Building Reserve Funds in Privately Owned Flats: Making the Case
The Chartered Institute of Housing
The Chartered Institute of Housing (CIH) is the professional body for people involved in housing and communities. We are a registered charity and not-for-profit organisation. We have a diverse and growing membership of over 22,000 people worldwide, with over 2,800 in Scotland. Our members work in both the public and private sectors. We exist to maximise the contribution that housing professionals make to the wellbeing of communities. We also represent the interests of our members in the development of strategic and national housing policy and aim to be the first point of contact for anyone involved or interested in housing.

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Introduction

In 2004 CIH Scotland prepared a policy briefing, *Safe as Houses?: Building Reserve Funds – a tool to ensure the future repair and maintenance of Scotland’s homes*. CIH Scotland argued that disrepair in private property required more radical solutions and promoted Building Reserve Funds as a useful tool to address and prevent poor house conditions in the private sector.

This remains the case today.

Over a third of Scotland’s population lives in either a, flat, apartment or maisonette i.e. properties where there is likely to be a common or shared area. Of those, over 84% (398,000 flats) in the private sector have some form of disrepair. As the high levels of disrepair in private flatted accommodation show, owners do not appear to be taking action voluntarily. CIH Scotland believes that although recent legislation in the *Housing (Scotland) Act 2006*, *Title Conditions (Scotland) Act 2003* and the *Tenements (Scotland) Act 2004* provides some powers to tackle disrepair, none goes far enough. One of the key issues prohibiting repairs and maintenance works from being completed in communal parts of property is typically the lack of any formal arrangement to pay for the work required.

Building Reserve Funds are an essential tool to ensure arrangements and funding are in place to take early action to deal with repairs and maintenance in privately owned property. A Building Reserve Fund also ensures issues regarding the amount of fees and size of share to pay are defined from the outset (in line with current legislation) and are not affected by changes in property ownership.

CIH urges the Scottish Government to include the creation of Building Reserve Funds for all private residential properties sharing common parts in Scotland in the

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2 Census (2001), *Table CAS055 Dwelling and Accommodation Type by Households*
4 *Housing (Scotland) Act 2006*, www.opsi.gov.uk/legislation/scotland/acts2006/asp_20060001_en_1
5 *Title Conditions (Scotland) Act 2003*, www.opsi.gov.uk/legislation/scotland/acts2003/asp_20030009_en_1
current Housing (Scotland) Bill or the forthcoming Private Sector Housing (Scotland) Bill.

Specifically, CIH Scotland proposes that:

- **Building Reserve Funds** would be compulsory in all new flatted accommodation in Scotland and therefore be included in the associated title deeds.

- **Local authorities** would have the power to instruct all owners to create a Building Reserve Fund in existing flatted accommodation where there are persistent problems with repairs and maintenance. Similar to current powers associated with Maintenance Orders, the existence of a Building Reserve Fund would also require to be registered with the Land Registry.

- **The Scottish Government** tests the effectiveness of Building Reserve Funds by piloting them with a wide range of owners and property types across Scotland. Only after successful pilots should the Scottish Government commence the section of the Act pertaining to Building Reserve Funds.

In the remainder of this paper, CIH Scotland outlines its vision for Building Reserve Funds and the benefits they bring based on evidence from international case studies.

**Background**

The Scottish House Condition Survey (SHCS)\(^7\) shows that there is some form of disrepair in over 84% of all private flatted accommodation in Scotland. More alarmingly, in almost two thirds of all flats (303,000 flats) there is some form of disrepair to the critical elements of the property i.e. disrepair to the elements that keep the properties wind, water-tight and structurally stable.

The private sector does contain a higher proportion of older and larger properties that may be difficult and more costly to improve or update. In addition, until very recently, there has been little legislation providing powers to tackle disrepair and maintenance and also to assist in understanding how works can be organised in a communal situation.

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The first report of the Housing Improvement Task Force (HITF) in 2002 concluded there were significant problems with many people becoming flat owners without understanding their communal rights and obligations. There were few formal and continuing arrangements for owners to get together to make decisions on communal repairs and maintenance, and recovery of costs from obstructive owners was a continuing problem. *Stewardship and Responsibility*\(^8\), the final HITF report (2004) stated that, ‘relatively few owners contribute to reserve or sinking funds,’ in order to ensure enough money was available in advance of repairs and maintenance works being commissioned.\(^9\) Its final recommendations were that:

- The Scottish Executive should provide advice and information on the establishment and management of reserve or sinking funds. Different levels of advice will be required for owners and property managers; and for developers and their legal advisers drawing up title deeds.

- Local authorities should have discretionary powers to require owners subject to a maintenance plan notice to set up a reserve or sinking fund.

- Local authorities should also have the powers to provide grant aid to owners to encourage them to establish a reserve or sinking fund. This grant aid would be limited to meeting the costs of the work necessary to establish the reserve or sinking fund rather than contributions to the fund itself.

Since the 2004 recommendations, two key pieces of legislation have come into force to tackle these issues. Firstly, the Housing (Scotland) Act 2006 introduces new legislation to improve the quality and state of repair of private sector housing. It gives local authorities new powers and duties to address housing standards and to provide advice and assistance to owners to ensure their housing remains in good, well maintained condition. In particular, it gives local authorities the power to serve maintenance orders on properties that are unlikely to be maintained or where the benefit of works carried out will be lost due to a lack of maintenance. Local authorities are also given the power to pay missing shares into any maintenance accounts set up by owners and recover costs. However, the 2006 Act does not give

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\(^8\) Housing Improvement Task Force (2003), *Stewardship And Responsibility: A Policy Framework for Private Housing in Scotland*, Scottish Executive

local authorities the power to instruct owners to establish maintenance accounts: instead they are to encourage owners to do so\textsuperscript{10}. In addition, maintenance orders only last for five years and therefore do not encourage longer term repair and maintenance planning.

