UPPER TRIBUNAL (LANDS CHAMBER)

Neutral Citation Number: [2018] UKUT 32 (LC)
Case No: LRX/93/2017

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LANDLORD AND TENANT – Service Charges – Leaseholder's application for determination of charges due in specified years – quantification of charges – whether liability to pay service charge conditional on certification – leaseholder's liability to pay administration charges – leaseholder's liability for costs of proceedings – sections 20C and 27A, Landlord and Tenant Act 1985 – appeal allowed in part and application remitted to FTT

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

BETWEEN:

URBAN SPLASH WORK LIMITED

Appellant

and -

GARY RIDGWAY
MARY BRIDGET CUNNINGHAM

Respondents

Re: Loft Nine,
Concert Square Apartments,
34 Wood Street,
Liverpool L1

Martin Rodger QC, Deputy Chamber President

Liverpool Civil and Family Justice Centre

29 January 2018

Lawrence McDonald, instructed by JB Leitch Solicitors, for the appellant
Mr Ridgeway, in person, and on behalf of the second respondent

The following cases are referred to in this decision:

British Anzani (Felixstowe) v International Marine Management (U.K.) [1980] Q.B. 137

Clacy and Nunn v Sanchez [2015] UKUT 387 (LC)

Electricity Supply Nominees Ltd v IAF Group Ltd [1993] 2 E.G.L.R. 95

Elysian Fields Management Company v Nixon [2015] UKUT 427 (LC)

Lee-Parker v Izzet [1971] 1 W.L.R. 1688

Pendra Loweth Management Ltd v North [2015] UKUT 91 (LC), [2015] L. & T.R. 30

Rexhaven Ltd v Nurse and Alliance & Leicester Building Society (1996) 28 HLR 241

Star Rider v Inntrepreneur Pub Co. [1998] 1 E.G.L.R. 53

Introduction

1. This is an appeal from a decision of the First-tier Tribunal (Property Chamber) ("the FTT") made on 18 May 2007 in a dispute concerning the service charges payable by the leaseholders of an apartment at Concert Square Apartments, 34 Wood Street, Liverpool L1 ("the Building"). The Building was originally a warehouse but was converted to residential use in the mid-1990s and now comprises a three-storey block of nine loft-style apartments. It adjoins another building in the same ownership, with which it shares a number of services.

2. The appellant is the owner of the freehold interest in the Building and its neighbour. The respondents are long leaseholders of one of the apartments, referred to as Loft Nine, which they have owned since 1994.

3. At the hearing of the appeal the appellant was represented by Lawrence McDonald of counsel, and the first respondent, Mr Ridgway, represented both himself and the second respondent. I am very grateful to them both for their assistance.

4. The proceedings arose out of an application made by the respondents under section 27A, Landlord and Tenant Act 1985. That provision enables the FTT to determine whether a service charge is payable at all and, if it is, to determine the amount which is payable, the person who is liable to make the payment and the date on which the sum is payable. Usually a determination under section 27A will concern service charges payable in the past, but the section also allows the FTT to determine that a sum will become payable in future. A determination about a future liability may be required where the expenditure which the service charge is intended to recoup has not yet been incurred (section 27A(3)) or where a contractual condition which must be met before the service charge becomes payable has not yet been met. In this case the respondents asked the FTT to determine the service charges payable by them for the years 2011 to 2016 as well as the charges which would become payable by them in 2017.

5. The respondents made their application on 25 June 2016, shortly after the appellant had commenced proceedings in the County Court to recover unpaid service charges and other sums. In the broadest outline it was the respondents' case that they had paid all of the sums which had been claimed by the appellant as quarterly service charges but that they had not paid balancing charges, sums claimed on account for major works, and certain other sums which they considered had not been properly explained. This had led them into dispute with the appellant which continued for a period of years.

6. In the course of the dispute the appellant's agents levied a succession of fees, charges and incidental expenses for corresponding about the dispute or pursuing the respondents for the recovery of the disputed sums. The respondents also refused to pay these charges which were then added to the quarterly service charge statements, although strictly they were in the nature of variable administration charges, rather than service charges. The FTT is given jurisdiction to determine the extent to which variable administration charges are recoverable by section 158 and Schedule 11, Commonhold and Leasehold Reform Act 2002.

7. By its decision of 18 May 2017 the FTT determined the sums payable by the respondents in respect of services provided by the appellant for the four years from 1 November 2011 to 31 October 2015. It also determined the amount of the service charge payable on account for the first two quarters of the 2016-17 year. These sums totalled £11,324.08.

8. The FTT did not determine when any of the service charges it had identified had become payable.

9. The FTT also made no determination of the service charges payable in the years ending on 31 October 2010 and 31 October 2011, nor for the year to 31 October 2016. For those years it considered it had insufficient evidence, but it gave the appellant permission to apply for a further ruling when it could provide that evidence.

10. The respondents had already paid £15,978.39 in total for the disputed period and the FTT directed that £3,558.23 which had been appropriated by the appellant to the period ending on 30 November 2010, for which no determination had yet been made, should be reallocated to the later years for which it had been able to reach a conclusion.

11. The FTT also found that the variable administration charges were not payable. Finally, after making a number of criticisms of the appellant, it made an order under section 20C, Landlord and Tenant Act 1985 that none of the costs incurred by the appellant in the proceedings before it were to be added to any service charge payable by the respondents.

12. The appellant was dissatisfied with the FTT's decision and sought permission to appeal on two very general grounds. The first was that the FTT had failed to complete the task required of it by section 27A because it had not determined all of the issues. The second was that the FTT had been wrong to make an order under section 20C. Further details were given of both grounds and the FTT decided to give permission to appeal.

The issues

13. Mr McDonald proposed that the issues should be dealt with under five headings. The first three concerned the FTT's omission to determine the service charges payable for the years ending 31 October 2010, 2011 and 2016. The fourth concerned the refusal of the FTT to permit the recovery of the disputed administration charges added to the service charge account over the years by the appellant's agents. The final issue concerned the FTT's order under section 20C.

