**UPPER TRIBUNAL (LANDS CHAMBER)**

**UT Neutral citation number: [2014] UKUT 0561 (LC)**
**UTLC Case Number: LRX/54/2014**

**TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007**

***LANDLORD AND TENANT – service charges – tenants to pay fixed proportion of service charge payable by intermediate landlord to freeholder – intermediate landlord to pay proportion of costs incurred by head landlord to be determined by head landlord or its surveyor whose decision is final and binding – jurisdiction of tribunal in relation to apportionment by head landlord – ss. 18(2), 27A(6), Landlord and Tenant Act 1985 – appeal allowed***

**IN THE MATTER OF AN APPEAL AGAINST A DECISION OF THE FIRST TIER TRIBUNAL (PROPERTY CHAMBER)**

**BETWEEN:**

**JEANNA GATER AND OTHERS** **Appellants**

**and**

**(1) WELLINGTON REAL ESTATE LIMITED**
**(2) LCP COMMERCIAL LIMITED** **Respondents**

**Re: Flats 1, 2, 3, 5, 7 & 8 Telegraph House, Sheffield. S1 2EA**

**Before Martin Rodger QC, Deputy President**
**Sitting at: Sheffield Combined Court Centre**
**on**
**5 December 2014**

Mr George Gater for the Appellant
Ms Charlotte Black, instructed by Browne Jacobson, solicitors, for the Respondents

The following cases are referred to in this decision:

*Ashworth Frazer v Gloucester City Council* [2001] UKHL 59)

*Joseph v Joseph* [1967] Ch 78

*Levitt v London Borough of Camden* [2011] UKUT 336 (LC)

*London Borough of Brent* v *Shulem B Association Limited* [2011] EWHC 1663 (Ch)

*Pimms v Tallow Chandlers* [1964] 2 QB 547

*Re Rowner Estates Ltd* (2006) LT LRX/3/2006 (unreported)

*Ruddy v Oakfern Properties Ltd* [2007] Ch 335

*Schilling v Canary Riverside Development PTD Limited* (2005) LRX/26/2005 (6 December 2005) (unreported)

*Warrior Quay Management Ltd v Joachim* (2008) LT LRX/42/2006 (unreported)

*Windermere Marina Village Ltd v Wild* [2014] UKUT 163 (LC)

## DECISION

### Introduction

1. Telegraph House is the former home of the Sheffield Telegraph and Star newspaper which now houses shops, offices and flats on basement, ground and four upper floors. It is a Grade II listed building in a baroque style which was completed in 1916 and converted to its current uses in 2004. The ornate white façade of the building fronts the north side of the High Street in the centre of Sheffield and features elaborate mouldings, decorative columns and ranges of arched windows. Above the façade a large square lantern tower with further columns and buttresses supports a concave leaded roof with a clock dial on each face. At the western end of the frontage, a glazed circular staircase rises from ground level to the second floor, enclosed by columns supporting a dome on which stands a bronze statue of the god Mercury.

2. Telegraph House looks like an expensive building to maintain.

3. This appeal is against a decision of the First-tier Tribunal (Property Chamber) made on 10 February 2014 on an application brought by the tenants under long leases of six flats on the third and fourth floors of Telegraph House under section 27A, Landlord and Tenant Act 1985. Ostensibly the subject of the application was the reasonableness of the service charges payable by the residential tenants for the year ending 31 March 2013 and of the estimated charges for the year ending 31 March 2014. In fact the issues were rather narrower. As they noted in their decision, this was the third occasion on which the same members of the tribunal had been called upon to determine disputes arising out of the service charges payable for flats at Telegraph House.

4. At the hearing of the appeal Mr George Gater spoke on behalf of his daughter, the leaseholder of flat 2 at Telegraph House, and on behalf of the leaseholders of flats 1, 3, 5, 7 and 8, who are also appellants. Ms Charlotte Black, of counsel, instructed by Browne Jacobson, solicitors, appeared on behalf of the Respondents. I am very grateful to them both for their assistance.

5. The sole respondent to the application before the First-tier Tribunal was Wellington Real Estate Limited ("Wellington"), the owner of the freehold interest in Telegraph House. Wellington is not the immediate landlord of the eight flats on the third and fourth floors of the building. In order to understand Wellington's role, and the issues in the appeal, it is first necessary to consider the structure of leasehold interests in the building and the terms of the relevant leases.

### Ownership structure

6. Wellington is the owner of the freehold interest in Telegraph House. In 2004 it granted a lease of the third and fourth floors of the building to a developer, Mr Ian White. That lease, which I will

refer to as "the White Lease" was for a term of 150 years expiring on 26 August 2154 at a peppercorn rent.

7. Having granted the White Lease, Wellington then granted further leases of the remainder of the building. The shops on the ground floor were let to three commercial tenants, while the first and second floors were let to a firm of solicitors. The basement has not been let but Wellington has permitted the solicitor tenants of the first and second floors to use it for the storage of documents.

8. The premises comprised in the White Lease are on the third and fourth floors of Telegraph House, and extend to the whole of those floors with the exception of two staircases and the lift; the demise also excluded the structural and external parts of the building. The plans attached to the White Lease show the third and fourth floors laid out as offices, which they may have been when the lease was granted. Nonetheless, the permitted use of the demised premises was as eight residential private dwellings each for the occupation of one family only (clause 4(19)(a) of the White Lease). The obvious intention, as happened, was that Mr White would convert the office space into one-bedroom apartments.

9. Having completed the conversion of the third and fourth floors, Mr White granted sub-leases of the individual apartments to the appellants or their predecessors in title on various dates in 2005 and 2006. With minor exceptions the sub-leases are in a standard form, each being for a term of 150 years less 6 days from 27 August 2004.

