LRX/155/2007

LANDS TRIBUNAL ACT 1949

Landlord and Tenant - service charge

IN THE MATTER OF AN APPEAL FROM A DECISION OF THE LEASEHOLD VALUATION TRIBUNAL FOR THE LONDON RENT ASSESSMENT PANEL

BETWEEN **METROPOLITAN PROPERTY REALIZATIONS LIMITED** **Appellant**

and

ANA MAE SILVER and others **Respondents**

Re: Temple Fortune House and Arcade House Finchley Road London NW11

Before: His Honour Judge Reid QC

Sitting at: Procession House, 110 New Bridge Street, London EC4V 6JL on 6 November 2008

Mr A. Tanney instructed by Wallace LLP, One Portland Place, London W1B 1PN for the Appellant
Mr Richardson, Mr Staley and Ms Mavromatti, Respondents, appeared in person.
The remaining Respondents did not appear and were not represented

The following case is referred to in this decision:

Forcelux Ltd v Sweetman [2001] 2 EGLR 173
Veena SA v Cheong [2003] 1 EGLR 175

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DECISION

1. This is an appeal from a decision of the Leasehold Valuation Tribunal of the London Rent Assessment Panel which was sent to the parties on 7 July 2007. Permission to appeal was given to the Appellant (the landlord) on 26 November 2007. The decision of the LVT determined the liability of the Respondents (the leaseholders) to pay and the reasonableness of various service charge costs arising out of major works carried out on Temple Fortune House and Arcade House, Finchley Road, London NW11 ("the properties") in 2000 and 2002. The appeal raises two points on the LVT's decision, which may conveniently be described respectively as the "Roof Works point" and the "Contract Administrator point".

2. The properties are two blocks on the Finchley Road are listed Grade 2 buildings some 90 years old which comprise between them 27 flats set over shops and cafes. 25 of the flats are let on long leases and 2 are in hand. It was common ground that the relevant service charge provisions in the leases were the same and that the service charge costs in issue were prima facie recoverable under the terms of the leases.

3. The properties were in need of substantial works and in 2000 certain of the necessary works were carried out following consultations between the managing agents and the Arcade-Temple Residents Association Committee ("the RAC"). The final account for the 2000 works amounted to £38,966. Following completion of those works concerns were expressed by the RAC about the standard of the works and Mr Hyman of Ian Hyman of Ian Hyman & Co, chartered surveyors, was instructed by the RAC to comment on the standard of work. Following that further necessary works, the 2002 works, were put out to tender, tendered for and completed under a single contract for which a final account was rendered in May 2004 in the sum of £525,0005. On this occasion Ian Hyman & Co were contracted by the Appellant landlord to act as contract administrators.

4. The leaseholders were dissatisfied with the cost and quality of the works done and applied to the LVT pursuant to section 27A of the Landlord and Tenant Act 1985 to determine their liability to pay and the reasonableness of the various service charge costs arising out of the works. By section 19(1) of the Act:

> "Relevant costs shall be taken into account in determining the amount of a service charge payable for a period (a) only to the extent that they are reasonably incurred, and (b) where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a reasonable standard; and the amount shall be limited accordingly."

5. Before the LVT expert evidence was adduced by both landlord and leaseholders. The experts attempted to agree matters as far as possible and produced Scott Schedules for both the 2000 and 2002 works which the LVT found of great assistance. In its decision the LVT dealt with the works and costs in dispute in three parts: the 2000 works; the 2002 works at Temple Fortune House; and the 2002 works at Arcade House. The decision went through the various points in issue in detail and disallowed or reduced a number of items.

6. In particular, so far as the cost of roof repairs to Arcade House in 2002 was concerned, the LVT established that the tender price for the roof works was £26,610, but in error in the final account the contractor accepted various deductions totalling £31,987 in relation to the roof works. As the LVT observed "This was clearly a mistake because the sum of the deductions exceeded the cost of the works. That benefit accrues to the leaseholders." It is in relation to that error by the contractors and the treatment of it by the LVT that the Roof Works point arises. That point is a short stand alone point.

