

Resolution Foundation

Renting in the Dark: Creating a lettings market that works for tenants

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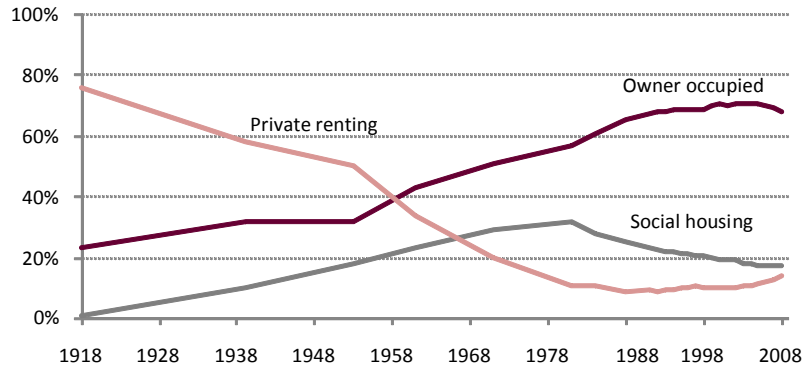
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Executive Summary

The private rented sector makes up 17 per cent of all housing stock today, up from 9 per cent in 1991.¹ The growth of the sector in the UK has brought with it growth in agents to help manage the process of letting. Approximately two thirds of tenancies involved a letting agent in 2006, up from 37 per cent in 1993/4.²

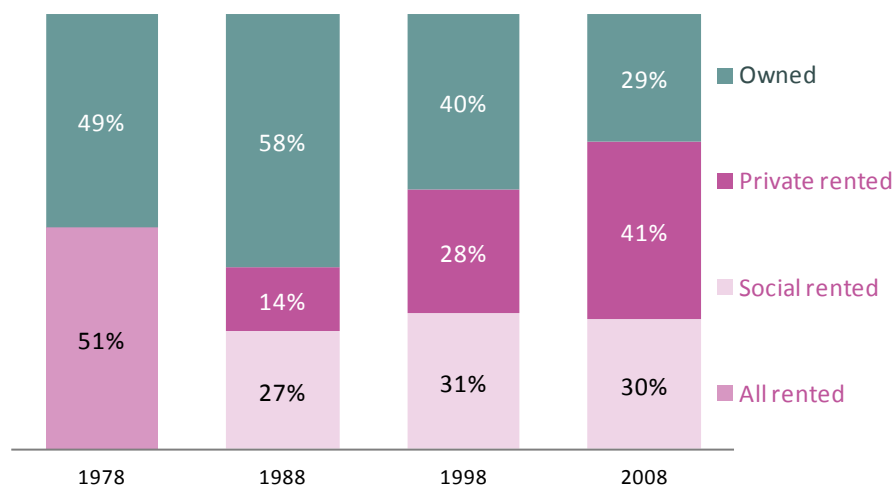
Chart 1: Trends in housing tenure: England 1918-2008



Source: CLG, *Survey of English Housing: Preliminary Report 2007-08*, Table 1

The rise in the number of letting agents has particular implications for low-to-middle income (LMI) households reliant on the private rented sector to provide a long-term home.³ Resolution Foundation analysis suggests that in today's housing market it would take the average LMI household 31 years to save for a deposit on the basis that they are putting aside 5 per cent of their income each year, up from just 8 years in 1993.⁴ At the same time cuts to the social housing capital grant mean that LMI households will find it more difficult to access social housing in the future.

Chart 2: LMI household tenure where the head of household is under 35 years of age: 1978-2008



Sources: Analysis of DWP, *Family Resources Survey and Family Expenditure Survey*

In a predominantly cottage industry of private landlords, where over two thirds are individuals and

¹ CLG live table 104: By tenure, England (historical series)

² Rugg, J. and Rhodes, D. *The Private Rented Sector: its contribution and potential*, 2008

³ The Resolution Foundation defines low-to-middle income households as those in deciles two to five of the household income distribution, excluding those who receive more than 20 percent of their income from means-tested benefits.