10. In 2009, having granted sub-leases of all eight apartments, Mr White assigned the White Lease to a management company which he controlled, Telegraph House (Sheffield) Management Company Ltd. In the following year that company was put into liquidation and on 19 January 2011 the liquidator transferred the White Lease to LCP Commercial Limited ("LCP").

11. Wellington and LCP are members of the same group of companies.

**The White Lease**

12. I have already referred to the extent of the premises demised by the White Lease. The structural parts of the building, and the access to the third and fourth floors through common parts and by means of the lift all remain vested in Wellington.

13. By clause 4(1) of the White Lease the Tenant covenanted to pay a service charge in return for the services which by clause 5(4) the Landlord covenanted to provide. The expression "Service Charge" is defined by clause 1(16), as:

> "an amount equal to a fair proportion (such proportion to be determined by the Landlord's Surveyor who determination shall be final and binding) of all sums incurred by the Landlord in and providing the Services."

The expression "Services" was defined by clause 1(15) to mean the services set out in Part 2 of the Third Schedule, which also contains all of the substantive provisions relating to the calculation and payment of the Service Charge.

14. Although the expression "Service Charge" had already been defined in clause 1(16), paragraph 2 of Part 1 of the Third Schedule provides a further definition. By that alternative, "the Service Charge shall be the Tenant's Share of the Service Cost in respect of each Accounting Year…" The "Service Cost" is defined by reference to the costs incurred in respect of the services and expenses set out in Part 2 of the Third Schedule. The expression "Tenant's Share" is defined by paragraph 1.5 of Part 1 of the Third Schedule as:

> "… a due and fair proportion of the Service Cost (such proportion to be determined by the Landlord or its surveyor (in each case acting reasonably) and taking into account the relevant floor areas within the Building or other reasonable factors in making the determination."

15. Fortunately there does not seem to be any significant difference between the Service Charge as defined in paragraphs 1 and 2 of Part 1 of the Third Schedule and as defined in clauses 1(15) and 1(16). In substance, the White Lease obliges the Tenant of the whole of the third and fourth floors to pay a proportion of the costs incurred by Wellington in providing the Services listed in Part 2 of the Third Schedule, that proportion being determined either by the Landlord's Surveyor (in both versions) or by the Landlord (in paragraph 1.5). Both versions stipulate that the proportion payable by the Tenant is to be "fair". An apportionment by the Landlord's Surveyor is said by clause 1(16) to be "final and binding", but is not so described by paragraph 1.5 which requires instead that the proportion is to be determined "acting reasonably and taking into account the relevant floor areas within the Building or other reasonable factors." There is no necessary inconsistency between any of these provisions, although it would appear that if the Landlord wants the result of the apportionment to be "final and binding" it must arrange for it to be undertaken by the Landlord's Surveyor.

16. The Services listed in Part 2 of the Third Schedule are very much as one would expect in such a lease and include, except to the extent that they are already the responsibility of any other tenant or occupier, the repair and maintenance of common parts, interior and exterior decoration and the repair of the foundations, roof, structure and exterior of the Building other than any shop fronts or fascias.

17. The machinery for payment of the Service Charge under the White Lease begins with a "proper estimate" of the amount of the Service Charge in the accounting year to 31 March which is to be made by the Landlord's Surveyor and notified in writing to the Tenant. This sum is defined in paragraph 1.3 of Part 1 of the Third Schedule as the "Estimated Service Charge" and by paragraph 3 it is required to be paid by the Tenant by equal quarterly instalments. The Estimated Service Charge is not a fixed amount for the whole year, and a different estimate may be notified to the tenant from time to time leading to an adjustment in the subsequent instalments for the remainder of the accounting year.

18. As soon as practicable after the end of each accounting year the Landlord is required by paragraph 4 of Part 1 of the Third Schedule to serve on the Tenant a summary of the Service Costs

(which summary is described as "conclusive save in the case of manifest error"). The difference between the Estimated Service Charge and the Service Charge is then payable by the Tenant to the Landlord or vice versa within 14 days of the date of the statement.

**The apartment sub-leases**

19. The parties to the sub-leases of the apartments are referred to as Landlord and Tenant, with Wellington as Head Landlord. Where appropriate for clarity I will refer to White or LCP as "the intermediate landlord".

20. Each of the sub-leases granted by White demises one of the eight apartments on the third and fourth floors of Telegraph House; the third and fourth floors themselves are referred to in the sub-leases as the "Property". The demised premises are defined in the First Schedule in such a way as to exclude any part of the structure of the building. The rights granted to the Tenant by Schedule 2 of the sub-lease include the use of a laundry bin store on the same floor.

21. Clause 2 of the sub-leases reserves as rent both a ground rent and a "Service Charge", an expression which first appears in the Particulars at the start of the sub-lease where (taking flat 1 as an example) it is said to be "15.39% of the Service Costs in respect of the Apartment". The expression "Service Cost" is defined in paragraph 1.4 of the Sixth Schedule as "all costs reasonably and properly incurred in respect of the services and expenses set out in Part 2 of the Schedule relating to the Property".

22. Although the Particulars define the Service Charge, as with the White Lease, the apartment sub-leases include a second definition of that expression which is found in paragraph 2 of Part 1 of the Sixth Schedule. There the Service Charge is defined as "the Tenant Share of the Service Cost in respect of each Accounting Year". The Tenant's Share is defined in paragraph 1.5 as the same fixed percentage of the Service Cost as appeared in the Particulars. There is therefore no discrepancy between the two definitions, the effect of which is that the Service Charge is a fixed percentage of the Service Cost, being the costs incurred by the intermediate landlord in providing services to the third and fourth floors.

