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FIRST - TIER TRIBUNAL

PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case Reference	:	CHI/00HY/LAC/2015/0002.
Property	:	20 Bedwin Street, Salisbury, SP1 3UT.
Applicant	:	20/20A Bedwin Street (Salisbury) Management Limited.
Representative	:	Miss Amanda Gourlay, Counsel.
Respondent	:	Imagine Property Rentals Limited.
Representative	:	Mr. Rupert Cohen, Counsel.
Type of Application	:	Liability to pay administration charges, Schedule 11, Commonhold and Leasehold Reform Act 2002.

AND

Case Reference	:	CHI/00HY/LSC/2015/0011.
Property	:	20 Bedwin Street, Salisbury, SP1 3UT.
Applicant	:	1. 20/20A Bedwin Street (Salisbury) Management Limited 2. Anne Pritchard (Flat 1) 3. Helen Wendy Bray (Flat 3) 4. William and Judith Dickinson (Flat 4) 5. Matthew and Charlotte Andrews (Flat 5).
Representative	:	Miss Amanda Gourlay, Counsel.
Respondent	:	1. Imagine Property Rentals Limited (Flat 6) 2. Patricia Osborne (Flat 2)
Representative	:	Mr. Rupert Cohen, Counsel for Imagine Property Rentals Limited Mr. Parsons for Patricia Osborne.
Type of Application	:	Liability to pay service charges, Section 27A Landlord and Tenant Act 1985.

Tribunal Members	:	Judge J G Orme (Chairman) Mr. S Hodges FRICS (Member)
Date and Venue of Hearing	:	1 July 2015. The Red Lion Hotel, Salisbury.
Date of Decision	:	27 July 2015.

Decision

For the reasons set out below, the Tribunal, in application number CHI/00HY/LAC/2015/0002, determines that:

1. **The costs claimed in the sum of £23,000.40 are not payable by the Respondent, Imagine Property Rentals Limited to the Applicant, 20/20A Bedwin Street (Salisbury) Management Limited as an administration charge under the terms of the lease of Flat 6 Bedwin Street.**
2. **The sum of £525.70 is payable by the Respondent to the Applicant in respect of interest on the sum of £13,000 which was unpaid for the period from 15 March 2014 to 5 February 2015.**

For the reasons set out below, the Tribunal, in application number CHI/00HY/LSC/2015/0011, determines that the administrative and legal costs incurred by the Applicant, 20/20A Bedwin Street (Salisbury) Management Limited are recoverable from the leaseholders of 20 Bedwin Street, Salisbury as part of the service charge in so far as they were reasonably incurred and the services were provided to a reasonable standard. The amount which is recoverable and the amount to be paid by each leaseholder will be determined at a further hearing. That hearing will take place on a date to be notified to the parties to take place on the day before the hearing in application number CHI/00HY/LSC/2015/0014 with a time estimate of 1 day.

The Tribunal will determine the applications under section 20C of the Landlord and Tenant Act 1985 on that occasion.

Reasons

Background

1. In about 2003 a block of 6 flats and maisonettes was built at 20 Bedwin Street, Salisbury ("the Property"). The flats have been sold on long leaseholds. The freehold of the Property is now vested in 20/20A

Bedwin Street (Salisbury) Management Limited ("the Company"). The members and shareholders of the Company are intended to be the leaseholders of the 6 flats. The Company is responsible for the management and maintenance of the Property and is entitled to collect a service charge from the leaseholders to cover the costs so incurred.

2. In 2012, a structural survey of the Property disclosed that urgent and costly works were required to the roof of the Property. Those works were carried out in 2013. The cost of those works was included in the service charge account for the year 2013 and resulted in the service charge demanded of the leaseholders being very much higher than in previous years.

3. The demands for payment of service charge for the 2013 year were sent to the leaseholders on 1 March 2014. The leaseholder of Flat 6 objected to the amount of the demand which, in his case was £15,224.94. As a result, the Company applied to the First-tier Tribunal for a determination of the reasonableness of that service charge. That application was dealt with under reference number CHI/00HY/LIS/2014/0014. Subsequently the parties entered into mediation and reached agreement which is recorded in a settlement agreement dated 8 January 2015. The leaseholder of Flat 6 agreed to pay £13,000 service charge for 2013, payment to be made by 5 February 2015. That payment was made.

4. The lease of Flat 6 was originally granted to Richard Alan Molton on 12 December 2003. At some time the lease was transferred to his son, Mr. Lloyd Molton. On 28 March 2014, Lloyd Molton transferred Flat 6 to Imagine Property Rentals Limited ("Imagine") whose title to the Flat was registered on 9 May 2014.

5. The Company has not employed a managing agent to manage the Property since 1 June 2013. In place of a managing agent, Mr. William Dickinson, one of the leaseholders of Flat 4, has carried out the administrative work of managing the Property. He is the managing director of the Company and works under a contract of employment.

6. The Company incurred administrative and legal costs in dealing with the application to the Tribunal which it says amounted to £23,000.40. On 21 January 2015 the Company issued an invoice to Imagine in that sum seeking payment as an administration charge due under the terms of its lease of Flat 6. Also on 21 January 2015 the Company issued an invoice to Imagine in the sum of £499.20 for interest which it said was due under the terms of the lease on the sum of £13,000 for the period from 15 March 2014 to 20 January 2015.

7. On 3 February 2015, the Company applied to the Tribunal (under reference number CHI/00HY/LAC/2015/0002) for a determination as to the liability of Imagine to pay the costs and the interest as an administration charge.

8. Also on 3 February 2015, the Company applied to the Tribunal (under reference number CHI/00HY/LSC/2015/0011) for a determination that, in the event that the legal costs were not recoverable as an administration charge, they were recoverable from all of the leaseholders by way of service charge. That application is supported by the leaseholders of Flats 1, 3, 4 and 5. It is opposed by the leaseholders of Flats 2 and 6.

9. On 24 March 2015, the Tribunal issued directions providing for the parties to exchange written statements of case and for the applications to be listed for hearing together.

