requires the tenant to pay the fee on, or in connection with the happening of a defined event;
2. the event is that title to the lease changes hands, a change in the occupancy of the property; or some other event which creates a third party interest in the lease; and
3. the fee is fixed or calculated in accordance with a formula.

Legal analysis

The consultation paper takes a detailed look at two broad areas of law which might apply or be made to apply to event fees – landlord and tenant and consumer protection. It also considers existing codes of practice in the sector.

Landlord and tenant law

The Commission considers:

- Variable service charges under the Landlord and Tenant Act 1985 (LTA 1985). This requires tenants to be consulted on major works and long term agreements and for service charge costs to be reasonable. Variable service charges must be payable directly or indirectly, for services, repairs, maintenance improvements or insurance or the landlord's costs of management. Some event fees may do so. However, charges must vary according to the cost of services to be caught by this law and while event fees can vary we are not aware of any event fee where the formula works in this way. The Commission correctly concludes that event fees are not variable service charges. It also notes (as the Supreme Court has recently confirmed in *Arnold v Britton*) that other kinds of service charges are not covered by the LTA 1985, which it does not intend to change.
- Variable administration charges under the Commonhold and Leasehold Reform Act 2002. Charges for consent under a lease or for the provision of documents relating to it must be reasonable, where the charge or a mechanism for calculating it is not specified in the lease. Again the Commission concludes that this has limited application to event fees. Only a small proportion of all event fees would be caught and landlords could easily avoid this law in future by tying the event fee to something else.
- Other law relating to consent under leases - about the reasonableness of costs charged by a landlord for consent to assign. Although some were payable on

change of ownership the Commission did not consider the event fees it reviewed were expressed as being payable for a consent to assign. Again, this would be easily avoided.

- Section 42 of the Landlord and Tenant Act 1987. This creates a statutory trust over variable service charges in a sinking or reserve fund. The Commission intends to expand this, as noted below.

A technical area given much attention relates to the legal distinction between leases as contracts and estates in land, in particular:

- The different rules on the passing of tenant responsibility on assignment before and after 1 January 1996. For leases granted on or after this date all tenant obligations pass with the title, unless expressly stated to be personal, which is rare. Before this date, the starting point is that the original leaseholder remains liable even after assignment. In practice the number of leases in the retirement community sector granted pre-1996 seems likely to be low, as is the likelihood of an operator pursuing a former tenant.
- Related to above, the Commission also highlights a risk of forfeiture (termination for tenant breach) for a breach committed by an outgoing tenant. It suggests this means aggrieved tenants may not test the validity of an event fee on assignment, because the buyer will insist on it being paid on or before completion and the tenant will not want to lose the sale. Forfeiture is indeed a risk. However, properly disclosed event fees should be at limited risk of causing concern.
- Although the law changed in 1996 the Commission's view is that it is not clear that when a lease is assigned it would be treated as a new contract between the landlord and the new tenant. The Commission is proposing to clarify the law in this area.

Consumer protection legislation

The Commission undertakes a relatively detailed analysis of the Consumer Rights Act 2015 (CRA), the Consumer Protection from Unfair Trading Regulations 2008 and the EU Unfair Terms Directive 1993 which underpins the English law. We have produced a separate note on the Consumer Rights Act as it applies to retirement community operators. In considering how this law applies to event fees, the Commission asks three questions:

- Does the "core exemption" apply? Under the CRA, a consumer contract term may not be assessed for fairness to the extent that the assessment is of the appropriateness of the price payable under the contract by comparison with the services supplied under it. However, this does not apply to terms on the "grey list" or to terms which are not transparent and prominent. The Commission considered a number of sample event fee clauses as part of its investigations and thought that several of them would fail the transparency test. The Commission notes a number of legal complexities in this area, partly stemming from different views expressed in the leading English and European cases about the link between the price and the services supplied under a contract. It also notes that even if the core exemption applies, aspects of a price clause could be assessed for fairness based on their structure, presentation and application. It proposes to clarify the law in this area, as noted below.
- Leases represent a contract between the first tenant and the landlord. What about subsequent tenants? The Commission suggests a lack of clarity in this area which it intends to remedy.
- The first regulations on unfair terms in consumer contracts came into force on 1 July 1995. Does consumer rights legislation have any retrospective effect on leases created before this date? The Commission's conclusion is that when an existing lease is assigned, the landlord should comply with the new legal requirements it is proposing. This is consistent with its approach to treating a lease as a new contract between the landlord and the new tenant on assignment.