⁴ Alakeson, V. *Making a Rented House a Home: Housing solutions for 'generation rent'*, 2011

couples, letting agents can be a useful means for both tenant and landlord to ensure that they are delivering and receiving a professional service. But the level and range of additional charges made by letting agents, alongside difficulties contacting agents, serious delays in getting repairs carried out, and inadequacies in the financial protection of deposits, were all identified as sources of dissatisfaction by clients of Citizens Advice in 2009.⁵ The lack of consumer confidence and professionalism in parts of the market has resulted in numerous calls from the industry, tenant and landlord groups for regulation. At the moment voluntary systems of regulation exist via membership of a professional body and ombudsman service, which covers about two thirds of the market.⁶

With the private rented market forecast to rise to 20 per cent by 2015⁷, and given its particular importance for members of the LMI group, this report looks at the process of renting via letting agents and in particular tenant fees. We find that:

- fees and charges pose a significant upfront cost for LMI households moving in the private rented sector;
- there is significant variation in the level of fees charged by different agents for the same service with no discernible differences in the quality of the service received;
- a lack of transparency alongside the housing shortage has created an ineffective market for price competition.

The report calls for:

- letting agents to be brought under the Estate Agents Act (1979), thereby giving the Office of Fair Trading powers to ban agents who act improperly;
- all letting agents to become members of an ombudsman service, giving tenants the opportunity to pursue redress in cases of poor practice;
- an amendment to the code of practice of the ombudsman service to make it a requirement for agents to present landlord and tenant fees on their websites, in adverts and in all paperwork in a way that is easily comparable across agents;
- government to make use of the 2012 retendering process for the tenancy deposit protection schemes to find ways to make it easier for tenants to use their old deposits when moving in the private rented sector;
- local authorities to extend rent deposit schemes to members of the low-to-middle income group.

What we did

We conducted a mystery shopping exercise of 25 letting agents in three English areas: London, Manchester and Gloucester. We used the *Find a Property* website to identify agents that had the largest number of properties on their books in each location. This included a mix of national and local brands. Agents were telephoned and asked for details of upfront charges as well as the cost of renewing a tenancy agreement and any costs on moving out of the property. We looked at their websites to see if they contained information on fees.

We also asked people to let us know about their experiences of renting through an agent. The comments from these tenants are incorporated into the report.

⁵ Phelps, L 'Let down', 2009

⁶ Jones, C 'Government review of regulation and redress in the UK housing market', 2009

⁷ The Guardian, 'Housing Strategy prices people out of homes', 22 November 2011

What we found

Tenant fees/costs

Tenants renting through a letting agent can experience costs at different stages of the process: at the beginning of the tenancy, midway through the tenancy and on exit.

Glossary of charges

Deposit

Most tenants with an Assured Shorthold Tenancy will have to pay a deposit, which the landlord can keep or from which the landlord can deduct an amount if the tenant leaves the property owing rent, damages the property, or does not pay their bills. Otherwise the tenant can expect to receive this money back in full. As part of the 2004 Housing Act deposits to secure Assured Shorthold Tenancies must be protected through one of three government approved schemes.

Rent in advance

Most tenants will have to pay the first month's rent in advance on moving into a property.

Administration fee

The majority of agents charge an administration fee which usually covers the cost of carrying out the credit and employment reference checks and drawing up the paperwork for the tenancy agreement. In some cases agents charge a separate credit and reference check fee.

Holding deposit

Some agents require a holding fee to secure a property while credit and employment reference checks are carried out. This is deducted from the first month's rent where the agreement goes through successfully. Agents may reserve the right to deduct any costs incurred from the holding deposit where a tenant pulls out of an agreement or where the reference or credit check does not meet the agent's or landlord's requirements.

Deposit administration fee

Some agents charge a fee to administer the deposit within one of the government approved tenancy deposit protection schemes.