The Law

10. The law relating to determination of the amount of administration charges is set out in Schedule 11 to the Commonhold and Leasehold Reform Act 2002 ("Schedule 11"). Schedule 11 defines an administration charge and what is considered to be a variable administration charge. For an administration charge to be payable, the lease must make provision for payment of the charge and, if it is a variable charge, it is payable only to the extent that it is reasonable.

11. The law relating to determination of the amount of service charges payable by a leaseholder is primarily set out in sections 18, 19, and 27A of the 1985 Act. In brief, if the parties to a lease cannot agree the amount of service charges payable, either the landlord or the tenant may apply to the Tribunal to make a determination. In making that determination, the Tribunal will consider whether the charge is recoverable under the terms of the lease and, if it is, whether the amount claimed has been reasonably incurred and whether the services or works were carried out to a reasonable standard. Where a service charge is payable before the costs are incurred, no greater amount than is reasonable is payable.

12. One of the remedies available to a landlord of property dealing with a tenant who is not paying service charges or other sums due under his lease is to attempt to forfeit the lease which means to bring it to a premature end unilaterally. Over time a number of restrictions have been placed on the powers of a landlord to forfeit a lease so as to prevent this draconian remedy being used unfairly. Section 146 of the Law of Property Act 1925 introduced a requirement for a landlord to serve a notice on the tenant requiring him to remedy the breach before the power could be exercised. Section 81 of the Housing Act 1996 provided that a landlord of premises let as a dwelling may not exercise his right to forfeit the lease for non-payment of an administration charge or a service charge unless the tenant has admitted his liability to pay the charge or a tribunal or court has finally determined that the charge is payable. These provisions have been the subject to a considerable amount of case law which will be referred to in relation to the parties' submissions.

13. A tenant may ask the Tribunal to make an order under section 20C of the 1985 Act. The Tribunal may make such an order if it considers that it is just and equitable in the circumstances. If an order is made, it prevents

the landlord from seeking to recover through the service charge any costs which it has incurred in connection with the application.

14. The full text of the statutory provisions referred to in this section is set out in the appendix to this decision.

The Lease

15. The Tribunal had before it a copy of a lease dated 12 December 2003 made between Marus Development Limited as lessor and Richard Alan Molton as lessee ("the Lease").

16. By the Lease, the lessor demised Flat 6 to the lessee for a term of 125 years from 5 December 2003 at a yearly rent of a peppercorn. (It should be noted that the service charge was not reserved as a rent.)

17. Recital number 2 in the Lease provides:

> *it is intended that on the sale of the last flat in the Development, the freehold of the Development will be transferred to a Management Company.*

18. Recital number 3 in the Lease provides:

> *The Lessor intends that the lease of the other flats will contain covenants similar to those contained in the Fourth Schedule hereto to the intent that any tenant for the time being of each flat may be able to enforce the observance of the said covenants by the owners and occupiers for the time being of the other flat.*

19. The Company was registered as the proprietor of the freehold interest in the Property on 28 January 2004.

20. The terms of the Lease have been varied following an application to the First-tier Tribunal under Section 37 of the Landlord and Tenant Act 1987. A copy of the Tribunal's decision under reference CHI/00HY/LVL/2013/0001 dated 25 October 2013 making an order to vary the terms of the Lease (and the leases of the other flats at the Property) was before the Tribunal.

21. By Clause 2 of the Lease (as amended), Imagine covenants with the Company to observe and perform the covenants contained in the 5th Schedule to the Lease. By Clause 3 of the Lease, the Company covenants with Imagine to observe and perform the covenants in the 6th Schedule to the Lease.

22. Clause 4 of the Lease contains a forfeiture clause in the following terms:

> *If any of the covenants on the part of the Lessee herein contained shall not have been observed or performed then and in any such case it shall be lawful for the Lessor at anytime thereafter to re-enter upon the Property or any part thereof in the name of the whole and thereupon this demise shall absolutely determine ...*

23. The following paragraphs in the 5th Schedule (as amended) are relevant:

(2) To pay interest at the rate of 4% a year over the base lending rate for the time being of Lloyds TSB Bank Plc on all monies hereby covenanted to be paid by the Lessee to the Lessor which shall remain unpaid for fourteen days after the same shall have become due such interest to be calculated from the date on which the same shall have become due to the date on which the same shall be paid.

(8) To pay all costs charges and expenses (including Solicitors' costs and Surveyors' fees) incurred by the Lessor for the purpose of or incidental to the preparation and service of a notice under Section 146 of the Law of Property Act 1925 notwithstanding that forfeiture may be avoided otherwise than by relief granted by a Court.

(12) To pay to the Lessor within 14 days of demand: (a) 27.80% of the expenses and outgoings incurred by the Lessor in carrying out its obligations under the Sixth Schedule and any other expenditure incurred by the Lessor in the performance of its obligations under this Lease such payments (hereinafter called "the Service Charge") being subject to the following terms and provisions:

(ix) The expression "the expenses and outgoings incurred by the Lessor" shall, for so long as the Lessor is a Residents Management Company also be deemed to include the following:

1. *All professional fees (which shall include, without limitation to the foregoing, the fees, disbursements and other outgoings of persons or organisations providing professional advice to the Lessor which is to include but is not limited to: architects, business management, engineers, financial management, health and safety, leasehold management, legal, surveyors) incurred by the Lessor in the performance or contemplation of the performance of its obligations under this lease*
2. *All costs incurred by the Lessor in operating the Residents Management Company.*

24. The 6th Schedule as amended contains the usual covenants by the Lessor to insure the Property, to maintain and repair the structure and roofs of the Property, to keep the common parts lit and clean and to decorate the exterior. The following paragraphs in the 6th Schedule (as amended) are relevant:

(1) Not to grant a Lease of any of the other flat unless such Lease shall be substantially in the form of this Lease and shall contain covenants in the same terms mutatis mutandis to those herein contained.

(3) At the request and expense of the Lessee to take such steps as shall reasonably be necessary to enforce any covenant on the part of any tenant of any part of the Development.

