Tenant-friendly revisions

With changes to the tenancy deposit scheme legislation expected to come into force in April, Edward Cracknell assesses the practicalities of the legislation

Edward Cracknell is a solicitor in the contentious property department at Russell Cooke LLP

'The 2011 Act received Royal Assent on 15 November 2011 and many of its provisions came into force in December of that year. Section 184, proposing changes to the tenancy deposit provisions of the 2004 Act are expected to come into force in April.'

The saga of the tenancy deposit scheme legislation, introduced in 2007, has taken another important turn, this time very much in favour of tenants. As those involved in letting properties on assured shorthold tenancies will know, the legislation has been the subject of a number of court cases and the government has now taken the opportunity to clarify the legislation.

The Housing Act 2004

The relevant provisions of the 2004 Act (ss212-215) came into force in England and Wales on 6 April 2007.

The effect of those provisions is that landlords who take a deposit from assured shorthold tenants after 6 April 2007 must, within 14 days of receiving the deposit:

- deal with the deposit in accordance with an authorised scheme (of which there are currently three: The Dispute Service, My Deposits, and The Deposit Protection Service); and
- give certain prescribed information to the tenant.

Tenants may apply to court to claim the return of the deposit, together with a penalty sum of three times the value of the deposit from the landlord in certain circumstances where the Act has not been complied with. Additionally, landlords who have not complied with the requirements may not serve a section 21 notice seeking possession. Deposits consisting of property other than money are prohibited.

The penalty sum

Inevitably some landlords, whether wilfully or inadvertently, failed to protect the deposit in an authorised scheme. Claims for the penalty sum began to appear in the county courts and it eventually fell to the Court of Appeal in the conjoined appeals of *Tiensia v Vision Enterprises Ltd (t/a Universal Estates); Honeysuckle Properties v Fletcher & ors* [2010] to decide whether the penalty was payable in circumstances where the landlord protected the deposit late, ie after the 14-day period. The court determined that question in favour of the landlord. It decided that as long as the deposit was protected before the hearing of the tenant's claim for the penalty sum, the penalty would not be payable. Giving the leading judgment, Rimer LJ said:

> The objective of the legislation is not the punishment of landlords but the achieving of proper protection of tenants' deposits. The legislation should not be interpreted in a sense that implicitly encourages the ambushing of landlords by tenants who have grounds for believing that the landlords have not complied with their s213 obligations. It should be interpreted in a way that avoids litigation. Litigation will or should be avoided if, following a letter before claim, the landlord promptly puts his house in order.

Rimer J acknowledged that this interpretation led to a situation where landlords could leave deposits unprotected unless and until litigation was threatened, saying:

> It will be an unusual landlord who will not, faced with a s214 claim, ensure that by the time of the hearing he has fulfilled his outstanding obligations under s213, with the consequence that in practice s214 will be likely only to bite in the most exceptional and unusual cases. I recognise all of that. Equally, however, it can also be said that in that

> overwhelming majority of cases the net result will be that the legislation will have achieved its primary objective, that of the due protection of the tenant's deposit. What more can reasonably be asked of it?

The issue of tenancy deposits came before the Court of Appeal again in *Gladehurst Properties Ltd v Hashemi & anor* [2011] when a differently constituted court decided that tenants would have no right to claim the penalty sum after the tenancy has ended.

The importance of giving the prescribed information to the tenant should not be overlooked. In the case of *Suurpere v Nice & anor* [2011], the landlord protected the deposit, and actually returned it by the time of the hearing but did not at any time give the tenant the prescribed information required by the Act. The High Court ordered the landlord to pay the triple penalty.

Those cases reflect the current state of the law: landlords must protect deposits taken after 6 April 2007 and provide the tenant with prescribed information, but if they do not do so they can avoid the financial penalty by complying with the requirements of the 2004 Act before the hearing of the tenant's claim.

The Localism Act 2011

The 2011 Act received Royal Assent on 15 November 2011 and many of its provisions came into force in December of that year. Section 184, proposing changes to the tenancy deposit provisions of the 2004 Act are expected to come into force in April.

The explanatory notes to the 2011 Act make Parliament's intentions very clear. In relation to what initially appear to be relatively innocuous changes to the mechanics of the protection process, the notes explain that the changes are intended to 'make clear that penalties for non-compliance will apply when the landlord has not complied within [the] time limits'. That is to say, that the time limits in the Act are to become important again: landlords cannot get away with late compliance.

The importance of giving the prescribed information to the tenant should not be overlooked.

If and when the amendments come into force, the new regime will be as follows:

- The landlord will have 30, rather than 14, days to protect the deposit and provide prescribed information.
- If the landlord does not comply within those 30 days the court must order the landlord to return the deposit and pay a penalty sum to the tenant.
- The court will have some discretion as to the amount of the penalty. It can be a sum between one and three times the amount of the deposit.
- The tenant may still apply to court for the return of the deposit and the penalty payment even after the tenancy has ended.
- The prohibition on serving a section 21 notice seeking possession is relaxed where either the deposit has been returned or where an application to court for the penalty payment has been made and has been determined, withdrawn or settled.