Check-in/ Check-out fee

A check-in and/or check-out fee can be charged to prepare the inventory on moving into the property and check against it when the tenant moves out of the property.

Tenancy renewal fee

A tenancy renewal fee covers the cost of redoing the paperwork to extend a tenancy agreement.

Table 1 below, identifies the average upfront costs that were reported by the agents we spoke to. This includes the deposit, rent in advance and administration fee which are standard costs for consumers renting through an agent. They averaged £1,500 for a household renting a two bed property where there are two adults on the tenancy agreement and £1,250 for a person renting a one bed property where there is one person on the agreement.

Table 1: Average upfront costs by number of adults on the tenancy agreement and size of property (£)

| | One adult in one bed property | Two adults in two bed property |
|--------------------|-------------------------------|--------------------------------|
| Administration fee | 199 | 236 |
| Deposit | 583 | 709 |
| Rent in advance | 464 | 573 |
| Total | 1246 | 1518 |

Deposits have been calculated on the basis of average English Local Housing Allowance monthly rents for a one and two bed property

These averages conceal significant variation across the geographical locations with the upfront costs charged by agents in London double those charged by agents in Manchester and Gloucester (Table 2). This is largely a result of different rent levels but deposit structures and higher administration fees also play a role. Six weeks' rent was the common deposit requirement in London and one month's rent more common in Manchester. Administration fees were nearly double the amount in London compared to Manchester.

Table 2: Average upfront costs for a one bed property where there is one adult on the tenancy agreement, by geographical location (£)

| | London | Manchester | Gloucester |
|--------------------|-------------|-------------|-------------|
| Administration fee | 248 | 129 | 185 |
| Deposit | 1099 | 487 | 519 |
| Rent in advance | 819 | 412 | 390 |
| Total | 2166 | 1028 | 1094 |

Variations in fee policies were even starker across the 25 agents that we looked at, reflecting different fee structures and policies.

Table 3: Range of fees based on one person on the tenancy agreement (£)

| Fee | Amount |
|---|--|
| Holding fee | 0-500 |
| Administration fee | 90-375 |
| Deposit administration fee | 0-30 |
| Deposit | 1 month's rent 1 month's rent + £100-200 6 weeks' rent |
| Rent in advance | 1 month's rent |
| Credit reference check | 50-54 |
| Cost to add an additional person to the agreement | 0-102 |
| Tenancy renewal | 0-90 |
| Check-in | 144 |
| Check-out | 0-120 |

Observations:

- All agents charged a deposit which ranged from one month's to six weeks' rent, with some agents charging one month's rent plus £100-200.
- All agents charged one month's rent in advance.
- All agents charged an administration fee which ranged from £90-£375. This was also usually a flat fee but in a small number of cases it was based on the weekly rent. Some agents reported charging a separate credit and reference check fee outside of the administration fee which ranged between £50-54.
- Nearly half of the agents made no extra charge for placing an additional person on the tenancy agreement, whereas others doubled the price.
- A tenancy renewal fee was only charged by roughly one third of the agents we spoke to. Other agents said that the tenancy would roll on a periodic basis.
- About half of the agents we spoke to said they charged a check-out fee. Sometimes this was a flat fee and other times based on the size of the property.
- Only a handful of the 25 agents charged a holding fee. In some cases this was a flat fee and in other cases it was based on the weekly rent.
- Two of the agents we spoke to said they charged a fee to administer the deposit in the deposit protection scheme. This averaged £30.
- Only one agent reported a separate check-in charge. Other agents said that this fee was covered by the landlord.

Fees charged to the tenant are connected to the fees charged to the landlord. All landlords will be charged a fee (usually a percentage of the rent) depending on the level of service being provided by the agent: some will be instructed to find a tenant whereas other will find a tenant and will also be in charge of managing the property for the landlord. We asked a small handful of agents for the fees that they charged and found that these agents were also charging the landlord for the same activities that were being charged to the tenant. These included an administration fee to draw up the paperwork for the tenancy, a tenancy renewal fee, a check-out and/or check-in fee.