Secondly, the Tenements (Scotland) Act 2004 introduced the Tenement Management Scheme as a default management scheme to ensure every tenement\textsuperscript{11} in Scotland - existing and future - has proper rules for maintenance and management. The major change the Tenement Management Scheme makes is that if title deeds do not make provisions on decision-making by owners, a majority of owners will be able to take decisions. The Tenement Management Scheme sets out rules on the following issues:

- What "scheme property" consists of
- The procedure for voting
- What the owners can decide
- How costs are to be apportioned
- What "maintenance" means
- How a manager can be appointed, and
- How owners can act in an emergency.

Although Tenement Management Schemes are only a useful tool when title deeds are silent or unclear, they do not apply where title deeds already outline rules for repairs and maintenance. It is CIH Scotland’s experience that only in very modern schemes do title deeds make provisions for repairs and maintenance and few make provisions for how monies will be collected and spent.

CIH Scotland welcomes both pieces of legislation as they assist in improving standards and conditions in the private sector. However, CIH Scotland argues that neither provides a compulsory framework for owners to arrange for monies to be collected and saved to ensure payment for repairs and maintenance to communal parts of buildings is easily organised. CIH Scotland believes that the introduction of a Building Reserve Fund will ensure this is the case.


\textsuperscript{11} A tenement is any building which comprises two or more flats which are designed to be in separate ownership and a divided for each other horizontally. (Section 23 Tenements (Scotland) Act 2004)
What is a Building Reserve Fund?

A Building Reserve Fund (BRF)\textsuperscript{12} is a fund into which owners in flatted accommodation make regular payments to cover the costs of any ongoing or future repair and maintenance needs of the common elements of the property. Common elements include roofs, external walls, drains, downpipes, shared staircase, close or stairwell and garden. In essence, a BRF will help owners to save toward future repair and maintenance to all common parts in which they have shared ownership and responsibility.

Advantages of a Building Reserve Fund

All too often owners can experience large bills for necessary repair work. These can cause financial hardship. A BRF can help spread the costs of this work as owners will contribute to the fund over time.

Owners are sometimes aware that there is a problem with the building but are unwilling to act for fear of financial consequences. Again a BRF, by spreading the cost, can alleviate these concerns.

Often essential repair work is not undertaken because owners cannot agree to proceed with it, or there are fears that the owners who do agree will find it difficult to recover the costs from owners who do not consent to the work. A BRF addresses this by ensuring that all owners contribute to the fund.

A BRF would also overcome issues of owners selling within a few years of purchase and therefore having no or little impetus to take an interest in the wider property condition and maintenance. A BRF would ensure all owners and prospective owners take an active interest in property conditions.

By having a BRF in place repair work will often be carried out sooner. This can mean the actual cost of the repair is less because it is dealt with before it gets worse and therefore more costly to fix. A BRF could be backed up by a regular survey of the tenement, paid for from the fund itself. This may take place every five years and will highlight upcoming repair issues that can be addressed before they become more costly.

\textsuperscript{12} Building Reserve Funds are sometimes also referred to as sinking funds.
Are there successful examples elsewhere?

Yes. Since 1961, Australia has operated a similar scheme to Building Reserve Funds known as Strata Title Schemes. In 1996 there was a significant overhaul of legislation which now forms the basis of the current scheme. The Australian system has also influenced similar legislation in New Zealand, South Africa, Singapore, Canada and also Britain’s statutes involving commonhold ownership.13 As a result, CIH Scotland has looked closely at the Australian model and seeks to replicate much of its good practice in our proposals.

In particular, key features of the Australian scheme include:

• The creation of a fund to collect monies for future repairs and maintenance costs.

• A ten year plan covering the renewal and replacement of building elements, cyclical repairs and maintenance of common parts which is reviewed every five years.

• Ownership of the fund is by the Body Corporate and this is an asset that is sold with the unit.

• Owners are not entitled to a refund of their contributions upon sale because these contributions, like the agreements, are sold with the unit.

• Any property management agents appointed by the Body Corporate must be licensed.

• A Strata Title Information Service was established to offer free advice.

• Mediation is mandatory before proceeding to an adjudicator or board to settle disputes in order to avoid court action where possible.

• Instead of the cost of debt recovery being shared by all owners, it is the responsibility of the individual debtor.

• The Body Corporate has the right to offer incentives for owners to pay in full and on time, such as a 10% discount on their annual contribution.

Further information on all our international case studies, including information on schemes in France, USA and China, is included in Appendix 1.

How would Building Reserve Funds be established?

The Scottish Government could use the current Housing (Scotland) Bill or the forthcoming Private Sector Housing (Scotland) Bill to legislate for Building Reserve Funds in Scotland. This could give the Scottish Government the power to direct home owners in Scotland to enter into a fund with their neighbours, where they hold joint interests in common property.

CIH Scotland proposes that:

- Building Reserve Funds would be compulsory in all new flatted accommodation in Scotland and therefore be included in the associated title deeds.

- Local authorities would have the power to instruct all owners to create a Building Reserve Fund in existing flatted accommodation where there are persistent problems with repairs and maintenance. Similar to current powers associated with maintenance orders, the existence of a Building Reserve Fund would also require to be registered with the Land Registry.

- The Scottish Government test the effectiveness of Building Reserve Funds by piloting them with a wide range of owners and property types across Scotland. Only after successful pilots should the Scottish Government commence the section of the Act pertaining to Building Reserve Funds.

It is often reported that it is particularly difficult to take forward maintenance and repair work in larger tenements. However, we should not preclude smaller flatted accommodation from being able to set up BRFs and access the same advice and support. Where there are persistent problems with some owners frustrating repair and maintenance work, local authorities should have the power to instruct all owners to develop and contribute to a BRF.