14. In the course of the hearing a further issue was identified. The appellant's general complaint that the FTT had not answered the questions posed by section 27A required consideration of the date when the various service charges had become payable. This drew attention to the service charge machinery in the respondents' lease and, in particular, to the question whether their liability was conditional on the provision by the appellant's accountant

of a certificate specifying the sum due in each year. It was common ground that no service charge certificates had been prepared by the accountants for any of the years in dispute until after the commencement of the proceedings in the FTT. Because that issue had not been focussed on before the hearing, I allowed the parties the opportunity to make further submissions on it in writing after the conclusion of the hearing.

The Lease

15. The Lease of Loft Nine was granted on 16 December 1994 for a term of 125 years. The apartment itself is referred to in the lease as "the Premises", the landlord is "the Lessor" and the tenant or leaseholder is "the Lessee." The Lease reserves a ground rent of £125 per annum and obliges the Lessee to pay a "Service Rent" defined in clause 2(1) and described fully in the third and fifth schedules, and a "Sinking Fund Contribution" explained in the sixth schedule.

16. In summary the Service Rent is to be a fair proportion of the cost of providing certain services specified in the third schedule together with a reasonable provision for anticipated capital expenditure in future. It also includes the fees of the Lessor's managing agents for the collection of rents and for the general management of the Building. The services themselves include "generally managing and administering the Building", "employing and paying a firm of managing agents" and "(in so far as the lessor shall reasonably think fit) enforcing … the observance of the covenants on the part of any individual lessee" (paragraph 6, third schedule).

17. Provisions for payment of the Service Rent are found in clauses 3 and 4(1) of the Lease. By clause 3, as a condition of the demise, the Lessee is to pay the Service Rent "at the times and in the manner stipulated in the Fifth Schedule." By clause 4(1) the Lessee covenants to pay the Rent, the Service Rent and the Sinking Fund Contribution "in full without any deduction counterclaim or set off against any payments due to the Lessor hereunder at the times and in the manner aforesaid."

18. Paragraph 1 of the fifth schedule stipulates that the Service Rent "shall be an amount determined as hereinafter provided and payable at the times and in the manner hereinafter mentioned."

19. The first step in ascertaining the Service Rent (as required by paragraph 2 of the fifth schedule) is for the Lessor's Surveyor to provide an estimate of the amount required from the Lessee to cover the Lessee's liability for the Service Rent for the following year. The estimate is to be based on the actual cost and expenses of providing the Services for the previous period together with a provision for any expected increase. The Lessor's Surveyor is required to serve written notice of the estimate on the Lessee.

20. By paragraph 3 of the fifth schedule the Lessee is required to pay quarterly instalments in advance and on account of the Service Rent for the Service Rent Financial Year then current on the first of March, June, September and December each year. The Service Rent Financial Year runs from 1 November each year.

21. Paragraph 4 of the fifth schedule then provides that:

> "The Service Rent in respect of each Service Rent Financial Year shall be ascertained and certified by a certificate (the "Certificate") signed by an independent qualified accountant as soon after the end of the Service Rent Financial Year as may be practicable which Certificate shall give credit for any payments received … and shall give credit for any advance payments made in respect of the Service Rent Financial Year to which it relates and a copy of which shall be supplied by the Lessor's Surveyor to the Lessee."

22. The content and effect of the Certificate are further prescribed by paragraph 5:

> "The Certificate shall contain a summary of the costs of the provision of the Services during the Service Rent Financial Year together with a summary of the relevant details and figures forming the basis of the Service Rent and the Certificate shall be conclusive evidence of the matters it purports to certify and if the Certificate shall show that the advance payments made by the Lessee are less or greater than the Service Rent then the Lessee shall forthwith pay or be credited with as the case may be the shortfall or surplus therein disclosed and in default of payment of any shortfall the same shall be recoverable as rent in arrears."

23. Separate provision is made in the sixth schedule for the Sinking Fund Contribution, defined in clause 2(1) as "the Lessee's contribution by way of provision towards major items of expenditure in respect of the Building." On each occasion when the Lease is assigned, the Lessee must pay 0.25% of the sale price of the Lease for each year it has been owned by the Lessee, subject to a minimum contribution of 1% of that price.

24. The Lease also includes two covenants which relate to other costs and expenses incurred by the Lessor. The first of these is clause 4(5), by which the Lessee covenants to pay "all proper and reasonable costs (including legal costs and fees payable to a surveyor)" incurred by the Lessor in contemplation of any proceedings under section 146 of the Law of Property Act 1925. The second is an indemnity covenant at clause 4(15), by which the Lessee covenants:

> "To keep the Lessor indemnified from and against all loss damage actions proceedings claims demands costs and expenses of whatsoever nature and whether in respect of any injury to or the death of any person or damage to any person moveable or immoveable or otherwise howsoever arising directly or indirectly from the repair or state of repair or condition of the Premises or from any breach of covenant on the part of the Lessee herein contained or from the use of the Premises or out of any works carried out at any time during the Term to the Premises otherwise than by the Lessor or out of anything now or during the Term attached to or projecting from the Premises otherwise than by the Lessor or as a result of any act or neglect or default by the Lessee or by the Lessee's respective servants or agents or by any persons in the Premises with the actual or implied authority of any of them."

25. The Lessor's covenants include a covenant to provide the services (clause 5(2)), a covenant that the remainder of the Building would be let on covenants similar to those in the Lease itself (clause 5(3)) and a covenant that at the request and expense of the Lessee the Lessor would enforce the covenants entered into by the lessees of other parts of the Building (clause 5(4)).

The proceedings

26. On 21 June 2016 the appellant commenced proceedings against the respondents in the County Court to recover arrears of service charges and other sums totalling £8,702.24. In response, having acknowledged service, the respondents issued their application in the FTT seeking a determination of the sums payable from 2010 to 2016 and on account for 2017. In due course the County Court proceedings were transferred to the FTT.

27. On 20 September 2016 the FTT directed the respondents to itemise any expenditure they alleged to be unreasonable, and required the appellant to provide the service charge certificates referred to in the fifth schedule to the Lease. At paragraph 17 of its subsequent decision the FTT found that the appellant had completely overlooked the certification process and that all of the certificates on which it relied had been signed on 8 December 2016, in response to the FTT's direction.

