LRX/124/2007
LRX/137/2007

LANDS TRIBUNAL ACT 1949

LANDLORD AND TENANT - Right to manage- RTM company- whether company complied with section 79(5) of the Act- Service charges – Whether on the proper construction of the leases the landlord could require payment to a sinking fund

IN THE MATTER OF TWO APPEALS AGAINST DECISIONS OF THE LEASEHOLD VALUATION TRIBUNAL OF THE LONDON RENT ASSESSMENT PANEL

BETWEEN **SOUTHALL COURT (RESIDENTS) LIMITED, SOUTHALL COURT COMPANY RTM COMPANY AND OTHERS** **Appellants**

and

BUY YOUR FREEHOLD LIMITED, SOUTHALL COURT MANAGEMENT LIMITED AND RS GUYARA **Respondents**

Re: Southall Court, Lady Margaret Road, Southall Middlesex

Before: His Honour Judge Reid QC

Sitting at Procession House, 110 New Bridge Street, London, EC4V 6JL on 22nd July 2008

Peter Ward (Chairman of Southall Court (Residents) Limited) by written representations for Southall Court (Residents) Limited

No other party made representations.

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DECISION

1. These are two consolidated appeals arising from determinations of the LVT on respectively 15 and 24 July 2007. By the first decision the LVT determined, inter alia, that Southall Court RTM Company Limited (“RTM”) was a company which complied with section 79(5) of the Commonhold and Leasehold Reform Act 2002 (“the 2002 Act”) and so entitled to make a claim under section 79 for the right to manage the property known as Southall Court (“the block”) and was entitled to acquire the right to manage. By the second decision the LVT determined, inter alia, that the long leases of the flats in Southall Court did not entitle the landlord Southall Court (Residents) Limited (“Residents”) to “raise the service charges required for [certain major works or repair and maintenance] by means of demands from each leaseholder for an appropriate contribution to a sinking fund, such sums to be payable on demand” and that it could not therefore grant Residents the order it wanted as to the manner in which certain prospective roof repairs should be paid for.

2. The two determinations form part of a lengthy series of proceedings relating to the block which is a 1930s block of 48 flats, the freeholder of which is Residents, a company the shareholders in which are a small number of the leaseholders. Happily for the purposes of these appeals it is not necessary to delve into the manifold issues relating to the block to any great extent.

3. So far as the first appeal is concerned the relevant facts can be shortly stated.

4. On 4 January 2007 RTM purported to give notice under section 79 of the 2002 Act of a claim to acquire the right to manage the block. It claimed to be entitled to do so as being an RTM company which complied with section 79(5) of the 2002 Act. Residents served no fewer than seven counter-notices each dated 5 February 2007. Accordingly on 6 February 2007 RTM applied to the LVT under section 84(3) of the 2002 Act for a determination of its entitlement.

5. At the hearing it emerged that at 4 January 2007 RTM did not have any register of members. There had been only one person (Mr Guraya) who was a subscriber to the memorandum of association of RTM. There was evidence that 24 leaseholders other than Mr Guraya had agreed to become members of RTM before 4 January 2007.

6. Residents argued that under section 79(3) only an RTM company which complied with section 79(4) or 79(5) of the Act could give a claim notice. Section 79(4), relating to cases where there are only two qualifying tenants in a block, was irrelevant and on the facts RTM did not comply with the requirements of section 79(5) which provides “In any other case [ie other than cases where there are only two qualifying tenants of flats] the membership of the RTM company must on the relevant date [ie the date of the application] include a number of qualifying tenants of flats contained in the premises which is not less than one-half of the total number of flats so contained.”

7. Residents submitted that by section 22(2) of the Companies Act 1985 members of a company other than the subscribers to the memorandum are those who have (a) agreed to become members of the company and (b) had their names entered on the register of members. Thus, it was said, the only person who could properly claim to be a member was Mr Guraya, the sole subscriber to the memorandum, and accordingly the membership of RTM did not include "a number of qualifying tenants of flats contained in the premises which is not less than one-half of the total number of flats so contained."

8. The LVT rejected this argument. It agreed that "the general rules as to what constitutes membership of a company apply" and that those rules are contained in section 22 of the Companies Act 1985 but then went on to say "The question, then, is whether the company has established on the balance of probabilities that on 4 January 2007 at least 23 leaseholders in addition to Mr Guraya had agreed to become members." It continued by referring to section 352 of the Companies Act which imposes on a company an obligation to keep a register of its members and said "We are satisfied that a failure to have a register of members complying [with] section 352 of the Companies Act does not invalidate a claim notice. Had the maintenance of such a register been required we would have expected such a requirement to be included in Chapter 1 of Part 2 of the [2002] Act."

9. In my judgment in reaching this conclusion the LVT fell into an error of law. The question it had to determine was whether RTM had established that on 4 January 2007 the members of the company included "a number of qualifying tenants of flats contained in the premises which is not less than one-half of the total number of flats so contained". In order for a person other than a subscriber to be a member that person must (a) have agreed to become a member and (b) had their name entered in the register of members: see section 22(2) of the Companies Act 1985. Those two requirements are cumulative: see for example *Nicol's case* (1885) 29 Ch D 421**,** *Re a Company* [1986] BCLC 391 at 393 per Hoffmann J and *National Westminster Bank v IRC* [1995] 1AC 119 at 127B per Lord Templeman.

10. In the absence of a register of members a person's name could not be entered on the register and so the person could not be a member, whether or not that person had agreed to become a member. It follows that none of the twenty four leaseholders who were said to have agreed to become members of RTM were members at the date of its application to the LVT, RTM did not fulfil the requirements of section 79(5) and its claim notice was invalid.