A pilot process would not only enable the testing of the BRF model but if necessary would refine the BRF model and help promote BRFs to other owners. Once successfully piloted the BRF model could be rolled out across Scotland, enabling owners to save for and carry out ongoing and future repairs.
How would a Building Reserve Fund be run and constituted?

A BRF would require the establishment of an Owners’ Association. Legislation should be used to enable this. The Owners’ Association would be the decision-making body. It would be charged with the statutory duty to maintain and keep in a state of good repair all the common elements of a property. An Owners’ Association would be created for each property where there are joint interests in common parts.

The constitution could only be changed at a specially convened meeting of the Owners’ Association. Every owner would have an equal vote in decisions about the Owners’ Association and consequently the BRF. In line with the Tenements (Scotland) Act 2004, majority voting could apply to all decisions.

Housing legislation could ensure that membership of an Owners’ Association is tied to ownership of a flat within the property. Upon a change of ownership, i.e. when an owner sells their flat, membership of the Owners’ Association would pass to the new owner. Therefore, each individual owner would be a member of the Owners’ Association by virtue of owning a flat in the property.

To assist the setting up of Owners’ Associations the Scottish Government should develop and promote a model constitution, guidance on set up and operation, and provide advice and assistance to individual schemes.

Owners Association’s may decide to appoint a Property Manager to carry out some or all of its duties in relation to maintenance and repairs of all common parts. As an Owners’ Association will have a statutory duty to maintain and keep in a state of good repair all the common elements of a property, CIH Scotland would argue that it would be good practice for them or their appointed property manager to be either:

- Registered with a local authority
- Registered with the Land Registry
- Registered with the Scottish Government, or
- Accredited by the Property Managers Voluntary Accreditation Scheme.
How would a Building Reserve Fund be managed?

The Owners’ Association would have the ultimate responsibility to manage the BRF. However, whilst the Owners’ Association would retain overall responsibility, the day to day management of the scheme could be assigned to another body or managing agent. This could be the local authority, a Registered Social Landlord, an accredited factoring or property management service. Alternatively, the Owners’ Association could choose to be responsible for the day to day management of the BRF.

The managing agent would make regular reports to the Owners’ Association with recommendations for action. The Owners’ Association would retain the power to accept or reject these recommendations based on majority voting principles.

Although CIH Scotland would like to see the future regulation of property managers in Scotland in the interim, it may be advisable to encourage bodies wishing to be management agents to be accredited by the Scottish Government’s forthcoming Property Managers Accreditation Scheme.\(^{14}\) This will ensure they comply with current legislation and meet certain standards.\(^{15}\) If an Owners’ Association is unhappy with the service it is receiving from a management agent it may take its case to the Property Managers Accreditation Scheme to investigate the complaint and refer to dispute resolution services provided alongside the scheme.

Ultimately, CIH Scotland would like to see a mandatory registration scheme for property managers which will not only protect Owners’ Associations but should help reputable managers to provide high quality services in a competitive market.

How much should an owner contribute?

The level of funds that an owner should contribute should be set by the Owners’ Association, and the share each owner pays would be in accordance with the title deeds or Tenements (Scotland) Act 2004. An appropriate way to do this is to commission a property survey at the outset that will detail any current repair issues.

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\(^{14}\) At the time of print the Scottish Government is consulting on establishing a voluntary Property Managers Accreditation Scheme.

\(^{15}\) This is similar to the Scottish Executive legislation and proposals on accrediting and registering private landlords to ensure high standards.
and make an assessment of the likely future repair and maintenance needs. The survey should then make an assessment of the monthly payment into the BRF that the property owners should make. The final decision on how much each owner will contribute would rest with the Owners’ Association, in line with title deeds and the Tenements (Scotland) Act 2004. The amount of funding to be contributed to the BRF would be assigned equally amongst all owners unless otherwise stated in title deeds.

Periodic property surveys, probably about every five years, can help to update the position and ensure neither too much nor too little is being placed in the BRF.

**Who owns the money in the Building Reserve Fund?**

As the BRF is property specific i.e. set up to help maintain and repair the common parts of a specific property, the money in the BRF would belong to the Owners’ Association and not to the individuals paying into the scheme.

The aim of a BRF is to ensure that the future condition of a specific property can be guaranteed. This may be put in jeopardy if individual owners retained ownership of their contribution, enabling them to withdraw it when they move.

**What will the fund pay for?**

Each owner’s contribution to the BRF would be held centrally by the Owners’ Association or its property manager. The BRF would then be used to pay for:

- The on-going maintenance of commonly owned parts of the property such as painting the common stair, servicing the entry system or the upkeep of the garden area.
- Required repair work to the commonly owned areas such as repairing the roof, fixing unstable or damaged masonry or replacing a broken stair door window.
- The property manager’s fee including the commissioning of regular surveys.
- The cost of the regular property condition survey.
- The set up and running costs of the Owners’ Association.
How will repairs issues be identified?

Repair issues would be identified largely through a regular property condition survey. However, individual owners may also become aware of repair issues that can be reported to the property manager or Owners’ Association for further action. Similarly, the Home Report\(^\text{16}\) commissioned with the sale of a flat within the property may highlight a repair issue for the common areas.

What happens when ownership changes?

When a flat within the property changes ownership, the funds paid into the BRF would remain in the BRF. This is because the funds would belong to the Owners’ Association and not the individual. As per the Australian system, owners are not entitled to a refund of their contributions upon sale because these contributions, like the agreements, are sold with the unit.\(^\text{17}\)

The information provided by the seller to the prospective buyer within the Home Report (Property Questionnaire) could include details of the BRF and the level of payment the new owner would be obliged to pay into the fund. The BRF could become one of the selling features of the flat and may perhaps be reflected in the price the flat can command.