The effect of this is that landlords who forget to protect the deposit within 30 days of receiving it, or who do not properly serve all of the prescribed information, for example, could be ordered to return the deposit and pay a penalty of up to three times the amount of the deposit. This will apply even if the application is made after the tenancy has ended though it is not clear whether this is intended to apply to deposits taken, and/or tenancies that ended before the changes come into force.

Perhaps in acknowledgement of the potential harshness of the new rules, the time for compliance has been extended and the court has been given some discretion as to the amount of the penalty. There is no guidance as to how that discretion is to be exercised. Courts might be prepared to award a lower penalty where, for example, the transgression is perceived to be an innocent mistake. Landlords faced with an application to court should consider protecting the deposit before the hearing, in the hope that this will prompt the court to be lenient in setting the amount of the penalty.

It is, however, not clear what order the court would make on costs in this situation. On one view, by protecting the deposit, albeit late, the statutory purpose has been met and the landlord should not be further punished by a costs award. The better view is probably that the tenant was entitled to claim the penalty and did so. He won, and costs usually follow the event. Though the court retains absolute discretion over what order to make about costs, in cases where the sum claimed is less than £5,000, only fixed costs will be recoverable, which will usually be a very small fraction of the actual costs.

A well-advised landlord in a claim worth £5,000 or more will make a Part 36 offer to pay a sum of somewhere between one and three times the amount of the deposit to protect itself on costs. If the tenant goes on to get a result that was no more favourable than the offer, it will have to pay the majority of the landlord's costs.

Inevitably some landlords, whether wilfully or inadvertently, failed to protect the deposit in an authorised scheme.

Unresolved issues

The changes to the legislation unfortunately do not address the position where a deposit was taken before April 2007 and the tenancy is later renewed. There is an argument that, if the landlord retains the deposit in relation to the new tenancy, it is, in effect, receiving a new deposit, albeit that it is the same money. Arguably, the same situation arises when a tenant remains in occupation after the end of a fixed term AST, because a new statutory periodic tenancy arises. It is advisable to protect the deposit and provide the prescribed information within 30 days of entering into the new tenancy.

Landlords and letting agents should also note that care must be taken in providing the right information to the tenant. While the deposit scheme providers sometimes provide a pro forma for the prescribed information, or wording to go into the tenancy agreement, further case-specific information usually needs to be provided, and sometimes some of the information is contained in a separate leaflet that also needs to be provided. It is not clear whether the inclusion of a link to a website containing the leaflet is sufficient.

In particular, the contact details for the parties must be recorded on the prescribed information document as well as details of the circumstances in which all or part of the deposit may be retained by the landlord, by reference to the terms of the tenancy. It is not clear what is to be done where the terms of the tenancy do not set out circumstances when the deposit may be retained. Finally, the prescribed information document must include a signed certificate indicating that the information given is true to the best of the landlord's knowledge and belief.

On a related issue, it is common practice for letting agents to serve a section 21 notice on the tenant in the initial meeting during which the tenancy agreement is signed. The purpose of this is to bring the tenancy to an end at the end of the fixed term, and get proof of receipt of the notice. Such notices have always been unreliable for the reason that there might be a dispute about whether the notice was served before or after the tenancy agreement was executed. If it was served before the tenancy was executed, the notice will be of no effect because the tenancy to which it relates was not in existence at the time of service. The section 21 notice will definitely be invalid if it is served prior to the deposit being protected and, again, if the two things happen on the same day, there may be an argument about which came first.

Most professional landlords are aware of their obligations and have been diligently complying with the legislation so the changes will therefore not adversely affect them. But the changes have the potential to be very detrimental to inexperienced landlords and those who simply forget to protect the deposit in time or are prevented from doing so for some administrative reason. The message for landlords is to protect deposits and provide the prescribed information as soon as possible, and preferably on the day of taking the deposit, so that the tenant can be invited to sign a copy of the prescribed information document to acknowledge receipt. ■

Gladehurst Properties Ltd v Hashemi & anor
[2011] EWCA Civ 604
Suurpere v Nice & anor
[2011] EWHC 2003 (QB)
Tiensia v Vision Enterprises Ltd (t/a Universal Estates); Honeysuckle Properties v Fletcher & ors
[2010] EWCA Civ 1224

In summary

- The present state of the law is that landlords must protect AST deposits and serve prescribed information within 14 days of receipt but that landlords will not have to pay a penalty sum to the tenant as long as the deposit is protected before the hearing of the tenant's claim to the penalty.
- The proposed changes, which are expected to come into effect in April 2012, will require the landlord to protect the deposit and provide the information within 30 days of receipt, failing which the court will be able to order the landlord to return the deposit and pay a penalty of between one and three times the value of the deposit.
- A landlord cannot serve a section 21 notice unless the deposit has been protected and the prescribed information served. Though when the new rules come into force, a section 21 notice may be served where the deposit has been returned or where penalty proceedings have been resolved.
- The tenant cannot bring a claim for the penalty sum after the tenancy has ended, though that will change when the new rules come into force.