28. In response to the FTT's direction the respondents provided a lengthy statement of case detailing their complaints, which they subsequently refined and presented in the form of a schedule. The schedule referred to a statement of account supplied by the appellant's managing agents, RMG, showing an outstanding balance of £12,768.54, and in it the respondents itemised the charges in each year from 2011 to 2016 which they disputed.

Issue 1: service charges for 2010

29. In its decision the FTT treated the years 2010 and 2011 together. 2010 was the last year in which the Building had been managed on the appellant's behalf by managing agents named Trinity, from whom RMG took over responsibility in November 2010. The Service Rent Financial Year to 31 October 2011 was therefore the first year of RMG's management.

30. The opening item on each of RMG's statements of account for each of the years in dispute was a sum of £3,894.50 described as "B/FWD balance from Trinity to 30.09.2011." It first featured on the annual service charge statement delivered to the respondents in the year ending 31 October 2011, which was the first year they challenged in their section 27A application. The respondents have refused to pay it ever since.

31. Little or no information was able to be provided by the appellant about the service charges claimed in respect of the year ending 31 October 2010. The appellant had changed both its managing agents and its accountants and as a result no accounts and no certificate had been prepared for the 2010 Service Rent Financial Year. All that was available to the FTT was a

running statement of account prepared by Trinity showing an aggregate amount due from the respondents of £3,894.50 for the period from October 2002 to 1 September 2011.

32. In their statement of case to the FTT the respondents explained that they had raised a series of issues with Trinity concerning the service charges and sinking fund contributions, as well as the quality of service and the liability for repairs to a flat roof over their apartment. They produced a spreadsheet based on the Trinity statement of account showing that service charges totalling £15,574.60 had been claimed by Trinity since 2008, of which the respondents had paid £13,597.83 and disputed the balance of £1,976.77.

33. The respondents questioned legal and "referral" fees amounting to £709 and unexplained charges levied by Trinity under the heading "other DR charges" which totalled £726.53. They also suggested that in the transition from Trinity to RMG ground rent (which appeared on the running account) had been double counted. The respondents demonstrated that the £3,894 included in the RMG account as the balance brought forward in 2011 could not be reconciled with the charges and payments claimed and received during the period of Trinity's management and that there was an unexplained shortfall of £586.50.

34. The respondents also claimed to have spent £946.31 in June 2007 in themselves repairing the flat roof over their apartment which Trinity had failed to remedy. They sought reimbursement of that sum as a credit against their service charge liability.

35. Having considered the Trinity running statement of account the FTT concluded at paragraph 42 of its decision that it had insufficient evidence to decide that the amount due for the period prior to 1 November 2011 was £3,984.50, or indeed any amount. It did not say that no sum was payable for that period, and it granted the appellant permission to produce additional evidence to enable the FTT to come to a decision in respect of it.

36. In his grounds of appeal Mr McDonald, for the appellant originally suggested that the FTT had had no jurisdiction to deal with the period to 31 October 2010 at all, as that year not been included in the respondents' application under section 27A. That is not a good point as it was quite clear from the application that the respondents sought a determination whether they were liable to pay the sum brought forward into 2011 from the period of Trinity's management.

37. At the hearing of the appeal Mr McDonald took a realistic approach to the prospect of the appellant ever being in a position to provide further evidence concerning the expenditure incurred in 2010. No more evidence would become available. He submitted that the FTT should have made a decision on the basis of the material before it and he took three points in support of the appellant's entitlement to the sum of £3,894.50 which had been carried forward as an outstanding balance when RGM took over from Trinity.

38. Mr McDonald's first point was that the running account prepared by Trinity was the best evidence of the respondents' share of the costs which had been incurred in providing services

during the period of their management. He was unable to explain what the "other DR charges" totalling £726.53 might refer to, but in relation to the balance of the charge he suggested that the question was whether the respondents had shown any defence to it.

39. Secondly, Mr McDonald submitted that where a leaseholder is required to pay rent and service charges "in full without any deduction counterclaim or set off against any payments due to the Lessor hereunder" as clause 4(1) required in this case, the leaseholder has no right to deduct the cost of works carried out to remedy an alleged breach of covenant by the landlord before paying the service charge.

40. Finally, Mr McDonald submitted that the appellant was entitled under clause 4(15) (the indemnity covenant) to recover the additional fees of its managing agents in dealing with non-payment of service charges. These included the sums shown as "referral fees" which were assumed to relate to the cost of referring a case to solicitors. Since the respondents had not been entitled to deduct the cost of roof repairs it was apparent that there had been arrears, and these justified the appellant in incurring administration charges in seeking to recover them.

41. I accept Mr McDonald's second submission, but not his first or third.

42. As to the first point, where a tenant has, from the outset, questioned the basis of a charge and seeks a determination from the FTT of the liability to pay it, as the respondents have done in this case regarding the sum of £726.53 identified only as "other DR charges", a burden falls on the landlord of explaining what that charge is for. It is not enough for the landlord to assert simply that the appearance of the sum on an account prepared by its managing agents is sufficient to establish an entitlement to it. Similarly, where the tenant shows that a discrepancy exists between the sum claimed and the sum suggested by the landlord's running account (totalling £586.50 in this case) it is for the landlord to provide an explanation.

43. As to Mr McDonald's second submission, there is credible evidence (which Mr McDonald accepted the appellant was not in a position to challenge) that the respondents incurred the cost of repairing the roof over their apartment after repeated requests to Trinity had gone unheeded. The entitlement of a tenant to recoup expenditure on repairs is described in Woodfall: Landlord and Tenant at paragraph 7.111 as follows:

> "Where the tenant carries out work of repair which falls within the express or implied obligations of his landlord, he has an ancient common law right to recoup his expenditure out of future rents payable by him to the landlord. The right arises only in relation to a sum certain which the tenant has paid, and in circumstances in which the landlord cannot really dispute its amount."

The leading modern authorities are *Lee-Parker v Izzet* [1971] 1 W.L.R. 1688 and *British Anzani (Felixstowe) v International Marine Management (U.K.)* [1980] Q.B. 137. The right provides an equitable set off against the tenant's liability to pay rent (or service charges).

44. The common law right of recoupment can be excluded by clear express words. A covenant to pay the rent "without any deduction or set off whatsoever" has been held to exclude the right of set-off in at least two reported cases: *Electricity Supply Nominees Ltd v IAF Group Ltd* [1993] 2 E.G.L.R. 95 and *Star Rider v Inntrepreneur Pub Co.* [1998] 1 E.G.L.R. 53.