(6) To maintain repair and renew (which expression shall include the addition replacement or repair of any part that has been omitted or is inherently defective, the replacement of existing parts with modern materials which provide reasonable life-cycle cost reduction) as appropriate

1) the main structures of the buildings on the Development and in particular the foundations external and load bearing walls and the main beams and timbers thereof including the joists or structural or load bearing members under the floors and balconies

2) the main roofs of the buildings on the Development including the joists or structural or load bearing members over the ceilings on the top floors thereof and the chimney stacks gutters and rainwater pipes thereof

3) the Services and Facilities used or enjoyed by the Lessee in common with the Lessor or the occupier of the other flat save that nothing in this Lease shall oblige the Lessor to maintain particular Facilities which in its reasonable opinion are not fully utilised provided that such discontinuance does not substantially affect the market value of the Property

4) All other external parts of the Development

5) All other Retained Parts

(10) To enforce the covenants on the part of the Lessees of the other flats contained in the leases thereof

(11) To defend insofar as may be reasonable any claims brought that may adversely affect the Development or any part of it and to bring insofar as may be reasonable any claims necessary to reasonably protect or preserve the Development

The Hearing

25. The hearing took place at the Red Lion Hotel, Milford Street, Salisbury on 1 July 2015. The Company was represented by Amanda Gourlay of Counsel. Mr. and Mrs. Dickinson were present at the hearing. The other Applicants were not present. Imagine was represented by Rupert Cohen of Counsel. Mr. Lloyd Molton and Miss Lindsay, a director of Imagine, were present. Ms Osborne was present at the hearing. She was represented by a friend, Mr. Parsons.

26. At the beginning of the hearing the following issues were identified:
    1) Whether the Company was entitled by the terms of the Lease to seek recovery of the legal costs and interest as an administration charge from Imagine;
    2) If not, whether the Company could recover the legal costs from all lessees as part of the service charge;
    3) If the answer to either of the above is yes, whether the amount claimed is reasonable.

27. In the event, the Tribunal only had time to hear submissions on the first 2 questions and it was agreed that the Tribunal would determine those questions. If it was determined that any of the costs were recoverable either as an administration charge or a service charge, the hearing would have to be adjourned to determine the question of reasonableness.

The Evidence and submissions

28. The Company filed a written statement of case with supporting documents. Imagine filed a statement of case in reply. Ms Osborne filed a witness statement in which she adopts Imagine's case in so far as it is relevant to her. The Company filed a statement in reply.

29. The facts which emerge from the documents filed with the Tribunal, in so far as they are relevant, are as follows:

    1) 29 January 2014 – The 2013 service charge accounts had been prepared showing a sum of £15,224.94 payable by the leaseholder of Flat 6. Mr. Dickinson sent a copy of the accounts and accompanying certificate by email to Mr. Bray and Mr. Andrews. It is not clear from the copy email filed with the Tribunal whether it was sent to Mr. Molton. However, Mr. Molton wrote to Mr. Dickinson on 14 February saying

    "Further to your recent emails and notes I am still obtaining advice and your timescales are therefore unworkable."

    2) 17 February 2014 – Mr. Dickinson wrote to Mr. Molton. After making certain points about letters being signed and communications from Mr. Molton's father, Mr. Dickinson said

    "The primary purpose of this, the last letter I will be writing to you before raising the service charge for 2013 is to document as FACT that I have given you multiple opportunities over a considerable period of time to seek independent legal advice if you wish to contest the circa £15k demand or apply for credit arrangements if it results in financial hardship."

    At the end of the letter he said

    "I have no desire to see these matters escalate into the courts where the end result will be a CCJ and forfeiture of your lease if you persist in your refusal to pay the lawful amount due and also fail to make an application to the LVT to adjudicate the reasonableness of the service charge demand for circa £15k. If you make such an application it will effectively block any action the RMC can take in relation to forfeiture of your lease. If on the other hand you simply refuse to make the payment you will leave the RMC with no choice but to initiate proceedings incidental to S.146 forfeiture of your lease and seek interest, damages and costs in the courts."

    3) 18 February 2014 – Mr. Dickinson wrote to Mr. Molton enclosing a copy of the 2013 service charge accounts and certificate. He refers to having previously sent these by email on 29 January. The letter informed Mr. Molton that if he failed to pay the sum due or request

credit facilities or apply to the Tribunal for a determination within 14 days, he would be considered to be in breach of covenant. Mr. Molton acknowledged receipt of that letter on 21 February saying that he was taking advice.

4) 1 March 2014 – Mr. Dickinson sent a service charge demand to Mr. Molton in the sum of £15,224.94. The due date for payment was stated to be 15 March 2014. A copy of the service charge accounts was enclosed with the demand. Mr. Molton acknowledged receipt by letter dated 7 March saying that he was still waiting for advice but that he considered the demand to be invalid.

5) 14 March 2014 – Mr. Molton wrote to Mr. Dickinson informing him that he had sold Flat 6 with completion due on 28 March.

6) 17 March 2014 – The Company applied to the Tribunal for a determination under Section 27A. On the same day Mr. Dickinson wrote to Mr. Molton enclosing a copy of the application. The letter was headed

"Legal action incidental to S.146 forfeiture of lease Failure to pay £15,224.94 service charge demand".

In the letter he said that the application had been issued

"incidental to an application to the courts to forfeit you lease under S.146 provisions within the fifth schedule of your lease ..."

Mr. Molton acknowledged receipt by letter dated 21 March saying that he considered the action to be premature and unreasonable as he was still obtaining advice.

7) 28 March 2014 – Flat 6 was transferred to Imagine.

8) 8 January 2015 – The application to the Tribunal was settled by agreement following mediation. The settlement agreement (which also related to 2 other applications) recorded in relation to the service charge

"In respect of matter 0014 that the amount of service charge payable by the Respondent to the Applicant for the year ending December 2013 is £13,000. Payment to be made by cleared funds received by 4pm on 05 February 2015."

The company agreed to withdraw the application.

9) 21 January 2015 – The Company issued 2 invoices to Imagine. Both are headed "*Administration Charge*". Both state that the invoice is due for payment by "*4-Feb-2014*". Both were accompanied by a copy of the summary of tenants' rights and obligations. The first was for the sum of £23,000.40

"in respect of costs incurred in respect of breaches of lease covenants and is pursuant to the Fifth Schedule, Paragraph 8 of your lease".