7. The other point (the Contract Administrator point) is a more general point. Amongst other reductions the LVT reduced the fees of Ian Hyman & Co by 50 per cent, holding that "Throughout this matter, the serious failures on the part of Ian Hyman & Co were apparent and repeated frequently." The landlord does not challenge the criticism of Mr Hyman and his firm and does not seek to challenge the individual determinations made by the LVT reducing or disallowing items. In many instances the LVT was critical of him and his role in allowing the cost to be incurred. What the landlord submits is that in the circumstances of the case, Mr Hyman having been proposed by the RAC, "his errors should at least be shared equally between [the landlord] and the lessees." On this appeal the landlord proposed that the issue of principle should be decided first, leaving the parties to attempt in the first instance to agree what adjustment should be made to the figures in the event that it was held the cost of the errors should be shared between the parties. This was the course adopted.

The Roof Works point

8. The Tribunal having noted that the contractor had made an error in the final account, so that in effect a credit of rather over £5,000 was being given in respect of the roof works, determined that the tenants should have the benefit of the error. What the LVT then did was to take the figure which the landlord's expert, Mr Martin, had assessed as the value of the roof works, £21,233, and decide that this figure should be deducted from the total cost of the works recoverable in relation to Arcade House. It stated

> "That figure [£21,233] should not have been included in the service charge account as part of the total cost payable by the leaseholders. The service charge account should have in fact have been reduced by this amount."

9. The LVT may have been led into determining as they did by a suggestion by Mr Martin to the effect that the windfall benefit of £21,233 worth of roof works received by the leaseholders should be used to offset some of the other reductions made by the LVT. This suggestion was not adopted by the landlord which accepted (1) that it could not seek to charge the tenants for the value of the roof works for which it had not had to pay and (2) that the credit of £5,000 odd had to be given to the leaseholders, which it said it had done.

10. The approach of the LVT would have been entirely logical and correct if the figure of £21,233 or some other figure in respect of roof works had been included in final account and if it had been sought to charge that figure to the leaseholders in the service charge account. However, it is clear that this is not what happened. The leaseholders were not billed on the

basis of any figure given by Mr Martin, but on the basis of the final account agreed between Ian Hyman and Co and the contractors. Mr Martin was not on the scene at the time of the billing. He was the expert brought in far later for the purposes of the LVT hearing and the figure was one at which he arrived when seeking to compute the amount that should properly have been charged by the contractor for the roof works. The final account included the negative figure, so effectively the roofing works were done for free.

11. When the leaseholders were billed on the basis of the final account they were not billed £21,233 for the roof works or any other figure: instead, and because of error on the part of the contractors, they simply received the small credit. The effect of what the LVT decided on this point was that not only (owing to the contractor's error) did they get the roof works free but the landlord was also required to give them credit for the amount they would properly have had to pay if they had been charged for those works.

12. In these circumstances the LVT were in error in deducting the sum of £21,233 from the total amount billable and the appeal should be allowed to that extent.

The Contract Administrator point

13. The landlord's case in relation to this point was based on the fact that Mr Hyman's firm was appointed as contract manager for the 2002 works at the instance of the RAC.

14. Mr Hyman had been engaged by the RAC in relation to the 2000 works and had made a report critical of various items. The RAC initially wished to appoint Mr Hyman to look after its interests in respect of the 2002 works, but by 4 July 2000 Mr Staley as Chairman of the RAC was writing to his members

> "We have suggested to [the landlord] that our consultant surveyor be employed as independent contractor administrator for these works…. If terms are agreed, then the Association will need to ensure that the surveyor remains independent and impartial."

This was a point not lost on Mr Hyman who later wrote to Ms Mavromatti, one of the leaseholders, in November 2002 that he was acting on behalf of the interests of both landlord and the RAC.