45. In principle therefore the respondents' common law right to deduct the cost they incurred in repairing the roof before paying the service charge is defeated by the language of clause 4(1) which requires them to pay "without any deduction counterclaim or set off." That does not mean that the respondents are not entitled to recover the costs they incurred from the appellant, only that they may not do so by set off. It also means that the issue of the respondents' entitlement to recoup the costs incurred in repairing the roof is one for the County Court to consider; it is not for the FTT, which is limited to determining the amount of the service charge (which, in the absence of a right of set off, is not reduced by the respondents' expenditure). If the parties are unable to reach agreement on the issue the value of the set off would need to be determined in the County Court proceedings.

46. I do not accept Mr McDonald's third submission. The indemnity covenant in clause 4(15) of the Lease is intended to cover claims made against the landlord by third parties. It is at the very least questionable whether it covers costs incurred by the landlord by its own voluntary decision to take legal action against the tenant who gives the indemnity to recover a sum unconnected to the indemnity. In any event, such covenants are liable to abuse. The managing agent has no right of its own to levy a charge, but only to recover sums which the tenant is liable to pay to the landlord. It is therefore necessary where a managing agent adds such a charge to the tenant's account that it be demonstrated that an additional cost has actually been incurred by the landlord and, if so, that the amount of the charge is reasonable (as required by paragraph 2 of Schedule 11 to the Commonhold and Leasehold Reform Act 2002).

47. In this case there was no evidence that Trinity was entitled to charge, or did charge, the appellant an additional sum for corresponding with tenants who were in default. The third schedule to the Lease, which lists the expenditure to be recovered through the service charge, suggest that such correspondence was intended to be a collective expense. The fees of managing agents for the collection of rents and for the general management of the Building, as well as "enforcing … the observance of the covenants on the part of any individual lessee" were amongst the expenses to be recouped through the service charge. That does not exclude the possibility that the managing agent was entitled to charge the appellant an additional fee for extra work, but such an entitlement cannot be assumed and would have to be deminstrated. Without knowing the terms of Trinity's contract with the appellant, and without evidence that additional costs were in fact incurred, there was no basis on which the FTT could assume that the administration charges were recoverable.

48. In my judgment, therefore, the FTT was right not to make a positive finding that service charges and administration charges totalling £3,894.50 had been incurred and remained outstanding from the period of Trinity's management. The total was uncertified and included at least £2,000 which was unexplained or for which there was no evidence of entitlement at all. The FTT was generous in allowing the appellant the opportunity to restore the application for

further consideration if further evidence became available but, as Mr McDonald acknowledged, there is now no prospect of further evidence becoming available. In those circumstances the proper determination is that nothing has been shown to remain payable in service charges or administration charges for the year ending 31 October 2010 and the disputed sum of £3,894.50 should be removed from the respondents' statement of account.

Issue 2: service charges for 2011

49. In paragraph 42 of its decision the FTT dealt with 2010 and 2011 together, and ruled that it had insufficient evidence on which to make a determination "for the period prior to 1 November 2011". In fact, as Mr McDonald pointed out, the FTT had an accountant's certificate and service charge accounts for the year to 31 October 2011. The certificate had been signed on 8 December 2016, at the same time as the remainder of the certificates referred to in the proceedings. It showed that the total service charge payable by the respondents for the year to 31 October 2011 was £3,281.37. This was quite separate from the sum £3,894.50 described as "B/FWD balance from Trinity to 30.09.2011" which appeared on each annual statement prepared by RMG.

50. The FTT did not overlook the certificate for 2011, which it referred to in paragraph 27 of its decision. It is not clear why it did not make a finding that the sum payable in respect of that year was £3,281.37. It may have considered that in order to determine the sum payable in 2011 it was first necessary to know the sum carried forward from 2010 but it did not say so in terms, and I do not consider that it would have been right to take that view.

51. In responding to the appeal Mr Ridgway suggested that, generally, the FTT had not got to grips with the issues he had raised, and had been distracted by its efforts to understand how the charges for the two blocks related to each other, on which it had received very little assistance from the appellant. Apart from these general criticisms he did not challenge any of the sums included in the 2011 certificate. The only specific points he had identified in his own schedule were the Trinity charge carried forward from 2010 (which was not included in the 2011 certificate, although it was part of the total demanded from 2011 onwards) and the appellant's failure to collect the Sinking Fund Contribution from outgoing leaseholders in that year. Neither of these undermined the appellant's entitlement to recover the certified sum of £3,281.37 in respect of routine service charge items.

52. I therefore allow the appeal in relation to the year to 31 October 2011, for which a service charge of £3,281.37 was payable. I will return to the question of when that sum became payable when I consider the issue of certification.

Issue 3: service charges for 2016

53. The FTT made no determination in respect of the claim for £7,787.35 for the year to 31 October 2016 because although it was provided with the annual accounts for that year they were not accompanied by a certificate. In paragraph 43 of its decision the FTT directed the appellant to provide a certificate within 3 months.

54. In fact, the material available at the time of the FTT hearing included a certificate for the year to 31 October 2016 signed by the appellant's accountant and dated 1 March 2017, showing the respondents' contribution as £7,787.35. Mr McDonald explained that the certificate was either not in the bundle or had not been pointed out, but I infer from paragraph 28 of the decision that the former is more likely.

55. Mr McDonald submitted that, notwithstanding the apparent absence of a certificate, the FTT should have determined the challenges which the respondents had raised to the 2016 service charge. Only two were specific to that year.

56. The first of these was a net balancing charge from the previous year of £438.35 which was included in the respondents' statement of account for 2016. In his statement of case to the FTT Mr Ridgway had said that "it has never been made clear why these deficits occur." Nevertheless, it is clear that the Lease provides for a balancing sum to be payable when the sum paid on account proves to be less than the sum certified as having been spent. That is the effect of paragraph 5 of the fifth schedule which requires that "… if the Certificate shall show that the advance payments made by the Lessee are less or greater than the Service Rent then the Lessee shall forthwith pay or be credited with as the case may be the shortfall or surplus therein disclosed and in default of payment of any shortfall the same shall be recoverable as rent in arrears."