How would Building Reserve Funds be enforced?

CIH Scotland is proposing that it becomes a legislative requirement to establish BRFs in all new flatted developments. This would mean that the requirement to establish a BRF will be written into the Title Deeds of the development and all new owners will be aware of their requirements to contribute to and participate in the BRF as part of the sale. This is similar to what is well established practice in Australia.

Whilst CIH Scotland would ideally like to see BRFs established for all existing developments, this may not be practical in some circumstances. For example, some flat owners may already have arrangements in place. Instead, CIH Scotland would

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\(^{16}\) From December 1, 2008, houses for sale in Scotland have to be marketed with a Home Report. This is a pack of three documents: a Single Survey, an Energy Report and a Property Questionnaire. The Home Report is made available, on request, to prospective buyers. For more information please refer to: www.scotland.gov.uk/Topics/Built-Environment/Housing/BuyingSelling/Home-Report

\(^{17}\) Bailey, N. and Robertson, D. (1998) Flat Management in Three Countries, Stirling: University of Stirling, p16
like to give the local authorities the powers to require owners, where there are serious concerns about the lack of repairs and maintenance of common parts, or where the wider amenity of the community may be at risk due to the lack of repairs and maintenance, to establish a fund. Where this is the case, local authorities, with support from the Scottish Government, should provide guidance and advice to owners to establish an Owners Association and a BRF. Where such an order is in place, this would be registered with the Land Registry. Therefore, where an affected flat is sold, the prospective new owners are aware of their rights and responsibilities from the outset.

How would disputes be resolved?

CIH Scotland would urge the Scottish Government to follow the original recommendations of the Housing Improvement Task Force and create a Private Housing Tribunal for Scotland. By doing so, this could be charged with addressing disputes. Ideally disputes would be resolved via mediation but where this fails the Private Housing Tribunal for Scotland should have powers to enforce a binding decision.

In the interim, dispute resolution and mediation services are proposed to form part of the forthcoming Property Managers Accreditation Scheme. CIH Scotland would urge the Scottish Government to enable Owners’ Associations to become accredited by the Scheme and therefore also have access to its services. Where an appointed property manager is in place, they too should be accredited with the national scheme.

What would happen if someone refuses to pay?

As per the Australian scheme, CIH Scotland would advise that there are incentives for owners to pay in full and on time. For example, a 10% discount. However, the scheme would also need to have sanctions that could be exercised against an owner who refuses to pay their share into the BRF. If an owner is not up to date on their

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18 The CIH has made proposals for a wider Housing Tribunal system in Scotland that can deal with both social rented, private rented and owner occupation issues.
contributions they may lose particular rights, such as not being entitled to vote at Owners Association meetings on repairs and maintenance decisions.\(^{19}\)

Where an owner refuses to pay their share of costs, depending on the constitution of the Owners Association and the property management arrangements in place, a number of options could apply:

1. The Owners Association or the appointed manager could make a charge against the flat. Therefore, if the owner sells, that proportion of the selling price equal to the unpaid debt and any interest that would have accrued can be reclaimed by the Owners’ Association. This is currently the case in France.

2. The Owners Association or the appointed manager, could transfer the debt to the new flat owner. Full disclosure through the Home Report will ensure the prospective buyer knows that a debt is associated with the property prior to purchase, which they will be required to repay. This could either make them less likely to buy or encourage them to negotiate a lower selling price for the flat to compensate the outstanding debt with the seller.

3. The Scottish Government could make it a civil offence not to contribute to the BRF therefore allowing the Owners Association or appointed property manager to use the court system or Private Housing Tribunal for Scotland to prosecute an individual owner for non-payment into the fund.

4. Where a local authority requires owners in existing flatted accommodation to establish a BRF, the local authority could pay the missing share on behalf of the owner and seek to recover the costs through the court system. This is similar to proposals to amend the Housing (Scotland) Act 2006\(^ {20}\) currently being put forward in the forthcoming Housing (Scotland) Bill\(^ {21}\).

**What happens if someone cannot pay?**

There may be circumstances where owner occupiers on low incomes, such as some older people, face difficulties in contributing into the BRF.

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\(^{19}\) Bailey, N. and Robertson, D. (1998) *Flat Management in Three Countries* Stirling: University of Stirling, p. 11

\(^{20}\) Housing (Scotland) Act 2006 www.opsi.gov.uk/legislation/scotland/acts2006/asp_20060001_en_1

\(^{21}\) Housing (Scotland) Bill 2009, www.scottish.parliament.uk/s3/bills/36-Housing/b36s3-introd.pdf
Part 2 of the Housing (Scotland) Act 2006 creates a new Scheme of Assistance for housing purposes, based on the principle that individual owners (including owners of privately rented houses) have primary responsibility for maintaining their properties in good condition, with assistance available when necessary. This Scheme allows local authorities to provide assistance for house repairs, improvements, adaptations and construction, as well as the acquisition or sale of a house. The assistance can take various forms, including grants, standard and subsidised loans, practical assistance, information or advice. In certain circumstances - for work required by a work notice or an adaptation to meet the needs of a disabled occupant (or reinstatement) - local authorities must provide assistance. Therefore, in creating Schemes of Assistance, local authorities may want to consider what assistance they would be able to provide more vulnerable households unable to make their contributions to BRFs.

Alternative options to consider could include:

- The possibility of releasing equity in the property to enable contributions.

- As per option 2 above, the debt could be transferred to any new owner. If there is full disclosure through the proposed Home Report then the prospective buyer will know that there is currently a debt associated with the property. This could either make them less likely to buy or encourage them to negotiate a lower selling price for the flat to compensate the outstanding debt with the seller.