23. The services in respect of which the Service Charge are payable are listed in Part 2 of the Sixth Schedule. Because they relate only to the interior of the third and fourth floors of the building they are rather limited, but include the inspection, repair, cleaning etc of the access ways and other common parts of the third and fourth floors, the cleaning of the windows in those access ways and the cleaning of a laundry bin store. Most other services described in Part 2 of the Sixth Schedule are ancillary to those very limited obligations.

24. Provision is made by paragraph 3 of Part 1 of the Sixth Schedule for the payment of an Estimated Service Charge by the Tenant to the intermediate landlord, which is to be the "[intermediate] Landlord's proper estimate of the Service Charge for the Accounting Year notified in writing to the Tenant from time to time". As soon as practicable after the end of each Accounting

year (on 31 March) the intermediate Landlord is required to serve on the Tenant a summary of the Service Cost which again is described as "conclusive (save in the case of manifest error)" (paragraph 4). Any balance payable by either party is required to be paid within 14 days of that statement (paragraph 5).

25. The apartment sub-leases also include a covenant by the Tenant at paragraph 3 of the Fourth Schedule "to pay the Maintenance Rent hereby reserved." The expression "Maintenance Rent" is defined in the Particulars at the commencement of the sub-lease as a fixed percentage of "the service charge" reserved by the White Lease; by clause 1 of the sub-lease the same expression is defined as the same fixed percentage of the "service rent" reserved by the White Lease. The expression "service rent" is not used in the White Lease, although the Service Charge is reserved as rent and the two expressions are presumably intended to bear the same meaning.

26. The percentage contributions of individual Tenants towards the Maintenance Rent range between 10.31% and 15.99% and in each case are the same as the Tenant's Share of the Service Charge. The tenants of the individual apartments therefore contribute in the same proportions to the cost of services provided by their immediate landlord, LCP, as they do to those provided by the head landlord, Wellington.

27. The contents of the White Lease were presumably known to the parties when the apartment sub-leases were granted and at paragraph 4 of the fourth schedule the Tenant covenants specifically to observe and perform the covenants on the part of the tenant in the White Lease (i.e. White) (except as to the payment of rent).

**The service charge regime in practice**

28. Following the acquisition of the White Lease by LCP in January 2011 the provision of all of the services in the building has been in the hands of LCP (so far as concerns the third and fourth floors) and Wellington (so far as concerns the remainder of the building, including the structure and the common parts). As members of the same group of companies there has clearly been some co-ordination in the management of service provision between the two, and to some extent this has led to a blurring of roles which the draftsman of the leases assumed would be clearly defined.

29. In particular, although both the White Lease and the apartment sub-leases each provide for an estimate of the service charge for the forthcoming accounting year, and for an annual summary of the service costs, so that both Wellington and LCP should produce such documents for their respective expenditure, in practice a single estimate and a single annual summary have been provided with consolidated figures representing costs of services provided by both Wellington and LCP. For example, the service charge certificate for the year ending 31 March 2013, which was referred to the First-tier Tribunal, is a document prepared on behalf of Wellington which includes expenditure on the building as a whole, to which all tenants contribute, and expenditure on the third and fourth floors, to which only the residential tenants contribute.

30. I was informed by Ms Black, who appeared on behalf of the both Wellington and LCP at the hearing of the appeal, that although the service charge estimates and summaries are prepare on behalf of Wellington, they are notified to the residential tenants by LCP which also issues service charge invoices and receives payment. Although these arrangements do not exactly mirror the scheme of the leases, there has so far been no suggestion that they disadvantage the residential tenants.

31. In the annual summary of expenditure the costs which have been incurred are separated into five "schedules". Schedule A relates to expenditure on the building as a whole to which all tenants contribute; Schedule B relates to expenditure to which both the residential tenants and the solicitors on the first and second floors contribute, but not the retail tenants on the ground floor; Schedule C is expenditure for which only the retail tenants are responsible; Schedule D is expenditure to which only the residential tenants contribute; and finally Schedule E is expenditure to which only the solicitor tenants contribute. The proportions in which the residential tenants contribute to these service cost schedules vary. In the case of flat 1, for example, the tenant contributes 2.93% of Schedule A, 5.62% of Schedule B, and 15.39% of Schedule D expenditure, with no contribution to Schedules C and E.

32. The apportionment of liability for the different schedules has been determined by Wellington's surveyor and asset manager, Mr Binner, who has based the allocation of liability on the net internal floor areas of lettable space within the building measured in accordance with the RICS Code of Measuring Practice. The lettable area of the building as a whole has been measured at 29,008 sq ft NIA, while the area demised by the White Lease, before its conversion to flats was 5532 sq ft, hence the contribution of the residential tenants to expenditure on the building as a whole is 19.07%.

33. This approach to the allocation of service costs is not foreshadowed in the White Lease or in the individual apartment sub-leases. These assume that there will be an apportionment of expenditure to the third and fourth floors as a whole (in the proportion determined by the Landlord's Surveyor) which will then be allocated between the individual tenants of the eight flats in the fixed proportions stipulated by their individual leases, in addition to their contribution to the costs of services to the third and fourth floors alone. There was no challenge to this approach as part of the appeal and it was not suggested that it disadvantages the residential tenants. The impression given by the decision of the First-tier Tribunal is that in their current form the schedules reflect suggestions which it had made in previous applications involving the same parties.