57. The net balancing sum from 2015 was added to the respondents' service charge statement with effect from 28 April 2016, but that did not make it part of the 2016 service charge, and it could not be relied on as a ground of challenge to the charges for 2016. The FTT did not refer to it at all in its decision.

58. The other ground on which the respondents challenged the sums claimed in respect of 2016 was the inclusion of legal and administrative charges totalling £1,261 (although the total sum added to the respondents' 2016 statement of account for administration fees, legal fees, court fees, a reminder fee and a land registry search would appear to have been £1,329). These were not sums included in the 2016 service charge payable by all leaseholders, but were variable administration charges levied against the respondents alone. They were therefore not relevant to quantification of service charges. I will refer to them later when I consider the issue of administration charges generally.

59. Mr McDonald submitted that the FTT ought either to have awarded the sum claimed, despite there being no certificate, because there was no substantial challenge to it, or ought at least to have determined that on account service charges of £470.20 per quarter totalling £1,880.80 had been payable during the year to 31 October 2016. Since the FTT appears not to have been asked to make any such determination, but was asked instead to determine the full annual sum without a certificate having been produced, it cannot be criticised for not taking the course now suggested.

60. On the evidence before it the FTT was justified in dealing with the matter in the way it did. If the parties are now able to agree that the sum payable for 2016 was £7,787.35 they should do so, but I do not consider it would be safe for me to make such a ruling. The 2016 certificate was not available to the FTT and I assume that means it was not available to the respondents. Moreover, the FTT did not deal with at least two general issues which Mr Ridgway had identified in his narrative statement of case as challenges to the 2016 service charge, though only one was included in the schedule he subsequently prepared.

61. The first of these outstanding issues related to charges for water, which Mr Ridgway said were unsubstantiated, and divided between the residential and commercial parts of the building on a basis which had never been explained. The second concerned the treatment of VAT. Mr Ridgway submitted that service charges relating to the upkeep of the residential parts of the building should be exempt, but that VAT was being charged as part of the service charge. No reference was made to these issues by the FTT. The respondents have not appealed against the FTT's determinations in respect of the years it did rule on the basis that their case on these points was not fully considered, but that cannot be taken as an abandonment of the points for years which have not yet been resolved.

62. In my judgment the better course is therefore to remit the issue of the service charge for the year to 31 October 2016 to the FTT for consideration. Unless within one month of the date of this decision the parties reach agreement on the 2016 service charge, they shall each apply to the FTT for it to give directions for their determination.

Issue 4: Certification

63. At paragraph 38 of its decision the FTT said that it agreed with the submission made on behalf of the appellant that the provision of a certificate was not a condition precedent to the respondents' liability to pay the service charge. It referred to the decision of this Tribunal in *Clacy and Nunn v Sanchez* [2015] UKUT 0387 (LC) and said that the certification arrangements in the Lease were "a mere machinery for the ascertainment of the service charge".

64. The respondents have not raised any issue in the proceedings concerning the absence of certificates, none of which had come into existence until 8 December 2016. The function of the certificates is nevertheless relevant to the questions posed by section 27A of the 1985 Act, which the appellant says the FTT ought to have answered. In particular the FTT did not say when the various sums it found to be due as service charges had become payable.

65. In his oral submissions Mr McDonald suggested that the requirement for certification was satisfied by the form in which annual accounts had been prepared by the appellant's accountants each year. In the alternative, as the FTT had found, the provision of a certificate was not a condition of the respondents' liability to pay the service charges. He developed these submissions in further written material provided after the hearing.

66. The annual accounts produced each year included a statement signed by the appellant's accountants that in their opinion the service charge statement was a fair summary complying with the requirements of section 21(5), Landlord and Tenant Act 1985, and was supported by accounts, receipts and other documents which had been produced to them. The accountants themselves were an independent firm.

67. Mr McDonald submitted that as a matter of substance the annual accounts fulfilled the purpose of the certificate required by paragraphs 4 and 5 of the fifth schedule to the Lease. It provided a summary of the relevant details and figures forming the basis of the Service Rent and the costs incurred. It did not ascertain the amount of the Service Rent for any individual apartment but that function was performed by the managing agents, and could be verified by leaseholders who would be aware of the apportionments assessed by the appellant's surveyor.

68. Mr McDonald also pointed out that the respondents themselves had never suggested that they did not understand the demands made of them and had not raised the issue of certification in their statement of case. The first of those points is not consistent with the respondents' case that they have made extensive and unsuccessful efforts to obtain clarification of items included in the service charge demands. While the second point may be correct it overlooks the fact that this is the appellant's appeal and it is they who complain that the FTT failed to say in clear terms when the various service charges had become due. The Tribunal's interest in the significance of the certificates arises out of the appellant's complaint, and not out of the respondents' case.

69. I do not accept Mr McDonald's first submission. The annual accounts clearly do not contain the information required by paragraphs 4 and 5 of the fifth schedule to the Lease. They do not provide or certify the Service Rent itself, nor do they give credit for sums paid in advance by any individual leaseholder. It is impossible to tell from the accounts how much the respondents or any of their neighbours is required to pay.

70. Mr McDonald's alternative submission was that, although the certificates required by the fifth schedule had not been provided for the years 2011 to 2015 until December 2016, that did not mean that the Service Rent was not due; this was because the certificate was not a condition precedent to a leaseholder's liability to pay the Service Rent.

71. Mr McDonald sought to make good this alternative submission by referring to a number of recent decisions of this Tribunal which were said to support the proposition that the provision of certified accounts will not generally be a condition precedent to liability to pay service charges.

72. The first of these authorities was *Pendra Loweth Management Ltd v North* [2015] UKUT 91 (LC). That appeal was concerned with estimated service charges payable in advance to the management company on account of a final service charge. The final service charge was to be a predetermined proportion of the company's total expenditure for the year which was to be verified by audited accounts certified by an accountant. To save what it considered to be

unnecessary expense, the management company had failed to have the accounts audited at all, and had never sought to balance the estimated sums it collected against its actual expenditure. The FTT held that as a result the tenants were not obliged to pay the estimated service charges. This Tribunal decided that, on a true interpretation of the standard form of lease, the preparation and certification of the annual accounts was not a condition of the tenants' liability to pay the estimated service charge.