We also looked at the websites of the agents that we spoke to. Only two of these had a comprehensive breakdown of the different fees and charges on their websites. Some had details of landlord fees but none of the agents had information on both parties' fees available for each side to consider.

Implications for renters

Significant upfront costs

The upfront costs charged by letting agents are a significant burden for LMI households. The average cost of renting a two bed property for two adults and any children is £1,500, which is nearly one month's income for the average low-to-middle income household. Given that two thirds of LMI households have less than this amount in savings⁸, and these relatively small sums are less likely to be loaned by mainstream banks, this will mean many households will have to borrow the money from friends and family, use a credit card or overdraft facility, or take out a sub-prime loan, as in the case of Karen and Daren below. This can add to the debt profile of a group that is already struggling. In its October 2011 poll for the Resolution Foundation, Ipsos MORI found that people on low-to-middle incomes in the private rented sector were more likely to be in debt than in the previous 12 months (15 per cent) than people on low-to-middle incomes who were renting from a local authority (10 per cent).⁹

Karen and Darren, both in their mid-30s, live in a private rented home with their four children. They found the property on the website 'Right Move' and approached the letting agent to view it before agreeing to go ahead with the tenancy. They were charged £180 for the agent's administration fee, one month's rent + £100 for the deposit and a month's rent in advance. They found out about these charges after they had accepted the property. They weren't able to use their old deposit for the new accommodation because they were disputing the deductions that the agent wanted to make. In order to find the money for the new deposit they had to take out a £600 loan from a doorstep lender. The interest means that they will pay back £1000 in total. Having lived in the property for eight months they have just discovered that the landlord wants to sell the property. This will mean finding more money to cover new upfront costs.

The deposit and rent in advance make up a big chunk of the upfront costs of renting, particularly at a time when rents are rising and median wages are not. However, higher deposit structures are also playing a role. It is standard practice for agents and landlords in London to charge a maximum of six weeks' rent for the deposit, but this has increased from a time when it was one month's rent. Some people report being charged more, as this tenant explained:

I was looking to rent elsewhere a few weeks ago and almost all the agents were starting to ask for six weeks rent + £100 for the deposit, instead of the regular four. It's a pretty astronomical amount to ask for, especially as people renting are less likely to be able to drum up so much extra cash.

An additional problem is the inevitable delay in getting a deposit back from the deposit protection scheme and the point at which a deposit is required to secure a new rental property. This means that new sums of money need to be found every time a household moves within the private rented sector.

One of the biggest challenges when moving between rented properties is that you need to pay your deposit up front, often before you have your current deposit back, so although you would have the cash two weeks after moving, it is not at your disposal when signing the new contract.

⁸ Whittaker, M 'Squeezed Britain: the 2010 audit of low-to-middle earners' 2010

⁹ MORI 'Commission for Living Standards poll', October 2011

Variable fees

The mystery shopping exercise identified considerable variation both in the level of additional charges made by agents and the activities that were being charged for. Administration fees ranged from £90-375 and were nearly double the amount in London compared to Manchester, and while some agents charged a flat fee others were basing fees on the weekly rents. Only two agents reported charging to administer the deposit in the deposit protection scheme, averaging £30, and less than half of agents reported charging a renewal or check-out fee.

Such variation not only makes it difficult to compare the services being offered by letting agents but also suggests that some of these fees are disproportionate, particularly given the actual cost of certain activities. The average cost to cover the administration of setting up a tenancy with credit and reference checks was £200, with some agents charging up to £375. A full credit check can be obtained online for approximately £20 and all agents will have a standard contract that can be edited and printed off. While there will be a time cost involved in these activities, it is difficult to see how such charges are proportionate to the costs incurred.

What I hate about administration fees when renting is there is no justification as to why the money needs to be paid - so how many hours administration have they done at what hourly fee. And often it feels like they have done practically nothing and are demanding a large amount of money.