34. The contributions of the three retail tenants are also apportioned by reference to net internal area. According to the schedule of accommodation drawn up in 2001, which is used as the basis of apportionment (a copy of which is at p.240 of the appeal documents) each of the retail units includes basement storage space, of 477 sq ft, 922 sq ft, and 1704 sq ft making 3103 sq ft in total. In calculating the service charge proportions of the retail tenants the basement space is taken into account and given equal weighting to retail or office space. Although the schedules do not say so specifically, I assume that the basement space is demised by the leases of the retail units.

35. One further feature of the apportionment is worth mentioning at this stage. The net internal areas of the third and fourth floors have been measured as in their former configuration as offices

before their conversion to apartments. One consequence of this appears to be that the corridors and laundry rooms which now exist (and which are common parts as far the residential tenants are concerned) are taken into account in determining the proportion of the service costs payable under the White Lease, whereas common parts and service areas, such as toilets, on the other floors are left out of account in the apportionment calculation.

**Jurisdiction and parties**

36. The greater part of the service costs incurred at Telegraph House are incurred in connection with the insurance, repair and maintenance of the building as a whole and are shared between the commercial and residential tenants. Through their individual covenants to pay the Maintenance Rent, the residential tenants each contribute a fixed proportion of the service charge payable by the intermediate landlord to Wellington under the White Lease. That fixed proportion is of a sum which itself represents an apportioned part of the total Service Costs incurred by Wellington in providing services to the building as a whole. The contribution payable in respect of the third and fourth floors is not a fixed percentage, but, as provided for by paragraph 1.5 of the Part 1 of the Third Schedule to the White Lease, is:

> "… a due and fair proportion of the Service Cost (such proportion to be determined by the Landlord or its surveyor (in each case acting reasonably) and taking into account the relevant floor areas within the Building or other reasonable factors in making the determination."

37. The residential tenants have no contractual relationship with Wellington. Their immediate landlord is LCP and, although costs are incurred by the superior landlord, Wellington, for which the residential tenants are ultimately responsible, it is only their immediate landlord, LCP, to whom they are obliged to pay the Service Charge and the Maintenance Rent. Such an arrangement is not uncommon, but before going any further with the appeal it is first necessary to consider the basis on which the First-tier Tribunal was entertaining an application by the residential tenants of Telegraph House concerning the apportionment of service charges under a lease, the White Lease, to which they are not parties.

38. By their application the residential tenants invoked the jurisdiction of the First-tier Tribunal under s. 27A, Landlord and Tenant Act 1985 to make a determination whether a service charge is payable, and if it is, as to the amount which is payable.

39. The meaning of "service charge" is provided for by s.18 of the 1985 Act, which, so far as material, provides as follows:

> "18. Meaning of "service charge" and "relevant costs".
> (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."

40. A service charge is therefore "an amount payable by the tenant of a dwelling". The 1985 Act contains the following definition of "dwelling" in s.38:

> ""dwelling" means a building or part of a building occupied or intended to be occupied as a separate dwelling together with any yard, garden, outhouses and appurtenances belonging to it or usually enjoyed with it"

41. In *Ruddy v Oakfern Properties Ltd* [2007] Ch 335 the Court of Appeal held that, for this purpose, a person may be a "tenant of a dwelling" even though their tenancy includes other property or comprises more than one dwelling. Thus where a building comprised commercial premises on the lower floors and residential apartments on the upper floors, a company which held the long lease of the upper floors, which contained 24 self contained flats, was "the tenant of a dwelling". The consequence was that sums payable for services by PPM, the tenant of the upper floors, to the head landlord, Oakfern, were "service charges" within the meaning of s.18 of the 1985 Act. Mr Ruddy, the tenant of one of the residential flats, was obliged by his lease to pay to his own landlord, PPM, a fixed proportion of the sum payable by it to Oakfern by way of service charge. The Court of Appeal held that PPM was the tenant of a dwelling and that the Leasehold Valuation Tribunal had jurisdiction to consider an application by Mr Ruddy under s.27A of the 1985 Act for a determination whether the sums payable by PPM to Oakfern were reasonable. It was not necessary that the application be made by the "tenant of the dwelling" under whose lease the service charge was payable.

42. In the same way, the First-tier Tribunal had jurisdiction on an application under s.27A by Ms Gater and the other residential tenants at Telegraph House to consider the service charge payable to Wellington by LCP under the White Lease, which would then be passed on through the Maintenance Rent payable under the apartment sub-leases.

43. In *Ruddy* the intermediate landlord was a company owned by 15 of the residential tenants and it did not become a party to the application, either as applicant or respondent. In this appeal LCP is an associate of Wellington and it has been aware of the proceedings throughout without feeling it necessary to apply to be joined. It seems to me to be preferable in cases such as these, as a matter of good practice, for an intermediate landlord always to be named as a respondent, or added as one, so that, even if it chooses not to participate, there will be no doubt about the binding effect of a determination by the First-tier Tribunal.

**The issues before the First-tier Tribunal**

44. The sole issues considered by the First-tier Tribunal concerned the apportionment of service charges between the various tenants in Telegraph House as a whole. In particular, the residential

tenants, on whose behalf Mr Gater spoke, challenged the treatment of three areas of the building in the apportionment exercise undertaken by Wellington's surveyor.

45. By far the most significant area in issue was that part of the basement of Telegraph House which extends to 4,740 sq ft and is used for document storage by the solicitors who occupy the offices on the first and second floors. The arrangement for the use of the basement is rent free, reflecting the fact that it is said to be unlettable as independent space having only limited access through the plant room and other service space on the ground floor of the building, limited lighting or heating and being undecorated. Although the First-tier Tribunal suggested that it did not benefit from the lift, it was common ground at the appeal that the lift did reach the basement and was used for the transportation of documents for storage. The First-tier Tribunal heard evidence from Mr Preston, a representative of Wellington's agents, that no costs were incurred solely for the use or benefit of the basement itself which made their way into the service charge. There was no possibility of the solicitors taking a formal lease of the basement on terms that they contribute towards the service charge on a pro rata basis. Wellington was in discussion with the solicitors over the possibility of their making a contribution at a reduced rate but no resolution had yet been achieved.