**How do BRFs fit with the Scottish Government’s proposals for improving quality of housing in private sector?**

The Housing Improvement Task Force was set up by Scottish Ministers in December 2000 to consider issues relating to housing quality in the private sector and the house buying and selling process. The Task Force's first report, *Issues in Improving Quality in Private Housing* (2002), confirmed that, although most private sector housing was in good condition, a significant proportion was in poor repair. In March 2003, the Task Force published its final report and recommendations, *Stewardship and Responsibility: A Policy Framework for Private Sector Housing in Scotland*. Legislative proposals based on these recommendations were consulted on in *Maintaining Houses - Preserving Homes* in 2004 and were widely welcomed by local
authorities and other stakeholders. The Housing (Scotland) Act 2006 was then enacted to build on all of this work.

The main purpose of the Act was to address, through encouragement and, where necessary, enforcement, problems of condition and quality in private sector housing, both owner-occupied and private rented (although some provisions also relate to the social rented sector). The underlying principles are that:

- Owners have primary responsibility for maintaining their houses, with assistance available where necessary
- Landlords should provide houses that are suitable and in good condition
- In order to improve the condition of private housing it is important for local authorities to have powers to deal with the issue
- Local authorities should have flexibility to allow for local solutions and should adopt a strategic approach.

The Scottish Government recognises that intervention may sometimes be necessary where disrepair affects other owners such as in common areas. A BRF reflects this position by giving owners a structure in which they can take full responsibility for maintaining the common parts of their home.

The Scottish Government does not believe that owners subject to enforcement action, to tackle disrepair, should have an automatic entitlement to grant aid. Proposals for a BRF ensure that repairs and maintenance issues do not deteriorate to the stage where significant intervention is required, thus enabling owners to budget and save for essential future repair and maintenance work. This can help to reduce the burden placed on public funds for financial assistance from owners facing high repair costs.

The Housing (Scotland) Act 2006 also introduced maintenance orders. These can be served on owners who are failing to maintain the common parts of their property. It requires all owners in an affected property to put in place and implement a maintenance plan. A Maintenance Order is similar in that it sets out how the future maintenance of the building will be conducted but it does not have the advantages of a BRF in that a BRF:
• Is implemented before the property condition deteriorates to a level where emergency intervention is required.

• Is developed and maintained over time by the owners and is not imposed on owners like the maintenance order as a result of enforcement from the local authority.

• Is not time limited and will therefore set a long term repair and maintenance plan, unlike a Maintenance Order that will run for a maximum of five years.

• Covers repair work as well as maintenance work.

• Sets up a process to pay for maintenance and repair works, outlines how it will be funded and ensures that a process is in place to save and pay for current and future works.

CIH Scotland is proposing that, in line with other countries, BRFs will act as a preventative measure through the longer term planning of repair and maintenance to keep buildings in a good state of repair. Current measures are only applicable when disrepair has become significant and costly and do not set out a process for collecting monies. Therefore, BRFs would reduce the need for last minute and expensive intervention.

Next steps

CIH Scotland urges the Scottish Government to consider the case for Building Reserve Funds and to include provisions within the forthcoming Housing (Scotland) Bill for the introduction of BRFs for all residential properties sharing common parts.

CIH Scotland asks the Scottish Government to:

• Make Building Reserve Funds compulsory in all new flatted accommodation in Scotland and therefore be included in the associated title deeds.

• Give local authorities the power to instruct all owners to create a Building Reserve Fund in existing flatted accommodation where there are persistent problems with repairs and maintenance. Similar to current powers associated with Maintenance Orders, the existence of a Building Reserve Fund would also require to be registered with the Land Registry.
• Test the effectiveness of Building Reserve Funds by piloting them with a wide range of owners and property types across Scotland. Only after successful pilots should the Scottish Government commence the section of the Act pertaining to Building Reserve Funds.
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Housing (Scotland) Act 2006,


Scottish Executive (2004), *Maintaining Houses - Preserving Homes*, Scottish Executive


Appendix 1

International Case Studies

A number of countries have Building Reserve Funds (BRFs), or variations of them. New Zealand, South Africa, Singapore and Canada all have variations of BRFs. For the purposes of this paper CIH considered schemes in:

- Australia
- China
- France
- USA

Australia – Strata Title Schemes

Background

Since 1961, Australia has operated a similar scheme to Building Reserve Funds known as Strata Title Schemes. In 1996 there was a significant overhaul of legislation which now forms the basis of the current scheme. The Australian system has also influenced similar legislation in New Zealand, South Africa, Singapore, Canada and also Britain’s statutes involving commonhold ownership.22

Strata Title Schemes were introduced largely to help facilitate more concentrated land use developments (similar to tenements) by ensuring that owners took responsibility for the upkeep of all common parts. Therefore, Strata Title Schemes apply to properties that are divided into units and share common property/areas.23

How it works

Owners will purchase a freehold of a unit and share ownership of the common property/areas indirectly through a body corporate which consists of all the unit owners. Collectively, the owners form the body corporate which is a registered unlimited liability company and therefore a separate legal entity as an agent for all owners. The body corporate has a statutory duty to maintain and keep in good repair all common property by holding regular general meetings where owners can vote on

day-to-day decisions, ensuring that a minimum number of votes are cast as required for certain decisions.

The body corporate then has a range of powers to organise maintenance and collect payment by establishing two separate funds\(^\text{24}\):

- An administrative fund which covers day-to-day repairs, insurance, service charges and management fees, and

- A sinking fund - a ten year plan which covers the cost of renewal and replacement of building elements, cyclical repairs and maintenance of common parts. This plan and the building’s future repair and maintenance requirements are reviewed every five years – this is also essential for insurance purposes. The sinking fund is owned by the body corporate and is an asset that is sold with the unit.