It contained a breakdown of the costs which were said to cover the period from 15 March 2014 to 21 January 2015. The second was for interest calculated at 4.5% on the sum of £13,000 from 15 March

2014 to 20 January 2015 calculated in the sum of £499.20. It was claimed under paragraph 2 of the 5th schedule of the Lease.

10) 23 January 2015 – Imagine wrote acknowledging receipt of the invoices, pointing out that the date for payment of the agreed sum had not yet passed, saying that there was no breach of the Lease and suggesting a meeting to discuss the claims or referring the matter to the Tribunal to determine the issue.

11) 3 February 2015 – Mr. Dickinson wrote to Imagine saying that it was clear from correspondence that Imagine had no intention of paying the administration charges, that he considered Imagine to be in breach and that

"We are therefore initiating proceedings as required by S.81 of the Housing Act 1996 as being incidental to service of an S.146 notice under the Law of Property Act 1925 with the intention of forfeiting your lease and recovering interest, costs and damages."

The letter was headed

"Notice of legal action incidental to forfeiture of lease refusal to pay administration charges."

12) 3 February 2015 – Both of the present applications were sent to the Tribunal.

13) 5 February 2015 – Imagine paid the sum of £13,000 to the Company.

The Submissions

30. Both Counsel filed written submissions setting out their detailed positions which the Tribunal found extremely helpful in their determination. On behalf of Ms Osborne, Mr. Parsons confirmed that Ms Osborne adopted Mr. Cohen's written and oral submissions in so far as it was relevant to her position. Following the hearing, the Tribunal asked the parties to file further written submissions to address the issue as to whether the legal costs had been incurred by the Company in pursuance of an obligation under paragraph 10 of the 6th schedule. Further written submissions were received from Miss Gourlay and Mr. Cohen.

Administration Charge – legal costs

31. Miss Gourlay relied on paragraph 8 of the 5th schedule to the Lease as allowing the Company to recover the costs as an administration charge. She referred the Tribunal to paragraphs 14 to 23 of the Supreme Court decision in *Arnold v Britton [2015] UKSC 36* for guidance as to how the Tribunal should construe that paragraph. In particular, *"the court is concerned to identify the intention of the parties by reference to "what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean"."*

32. She also referred the Tribunal to *Freeholders of 69 Marina v Oram and Ghoorun [2011] EWCA Civ 1258*, paragraphs 12, 18 and 20 and *Barrett v Robinson [2014] UKUT 0322*, paragraphs 46-57.

33. She said that there was very little information before the Tribunal as to the circumstances existing at the date of the grant of the Lease other than the facts that section 81 of the Housing Act 1996 was in force and that the original lessor intended to transfer the freehold to a management company. She submitted that the right to forfeit the lease arose on 14 March 2014 when the leaseholder failed to pay the service charge demand and that the Company was obliged to incur the costs in obtaining a determination of the Tribunal to satisfy section 81 before proceeding to issue a notice under section 146 of the Law of Property Act 1925. Forfeiture was ultimately avoided on 5 February 2015 when payment of £13,000 was made. The costs incurred by the Company during that period were incurred for the purpose of and incidental to preparing such a notice. The wording of paragraph 8 was clear and unambiguous and allowed the recovery of the costs from the leaseholder. The absence of the words "*in contemplation of*" from paragraph 8 did not matter. It cannot have been the intention of the parties for the lessor to grant the leases without a mechanism for funding the management company.

34. Mr. Cohen's primary submission was that paragraph 8 does not permit the recovery of the costs. He says that the costs were not incurred "*for the purpose of*" or "*incidental to*" "*the preparation and service of a notice*". He distinguished the decisions in *69 Marina and Barrett v Robinson* on the basis that the relevant clauses in both of those cases included the words "*in contemplation of*". He referred the Tribunal to decisions of the First-tier Tribunal (which are not binding on this Tribunal) in *Godden v Vairaven CHI/29UL/LSC/2011/0140* and *Fisher v PR's of U Graham deceased LON/00AC/LSC/2011/0250*. Both of those decisions concerned construction of the phrase "*incidental to the preparation and service of a notice under section 146*". In both cases the Tribunal determined that the costs of previous proceedings were too remote to be recoverable under the relevant clause.

35. As a further submission, Mr. Cohen said that "*purpose*" pre-supposes that there is a breach. He says that there was no breach at any time because Imagine paid £13,000 within the time allowed by the agreement. As a result there was no opportunity to forfeit the lease. He relied on paragraph 49 of *Barrett v Robinson* in support of this submission.

36. Mr. Cohen further submitted that if the costs are recoverable under paragraph 8, there will be a perverse cycle of unwarranted cost recovery because the Company will then be able to recover the costs of these proceedings as an administration charge even if the Company's costs are assessed at nil. Section 20C would not provide the leaseholder with any protection in this case.

Administration charge – interest

37. Miss Gourlay submitted that the service charge was payable within 14 days of the date of demand, namely 14 March 2014. It had not been paid until 5 February 2015 and so the Company was entitled to interest under paragraph 2 of the 5th schedule. She did not accept Mr. Cohen's submission that nothing was due until after determination of the reasonableness of the service charge and relied on *Southend-on-Sea borough Council v Skiggs LRX/110/2005* as authority to support her.

38. Mr. Cohen submitted that as a result of the settlement agreement, the sum of £13,000 did not become payable until 5 February 2015, payment was made by that date and no interest became payable. He said that interest could not accrue until the amount payable was determined by the Tribunal.

Recoverability as a service charge

39. Miss Gourlay submitted that if the costs are not recoverable as an administration charge, then they are recoverable from all the leaseholders as part of the service charge. She relied on paragraph 12(ix) of the 5th schedule to allow the Company to recover the costs. There were 3 possible routes to recovery under that paragraph.

40. First she relied on paragraph 12(ix)(1) which allows recovery of professional fees "*incurred ... in the performance of its obligations under this lease*". She submitted that the Company was obliged to incur the costs as a result of its obligations under paragraphs 6 or 11 of the 6th schedule. Under paragraph 6, she said that the Company was obliged to maintain the building and that it could not do so if it had no funds to pay for maintenance, that its only source of funds was the service charge and therefore paragraph 6 should be construed as including an obligation to collect the service charges. Alternatively, she said that such an obligation should be implied. In this respect she relied on the decision in *Embassy Court Residents' Association Ltd v Lipman [1984] 2 EGLR 60.*

41. Secondly, she said that the Company was obliged to incur the costs as a result of paragraph 11 of the 6th schedule. She said that the applications had been made and the legal costs incurred in order to protect and preserve the development. If the Company had not taken proceedings, it would not have had any funds with which to maintain and hence to preserve the building.