46. The area of the basement has not been taken into account by the Landlord's surveyor in apportioning liability for the service costs in Schedules A or E. Mr Gater had submitted to the tribunal that, if the basement was given equal weighting in the apportionment of service charge contributions, the residential tenants' aggregate contribution towards Schedule A expenditure would reduce from 19.07% to approximately 16%, with a further reduction in relation to Schedule B.

47. The second area in issue comprised two toilets on the first and second floors which are used exclusively by the solicitor tenants although they are located outside the area demised to them in what is nominally the common parts of the building. The floor area of these facilities (188 sq ft) is not taken into account in the apportionment of service charge contributions because they are common parts and not part of the 29,008 sq ft of demised space. Additionally, as Mr Binner explained in his written material supplied to the First-tier Tribunal, applying the RICS Code of Measuring Practice, the measurement of net internal area does not include toilets, toilet lobbies, bathrooms, cleaners' rooms and the like, so even if the toilets were treated as being demised to the solicitor tenants who have the use of them that would not alter their treatment in the apportionment exercise.

48. The final area in contention was a store room adjoining the laundry on the third floor of the building (it is not clear whether there is also a dispute about the similar space on the fourth floor). The area is very small but is undoubtedly part of the common parts of the third and fourth floors over which the apartment sub-leases grant rights to the residential tenants.

49. The First-tier Tribunal considered the challenge by the tenants to the apportionment on the basis that its task was to satisfy itself that the apportionment undertaken by Wellington was a reasonable one; it was not to ask itself how it would carry out a reasonable apportionment. That is clear from the following passage from the tribunal's decision:

> "There is a plethora of decided cases which make it clear that a tribunal should not seek to impose its own view of a reasonable process. The approach must be to determine, having regard to all relevant circumstances, if the approach of the landlord is not unreasonable. There is rarely only one reasonable view, but a range of reasonableness within which several views may be encompassed."

50. Applying this approach the First-tier Tribunal decided that each of the apportionment decisions made by Wellington's surveyor had been reasonable. It described the overall effect of the approach adopted in these terms:

> "Despite the simplicity of the wording of the Lease and the lack of formulaic guidance [Wellington] has devised a moderately complicated but basically fair way of attributing costs to the different classes of tenant. "

51. In considering the most important individual area in dispute, the basement, the tribunal went further in its assessment. Having described the very limited facilities afforded by the basement and the very limited services provided to it, the tribunal concluded:

> "Given that it would produce an imbalanced calculation to include the whole of the basement in the apportionment calculation we can see no fairer (i.e. reasonable, taking into account floor areas and other reasonable factors) way of dealing with the issue than that adopted by WRE."

52. As far as the other areas were concerned the First-tier Tribunal noted that costs incurred in connection with the toilets in the common parts which, in practice, were used only by the solicitors, were now charged only to the solicitors (in Schedule E). That method was reasonable and although the toilets could be demised to the solicitors that would not result in an adjustment to the apportionments if net internal area continued to be the yard-stick. The tribunal concluded that Wellington's approach was "not unreasonable".

53. The First-tier Tribunal also concluded that the small store room next to the laundry was properly included in the area apportioned to the White Lease, as it was within its demise.

**The appeal**

54. In their application for permission to appeal the residential tenants identified both LCP and Wellington as intended respondents. Although LCP had not been party to the original decision Ms Black, who appeared on behalf of both companies, indicated that LCP was content to be joined as a respondent to the appeal and I so direct.

55. The appellants' main ground of appeal was that the current basis of allocating annual service charges was unfair and ought to be adjusted to reflect the proportion which the residential floors bear to the building as a whole, including the whole of the basement. The service charge for individual flats had increased from less than £1,000 in 2006 to £3,300 in 2010. It is expected to increase

significantly in the immediate future, with external decoration and roof repairs proposed at a cost exceeding £200,000, resulting in an annual charge in the order of £5,000 for modest one bedroom flats in Sheffield. The residential tenants therefore believe that even small adjustments to the apportionment of liability between the third and fourth floors and the remainder of the building may result in real savings to them.

56. Through Mr Gater the appellants also expressed particular dissatisfaction with the willingness of the First-tier Tribunal to overlook the prolonged and inconclusive negotiations over an additional contribution by the solicitor tenants to reflect their use of the basement.

57. Neither the manner in which the service charge arrangements were operated in practice nor the relationship between Wellington and LCP were apparent from the decision of the First-tier Tribunal or the grounds of appeal. In saying that I intend no criticism of the First-tier Tribunal; the same parties had been before it on two previous occasions and all involved were well aware of the leasehold structure and the manner in which the service charges had been dealt with in practice after the acquisition of the White Lease by LCP. There was no need for these non-contractual arrangements to be explained in any detail in the decision, but, as they seemed to be at variance with the contractual scheme, permission to appeal was granted by the Tribunal on the general issue of the extent to which the residential tenants were liable to contribute to the cost of services provided by Wellington.

58. With the benefit of the much fuller understanding of the current arrangements which emerges from the documents now available to the Tribunal and the helpful explanation provided by Mr Binner as part of the respondent's case, it is apparent that the current service charge arrangements (in particular the consolidated service costs estimate and end of year accounting) are an informal but practical modification of the contractual scheme with which all parties are prepared to live, for the time being at least.