Unlike the deposit and rent in advance, these are deadweight costs that tenants experience every time they move in the private rented sector. While many LMI households stay in the same rented property for several years, others will be moving within the sector more frequently: nearly 60 per cent have lived at their current private rented address for less than two years.¹⁰ Insecurity in the private rented sector, due to the use of short-term contracts, means that some households do not have a say in how frequently they move within it, as Danielle's case below highlights.

Danielle lives in a three bedroom private rented house with her two teenage children. She has been living there for three years having previously moved out of the private rented property she had been in for one year because the landlord decided to sell. When she contacted the agent they arranged a viewing and she subsequently went back and asked to go ahead with preparation for the tenancy. She paid a £300 holding deposit and following that £1,100 deposit, £1,100 rent in advance, £95+VAT admin fee, £50+VAT referencing fee for herself and then a further £50+VAT fee for a guarantor, which she was required to have because she worked part-time. The total cost was £2,370.88 which, alongside £500 to pay for a removal van, was one and a half month's income. She didn't have any savings, and didn't get her old deposit back soon enough, so she had to borrow the money from a friend. She has just been told that her current landlord wants to sell the property leaving her to find this sum of money yet again.

When you consider that the landlord may also be charged for the same set of activities, these fees become even harder to explain. In other similar markets, like the employment agency market, costs are covered by the person that instructs the agent i.e. the employer or in this case the landlord.

Why are we paying the letting agency, when they are providing a service for the landlord not for us?

Renewal fee is a bit over the top, since I know they also charge the landlord for the same service. It's a lot of money for posting a new contract for us to sign.

¹⁰ Whittaker, M 'Squeezed Britain: the 2010 audit of low-to-middle earners' 2010

Lack of transparency

The lack of transparency in fees puts little pressure on agents to offer competitive prices. Of the agents we looked at only two had a comprehensive breakdown of fees on their website, but even then landlord fees were also not available for the tenant to see what they were being charged for, making it easier for double charging of landlord and tenant to occur.

This can mean that tenants don't find out about the fees an agent charges until too late in the process to shop around i.e. after they have made a decision on a property. In some cases it may mean they are not aware of the full extent of fees until they come to sign the contract. Where fees are hidden within contracts they may not be discovered until the point of payment.

I have a dog but after one of the routine inspections, which I wasn't in the flat for, I received a letter telling me that in future either I had to be there, or the dog out of the flat, during these inspections, or I would be fined £25 (plus VAT of course).

The growth in property search websites such as *Find a Property* and *Rightmove* are making it even more difficult for tenants to shop around. Tenants increasingly search for properties themselves via property search websites, rather than choosing a letting agent to use and asking them to conduct a search for them. These websites include information on rents but not on agent fees or other costs. Websites like *All Agents* have been set up to enable consumers to write reviews of different agents and assist others to make a more informed decision about which agent to use.¹¹

Added to this, a housing shortage, and growth in demand for private rented property places the consumer in an even weaker position to negotiate terms of an agreement. Estate agents have reported a battle for private rented properties with Countrywide, the UK's largest letting agency, reporting properties being let now within 12 days of being advertised and within hours in some parts of the country.¹²

The rental market is a rat race in London. You have no choice in terms of which agent you work with - because you're so desperate to get hold of a flat. This means that agents can afford to be lazy, negligent and unreasonable in their demands.

They do not state their fees and this makes it difficult to compare letting agencies. The rental market is so tough in London anyway that you can't use letting agency fees to screen out letting agents - if you see a property you want, you have to sign for it there and then and pay whatever fees they ask for or risk losing the property.