15. Mr Hyman was not a surveyor who had on any previous occasion been engaged by the landlord or any other company in the same group, though he had acted for tenants against members of the group. The landlord felt that his appointment as the contract administrator of the project would mollify the leaseholders and prevent problems with the proposed works, particularly as it felt that the leaseholders would object to having to pay for two surveyors. On 5 July 2000 Mr Solomon of the landlord wrote to Mr Staley a letter containing the passage:

> "… Chris Hall will therefore now instruct Ian Hyman & Co, the firm that you have indicated to us is acceptable to you as Consultant Surveyors for the project, to prepare a detailed specification of works." On 31 July 2000 Mr Hyman wrote to Mr Hall of

> the landlord with a copy to Mr Staley setting out his firm's charges. He asked for a letter "confirming my appointment on your behalf".

Mr Hall sought confirmation from Mr Staley that he accepted the fees to be charged in respect of the works. No letter of confirmation from Mr Staley was produced but the landlord engaged Ian Hyman & Co.

16. The RAC was anxious to obtain safeguards to ensure Mr Hyman truly represented their interests. In the event apparently Mr Hyman gave the RAC an undertaking he would not act for the landlord in respect of any other property until the 2002 works were complete. In October 2000 Mr Staley and Mr Gross, the treasurer of the RAC, were writing to Mr Hall referring to Mr Hyman as "our surveyor"

17. By August 2002 the works were on the point of commencement. It appears that there had by this time been some internal rift in the RAC and Mr Staley had ceased to be chairman. On 22 August 2002 there was a meeting to discuss "the impending works and all inter-related matters" attended by representatives of the landlord, the builders and the RAC and Mr Hyman. An elaborate liaison scheme was set out and amongst other things it was agreed

> "Formal meetings with representatives of the Residents' Association will probably be carried out at roughly 3-4 weekly intervals unless any important matters arise and their attendance is requested."

18. The contracted works got under way and meetings with the RAC representatives were duly held. Ms Mavromatti attended a number of meetings as a resident although not a member of the RAC. She complained that in effect the residents just sat and listened. Mr Hyman's view was rather different. He said:

> "Throughout the entire contract, there were numerous meetings and discussions in connection with the scope of the works and in particular with regard to costs. In my career, in excess of 30 years, this has been the only occasion where residents/Residents Association have been involved with decision making and shared in the running of a contract."

19. In the LVT the landlord submitted that what it had done was done in the interests of harmony. It was felt that the appointment of a surveyor identified by the RAC would prevent difficulties and that it would save the RAC the costs of engaging its own surveyor. In its final submissions to the LVT the landlord submitted that money spent on Mr Hyman's advice was money reasonably spent unless there was some manifest error on his part.

20. The LVT did not initially deal with this submission in its decision but in response to a letter from the landlord's solicitors rejected the point. Having noted in its decision that Mr Hyman was appointed "at the insistence of the leaseholders", in its supplemental reasons it determined

> "the reliance on Mr Hyman should not be a method for the Respondent to state that the costs and works are reasonable. Although the Applicants had some input into the appointment of Mr Hyman's firm, he was still employed by the Respondent and it should have ensured that it was happy with the standard of works and costs and its professional advisers. It was solely responsible for the failings or otherwise of Mr Hyman in the first instance."

21. On appeal the landlord submitted that the LVT was wrong in law. The question was whether the costs incurred by the landlord were "reasonably incurred". Reference was made to the decision of Mr Peter Clarke in the Lands Tribunal in *Veena SA v Cheong* [2003] 1 EGLR 175 at 182L

> "The question is not solely whether costs are reasonable but whether they were 'reasonably incurred', that is to say whether the action taken in incurring the costs and the amounts of those costs were both reasonable."

It was not necessary to show that the amount of costs were the cheapest or that all landlords would have acted in the same way.

22. The landlord did not seek to challenge the decision of Mr Francis in the Lands Tribunal in *Forcelux Ltd v Sweetman* [2001] 2 EGLR 173 in which it was unsuccessfully argued that a landlord who adopted a reasonable tendering procedure for appointing a contractor should be held for that reason to have "reasonably incurred" the resulting cost. It sought to distinguish the case pointing out that in this case the leaseholders were protected by the appointment of a surveyor with the approval of the RAC who had up to that point been the surveyor for the RAC. This was intended to protect the interests of the leaseholders: in fact it had the same objective as the statute. Any spending decision then made as a result of adhering to the scheme put in place with the assent of the leaseholders should be regarded as reasonable, unless the landlord ought to have observed the deficiencies of the surveyor and stepped in. An example suggested in argument was a case in which it emerged that the surveyor was a hopeless drunk. This case was entirely different to a case in which the landlord appointed a contract administrator without reference to the leaseholders.