73. The second case relied on was *Elysian Fields Management Company v Nixon* [2015] UKUT 427 (LC) which again concerned estimated service charges payable on account of the tenant's final liability. The tenant covenanted to pay the estimated charge by quarterly instalments and to pay on demand any shortfall between those quarterly contributions and the tenant's agreed proportion of the landlord's total expenditure for the year which was to be certified by an accountant. Once again (reversing the FTT) this Tribunal held that as a matter of interpretation of the lease in that case the tenant's obligation to pay the quarterly instalments of the estimated service charge was not conditional on the preparation of certificates showing actual expenditure in any previous year.

74. Finally Mr McDonald referred to *Clacy and Nunn v Sanchez* [2015] UKUT 0387 (LC). After reviewing a large number of cases, in some of which it had been determined that liability to pay a service charge was conditional on the provision of a certificate, while in others the contrary view was taken, the Tribunal ruled that, on the terms of the lease in that appeal, the tenant was liable to pay the service charge despite the certificates not having been provided. That decision was reached because the provision for certification was described in the lease as being "without prejudice" to the primary obligation to pay the service charge on written demand, and because copies of the certificates were only to be supplied by the management company to the tenant on written request. These features indicated to the Tribunal that the certificates were not critical to the tenant's liability to pay, but were simply "machinery."

75. None of the authorities relied on by Mr McDonald establishes any principle of general application. The sole statement of principle on which he relies was from *Emmet & Farrand on Title* at paragraph 26.596 which cited *Clacy* and *Elysian Fields* for the proposition that "the provision of certified accounts will not generally be a condition precedent to liability to pay service charges." By contrast the general statement of principle recorded in *Woodfall on Landlord and Tenant* at paragraph 7.180 is to the opposite effect:

> "Where a lease provides for the amount payable to be certified by the landlord's surveyor or accountant, the issue of a valid certificate will usually be a condition precedent to the tenant's liability to pay."

76. I do not agree that the cases referred to in *Emmet & Farrand on Title* establish the suggested principle for which they are cited. On the contrary, each of those decisions turns on the particular language used in the lease under consideration. The review of earlier decisions in *Clacy* demonstrates that different leases adopt different approaches.

77. It may well be the case that, ordinarily, non-compliance with a certification regime will not prevent a landlord from recovering service charges payable *on account* (as in both *Pendra Loweth* and *Elysian Fields*) but, if so, that is because payments on account are likely to be set by reference to an estimate of future expenditure, rather than by the definitive certification of past expenditure. Even on account charges may require certification before they become payable (as in *Rexhaven Ltd v Nurse and Alliance & Leicester Building Society* (1996) 28 HLR 241). In every case the function and significance of the certificate will depend on the terms of the agreement.

78. In this case the terms of the Lease are clear. The Service Rent is payable "at the times and in the manner stipulated in the Fifth Schedule." Paragraph 4 of the fifth schedule provides that the Service Rent is to be "ascertained and certified by a certificate … signed by an independent qualified accountant." The Service Rent is not a sum which can be identified by the appellant or its managing agent acting unilaterally. That is the function of the certificate.

79. Other than for the quarterly advance payments, the certificate also performs the important function of identifying the amount to be paid, and the time of payment, as paragraph 5 of the fifth schedule makes clear:

> " … if the Certificate shall show that the advance payments made by the Lessee are less or greater than the Service Rent then the Lessee shall forthwith pay or be credited with as the case may be the shortfall or surplus therein disclosed and in default of payment of any shortfall the same shall be recoverable as rent in arrears."

The lessee's obligation to pay any shortfall between the quarterly advance contributions and the total Service Rent depends on the certificate. Until the certificate is provided it cannot be known with the necessary authority whether any additional sum is payable at all. Once the certificate is provided the obligation to pay any shortfall arises "forthwith." Since the Lessee will not know how much to pay until a copy of the certificate is served (as required by paragraph 4), "forthwith" must mean as soon as the certificate is served (and not as soon as it is signed by the independent accountant).

80. In contrast, however, the Lessee's obligation to make the quarterly advance payments themselves is not conditional on the certificate; it arises independently of the certification process as a result of the service on the lessee of written notice of the estimate made by the Lessor's Surveyor, as provided by paragraphs 2 and 3 of the fifth schedule.

81. The FTT was therefore wrong to accept Mr McDonald's submission that the respondents' obligation to pay the annual balancing charges did not depend on the certificates.

82. The FTT did not consider the sufficiency of the certificates relied on by the appellant. None of those which I have seen includes a statement of the sums already paid by the respondents in the year in question. Instead the certificates record only the respondents' share of the appellant's total expenditure, with lines to record "on account charges paid" entered as

£0.00. In short the certificates relied on do not comply with paragraph 5 of the fifth schedule and, as a result, none of the balancing charges have yet become due from the respondents.

83. The quarterly charges payable on account in each year are unaffected by this conclusion. The respondents say that they paid those charges as they fell due, and the FTT accepted that the respondents had paid £15,978.39, although it made no specific finding concerning the period in which those payments were made. It should be possible, without too much difficulty, for the independent accountant to certify the sums paid by the respondents on account and to calculate the net position for each year. Any net amount payable will become due only on the service of compliant certificates.

84. If the parties are unable to agree the amounts, if any, which are due once compliant certificates have been provided, they should restore the application to the FTT for it to make the necessary determination.

Issue 5: Administration charges

85. A substantial grievance underlying the respondents' application to the FTT for a determination of their service charge liability was the practice of the appellant's agents in adding fees and charges to the respondents' statement of account whenever it wrote requiring payment of disputed sums.

86. I have already dealt with the administration charges levied by Trinity, the appellant's original managing agents. There was no evidence that the appellant was obliged to pay Trinity more for corresponding with leaseholders over unpaid service charges, nor whether that was part of the service for which its management fee was payable. In the absence of such evidence no entitlement to the administration charges carried forward from the period before 31 October 2010 has been made out.

87. The charges added to the respondents' account under the management of RMG were said by the respondents to have included reminder fees of £83.00, fees for Land Registry searches of £126.00, legal fees of £1536.00, court fees of £455.00 and administration charges of £384.00. All of these charges were potentially variable administration charges within Schedule 11 to the Commonhold and Leasehold Reform Act 2002, rather than service charges, but the FTT nevertheless had jurisdiction to determine whether they were payable.