42. Thirdly, she relied on paragraph 12(ix)(2) of the 5th schedule. She said that the costs were part of the costs of operating the residents' management company. She referred the Tribunal to the memorandum and articles of association of the Company. The Company had power to incur these costs. It could only continue to operate if it obtained income from the service charge. If leaseholders refused to pay the service charge, it could not continue to operate. Taking steps to enforce payment of the service charge was part of the costs of operating the Company.

43. Mr. Cohen submitted that a proper interpretation of paragraph 12(ix) did not allow the Company to recover legal costs as part of the service charge. He pointed out that the Lease had been varied in 2013 and the opportunity had not been taken to clarify the Lease at that point to allow recovery of legal costs. He did not accept that the Company was obliged to incur the costs under either paragraph 6 or 11 of the 6th schedule. He did not consider that the costs were part of the costs of operating the Company. He urged a much more restrictive interpretation of paragraph 12(ix)(2) so as to refer to the administrative costs of running the Company such as drawing up statutory accounts and filing returns with Companies House.

Further submissions on recoverability as a service charge

44. Miss Gourlay submitted that paragraph 10 of the 6th schedule must be read in the context of the other terms of the Lease which includes recital number 3 and paragraphs 1 and 3 of the 6th schedule. Paragraph 10 should be construed to place a cross-development obligation on all of the lessees to contribute equally to the enforcement costs where a lessee is in breach of covenant. The variations made to the terms of the leases in October 2013 allowed the Company to recover the costs of performing its obligation to enforce the covenant of the lessees of the other flats. It would be unjust to demand the costs of remedying the breaches of covenant against only the non-defaulting lessees.

45. Mr. Cohen submitted that the costs were not recoverable under paragraph 10 of the 6th schedule for 3 reasons:
    1) A proper construction of paragraph 10 in the context of the terms of the Lease in its original form without subsequent variations was that it only allowed the costs of enforcing the covenants in the lease of flat 2 which was the only other flat which had been demised at the date of the Lease;
    2) Paragraph 10 refers only to costs incurred in enforcing the covenants on the part of the other lessees in the Property. So, on the assumption that the leases of the other flats contained the same clause, the costs of enforcing covenants against the leaseholder of flat 6 could be recovered from the other lessees but not from the leaseholder of flat 6.
    3) As at the date of the Lease, the parties did not conceive that costs incurred by the lessor pursuant to paragraph 10 would be recoverable. Rather, the recovery of the lessor's costs of enforcing a covenant was to be provided by paragraph 3 of the 6th schedule.

Conclusions

46. There was no dispute about the facts as recorded at paragraph 29 above. The Tribunal will proceed to determine the legal issues which arise on the basis of those facts.

47. Although Imagine's statement of case suggested that it would argue that the costs and interest were included in the settlement agreement dated 8 January 2015, Mr. Cohen accepted that they were not so included.

48. Mr. Cohen accepted that it was not open to Imagine to argue that the Company did not have the intention to proceed to forfeiture when it incurred the costs. The Company's correspondence makes that intention clear.

Administration charges – costs

49. When considering whether the costs can be recovered from Imagine as an administration charge, the Tribunal must consider whether paragraph 8 of the 5th schedule can be interpreted so as to allow such recovery.

50. When interpreting the terms of the Lease, the Tribunal is guided by the Supreme Court in *Arnold v Britton* where, at paragraph 15, Lord Neuberger says

> *"When interpreting a written contract, the court is concerned to identify the intention of the parties by reference to "what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean", ... And it does so by focusing on the meaning of the relevant words, in this case clause 3(2) of each of the 25 leases, in their documentary, factual and commercial context. That meaning has to be assessed in the light of (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions of the lease, (iii) the overall purpose of the clause and the lease, (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions."*

51. At paragraphs 17 to 23 he emphasises 7 factors:
    1) The reliance on commercial common sense and surrounding circumstances should not be invoked to undervalue the importance of the language of the provision which is to be construed;
    2) The worse the drafting of the centrally relevant words, the more ready the court can properly be to depart from their natural meaning;
    3) Commercial common sense is not to be invoked retrospectively;
    4) A court should be very slow to reject the natural meaning of a provision as correct simply because it appears to be imprudent for one party to have agreed it;
    5) Only facts and circumstances which existed at the time that the contract was made and which were known or reasonably available to the parties may be taken into account;
    6) In the event of an event occurring which was plainly not contemplated by the parties, if it is clear what the parties would have intended, the court will give effect to that intention;
    7) Service charge clauses are not subject to any special rule of interpretation and are not to be construed restrictively.

52. In *Assethold Limited v Watts [2014] UKUT 0537* at paragraph 58, the Deputy President of the Upper Tribunal said,

> *"I accept that, as a general principle of interpretation, if contracting parties intend that a payment obligation such as a service charge should cover a particular type of expenditure they will wish to make that clear. Unclear language should therefore be read as having a narrower rather than a wider effect. Nonetheless, I do not think that principle should be pushed to the point where language which was clearly intended to encompass expenditure in a wide variety of situations which the parties have not explicitly catalogued should be so restrictively construed as to deprive it of any real effect."*

53. Applying those principles to the wording of paragraph 8 of the 5th schedule, the Tribunal is not persuaded that their natural meaning includes the costs of proceedings leading up to the preparation of a section 146 notice. The Tribunal determines that the costs claimed by the Company are not recoverable from Imagine as an administration charge under paragraph 8.

54. The Tribunal accepts that the parties should have known at the time of entering into the Lease (and in 2013 when it was varied) that it would be necessary to comply with the requirements of section 81 before the Company would be in a position to issue such a notice following non-payment of service charges. The parties would also have known that the freehold was to be transferred to a residents' management company which would be dependent on receipt of funds through the service charge in order to allow it to fulfill its obligations.