11. The consequence is that at the date of its application RTM was not entitled to give a claim notice to acquire the right to manage and the LVT was in error in holding that it was entitled to acquire the right to manage the block. The first appeal must therefore be allowed and the order of the LVT set aside.

12. The second appeal arose out of the need to effect major roof repairs on the block and Residents' desire to recover money upfront from the tenants to finance the works. The LVT reached its decision that the long leases of the flats in Southall Court did not entitle Residents to "raise the service charges required for [certain major works or repair and maintenance] by means of demands from each leaseholder for an appropriate contribution to a sinking fund,

such sums to be payable on demand" with regret. It acknowledged the desirability of establishing a sinking fund against major expenditure and that the view it reached was a different one from that reached by a previous Tribunal and by a Deputy District Judge in the County Court but felt constrained by the words of the leases.

13. The relevant parts of all the leases of flats in the block are now for practical purposes in the same terms (some of the leases having been varied by an order of the LVT dated 8 November 2006). In some leases the parties are described as "lessor" and "lessee" and in others "landlord" and "tenant".

14. The relevant part of the lease in the leases varied by the LVT is to be found at the newly inserted Fourth Schedule which sets out the lessee's further covenants with the lessor. After a covenant to pay the rent there is a further lessee's covenant in the following terms (so far as material):

> "2) To pay to the lessee in addition to the rent hereby reserved:
>
> (a) the annual sum of ONE HUNDRED AND FIFTY POUNDS or such other sum that the lessor may decide in accordance with clause 3(e) of this Fourth Schedule ("the maintenance charge") as a contribution on account towards the expenditure incurred by the Lessor in carrying out its obligations under the Sixth Schedule hereof….
>
> (c) If the expenditure incurred by the Lessor in any accounting period of twelve months in carrying out its obligations under the Sixth Schedule hereof (hereinafter called "the annual cost") exceeds the aggregate amount payable (or deemed to be payable) on account as aforesaid by the Lessees of all flats in the Building in the accounting period in question (hereinafter called "the annual contribution") together with any unexpended surplus as hereinafter mentioned and a certificate of the amount by which the annual cost exceeds the total of the annual contribution and any such unexpended surplus be served upon the Lessee by the Lessor or its Agents with audited accounts in support thereof then the lessee shall pay the Lessor within twenty-eight days of the service of such certificate (which said certificate shall as respects the matters therein contained bind the lessor and Lessee unless some manifest error shall be found therein or in such accounts in which case such error shall be rectified) a proportionate part (hereinafter called "the excess contribution") determined by the Lessor or the Surveyor of the lessor of the amount of such excess shown therein such sum to be recoverable from the Lessee in case of default as if the same were rent in arrear PROVIDED that if in any such accounting period as aforesaid the annual cost is than the annual contribution the difference (being the unexpended surplus) shall be accumulated by the Lessor and be applied in or towards the annual cost in the next succeeding or future accounting period or periods as aforesaid."

15. Clause 3) of the Fourth Schedule then provides (so far as material):

> "3) For the purposes of Clause 2 of this Fourth Schedule and its sub-clauses IT IS HEREBY AGREED AND DECLARED as follows:- ….
>
> (b) The excess contribution payable hereunder shall be one forty-eighth part of the total excess expenditure incurred in respect of the building , roads footpaths and grounds appurtenant thereto…
>
> (d) The Lessor shall be entitled to retain such sum or sums from time to time as the Managing Agents of the lessor shall certify as desirable as a reasonable provision by way of a sinking fund for prospective service charges.
>
> (e) The Lessor shall have the right to increase the maintenance charge by a sum equal to the excess contribution (as defined) for the previous year."

16. The schedule is not happily drafted. The obligation on each lessee is to pay (a) the maintenance charge and (b) an excess contribution. The maintenance charge is £150 or (if the lessor exercises his right under clause 3)(e)) a greater sum amounting to £150 plus the previous year's excess contribution. The method of calculating the excess contribution for each year is spelt out: it is calculated by reference to "the expenditure incurred by the Lessor" in the relevant accounting period and takes account of the maintenance charges paid for that period and anything left over already "in the kitty" ("unexpended surplus"). The terms of clause 4)(d) enable Residents to retain sums for a sinking fund, but there is no express provision that entitles Residents to demand or requires the lessee to pay any sum towards a sinking fund for prospective service charges.

17. This leads to the position where any sinking fund will be one which has simply grown up because the maintenance charges recovered from the lessees for previous years have exceeded the amount actually expended. It will then run down in following years because the excess contribution recoverable from each lessee in each year has to be calculated by reference to the funds in hand.

18. There is another unfortunate consequence: if there is no provision which enables the lessor build up a sinking fund, then following any year in which a major expenditure is incurred there will inevitably be a substantial excess contribution payable by each lessee and furthermore in the year after that the lessor will be able to demand from each lessee a very substantial maintenance charge (ie £150 plus the amount of the previous year's excess contribution).

19. Not surprisingly considerations such as these led the LVT to express the view that "it would be desirable for the landlord, in the interests of good management, to be able to recover in advance and in full the cost of works which are required to the block". The problem which the LVT found insurmountable was the wording of the leases. The obligations to pay are clearly defined. There is nowhere any provision which entitles Residents to require payment to a sinking fund. Nor is it possible to see how an obligation to pay a sum (recoverable as rent) towards a sinking fund can be implied. The wording of clause 4)(d) is too tenuous a thread to support such a term and whilst it is true that the right to require payment to a sinking fund would be desirable it is impossible to say that such a term must be implied so as to give business efficacy to the leases.

20. It follows that whilst I share the regrets of the LVT that the leases do not include a provision which entitles Residents to demand payments from the tenants for the purposes of a sinking fund, in my judgment the Tribunal reached a correct conclusion and the second appeal must be dismissed.

Dated 23 July 2008

His Honour Judge Reid QC