The body corporate appoints a treasurer who is responsible for notifying owners of contributions, recording payments made, and keeping financial records and audits. The body corporate also has the freedom to hire a professional management agent to carry out some or all of its duties. However, management agents must be licensed under the Property, Stock and Business Agents Act, and smaller developments tend to be self-managed because of the costs involved in contracting an agent. A separate caretaker can also be appointed to manage, maintain and repair common property.

Whether the funds are managed by a treasurer or a managing agent, the accounts must be kept in a particular form and all monies paid to them on trust. Agents are mandated to provide access to financial records and to hand them over to the body corporate if the agent’s contract is terminated.

Subsequent owners and assignees are bound to the initial agreement made by the original owner, such as by-laws and the assessed unit entitlement. Owners are not entitled to a refund of their contributions upon sale because these contributions, like the agreements, are sold with the unit.

The body corporate also has a responsibility to carry insurance, such as full buildings insurance, workers’ compensation and insurance for voluntary workers. As the body corporate is an unlimited company and the unit owners are fully liable for its debts

collectively, it is important to maintain public liability insurance. Australia is unique in that the body corporate purchases a master insurance policy for the entire building to cover rebuilding upon destruction.

**Dispute Resolution**

In reviewing the original legislation, a mechanism for alternative dispute resolution was instituted to deal with minor complaints quickly and cheaply, as opposed to being dealt with in court. A commissioner was appointed to decide cases at a nominal charge. Either party can appeal to the registering board if unsatisfied with ruling for adjudication. An adjudicator can rule on disputes involving repairs to common property and enforcing by-laws. A final right of appeal is reserved for a supreme court. As a mediation service, community justice centres were also established to deal with minor complaints.

As part of this effort to prevent disputes from escalating or occurring at all, a Strata Title Information Service was established to offer free advice. Mediation is now mandatory before proceeding to an adjudicator or the board to settle disputes in order to avoid a pervasive confrontational approach associated with this tenure. Mediation is limited in what it can offer aggrieved parties and cannot appoint a property manager, issue interim orders or stays, revoke previous orders, or impose civil orders. Settlements decided in mediation are, however, binding on both parties and can be made into an enforceable order.

**Enforcement**

If an owner is not up to date with their payments they are termed “unfinancial” and lose particular rights, such as not being entitled to vote at body corporate meetings.

Enforcement has been an issue and there have been problems with prompt and full payment. Instead of the cost of debt recovery being shared by all owners, it is the responsibility of the individual debtor. New amendments to the Strata Title Act now give the body corporate the right to offer incentives for owners to pay in full and on time, such as a 10% discount on their annual contribution.  

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For severe cases where the body corporate as a whole fails to perform its statutory duties, the registering board may appoint a managing agent. This typically happens when the body corporate is in debt, there is a lack of maintenance or if the body corporate fails to hold regular meetings.  

**China – Reserve Maintenance Funds**

The concept of private ownership was legally recognised in 1988, and the concept of transferable land use rights was incorporated into China’s constitution in 2004. Article 70 of national property law (2007) defines apartment ownership as where:

‘an owner shall enjoy the ownership in respect of such exclusive parts within the apartment building as the apartments for residential or commercial purposes, and the co-ownership and common management right with regard to jointly-owned parts other than the exclusive parts.’

Apartment ownership in China is similar to Strata Titles in Australia where there is private ownership of individual units, collective ownership of common parts and a mandatory membership of Owners Associations. Apartment owners are jointly responsible for the cost of maintenance and repairs of common areas and all owners automatically become members of the Association when they acquire ownership of an apartment.

**How it works**

Existing state owned housing that was privatised during the 1988 economic reforms was required to establish Reserve Maintenance Funds. These maintenance funds are contributed to by the housing seller and buyer at the time the property is privatised in order to pay for the maintenance and repair of common parts. The Owners Association and the Owners Committee have the right to allocate the maintenance fund. It is the responsibility of the Owners Committee to create a strategic plan for maintenance. Spending from the Reserve Maintenance Fund is

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usually on reactive repairs reported by owners. The Owners Committee is responsible for making sure this fund is sustainable and does not deplete.

An Owners Association is made up of all individual owners responsible for the management and administration of the buildings and associated facilities. All owners automatically become members of the association when they acquire ownership of an apartment. Owners Associations elect members to the Owners Committee which can, in accordance with law, decide matters such as:

- The constitution and rules for the owners’ meeting
- The constitution and modification of management regulations with regard to the apartment buildings and associated facilities
- Election of members to the owners’ committee
- Employment and dismissal of any realty service organisations or other managerial personnel
- Raising and utilisation of funds pertaining to the maintenance of the property and associated facilities
- Repairing, reconstructing, rebuilding the buildings and their associated facilities, and
- Other major and important events with regard to the co-ownership and right of common management.

Owners are entitled to attend meetings of the Owners Association, exercise their right to vote members of the committee of property owners, and also run for committee. Voting rights are determined by the size of the property and the number of units they own. All owners participate in the decisions and resolutions reached by the Owner’s Association and these are binding on all owners.

The management model for apartment buildings combines owners’ self governance and professional management by a property management company. Owners have a principle-agent relationship with the property management company where the contract between the two parties dictates the services to be provided. The owners

determine the covenants and rules of procedure of the Owners Association and the property management company is charged with implementation.

Maintenance funds are held by either the property management company or the Owners Association (if incorporated) in which each owner has a direct interest. Owners Associations require to be incorporated in order to allow it to sue and be sued, enter into contractual agreements with property management companies, collect contributions from owners, establish management and maintenance funds, pay taxes, and provide adequate insurance for common owners to protect them against tort liability.31

Every owner is charged two separate fees for property management, one for security and cleaning and the other for general housing management. Property management fees pay for services including maintenance, security, cleaning and lawn keeping.