55. However, those circumstances should not undervalue the importance of the language used in the paragraph. What the Company is entitled to recover under paragraph 8 is costs incurred *"for the purpose of or incidental to the preparation and service of a notice under Section 146."* The Tribunal does not consider that the natural meaning of those words is such as to include the costs of proceedings which, although necessary as a precursor to issuing a notice under section 146, did not involve the preparation or service of such a notice. The purpose of the 2014 application to the Tribunal was to determine the amount of service charge payable by Imagine. It may have been a necessary first step towards preparing a section 146 notice but it is stretching the language too far to say that the purpose of the section 27A application was to prepare and serve a section 146 notice. Equally, it is stretching the language too far to say that those proceedings were incidental to the preparation and service of such a notice. Had the parties intended that such costs were to be included within paragraph 8, they could have done so quite easily by adding the words *"in contemplation of proceedings under section 146"* or similar as was done in *69 Marina* and *Barrett v Robinson*. As Miss Gourlay said in her skeleton argument, there is no ambiguity or poverty in the drafting of the provision. The words mean what they say.

56. Having determined this issue in favour of Imagine, the Tribunal should deal with the second and third submissions of Mr. Cohen in relation to this issue. The Tribunal did not consider that they added anything to Mr. Cohen's primary submission and was not persuaded that they had any validity.

Administration charges – interest

57. The Tribunal accepts Miss Gourlay's submissions in this respect. The terms of the Lease are quite clear. Paragraph 12 of the 5th schedule provides that the leaseholder must pay the service charge within 14 days of demand. Paragraph 2 of the 5th schedule provides that interest is payable if sums are not paid within 14 days of the due date. It does not matter that there may be a dispute about the amount actually due. On the one hand, the receiving party is protected by an entitlement to interest if the paying party delays payment by raising issues which are ultimately not successful and on the other hand, the paying party is able to protect its position by making a payment of the sum which it says is due. Imagine chose not to do so. It transpired that it owed £13,000 by way of service charge and the Company is entitled to interest on that sum from 15 March 2014 until payment on 5 February 2015. There appears to be no dispute that the applicable rate is 4.5%. Interest at 4.5% on £13,000 from 15 March 2014 to 5 February 2015 (328 days) amounts to £525.70.

58. The Tribunal does not accept Mr. Cohen's submission that the due date for payment for the purposes of calculating interest was altered by the settlement agreement. The agreement records no change to the terms of the Lease in respect of interest. It merely provides for the date by which the agreed sum must be paid without affecting the entitlement to interest.

Recoverability as a service charge

59. The terms of paragraph 12 of the 5th schedule are clear. In order for costs to form part of the service charge and to be recoverable under that paragraph, the Company must be able to establish that the costs were incurred "*in carrying out its obligations under the 6th schedule*" or "*in the performance of its obligations under this lease*". The Company must show that it incurred the costs when performing one of its obligations under the Lease.

60. The provisions of sub-paragraph (ix) do not assist the Company to argue otherwise because that sub-paragraph is subservient to paragraph 12 and merely defines what is meant by "*the expenses and outgoings incurred by the Lessor.*" The words "*in the performance or contemplation of the performance of its obligations under this lease*" in sub-sub-paragraph 1 are duplication and merely express what is already stated in paragraph 12. That duplication does not occur in sub-sub-paragraph 2 but as that sub-sub-paragraph is part of paragraph 12, any costs incurred in operating the residents' management company must still be incurred in carrying out an obligation under the 6th schedule or in performance of an obligation under the lease. What sub-paragraph (ix) (which was added

in 2013) does achieve is to make it clear that the costs which form part of the service charge under paragraph 12 may include professional fees and the costs of running the management company.

61. It was not suggested by either party that the Company had any obligations under the Lease other than those contained in the 6th schedule, so it is necessary to look at the obligations relied upon by Miss Gourlay, namely paragraphs 6, 10 and 11 of the 6th schedule.

62. When considering those paragraphs, the Tribunal takes into account the same matters as referred to at paragraphs 50 to 52 above.

63. The Tribunal does not accept Miss Gourlay's submission that the costs were incurred in performance of the Company's obligations set out at paragraph 6 of the 6th schedule. That paragraph is in common form and covers the obligation to maintain and repair the building and its common parts. It is stretching the language too far to suggest that it also includes an obligation to take proceedings to enforce payment of service charges to fund the work which is necessary to comply with this paragraph.

64. Likewise, the Tribunal does not accept Miss Gourlay's submission that the costs were incurred in performance of the Company's obligations set out in paragraph 11 of the 6th schedule. Giving that paragraph its ordinary meaning, it is clear that it is intended to cover the situation where a third party commences proceedings against the Company which need to be defended or where a third party is doing something which jeopardises the Property in some way such as withdrawing support or interfering with a right to light which requires the Company to issue proceedings against a third party. It is, again, stretching the language too far to suggest that it includes taking proceedings to enforce payment of service charges because without funding, the Company would be unable to carry out necessary work and the Development might be put into jeopardy.

65. However, the Tribunal does accept Miss Gourlay's submission that the costs were incurred in performing an obligation under paragraph 10 of the 6th schedule. Recitals number 2 and 3 in the Lease make it clear that it was the intention of the parties to the Lease that the freehold would be transferred to a residents' management company and that the leases of the other flats would be in similar terms. Paragraph 1 of the 6th schedule obliges the lessor to grant the leases of the other flats in the Property in substantially the same terms. Therefore it would have been clear to all the parties entering into the leases of the flats that the management of the flats would be financed by the lessees of the flats working together. Paragraph 10 of the 6th schedule in the Lease (as varied by the Tribunal decision in October 2013) obliges the Company to enforce the covenants in the leases of the other flats. There would be a similar provision in the leases of the other flats so that the Company is obliged to ensure that all the lessees comply with the terms of their leases. One of the mutual obligations which must be enforced is the payment of the service charge.

66. It seems to the Tribunal that a reasonable person having that background knowledge, would understand paragraph 12 of the 5th schedule read together with paragraph 10 of the 6th schedule to mean that the Company was obliged to ensure payment of the service charge by all the lessees and that the cost of such action would form part of the service charge recoverable under paragraph 12 of the 5th schedule.