23. The landlord further submitted that in the present case it was wrong to say that because the surveyor was the employee of the landlord the surveyor's errors were the landlord's errors. The leaseholders did not suggest that the surveyor's performance was so manifestly inadequate that the landlord should have stepped in. The fact that the landlord itself was receiving a fee of 2 per cent for management of the works (including supervising Mr Hyman) did not mean it was underwriting his performance. It did not follow that because the landlord might have a right of action against the surveyor which was not available to the leaseholders, the landlord should pay for the errors of the surveyor. The arrangement between the RAC and the landlord was a reasonable one and the payments made under it were reasonable payments reasonably incurred.

24. It was suggested that the LVT's decision was unfortunate as a matter of policy because it left the landlord no better off than if it had simply appointed its own contract administrator without reference to the leaseholders and that the decision would discourage landlords from

seeking to involve the tenants in the selection of a surveyor. It was also unfortunate because it left the landlord with the option of either suing the contract administrator if his work was impugned or subjecting every decision of the contract administrator as work went along to the same degree of scrutiny as an LVT might do later, subjecting it to the reasonableness test. The leaseholders were adequately protected and had adequate recourse in that it was they who had chosen Mr Hyman's firm and in that they had an agreed right to attend site meetings and receive information which they had exercised. In the circumstances the fair thing to do was to split the cost of the surveyor's errors between the landlord and the leaseholder.

25. On behalf of the leaseholders it was submitted that it had been the landlord's choice to appoint Mr Hyman's firm. It was never suggested to the leaseholders that if he turned out to be incompetent they would have to pay for his errors. Having appointed Mr Hyman's firm, the landlord had then not only charged for supervising him (in its 2 per cent fee) but actually done so through its own in-house surveyor. Indeed there was at least one document showing the landlord's reservations about his work even before the contract started.

26. The contractual relationship, the leaseholders submitted, was between the landlord and the administrator. Thus on 13 September 2001 Mr Solomon had written to Mr Staley

> "As it is the Landlord Company which is the Client, it will be necessary for either Chris Hall or Terry Dimmer of this office to attend regular site meetings during the course of the works with Ian Hyman and a representative of your Association (if you wish them to attend) in order to protect the interests of both the Landlord Company and the Residents' Association and to ensure that Ian Hyman is overseeing the contract in a competent manner."

This made it clear that responsibility for Mr Hyman lay with the landlord. The leaseholders had been able to attend meetings but only to observe, comment and recommend. The decisions were not theirs. The cost of the works had been properly reduced by the LVT and the leaseholders were obliged only to pay the reasonable costs. There was no reason why the landlord should recover anything over the amount fixed by the LVT.

27. In my judgment the first hurdle that the landlord has to surmount is one of construction. By section 19 the amount recoverable is limited by the requirement that the costs (a) are reasonably incurred, and (b) where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a reasonable standard. The essence of the landlord's case is that the costs were reasonably incurred because they were certified by the surveyor who was acting as contract administrator, irrespective of the fact that he had not performed his function properly and so had certified sums substantially in excess of those which should have been certified. This glossed over the fact that the section contains a double requirement. Even assuming that it could be said that the costs were reasonably incurred because they were certified by the properly qualified contract administrator, it does not follow that the second hurdle is surmounted. In respect of the item for external decoration of Temple Fortune House where the LVT's findings was to the effect that it was not done to a reasonable standard, it seems to me that the landlord cannot seek to recover any additional cost above that

awarded by the LVT irrespective of any responsibility the leaseholders may have for the deficiencies of the contract administrator.