Building reserve maintenance funds are established at the time the multiple ownership of the apartment building is created, with both the buyer and the seller contributing to the fund. This fund is contributed to regularly for ongoing improvement costs but there are issues in enforcing contributions by successive owners. As a result, this fund is typically spent on reactive repairs rather than planned maintenance. Larger repair and maintenance works can be difficult to initiate since voting in favour of them requires a legal quorum and expensive improvement works are usually vetoed by owners.32

**Dispute Resolution**

The Owners Committees receive complaints and are responsible for trying to solve disputes between owners. According to Article 78 of the property law the “decision made by the owners’ meeting or committee shall be binding upon the owners. Where the decision made by the owners’ meeting or committee infringes upon the legitimate rights and interests of the owner, they may apply for cancellation with the People’s

The code prescribes the majority of vote needed for resolutions that substantially impact the property rights of individual owners.

**Enforcement**

“Street level” government agencies do exist to instruct and supervise Owners Committees. Where Owners Committees are not proactive, the city planning authority or property management company can step in and temporarily function as the Owners Association.

However, despite this legislation, no legal obligation exists to guarantee payment of maintenance fees for common property. The law does not give the Owners Association or the Owners Committee any enforcement means to implement their decisions. Even if enforcement measures exist, the law does not impose them since foreclosure procedure is cumbersome and associations have not been willing to apply it.

The property management company is responsible for enforcing sanctions but often they prefer not to for fear that the owner will push to veto their work contract at the next Owners Association meeting. There are also few regulations at the national or local level regarding sanctions for non compliance.

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France – Co-propriété System

France is credited with being the first country to create a nationwide statutory system to deal with flat ownership in 1804. It currently operates a Co-propriété system. Legislation in 1965 overhauled previous systems and provides for the current statutory framework. One fifth of France’s households live in properties covered by the Co-propriété system, many of them in older tenemental style properties similar to Scotland.

How it works

Co-propriété applies to any property owned by two or more people where an owner owns a unit representing individual ownership of a flat, together with a share in the common parts of the building. Co-propriété schemes can also apply to detached houses with shared common property. The distinguishing feature of co-propriété is that the ownership of the private parts cannot be separated from ownership of the common part. Also, the ownership of the common part cannot be divided among owners but remains wholly in co-ownership.

Every scheme has a co-ownership agreement with a schedule of division, which is recorded on the local register with the property deed and has the status of a contract. The constitution of the bodies set up to manage the scheme is determined by statute and cannot be overridden by contract. The agreement contains information about the intended purpose or character of the property and is a concept that helps to protect the rights of individuals against those of the majority. The agreement also informs owners of their rights and responsibilities, and clearly defines individual and common property.

Each owner’s share in the common property is included in the agreement and if this is not included then the shares are determined by the relative value of the flats at the point of registration. The share determines how much the owner is responsible for,

the cost of maintenance and management of common property and the weight of their vote at general meetings.

All co-owners are also mandatory members of an Owners Association which is a body corporate that has unlimited liability. The purpose of the association is defined by statute and it must ensure proper management and maintenance of a property and defend the collective interest of all owners. The association is liable to individual owners and third parties, and is a separate legal entity that may enter into contracts, sue, and be sued. The constitution of the association is determined by national statute and the decision making rests with the association at general meetings.

Since 1985 it has been mandatory for owners to elect a council unless it specifically decides not to. The council is an intermediary that assists the appointed managing agent in decision making and to supervise their work. The council cannot spend money or take decisions and is not a separate legal entity. Councillors are elected at general meetings and hold posts for a period of up to 3 years.

In addition to electing a council, the owners association must appoint a managing agent who has statutorily defined powers and responsibilities. The managing agent may be a voluntary co-owner but is typically a professional. The managing agent cannot sit on the owner association’s council. If an agent is not appointed an owner may apply to the courts to have one appointed for them.

Since 1994 the managing agent of the co-proprietor is responsible for raising a motion at ownership association general meetings once every three years for maintenance planning by setting up a special fund which will cover the maintenance required over the next three years. The association can vote down the management agent’s recommendations or can pass this motion with a simple majority at two consecutive general meetings.

Managing agents are responsible for implementing the decisions of the association at a general meeting, except in an emergency, where they can act without calling a

meeting. The agent can be allowed more freedom if the association approves a fixed budget for it to use without advance approval.\(^2\)

The agent is responsible for general administration, for calling general meetings, keeping minutes and informing all owners of all decisions made. They also draft annual budgets and ensure that the running of the building does not contravene any statutes, are responsible for managing accounts and operate an account for the property.\(^3\)

Self-management is an option for co-owners who choose not to hire a professional managing agent. Voluntary managing agents are usually one of the co-owners and are appointed by other owners. Voluntary managing agents are not bound by statutory regulations the same way professional agents are and do not need to be registered. Unlike professional managing agents, voluntary agents cannot charge but can claim expenses.

About 40% of co-ownership schemes in France are self managed, due to the perceived benefits of lower costs, the freedom to make changes to the scheme, or simply because of previous bad experiences with professional managing agents.\(^4\)

As an alternative to voluntary or professional management, a scheme can elect by a two-thirds majority to turn itself into a cooperative where the council becomes responsible for management (instead of just supervision) and management is carried out collectively. The council elects one councillor to be president who has the powers of a managing agent and represents the council. There are also private organisations available that offer education, training and expert advice for owners wishing to self manage.

**Enforcement**

All disputes are dealt with in court, which is expensive since aggrieved parties are required to employ a barrister. In 1994 there were revisions to the law to allow courts to get involved with troubled schemes and to reinforce requirements for maintenance

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[www.cihscotland.org](http://www.cihscotland.org)  Your work is our business  31
planning by appointing a provisional manager.\(^{45}\) This manager can arrange works and collect payments without consulting owners. The courts will also appoint a managing agent if an association fails to do so.