59. There remains in issue the complaint on which the appellants sought permission to appeal, namely that, contrary to the decision of the First-tier Tribunal, the apportionment of service charges by Wellington's surveyor was unfair.

**Apportionment – the tribunal's role**

60. I have referred in paragraph 49 above to the basis on which the First-tier Tribunal approached its task in this case. It considered that it was not its role to determine what the "due and fair proportion of the Service Cost" referred to in the White Lease ought to be "taking into account the relevant floor areas within the Building or other reasonable factors". That task was assigned by paragraph 1.5 of the Third Schedule to the White Lease to the Landlord, Wellington, or its surveyor (in each case acting reasonably). The tribunal saw its job as being to consider whether the apportionment settled on by Wellington's surveyor was fair. There was a range of different ways in which the apportionment could be undertaken, and so long as the method selected by the person to whom the parties had allocated the task was a fair method, the tribunal considered that it had no power to substitute a different method.

61. The First-tier Tribunal referred to there being "a plethora of decided cases which make it clear that a tribunal should not seek to impose its own view of a reasonable process". It is not clear to me what decided cases the tribunal had in mind. There are certainly cases where the parties have agreed that service charges will be apportioned by a predetermined formula, such as a fixed percentage, or by reference to relative floor area or rateable value. In such cases the tribunal has no jurisdiction under ss.19 or 27A of the 1985 Act to substitute a different apportionment. That was made clear by the Lands Tribunal (HHJ Rich QC) in *Schilling v Canary Riverside Development PTD Limited* (2005) LRX/26/2005 (6 December 2005)(unreported) at paragraph 19, referring to s.19:

> "Costs are to be taken into account 'only to the extent that they are reasonably incurred', but if reasonably incurred they fall to be apportioned in accordance with the terms of the lease, except if excluded by a failure to consult or otherwise under for example ss20B and 20C."

62. The lease in *Schilling* quantified the lessees' liability to contribute towards the costs of services in fixed percentages, one for costs incurred in respect of the building as a whole and a different percentage for the costs of the car park (see paragraph 18). Other similar decisions include *Re Rowner Estates Ltd* (2006) LT LRX/3/2006 (unreported) and *Warrior Quay Management Ltd v Joachim* (2008) LT LRX/42/2006 (unreported).

63. Direct authority on service charges to be apportioned on the basis of a "due and fair proportion" to be determined by the Landlord or its surveyor acting reasonably is more sparse. In *Levitt v London Borough of Camden* [2011] UKUT 336 (LC) the Tribunal (HHJ Walden-Smith) followed *Schilling* in a case where the lease gave the landlord the choice of different methods of apportionment, including apportionment on a "fair and reasonable basis". Approving the apportionment advocated by the landlord as "not unreasonable" the Tribunal said at paragraph 36 that:

> "Section 19 does not permit the tribunal to ascertain what is a reasonable apportionment of the relevant costs."

64. On general principles where one party to a contract is given the power to decide a matter subject to a proviso that the decision must be fair or reasonable, a challenge to the decision will only succeed if no reasonable person in the position of that party could have reached the same decision (see, for example, cases on unreasonable refusals of consent to assign a lease, such as *Pimms v Tallow Chandlers* [1964] 2 QB 547, and *Ashworth Frazer v Gloucester City Council* [2001] UKHL 59). As an application of the common law, therefore, without considering the effect of statute, the First-tier Tribunal's approach to the issue of apportionment was unimpeachable.

65. However, in *Windermere Marina Village Ltd v Wild* [2014] UKUT 163 (LC), (which was decided on 28 May 2014, 3 months after the First-tier Tribunal's decision in this case) this Tribunal decided that s.27A(6) of the 1985 Act was relevant to a contractual provision by which a landlord or its surveyor was given responsibility for the apportionment of service charges on a fair basis. S.27A(6) provides as follows:

> "(6) An agreement by the tenant of a dwelling (other than a post-dispute arbitration agreement) is void in so far as it purports to provide for a determination—

(a) in a particular manner, or

(b) on particular evidence,

of any question which may be the subject of an application under subsection (1) or (3)."

Subsection (1) of s.27A gives the appropriate tribunal jurisdiction to determine the quantum of a service charge and the questions by whom, to whom, when and in what manner it is to be paid; subsection (3) gives a similar jurisdiction in respect of costs not yet incurred.

66. In *Windermere* the leases of residential boathouses forming part of a marina estate of mixed flats, houses, boathouses and moorings provided for the tenants to pay

> "a fair proportion (to be determined by the Surveyor for the time being of the Lessors whose determination shall be final and binding) of the expense of all communal services …"

67. The Tribunal decided that s.27A(6) of the 1985 Act rendered the words in brackets in that provision void. The Tribunal accepted the submission of the tenants that the jurisdiction of the LVT under section 27A(1)(a) was to determine "the amount which is payable" as a service charge. One element of that determination was the proportions in which the total expenditure incurred by a landlord was to be apportioned amongst those who were to contribute towards it. The leases purported to provide for that element of the ascertainment of the amount payable to be determined "in a particular manner" namely by a binding decision of the surveyor. In those circumstances section 27A(6) rendered the words in brackets void and deprived the landlord's surveyor of any role in the process. That possibility had been adverted to, but not decided, by Morgan J in *London Borough of Brent* v *Shulem B Association Limited* [2011] EWHC 1663 (Ch).