88. The FTT dealt with the subject of the administration charges added by RMG in paragraphs 47-50 of its decision. It did not consider the disputed charges individually. Instead it noted that they were claimed under clause 4(15) of the Lease but that no signed copy of a contract between the appellant and its managing agents RMG had been produced. It transpired on investigation that the contract provided to RMG by the appellant's solicitors had never been signed, and this led the FTT to conclude that:

> "In the absence of unequivocal evidence of the claimant being required to indemnify RMG under the agreement, and therefore any losses which it might suffer under clause 4(15), the Tribunal concluded that the claimant had not suffered any lose for which it could claim indemnity under the Lease."

89. For the appellant Mr McDonald submitted that the FTT had applied too stringent a requirement of proof and had been wrong to find that "unequivocal evidence" was necessary before it could be satisfied that the appellant had incurred additional charges. I accept that submission.

90. The evidence established that RMG had acted as the appellant's managing agent since 2011 and unsigned copies of a standard form of management contract between RMG and the appellant were supplied. The earliest of these ran from 19 August 2011 to 18 August 2012 and provided for payment of a fee of £2,520 plus VAT by quarterly instalments. Three further contracts in the same form (with higher fees each year) covered the period to 31 October 2015. A slightly different form of contract was produced for the following two years.

91. There seems no reason to doubt that RMG provided its services to the appellant on the terms of these agreements. The annual accounts showed that management fees were being incurred. The absence of either party's signature from the documents did not make it more likely that RMG provided its services on different terms.

92. The FTT ought therefore to have considered whether the charges added to the respondents' account were justified, having regard to the charging arrangements under the unsigned management contracts.

93. The contracts covering the period from August 2011 to October 2015 entitled RMG to be paid its management fee, and from time to time to invoice the appellant "in respect of costs and expenses incurred by the managing agent in performing its duties under the Agreement" (clause 4.2). The managing agent's duties included rent and service charge collection, and by clause 11.2 it was to use its reasonable endeavours to collect all arrears of ground rent, service charges and other amounts owed to the appellant by the lessees. Where necessary, and with the appellant's consent, the agents was to instruct solicitors to institute proceedings. The appellant agreed to indemnify RMG against costs and expenses incurred in performing its duties under clause 11.2.

94. The two later contracts stipulated that "using best endeavours to collect current and on-going routine service charge arrears but not action requiring legal work or tribunals" was part of the service covered by the management fee.

95. It therefore appears that RMG was not entitled to charge the appellant additional fees in respect of its own efforts to collect rent and service charges. It was entitled to be indemnified if it incurred a cost or expense in performing its obligations, including any costs it incurred in instructing solicitors. Provisionally therefore it looks at least arguable that the reminder fees of

£83.00 and administration charges of £384.00, both of which sound like charges levied by RMG itself, were sums which the appellant was not liable to pay to RMG, or at least they would require a proper explanation before it could be concluded that they were.

96. Before it could be determined whether the third party costs, in the form of Land Registry fees of £126.00, legal fees of £1536.00, court fees of £455.00 were recoverable it would need to be established that the costs had been incurred and that the amount of the charges were reasonable, as required by paragraph 2 of Schedule 11 to the 2002 Act (in future if such costs are incurred in respect of proceedings commenced after 6 April 2017 the County Court or tribunal will have a wider jurisdiction under paragraph 5A of Schedule 11 to reduce or extinguish a tenant's contractual liability if it considers it just and equitable to do so).

97. If it transpires that costs were incurred in pursuing the respondents for service charges which they were not yet liable to pay, because the appellant had failed to have the amount of the Service Rent certified as required by the fifth schedule, so that proceedings in respect of which the legal and court fees were incurred were premature, any charge is likely to have been unreasonable.

98. The FTT was wrong to refuse the claim for administration charges for the reasons it gave. Before it can be determined whether any of the administration charges were properly payable, however, it will first be necessary to answer the questions indicated above. It will only be possible to do that once it is known whether the respondents were ever in arrears, having regard to the appellant's failure to procure the certification of the Service Rent, and the quarterly payments made by the respondents.

99. The issue of the respondents' liability to pay the disputed administration charges levied by RMG must therefore be remitted to the FTT for further consideration.

Issue 6: The order under section 20C, Landlord and Tenant Act 1985

100. The respondents asked the FTT to make an order under section 20C providing them with protection against any liability to contribute through the service charge to costs incurred by the appellant in the proceedings.

101. The FTT considered that it was just and equitable to make an order preventing the appellant from recovering any part of the costs of the proceedings through any service charge payable by the respondents. Its reasoning was contained in paragraph 53 of its decision:

> "In deciding the application, the Tribunal had regard to the claimant's conduct in this matter. They noted that the claimant had failed to provide accountant's certificates until required to do so by the Tribunal. They had also indirectly caused the respondents loss by failing to enforce the requirement to contribute the sinking fund on a change of ownership. They had failed to conclude a written management agreement with RMG thus putting the development in danger of RMG resigning as managing agents and

> leaving the development with no management. The actions of the claimant were tantamount to it washing its hands of the development to the detriment of the owners. The Tribunal considered these matters were evidence of mis-management by the claimants. No criticism is made of RMG. If these matters had been attended to timorously, then possibly the application could have been avoided."

102. Mr McDonald criticised the FTT's reasoning and suggested that, even assuming its decisions on other issues had been correct, the order had been too harsh on the appellant. If the Tribunal decided the issues in the appeal in the appellant's favour the case for refusing an order would (he submitted) be even stronger.

103. In my judgment the FTT was entitled to make the order it did substantially for the reasons it gave, although I would not myself attribute weight to the failure to conclude a written management agreement with RMG. Because I have set aside parts of its substantive decision it is necessary that I reconsider whether the order is still appropriate, but having done so I am entirely satisfied that it is.