Resolving disputes within the courts involves an owner challenging an association’s decisions only if they voted against or were absent during the vote. To do so they must appeal within two months of being notified. Challenges can arise if the association did not follow procedures and acted ultra vires, or if a majority vote alters the designation of the property and is an abuse of majority rights.\(^{46}\)

The managing agent has a statutory obligation relating to the financial management of the association. They are responsible for billing each owner for their share of the costs and for ensuring payment. The managing agent must police and enforce this agreement. In the case of legal action, the managing agent represents the association.\(^{47}\) The managing agent is responsible for pursuing property and service charges from owners, and does not require permission from the general meeting. Unpaid property charges result in a charge on the property, which is ultimately enforced by attachment and sale if remaining unpaid.

By protecting the rights of the individual over the interest of the majority, French statute prohibits the enforcement of by-laws by co-owners excluding an owner from their property or forcing them to sell their property. If a tenant is in violation of the by-law the co-owners can apply to the courts to have their lease terminated.

The burden of extra maintenance falls on all owners jointly, which has caused conflict when one owner is believed to have been more the cause of this extra maintenance than others. Specific damages may be liable to an individual if set out in the agreement but this is difficult to enforce.

\(^{45}\) Bailey, N. and Robertson, D. (1998) *Flat Management in Three Countries* Stirling: Stirling University, p22


United States of America – Common Interest Ownership

In the USA home ownership has always been an important feature of society. However, until the 1960s this usually meant individual detached properties. However, increasing land and construction costs, coupled with local government no longer being prepared to pay for the provision and upkeep of infrastructure led to the rise of flatted urban accommodation. This gave rise to Common Interest Ownership which encompasses a form of BRF. Common Interest Ownership is also used for developments that consist of detached houses that share some common elements.

How it works

Common Interest Ownership is provided via Common Interest Communities (CICs). These are forms of property ownership involving ‘a real estate development or neighbourhood in which individually owned lots or units are burdened by a servitude, that imposes an obligation that cannot be avoided by non-use or withdrawal, to:

1) pay for the use of, or contribute to the maintenance of, property held or enjoyed in common by the individual owners, or

2) pay dues or assessments to an association that provides services or facilities to the common property or to the individually owned property, or that enforces other servitudes burdening the property in the development or neighbourhood.\textsuperscript{48}

Community associations, or owners associations, are a defining feature of CICs. They are fixed in statute to administer the operation of common property. Membership of the association is mandatory for all residents, who elect a board of directors (who are also residents) to represent the interests of other unit owners. Association board members have an entrusted responsibility to other unit owners as they have the power to levy assessments, make spending decisions and determine residency and operational rules. Board membership is strictly voluntary and unpaid.

Community associations can be unincorporated or incorporated. Some associations govern by simple majority consensus (democracy rule) and others are given wider discretionary powers depending on by laws, deeds as well as state and federal law.\textsuperscript{49}

\textsuperscript{48} Restatement (Third) of Property: Servitudes of 2000 (property can be burdened by three types of servitudes: profits or the right to remove resources from another’s land, easements or the right to use another’s land or common property, and covenants or the right to receive compensation or services or the right to have other landowners abide by use affirmative or negative restrictions or obligations)
Community Association assessments are the assets of the association (and not refundable to owners) that cover the costs of administering, maintaining, repairing and replacing common elements. Unit owners are bound by the terms of the declaration to pay their shares of the assessment.

**Enforcement**

Failure to pay assessment fees, or other fees required in the declaration such as late fees or transfer fees, becomes an automatic lien\(^50\) that attaches to the homeowner’s property and that is given priority over all other liens. To satisfy delinquent debts, the association can seek from the courts permission to foreclose on the property, and the proceeds from the sale are first applied to the assessment debt before mortgage debt. Even without executing a foreclosure sale, a lien on the property becomes a cloud on the title which prohibits any further transactions and refinancing.\(^51\)

Associations are generally mandated by state law and because they are quasi-governmental in nature, they enjoy a judicial presumption of validity. If conflict between an owner and the association escalates to the point of litigation, courts will typically apply the business judgement rule of corporate law. The court will refuse to examine board conduct unless the disgruntled owner can satisfy their burden of proof by showing that the board acted fraudulently, in bad faith, or with a conflict of interest.\(^52\)

The reason for this high level of deference the courts are willing to afford association boards is the acknowledgment that common interest ownership represents a voluntary agreement (when the association is in full compliance with disclosure law) to submit to a decision-making authority and that there is always the freedom not to participate in this form of tenure.\(^53\)

The reason why Community Associations are so effective in the USA is because by virtue of living in a CIC an owner wilfully submits to the governance of an Association. This wilful submission enables the Association to have wide

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50 Lien is the legal right to keep or sell somebody else’s property as security for a debt.


53 Levandusky v. One Fifth Apartment Corp. Court of Appeals of New York (1990)
discretionary powers that are largely protected from the risk of litigation whilst also offering consumer protection through disclosure laws.

Dispute resolution involving CICs has become an increasing issue in the USA as this form of ownership increases and Community Associations exercise more discretionary powers of governance. For most states these disputes burden the court system since there are no other formal bodies specifically created to deal with common interest ownership matters. As an alternative, some states have established bureaux to prevent disputes from arising through public education and to address disputes through swift and inexpensive mediation. These also inform potential buyers about the responsibilities associated with this type of ownership, offer information and advice for existing owners and provide legal assistance and training for association boards of directors.\textsuperscript{54}

\textsuperscript{54} State of California Law Revision Commission (2004), Tentative Recommendation for State Assistance to Common Interest Developments p2