67. The Tribunal does not accept Mr. Cohen's submissions in this respect.

68. In relation to the first submission, the Tribunal considers that it is fanciful to suggest that paragraph 10 was only intended to allow recovery of costs of enforcing the covenants in the lease of flat 2. That submission entirely ignores the recitals numbered 2 and 3 and paragraph 1 of the 6th schedule.

69. In relation to his second submission, Mr. Cohen seeks a very strict interpretation of the words of paragraph 10. What he says is that when considering the action taken against Mr. Molton and Imagine, the Company was fulfilling an obligation in the leases of the other flats and therefore the costs can only be recovered from the lessees of the other flats. This would result in the other 5 leaseholders paying the costs of taking action to recover the service charge from the leaseholder of flat 6, with the leaseholder of flat 6 not being liable for any part of the costs. As Miss Gourlay submits, that result would be unjust. Given that all the leases are intended to be in the same form, it seems that the clear intention of the parties was that the Company should enforce the terms of the leases and that the costs should form part of the service charge.

70. There is some force in Mr. Cohen's third submission because at the time of the granting of the Lease, it is questionable whether legal costs would have been recoverable at all as they were not mentioned other than in paragraph 3 of the 6th schedule. However, the Lease was varied in 2013 to make it clear that costs were recoverable. What the Tribunal has to do, and has done, is to interpret the terms of the Lease as they are now.

71. Mr. Cohen submitted that there is tension between paragraphs 3 and 10 of the 6th schedule. The Tribunal does not accept that submission. The Company may determine to take action to enforce a covenant against an individual leaseholder because it is for the common good of all of the leaseholders that it should do so. In such circumstances it would be action under paragraph 10. There may be other situations where a leaseholder is asking for action to be taken against another leaseholder which the Company does not consider to be for the common good. In such cases it may proceed to take action under paragraph 3 but on condition that the requesting leaseholder is responsible for the whole costs of that action.

72. For those reasons, the Tribunal is satisfied that, in principle, the costs incurred by the Company may be recovered as part of the service charge. Those costs will have to satisfy the requirements of section 19 of the

Landlord and Tenant Act 1985 in that they are subject to the limitation that they must have been reasonably incurred and the works and services supplied must be of a reasonable standard. There will need to be a further hearing for the parties to make submissions on those issues.

Section 20C

73. At the end of the hearing, the parties made submissions as to whether the Tribunal should make an order under section 20C. That was done in case the Tribunal determined against the Company on both issues. As there will now be a further hearing, the Tribunal will invite further submissions on this issue and determine this issue at the end of the adjourned hearing.

Right of Appeal

74. Any party to this application who is dissatisfied with the Tribunal's decision may appeal to the Upper Tribunal (Lands Chamber) under section 176B of the Commonhold and Leasehold Reform Act 2002 or section 11 of the Tribunals, Courts and Enforcement Act 2007.

75. A person wishing to appeal this decision must seek permission to do so by making written application to the First-tier Tribunal at the Regional office which has been dealing with this application. The application must arrive at the Tribunal within 28 days after the Tribunal sends to the person making the application written reasons for the decision. If the person wishing to appeal does not comply with the 28 day time limit, the person shall include with the application for permission to appeal a request for an extension of time and the reason for not complying with the 28 day time limit. The Tribunal will then decide whether to extend time or not to allow the application for permission to appeal to proceed. The application for permission to appeal must identify the decision of the Tribunal to which it relates, state the grounds of appeal and state the result the party making the application is seeking.

76. The parties are directed to Regulation 52 of the *Tribunal Procedure (First-tier Tribunal)(Property Chamber) Rules 2013 SI 2013/1169*. Any application to the Upper Tribunal must be made in accordance with the *Tribunal Procedure (Upper Tribunal)(Lands Chamber) Rules 2010 SI 2010/2600*.

J G Orme
Judge of the First-tier Tribunal
Dated 27 July 2015

Appendix of relevant legislation

Commonhold and Leasehold Reform Act 2002
Schedule 11.

1. –
   1) In this part of this Schedule "administration charge" means an amount payable by a tenant of a dwelling as part of or in addition to the rent which is payable, directly or indirectly –
      a. for or in connection with the grant of approvals under his lease, or applications for such approvals,
      b. for or in connection with the provision of information or documents by or on behalf of the landlord or a person who is party to his lease otherwise than as landlord or tenant,
      c. in respect of failure by the tenant to make a payment by the due date to the landlord or a person who is party to his lease otherwise that as landlord or tenant, or
      d. in connection with a breach (or alleged breach) of a covenant or condition in his lease.
   2) ...
   3) In this Part of this Schedule "variable administration charge" means an administration charge payable by a tenant which is neither –
      a. specified in his lease, nor
      b. calculated in accordance with a formula specified in his lease.
   4) ...

2. A variable administration charge is payable only to the extent that the amount of the charge is reasonable.
3. ...
4. ...
5. –
   1) An application may be made to the appropriate tribunal for a determination whether an administration charge is payable and, if it is, as to-
      a) the person by whom it is payable,
      b) the person to whom it is payable,
      c) the amount which is payable,
      d) the date at or by which it is payable, and
      e) the manner in which it is payable.
   2) Sub-paragraph (1) applies whether or not any payment has been made.
   3) The jurisdiction conferred on the appropriate tribunal in respect of any matter by virtue of sub-paragraph (1) is in addition to any jurisdiction of a court in respect of the matter.
   4) No application under sub-paragraph (1) may be made in respect of a matter which –
      a) has been agreed or admitted by the tenant,
      b) has been, or is to be, referred to arbitration pursuant to a post dispute arbitration agreement to which the tenant is a party,
      c) has been the subject of determination by a court, or

d) has been the subject of determination by an arbitral tribunal pursuant to a post-dispute arbitration agreement.

5) But the tenant is not to be taken to have agreed or admitted any matter by reason only of having made payment.

6) ...

6. ...