68. The Tribunal's reasoning in *Windermere* was at paragraphs 37 to 42 where it said this:

> "37. It is perfectly possible to contemplate an application to the first-tier tribunal under section 27A(1) where the only question in issue concerns the proper method of apportionment of a sum which is agreed to have been incurred reasonably on services provided to a reasonable standard and which otherwise falls within a tenant's contractual liability. An issue might arise about the correct classification of a particular item of expenditure where different proportions were payable for different items; or the method of apportionment itself might be open to different interpretations. In this case, as the LVT said in paragraph 97 of its decision, "the heart of the dispute" is the apportionment. It was not submitted by Mr Gilchrist that an issue of apportionment could never be the subject of a determination under section 27A(1), and such a submission would be unsustainable.
>
> 39. Having identified that section 27A(1) is not confined to issues of quantification, and may include issues of apportionment, it is then necessary to consider section 27A(4). This has the effect that no application may be made under section 27A(1) or (3) in respect of a matter which has been agreed or admitted, or which is to be, or has already been, the subject of a determination either by the court or by arbitration pursuant to a post dispute arbitration provision. Where the amount which is payable as a service charge, or some component or issue relating to that amount, has been agreed, it may not subsequently be referred to a first-tier

tribunal for determination. In the same way, where the parties have agreed in their lease how service charges are to be apportioned (for example, in fixed proportions or percentages, or in proportions referable to floor area or rateable value) section 27A(4) will preclude an application under section 27A(1) in respect of that matter. ….

40. The prohibition in section 27A(4) on re-opening matters which have been agreed must, however, be considered in the light of section 27A(6). This renders void any agreement by the tenant in so far as it "purports" to provide for the determination of any question which could be the subject of an application under sub-section (1) or (3) "in a particular manner" or "on particular evidence". The purpose of the provision is clearly to avoid agreements excluding the jurisdiction of the first-tier tribunal on questions which could otherwise be referred to it for determination.

41. In a statutory anti-avoidance provision such as section 27A(6) an agreement will "purport to" provide for an outcome if it has the effect of providing for that outcome. In *Joseph v Joseph* [1967] Ch 78 the Court of Appeal held that in section 38(1), Landlord and Tenant Act 1954 the expression "purports to preclude the tenant from making an application or request" for a new tenancy means "has the effect of precluding the tenant" so that an agreement for the tenant to surrender their tenancy at a future date was void. The same broad approach is appropriate in the case of section 27A(6) so that the question in the case of any particular agreement by a tenant is whether it has the effect of providing for the determination of any question which could be the subject of an application under sub-section (1) or (3) "in a particular manner" or "on particular evidence".

42. The question referred to the LVT in this case was what proportion of the expenses incurred by the appellant was to be paid by the respondents. By paragraph (2) of the Schedule to their leases the respondents had already agreed that the answer to that question was that they were to pay such proportion as was determined by the appellant's surveyor, whose decision was to be final and binding. In my judgment that agreement was void because it had the effect of providing for the manner in which an issue capable of determination under section 27A(1) was to be determined, namely by a binding decision of the appellant's surveyor. I cannot accept Mr Gilchrist's submission that the apportionment of service charges is not a question which arises under sub-section (1) or that sub-section (6) is directed only at provisions which purport to make a determination of the relevant expenditure by the landlord's surveyor or accountant determinative."

69. In *Windermere* the service charge expenditure was incurred by the immediate landlord and the provision for apportionment by the landlord's surveyor was contained in the leases of the individual boathouses themselves. This case is different, in that the service charge expenditure incurred by Wellington, the freeholder, is to be divided in accordance with the proportions determined by its surveyor under the terms of the White Lease, and will be paid in the first instance by LCP which will then pass it on to the residential tenants. The liability of the residential tenants under their own apartment sub-leases is to pay a fixed proportion of the sum payable by LCP to Wellington. There is no contractual relationship between the tenants who will ultimate pay the service charge and the head landlord whose surveyor carries out the apportionment which determines the aggregate total of their contributions. An important question which arises in this appeal for the first time is how s.27A(6) impacts on this arrangement.

70. Ms Black acknowledged that the effect of the Court of Appeal's decision in *Ruddy* was that for the purpose of ss.18-30 of the 1985 Act LCP was a tenant of a dwelling by virtue of the White Lease.

71. It also follows from *Ruddy* that the question of what sum is payable by LCP to Wellington as a service charge under the White Lease may be the subject of an application to the appropriate tribunal under s.27A(1) or (3) of the 1985 Act. Moreover, such an application may be made by the residential tenants, notwithstanding the fact that they are not parties to the White Lease, in the same way as Mr Ruddy was entitled to make his own application although he was not part to the head lease between Oakfern and PPM. The application made by the appellants in this case for a determination of the service charges for 2013 and the estimated charges for 2014 were rightly entertained by the First-tier Tribunal and Ms Black did not suggest otherwise.

72. It necessarily follows that s.27A(6) operates to render void a contractual provision in the White Lease which has the effect of providing for the determination "in a particular manner" of the main issue in the applications, namely the proper apportionment of the service costs under the White Lease. For the reasons given by the Tribunal in *Windermere* the words "such proportion to be determined by the Landlord or its surveyor (in each case acting reasonably)" which appear in the definition of the Tenant's Share in paragraph 1.5 of the Third Schedule to the White Lease are void. For the same reasons the words "(such proportion to be determined by the Landlord's Surveyor whose determination shall be final and binding)" which appear in the definition of Service Charge in clause 1(16) of the White Lease are also void.