¹¹ See website at <http://www.allagents.co.uk/>

¹² Guardian, 'Rental properties snapped up in record time', 8 November 2011

Policy proposals

Professionalising the market

Unlike in the estate agents sector, membership of a redress scheme is voluntary for letting agents with the result being that about two thirds of the market is totally unregulated.¹³ All letting agents should be signed up to an ombudsman service and be governed by the ombudsman's code of practice. This would give certainty to tenants and landlords that they are using an agent who is committed to professional practice and would provide an independent route of redress. The Property Ombudsman (TPO) has about 8,000 letting agent members who are signed up to a code of practice, and the TPO can investigate complaints about members who fail to comply and issue compensation of up to £25,000.

At the moment the onus is on the tenant to check whether the agent they are using is signed up to an ombudsman service which leaves a lot of scope for poor practice: consumer research has found that the majority of people think that the government has an active role in the regulation of letting agents¹⁴ which suggests that there is a lack of awareness among consumers of the need to check whether or not an agent is regulated. According to the National Landlords Association's landlord survey nearly one third of landlords do not consider whether or not a letting agent is a member of a trade body when choosing which one to use.¹⁵

In addition, letting agents should be brought under the definition of 'estate agency' within the Estate Agents Act (1979) to give the Office of Fair Trading the ability to ban agents who act improperly.¹⁶ This change would bring letting agents in line with estate agents. The estate agents' code of practice is underpinned by The Estate Agents Act (1979) and the related Property Misdescriptions Act (1991) and gives the Office of Fair Trading powers to ban an agent who is found to have acted improperly. Since letting agents do not fall under this legal framework, an estate agent who has been found to have acted improperly and is banned from the market can start up a business as a letting agent.

Introducing structured transparency

The lack of transparent information on fees makes it difficult for consumers to shop around which in turn creates little incentive for agents to compete on price. This is reflected in the variation in fees that agents reported. The Unfair Terms in Consumer Contracts legislation applies a test of fairness and stresses the importance of terms being made in clear and intelligible language in the contract but this can be made available too late in the process of searching for a property to enable a tenant to shop around.

Some countries have tackled this by introducing legislation on the level and extent of activities that can be charged for. In Scotland this hasn't been enforced but the Government are currently in the process of introducing greater clarity as part of the Private Rented Sector (Scotland) Act 2011. While this would prevent agents charging disproportionate amounts for low-cost activities it is not entirely clear what impact doing this would have on rents as letting agents would look for new ways to recoup the money. At a time when private rented sector rents have risen by 16 per cent in London in the last year, introducing legislation might place greater upwards pressure on rents, putting a further strain on LMI household budgets.

In British Columbia, **Canada**, landlords are also not allowed to charge a person for accepting an application for a tenancy, processing the application, investigating the applicant's suitability as a tenant, or accepting the person as a tenant. In relation to deposits, they cannot be more than ½ month's rent plus an additional ½ month's rent where the tenant has a pet.

¹³ Jones, C 'Government review of regulation and redress in the UK housing market', 2009

¹⁴ ComRes survey for RICs cited in Carsberg, B 'Carsberg review of residential property' 2008

¹⁵ National Landlords Association, 'Landlords Survey', Q3 2011

¹⁶ The Property Ombudsman, 'Annual report 2010', 2011

In **Scotland**, under the Rent Scotland Act (1984) charging premiums to set up a tenancy is illegal. There are conflicting interpretations of this legislation with some legal experts taking the view that all fees are premiums and others taking the view that landlords and letting agents are entitled to charge a fee that is reflective of the actual costs incurred. This has resulted in the majority of agents charging fees –identified by a mystery shopping exercise conducted by Shelter Scotland.¹⁷ The Scottish Government is in the process of clarifying this, and deciding which fees and the scale of fees that should be prohibited, as part of the Private Rented Sector (Scotland) Act 2011.

In New South Wales and Victoria, **Australia**, letting agents are not allowed to charge a fee for making, renewing or ending a tenancy agreement. In New South Wales the maximum deposit is four weeks for unfurnished premises, six weeks for furnished premises with rent of less than \$250 a week and an unlimited amount for furnished premises with weekly rents of more than \$250. The maximum rent advance is two weeks rent if the rent is less than \$300 a week; otherwise, four weeks. In Victoria, the maximum deposit is four weeks rent, for tenancies worth less than \$350 per week. Deposits for properties with rents over this amount are decided at tribunal on application by the landlord.