Codes of practice

The consultation paper undertakes a review of eight existing codes of practice which relate in some way to managers of specialist housing.

One of these is the ARCO Consumer Code, which requires members to provide comprehensive information about event fees to prospective buyers before they pay any deposit to reserve a property. ARCO members must also ensure that marketing, advertising and sales materials comply with advertising codes of practice. Because other codes (notably the UK Code of Non-broadcast Advertising, Sales Promotion and Direct Marketing (CAP) Code) require clarity on price in marketing communications, the Commission considers that all ARCO member advertisements must mention event fees.

The Association of Retirement Housing Manager's code (ARHM), which is being updated for 2016, is noted as the only code with the Secretary of State's approval under legislation, which means it can be taken into account by a court or tribunal even if neither party to the proceedings is a member of the ARHM.

Proposed reforms

Law changes

The Commission proposes three main reforms to the law in light of its findings:

- There will be an addition to the grey list under the CRA covering event fee clauses which do not comply with a designated code of practice. Grey list terms carry a suspicion of unfairness which complying with the code of practice would avoid. The CRA creates a less onerous test of transparency and prominence for "core" terms relating to the appropriateness of the price in comparison with the services provided – as long as they are not on the grey list. Most event fees could benefit from this "core exemption" by complying with the new code of practice and staying off the grey list. The Commission believes this offers considerable comfort to the sector. However, it does not seem to be going as far as to say that all event fees which avoid the grey list will benefit from the core exemption or will be entirely free from challenges as to their fairness. The key benefit for both operators and consumers in this new set of requirements appears to be the code of practice itself. Compliance with it will not only avoid grey list suspicion but also ensure full disclosure of relevant facts by prescribed methods, ensuring information is

accurate and complete and the risk of event fees being later held unfair is low.

- Consumer protection legislation will confirm that event fees are contract terms subject to consumer protection law, even where the original lease has been assigned. This will include leases which pre-date the new law. The Commission reasons that as the emphasis will be on the landlord's conduct in explaining the term to the new tenant (which it can control on assignment), not the lease term itself (which is already fixed), there is no significant risk to landlords despite the law applying to leases which preceded it. Care will be required regarding the impact of this new law in other areas - since 1996 the law about what happens when leases are assigned has been settled and works effectively.
- Event fees charged exclusively for property maintenance, repair or improvement will be subject to a statutory trust for the benefit of occupiers, an extension of existing law applicable to sinking funds held by private sector landlords. Unless funds are specifically ring-fenced for these uses this requirement will not apply. Funds held in this trust arrangement will not be subject to the assumption that they are on the grey list if not compliant with a code of practice. This point will require further clarification. For example, at present the statutory trust requirement does not apply to registered providers – will it in this area?

Amendment to landlord and tenant law is not supported. We think this is eminently sensible as the law in this area would require substantial amendment to cover event fees, which may create unintended consequences in an already complex area. Additionally, tying event fees to mechanisms intended to apply where costs vary by reference to the services provided would not fit with deferred payment models under which the operator takes the risk on services costs in order to provide consumers with future certainty.

Proposed new code

The consultation suggests that the Secretary of State approve a chapter on event fees which could more easily be adopted into existing codes so as to be admissible in evidence in legal proceedings. It includes a number of suggestions and requests for input on the nature and content of the code:

- Landlords should not charge event fees except on sale or sub-letting. We doubt this would be seen as contentious by operators and reflects the outcomes of the 2013 OFT investigation.
- Subletting fees should not be the same as for assignments. While there is some logic to this, the final settlement in this area will require a careful balance to ensure subletting is not used to actively avoid agreed event fees linked to assignment.
- Should tenants be offered the option to pay event fees in advance? This expands on OFT concerns about certainty and avoiding behavioural biases in purchasers balanced against overloading consumers with too many options. Some operators do this already. Those who do not should consider whether they would be willing to, on what terms, and the likely take-up.
- Sales and marketing advertising should state that event fees are payable. This reflects the Commission's views on the existing law under the CPRs. Work will be required on how best to deal with more complicated exit fees which may not be easily summarised.
- Prospective purchasers should be given a disclosure document providing details of event fees. This has been pre-empted by ARCO though the Key Facts document required by its Consumer Code. It would be provided early - on expression of interest in the property or the first visit to it. The Commission makes various

suggestions about the way a disclosure document might work, including:

  - standardising terminology so that consumers can readily see what is and is not an event fee, which would assist as the retirement community sector grows;
  - disclosure statements might explain alternative payment options and give contact details for advice organisations; and
  - illustrated examples could be required, in a specified form and based on representative current prices for the specific site and showing what is payable on standardised time interval and inflationary increase variables – these too could help as the market develops as they would become routine for anyone engaging in it.

- Where agents deal with sales for landlords, the landlord could be required to impose the above obligations on the agent, with a failure by the agent treated as a failure by the landlord. Agents could be liable to pay compensation under prescribed redress schemes.
- Where the sale is by the tenant, suggestions are sought for a mechanism which will ensure a purchaser has access to the same information a landlord would provide. The Commission suggests an online database for agents to access or dedicated information access routes made available by landlords. Operators should consider these and other options in light of their own costs of administration.
- The Commission suggests that to reduce uncertainty regarding existing leases, where an event fee is linked to a future sale price it should only be charged where the effect of the fee was clearly illustrated before the tenant bought the property. In other cases, the fee should be charged as a percentage of the lower of the original purchase price or the sale price. Some ARCO members would be affected by such a requirement. The Commission's view here is at odds with its analysis in the consultation about applying new law retrospectively and could be challenged on that basis. Our view is that lease terms agreed in the past should be assessed in light of the applicable law at the time.

Conveyancing protocols

Interestingly, information gathering by the Commission raised concerns that conveyancers were not reporting fully on event fee terms and as a result it suggests a standard procedure for conveyancers to discuss event fees and their implications with their clients. Our view is that the need for disclosure is obvious – conveyancers risk negligence otherwise - and requires no special procedure. For landlords (and tenants) dealing with sales the importance of using legal advisers who understand the sector specific nature of leases and charges under them cannot be overstated.

Conclusion and next steps

The Commission feels that event fees fall into a gap in the law, with defects in the way current legal protections apply - landlord and tenant law is largely inapplicable, while it finds undue complexities in their application under consumer rights law. The Commission has expressly discounted banning event fees entirely, noting among other findings that this has not been the approach in other jurisdictions. It has also commented that event fees can be a useful tool for residents as it allows them to reduce their service charges. The additional certainty around event fees for operators might also lead to an expansion of the sector, which the Law Commission recognises as providing a much needed housing and care option for older people.

The amendments proposed are subtle and intended to drive the sector towards a clear and pre-defined set of disclosure requirements which will reduce the risk of terms being found to be unfair and unenforceable. While further developments are awaited the consultation offers a clear line of sight as to the likely approach to reform. Much of what is proposed is or might be enforceable under current law - the position between landlords and new tenants on assignment is not entirely clear, while existing consumer rights law could be used to test current event fee terms and disclosure practices. By operating in accordance with published CMA guidance on contract terms, supplemented by the recommendations made in the consultation paper (much of which is already reflected by the ARCO Code), operators can minimise the risk of challenges pending implementation of any new law in this area.

Operators are encouraged to consider and respond to the consultation questions.

Trowers & Hamlins has a leading practice in health and social care. Our work as Corporate Supporters of ARCO has allowed us to develop a deep insight into the housing-with-care market. Our team adds value to clients by combining core legal practice areas with a clear understanding of the legal and regulatory frameworks and the market drivers relevant to the sector. If you have any questions or would like more advice relating to the application of the CRA to your business please don't hesitate to contact us.

Please contact:

Kyle Holling
Partner

e kholling@trowers.com
t +44(0)20 7423 8292