73. It was submitted by Ms Black that the only effect of s.27A(6) was to render void the words "whose determination shall be final and binding" and that the role of the Landlord's surveyor in determining the fair proportion of the service costs remained intact. I do not accept that. The statutory anti-avoidance provision renders void so much of the agreement as has the effect of providing for the determination in a particular manner of any question which could be referred to the appropriate tribunal under s.27A(1). A determination of proportions by the landlord's surveyor is such a provision, whether it is said to be final and binding or not. The Tribunal said as much in *Windermere* at paragraph 48:

> "Section 27A(6) deprives the landlord's surveyor of his role in determining the apportionment. Paragraph (2) is to be read as if the method of ascertaining a fair apportionment was omitted altogether. Mr Pogson's [the surveyor] conclusions cannot therefore have any contractual effect. That being the case, it was for the LVT to decide what was a fair proportion of the expense of communal services payable by the respondents."

74. As is apparent from this passage, where a provision for determining an apportionment is rendered void by the operation of s.27A(6) of the 1985 Act, and the parties cannot agree what is fair, the consequence is that the fair proportion falls to be determined by the appropriate tribunal. That is a fundamentally different exercise from the one undertaken by the First-tier Tribunal in this case, when it asked itself whether the respondent's method of apportionment was fair rather than asking itself what the fair apportionment should be.

75. In carrying out an apportionment the appropriate tribunal will have regard to the parties' agreement, so far as it remains. In this case the parties agreed that the Tenant's Share would be a due and fair proportion of the service costs which would be apportioned "taking into account the relevant floor areas within the Building or other reasonable factors". That is not a provision the effect of which is to provide for a determination "in a particular manner" and it survives the intervention of s.27A(6).

76. I therefore conclude that the First-tier Tribunal was wrong in the limited view it took of its role in relation to apportionment. That is understandable because neither party was legally represented before the tribunal, this Tribunal's decision in *Windermere* had not been published and, as I have already made clear, the decision was in accordance with normal contractual principles.

**Consequences**

77. The final matter for consideration in this appeal is whether the First-tier Tribunal's misapprehension of the scope of its role made any difference to the outcome, such that this Tribunal should interfere with its determination.

78. Ms Black submitted that the decision made by the First-tier Tribunal in approving the apportionment by the respondents' surveyor was correct. The small laundry areas were included in the demise under the White Lease. The first and second floor toilets were properly left out of account in determining net internal areas in accordance with the Code of Measuring Practice, and any sums expended on them were included in Schedule E to be paid by the solicitors alone. The basement used by the solicitors was unlettable and the tribunal had found specifically that there was "no fairer (i.e. reasonable taking into account floor areas and other reasonable factors) way of dealing with the issue" than that adopted by Wellington.

79. The First-tier Tribunal had the benefit of inspecting the basement space used by the solicitors, and the remainder of the building. Its view that the there was no fairer way of apportioning responsibility than by leaving the basement out of account is entitled to considerable respect, not least because of its extensive experience of this building. Nonetheless I have come to the conclusion that the appeal should be allowed and the decision set aside and remitted to the First-tier Tribunal for re-determination.

80. I reach that conclusion reluctantly, since it prolongs the dispute and may make little or no difference in practice. I do so for the following reasons.

81. First, the First-tier Tribunal was mistaken as to the scope of its function, and therefore asked itself the wrong question. In my judgment, in the event that a fair apportionment cannot be agreed between the parties, the residential tenants are entitled to a determination from the tribunal of the fair proportions in which the second and third floors should be liable to contribute to the service charges payable under the White Lease.

82. Secondly, the tribunal appears not to have taken into account the fact that the basement was served by the lift, saying specifically "it shares none of the benefits, such as heat, shared parts decoration, lift, … of the rest of the building". It may be that this was simply a slip which made no difference to the tribunal's assessment, but it does seem to be relevant to the issue and has been relied on by the appellants.

83. Thirdly, other basement areas within the building are taken into account in the apportionment exercise, a fact which was not acknowledged (and made not have been appreciated) by the tribunal. Those areas may well be included in the leases of the retail tenants, whereas the areas occupied by the solicitors appear to be held on an informal licence, but whether that is a sufficient reason for a difference of treatment is worthy of consideration which it did not receive in the tribunal's assessment of the fairness of the current apportionments. The basis of the arrangement appears not to have been investigated in much detail in the evidence. The availability of the space is clearly of benefit to the solicitors, saving them the expense and inconvenience of remote storage, and their occupation of the basement may also have benefits to the respondents (if they assume responsibility for any non-domestic rates, for example).

84. Fourthly, there are apparent inconsistencies in the treatment of the common parts on different floors (the toilets, laundry rooms and corridors). Any adjustment to these may make little difference, but there is force in the appellants' complaint that a fair apportionment requires that all of the tenants of the building should be treated in the same way.

85. How the fair apportionment should be carried out is a matter for the First-tier Tribunal to determine, and I say nothing about that other than it should respect the parties' agreement by "taking into account the relevant floor areas within the Building or other reasonable factors".

86. It was apparent at the hearing of the appeal that there is a considerable sense of grievance amongst the residential tenants that they are expected to contribute substantial sums to the upkeep of the building, yet (from their perspective) are regarded as a nuisance by the respondent and its agents and receive very little information. Mr Gater emphasised that it was a lack of proper explanation of the basis of apportionment which prompted the application. As a result of the application a very full explanation has been provided by the respondents, which includes measurements and calculations which should significantly improve the tenants' understanding of how the apportionment has been carried out so far. I very much hope that, with the benefit of that information and in view of the expense and inconvenience which a further hearing before the First-tier Tribunal will involve, the parties will now be able to reach agreement on a basis of apportionment with which all are content.

87. If such an agreement cannot be reached the appellant's should apply to the First-tier Tribunal within 28 days of the date on which this decision is sent to them, for directions for the reconsideration of their applications under s.27A of the 1985 Act.

Martin Rodger QC

Deputy President

17 December 2014