To make it easier for tenants to shop around for letting agent services, an addition should be made to the ombudsman’s code of practice within the Office of Fair Trading guidance on unfair terms in tenancy agreements to make it a requirement for agents to clearly state information on fees in a standardised and comparable format in all material for both prospective tenants and landlords. This would mean making it available on the agent’s website, within property search website adverts alongside the rental asking price and in all paperwork. Landlord and tenant fees would need to be available alongside each other and the purpose of each charge would need to be made clear.

Introducing this requirement would go some way towards addressing the lack of transparency that enables some agents to operate high fee structures. But it would not entirely solve the power imbalance which currently enables letting agents to set the terms. The housing shortage and level of demand for private rented accommodation mean that agents will still be in a good position to set terms. The impact of an increase in transparency on the level of fees should be monitored with an option to legislate on fees further down the line if problems with disproportionate fees persist.

Meeting upfront costs

Prospective tenants currently face significant upfront costs when moving into private rented accommodation, averaging £1500 for two adults and any children moving into a two bed property. These can pose a particular challenge for low-to-middle income households: two thirds have less than this amount in savings. Rising rents alongside higher deposit requirements have contributed to this. Where a household moves within the private rented sector, the inevitable time delay between getting back an old deposit from the deposit protection scheme and the point when a new one is needed, means that new sums of money have to be found each time.

Under the 2004 Housing Act deposits must be paid into one of three government approved deposit protection schemes designed to protect tenants and landlords from loss of money if there is a dispute about damage at the end of the tenancy. These include a custodial Deposit Protection Service (DPS) scheme where the money is transferred to a separate bank account held by the DPS, and two insurance based schemes (MyDeposits, Tenancy Deposit Scheme) where the money is retained by the landlord or agent and insurance premiums are paid to protect the tenant in the event that the landlord fails to pay. Tenants can expect to get this money back within ten days of the amount any deductions being agreed by both parties.

¹⁷ Shelter Scotland, ‘Premiums in the Private Rented Sector, 2011

The approved schemes' contracts come to an end in 2012 which provides government with an opportunity to ask providers to identify ways in which the schemes can bridge the gap between the point at which a tenant gets back an old deposit and the point at which they need a new one, to help prevent households falling into debt.

Another way that this issue could be overcome is if local authority rent deposit schemes were extended to low-to-middle income households in the private rented sector. Under these schemes the local authority provides a guarantee that the deposit will be paid if there are any deductions to be made at the end of the tenancy agreement. These guarantees are usually limited to people on means-tested benefits but, in light of the growing reliance of low-to-middle income households on the private rented sector and the low savings profile of this group, local authorities should consider extending this support.

Summary of recommendations

The report calls for:

- letting agents to be brought under the Estate Agents Act (1979), thereby giving the Office of Fair Trading powers to ban agents who act improperly;
- all letting agents to become members of an ombudsman service, giving tenants the opportunity to pursue redress in cases of poor practice;
- an amendment to the code of practice of the ombudsman service to make it a requirement for agents to present landlord and tenant fees on their websites, in adverts and in all paperwork in a way that is easily comparable across agents;
- government to make use of the 2012 retendering process for the tenancy deposit protection schemes to find ways to make it easier for tenants to use their old deposits when moving in the private rented sector;
- local authorities to extend rent deposit schemes to members of the low-to-middle income group.

The Resolution Foundation

The Resolution Foundation is an independent research and policy organisation. Our goal is to improve the lives of people with low-to-middle incomes by delivering change in areas where they are currently disadvantaged. We do this by:

- undertaking research and economic analysis to understand the challenges facing people on a low-to-middle income;
- developing practical and effective policy proposals; and
- engaging with policy makers and stakeholders to influence decision-making and bring about change.

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