Landlord and Tenant Act 1985 (as amended)
Section 18

(1) In the following provisions of this Act "service charge" means an amount payable by a tenant of a dwelling as part of or in addition to the rent -

(a)which is payable, directly or indirectly, for services, repairs, maintenance, improvements or insurance or the landlord's costs of management, and

(b)the whole or part of which varies or may vary according to the relevant costs.

(2) The relevant costs are the costs or estimated costs incurred or to be incurred by or on behalf of the landlord, or a superior landlord, in connection with the matters for which the service charge is payable.

(3) For this purpose -

(a)"costs" includes overheads, and

(b)costs are relevant costs in relation to a service charge whether they are incurred, or to be incurred, in the period for which the service charge is payable or in an earlier or later period.

Section 19

(1) Relevant costs shall be taken into account in determining the amount of a service charge payable for a period -

(a)only to the extent that they are reasonably incurred, and

(b)where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a reasonable standard;

and the amount payable shall be limited accordingly.

(2) Where a service charge is payable before the relevant costs are incurred, no greater amount than is reasonable is so payable, and after the relevant costs have been incurred any necessary adjustment shall be made by repayment, reduction or subsequent charges or otherwise.

Section 20C

1) A tenant may make an application for an order that all or any of the costs incurred, or to be incurred, by the landlord in connection with proceedings before ... the First-tier Tribunal ... are not to be regarded as relevant costs to be taken into account in determining the amount of any service charge payable by the tenant or any other person or persons specified in the application.

2) ...

3) The court or tribunal to which the application is made may make such order on the application as it considers just and equitable in the circumstances.

Section 27A

(1) An application may be made to the appropriate tribunal for a determination whether a service charge is payable and, if it is, as to-
  (a)the person by whom it is payable,
  (b)the person to whom it is payable,
  (c)the amount which is payable,
  (d)the date at or by which it is payable, and
  (e)the manner in which it is payable.

(2) Subsection (1) applies whether or not any payment has been made.

(3) An application may also be made to the appropriate tribunal for a determination whether, if costs were incurred for services, repairs, maintenance, improvements, insurance or management of any specified description, a service charge would be payable for the costs and, if it would, as to -
  (a)the person by whom it would be payable,
  (b)the person to whom it would be payable,
  (c)the amount which would be payable,
  (d)the date at or by which it would be payable, and
  (e)the manner in which it would be payable.

(4) No application under subsection (1) or (3) may be made in respect of a matter which -
  (a)has been agreed or admitted by the tenant,
  (b)has been, or is to be, referred to arbitration pursuant to a post-dispute arbitration agreement to which the tenant is a party,
  (c)has been the subject of determination by a court, or
  (d)has been the subject of determination by an arbitral tribunal pursuant to a post-dispute arbitration agreement.

(5) But the tenant is not to be taken to have agreed or admitted any matter by reason only of having made any payment.

Law of Property Act 1925
Section 146

1) A right of re-entry of forfeiture under any proviso or stipulation in a lease for a breach of any covenant or condition in the lease shall not be enforceable, by action or otherwise, unless and until the lessor serves on the lessee a notice –
  a. specifying the particular breach complained of; and
  b. if the breach is capable of remedy, requiring the lessee to remedy the breach; and
  c. in any case, requiring the lessee to make compensation in money for the breach;

And the lessee fails, within a reasonable time thereafter, to remedy the breach, if it is capable of remedy, and to make reasonable

compensation in money, to the satisfaction of the lessor, for the breach.

2) ...

3) A lessor shall be entitled to recover as a debt due to him from a lessee, and in addition to damages (if any), all reasonable costs and expenses properly incurred by the lessor in the employment of a solicitor and surveyor or valuer, or otherwise, in reference to any breach giving rise to a right of re-entry or forfeiture which, at the request of the lessee, is waived by the lessor, or from which the lessee is relieved, under the provisions of this Act.

4) ...

5) ...

6) ...

7) ...

8) ...

9) ...

10) ...

11) This section does not, save as otherwise mentioned, affect the law relating to re-entry or forfeiture or relief in case of non-payment of rent.

12) ...

13) ...

Housing Act 1996
Section 81

1) A landlord may not, in relation to premises let as a dwelling, exercise a right of re-entry or forfeiture for failure by a tenant to pay a service charge or administration charge unless-
   a. it is finally determined by (or on appeal from) the appropriate tribunal or by a court, or by an arbitral tribunal in proceedings pursuant to a post-dispute arbitration agreement, that the amount of the service charge or administration charge is payable by him, or
   b. the tenant has admitted that it is so payable.

2) The landlord may not exercise a right of re-entry or forfeiture by virtue of subsection (1)(a) until after the end of the period of 14 days beginning with the day after that on which the final determination is made.

3) For the purposes of this section it is finally determined that the amount of a service charge or administration charge is payable –
   a. if a decision that it is payable is not appealed against or otherwise challenged, at the end of the time for bringing an appeal or other challenge, or
   b. if such a decision is appealed against or otherwise challenged and not set aside in consequence of the appeal of other challenge, at the time specified in subsection (3A).

3A) The time referred to in subsection (3)(b) is the time when the appeal or other challenge is disposed of –

a. by the determination of the appeal or other challenge and the expiry of the time for bringing a subsequent appeal (if any), or
b. by its being abandoned or otherwise ceasing to have effect.

4) ...

4A) References in this section to the exercise of a right of re-entry or forfeiture include the service of a notice under section 146(1) of the Law of Property Act 1925 (restriction on re-entry or forfeiture).

5) In this section
   a. "administration charge" has the meaning given by Part I of Schedule 11 to the Commonhold and Leasehold Reform Act 2002,
   b. ...
   c. "dwelling" has the same meaning as in the Landlord and Tenant Act 1985 (c70), and
   d. "service charge" means a service charge within the meaning of section 18(1) of the Landlord and Tenant Act 1985, other than one excluded from that section by section 27 of that Act (rent of dwelling registered and not entered as variable).

5A) ...

6) Nothing in this section affects the exercise of a right of re-entry of forfeiture on other grounds.

7) For the purposes of this section, "appropriate tribunal" means –
   a. in relation to premises in England, the First-tier Tribunal or, where determined by or under Tribunal Procedure Rules, the Upper Tribunal; and
   b. in relation to premises in Wales, a leasehold valuation tribunal.