28. So far as the reminder of the works were concerned, the landlord is suggesting in effect that the shortfall created by Ian Hyman & Co certifying, and the landlord paying, more than the LVT considered the reasonable cost of the works should be split. The LVT decided that although the leaseholders had some input into the appointment of Mr Hyman's firm, he was still employed by the landlord and it was up to the landlord to ensure that it was happy with the standard of works and costs and its professional advisers. The appointment of Mr Hyman's firm was in the hands of the landlord and the landlord alone. The reason for the appointment may have been to keep the RAC sweet but, as the LVT held, that the landlord was solely responsible for the appointment and for the failings or otherwise of Mr Hyman in the first instance. In my judgment these were conclusions of fact to which on the material before it the LVT was entitled to come. This alone is sufficient to dispose of the landlord's argument on this point.

29. However even if it were tempting to say that as a matter of some sort of fairness the effect of Ian Hyman & Co's deficiencies should be visited on the parties responsible for the appointment in equal shares, but the landlord never grappled with how this could be achieved within the framework of the statute. The submission (although expressed more elegantly) boiled down to saying that insofar as the costs incurred exceeded the proper costs of the works one half of the excess was reasonably incurred because one half of the responsibility for appointing Ian Hyman & Co lay with the leaseholders. Even if the landlord had been able properly to say that one half of the responsibility for the appointment lay with the leaseholders it would be overstretching the words of section 19(1)(a) to suggest that a part of the excessive cost was reasonably incurred because part of the blame for appointing the contract administrator responsible for excess payment being made could be laid at the door of another. It would, in my judgment, be impossible to say that the excess payment could be split in the way that was suggested: either the excess cost arising from Ian Hyman & Co's errors was reasonably incurred or it was not and the landlord is not seeking to suggest that the whole of the excess cost was reasonably incurred because the contract administrator was the tenant's nominee.

30. The fact that the landlord may have a right of action in contract against the contract administrator is in this case of no assistance to either side. It might well be that in a case such as this the leaseholders would have an action in negligence against him if they had to pay over an excessive service charge as a result of the contract administrator's activity. Their possible right of action does not make a payment otherwise not reasonably incurred one which is to be treated as reasonably incurred. Similarly if in the present case the landlord can prove that the contract administrator acted in breach of contractual duty it has a right of action. This potential claim might enable the landlord to recover some or all of the overpayment which may mitigate its loss but this would not make a charge reasonably incurred unreasonably incurred. Nor would the fact that the landlord might be reluctant to try to exercise its right mean that the excessive charges were reasonably incurred or that it can recover the excess service charge from the tenants.

31. The suggestion that to refuse the landlord the additional recovery which it seeks would mean that in future it would have to exercise eagle-eyed supervision over its contract administrators is not an argument of any force. The landlord can choose the contract administrator it wishes to have. It did so in this case, though perhaps it made its choice for the wrong reasons. It can (and does) exercise a power of supervision. The extent to which it chooses to oversee the supervisor must be one for it to determine in each individual case

32. The suggested policy reason for splitting the excess charge between landlord and leaseholders does not assist the landlord. The fact that it might be desirable to encourage landlords and tenants to co-operate more in relation to building works such as the ones in issue in this case cannot make any particular cost reasonable or reasonably incurred.

33. The LVT held that various of the amounts paid were in excess of the reasonable amount. In its skeleton argument before the LVT the landlord identified one of the issues on the question of whether the costs were reasonably incurred as being "Was the final account price reasonable….?" In my judgment the LVT was entitled to hold that the excess was not reasonably incurred even though it was paid as the result of the activities of a contract administrator appointed by the landlord at the instance of the leaseholders. There is in my judgment no basis for treating some part of this excess as being reasonably incurred because of the leaseholders' role in procuring the landlord to appoint Ian Hyman & Co. This part of the appeal must be dismissed.

34. It follows that the appeal is allowed in respect of the Roof Works point and dismissed in relation to the Contract Administrator point. The consequence is that, to refer back to paragraph 104 of the LVT decision, the sum of £21,233 must be added back to the total cost allowed in respect of the works recoverable in relation to Arcade House.

Dated 12 November 2008

His Honour Judge Reid QC