104. I have found that the FTT was wrong in certain of its conclusions, but those have not all been in the appellant's favour. I have substituted a determination excluding the sums carried forward into the 2011 statement of account, which the FTT would have allowed the appellant a further opportunity to establish. I have accepted the appellant's case that the Service Rent for the year to 31 October 2011 will be £3,281.37, but I have found that that sum is not yet payable (to the extent that it has not already been paid by the respondents' quarterly advance payments) because no valid certificates have yet been produced. Similarly, I have found that the balance of the charges for 2012 to 2015, which the FTT identified, are not yet payable for the same reason. The sum payable for 2016 is still to be considered by the FTT, and is not yet payable, and it remains to be seen whether any of the administration charges can be substantiated.

105. This inconclusive state of affairs is profoundly unsatisfactory. Three days of hearings have been devoted to these proceedings by the FTT and by this Tribunal, not to mention the very substantial time and expense committed to preparation by the parties. Responsibility for the state of uncertainty lies very substantially with the appellant, which failed to procure the certificates required by the Lease and failed to provide the evidence required to support its case.

106. In all these circumstances it is just and equitable that the respondents should not be liable to contribute towards the appellant's costs incurred before the FTT.

107. During the hearing it was agreed that the application made to the FTT would be treated as sufficient to cover the proceedings in this Tribunal without the need for the respondents to issue a further formal application. The appellant was given the opportunity while this decision was in draft to make submissions why a different order is appropriate in respect of the appeal. It has chosen not to do so. I therefore direct that no part of the costs incurred by the appellant in connection with this appeal shall be recoverable through any service charge payable by the respondents.

"Exit fees"

108. I should finally mention the issue of the appellant's failure to collect the "exit fees" or Sinking Fund Contributions provided for in the sixth schedule to the Lease, which was raised by the FTT as a reason for making an order under section 20C. The issue had been raised by the respondents as a reason why they should not be required to pay very substantial contributions on account towards the cost of major works.

109. In paragraph 45 of its decision the FTT found that the contribution towards the cost of major works which had been demanded on account was reasonable and payable. It explained that the respondents could nevertheless apply for the determination of the final amount payable once any further consultation had been completed or the works themselves carried out.

110. In relation to the "exit fees", at paragraphs 51 and 52 of its decision the FTT said this:

> "Counsel for the claimant argued that there was no obligation on its part to collect the sinking fund contribution. The Tribunal agreed. There is no obligation to do so. However the failure to collect it is, in the Tribunal's opinion, evidence of mis-management of the development by the claimant. Had it done so, the shortfall in reserve for the management of the development might have been mitigated. Unfortunately this is of no help to the respondents. They produced no evidence of the actual amounts which the claimant failed to recover by enforcing, if it wished to do so, the obligation to pay on the lessees who flats changed hands. The Tribunal made no order on this point."

The FTT appears to have overlooked the fact that it was common ground that no exit fees had been charged before 2014 and that the respondents in their statement of case had produced a schedule in which 18 transfers had been identified as having occurred between 1999 and April 2014 which, by the respondents' calculations based on Land Registry information, ought to have yielded a total contribution of more than £21,000 towards the reserve fund. It is not clear to what further evidence the FTT was referring in paragraph 52 of its decision, nor is it clear why the respondents were not given the opportunity to adduce such evidence in the way that the appellant was given that chance in relation to other issues.

111. It is far from clear to me that the FTT was correct when it said that the appellant was under no obligation to collect the Sinking Fund Contribution, or at least, if it chose not to collect contributions from outgoing leaseholders that it should nevertheless take the sums it had voluntarily foregone into account when determining what contribution it could reasonably expect the continuing leaseholders to make towards the major works. After all, the appellant had covenanted that all of the leases in the Building would be on the same terms, and by clause 5(2) it had covenanted to provide the services in the third schedule which included, at paragraph 6, "(in so far as the Lessor shall reasonably think fit) enforcing or attempting to enforce the observance of the covenants on the part of any individual lessee." A decision by the appellant not to enforce compliance with the Sinking Fund Contribution covenant could therefore only be made on reasonable grounds. Paragraph 2 of the fifth schedule also requires the appellant "as far as it considers practicable [to] equalise the amount from year to year of its

costs and expenses by creating reserve funds and in subsequent years expending such sums as it considers reasonable."

112. The respondents were dissatisfied with the FTT's conclusion but they did not seek permission to cross appeal its decision in relation to the uncollected Sinking Fund Contribution and I therefore express no further view on it. The only question for the FTT in these proceedings was whether a contribution towards the cost of anticipated major works should be reduced to reflect sums which might already have been available to the appellant had it chosen to collect them. As the FTT made clear, however, the sum which the respondents may be required to contribute towards expenditure on the major works in future years will require to be considered on its own merits; if the matter comes back before the FTT to consider a challenge to future demands, it should address the terms of the Lease and the evidence provided by the respondents in greater detail.

Disposal

113. My decision on the issues in the appeal is therefore as follows:

(1) the decision of the FTT leaving open the respondents' liability for charges first claimed by Trinity before 2011 is set aside, and I determine that those charges are not recoverable;

(2) the Service Rent for 2011 was £3,281.37, and the decision of the FTT leaving open that issue is set aside, but the sum which remains payable by the respondents (after taking into account contributions already made) must first be ascertained by the independent accountant's certificate, on the service of which any balance will become payable, and it will then be open to either party to seek a determination by the FTT in these proceedings of the amount so payable;

(3) the Service Rents for 2012 to 2015 are as determined by the FTT, but whether any sums remain payable by the respondents (after taking into account contributions already made) must first be ascertained by the independent accountant's certificate, on the service of which any balance will become payable, and it will then be open to either party to seek a determination by the FTT in these proceedings of the amounts so payable;

(4) the amount of the Service Rent for 2016 is remitted to the FTT for further consideration if it cannot be agreed within one month of the date of this decision;

(5) the question whether any administration charges are payable by the respondents is remitted to the FTT for further consideration if it cannot be agreed within one month of the date of this decision;

(6) no part of the costs incurred by the appellant in the proceedings before the FTT may form part of any service charge payable by the respondents;

(7) no part of the costs incurred by the appellant in the appeal to this Tribunal may form part of any service charge payable by the respondents.

Both parties are directed to write to the FTT by 3 April 2018 to report on the progress made, if any, towards resolving the remaining issues and to invite it to give further directions for their final resolution.

Martin Rodger QC
Deputy Chamber President

1 March 2018