Residential property update

Natasha Rees and **Emma Gosling** assess the changes to residential service charges in the light of cases on notification requirements, time limits and consultation before qualifying works

It has been an eventful year for residential property litigation so far, with a number of cases that have helped clarify the law, and in some instances, changed our understanding of the law completely.

One area in particular is residential service charges. Most landlords are aware of the need to review leases carefully and maintain a reasonableness mantra, but there are three issues which crop up time and time again: demand requirements; time limits; and consultation.

Meeting the demand requirements

In *Beitov Properties Ltd v Martin* [2012] UKUT 133 (LC) it was held that the requirement to give the landlord's address in section 47 of the Landlord and Tenant Act 1987 (LTA 1987) is not satisfied by giving the landlord's agent's address.

On appeal to the Lands Chamber the landlord argued that the Act does not prescribe the particular address to be used by the landlord, and provided it is one with sufficient connection with the landlord at which it could receive communications, section 47 is satisfied.

The case of *Triplerose Ltd v Grantglen Ltd* [2013] UKUT 204 (LC) made it clear that the requirement to provide the landlord's name will also be strictly interpreted. In that case the demands were given in the name of "Cane Developments, Paul Marsh and Holly Marsh" instead of "Cane Developments, Grantglen Limited and Holly Marsh". Paul Marsh was a director of Grantglen. The LVT decided that the error had caused no prejudice and that the demand was valid. However, on appeal the Upper Tribunal held that the statutory requirement to name the landlord had not been met. The notice was invalid and no question of prejudice arose.

Some comfort is afforded to landlord's by way of *Harry Johnson, June Johnson & others v County Bideford Ltd* [2012] UKUT 457 (LC) in which it was held that an invalidity that arises by virtue of a failure to comply with the requirements of section 47 is one that can be corrected with retrospective effect. On appeal to the Lands Chamber the tenants argued that a service charge demand which did not comply with section 47 was not a valid demand, and could not therefore be treated as "a demand for payment of the service charge" within the meaning of section 20B(1) LTA 1985. This section imposes a limitation on the recovery of costs that have been incurred more than 18 months before a demand is made.

The tenants relied upon the case *LB Brent v Shulem B Association Ltd* [2011] EWHC 1663 (Ch) to support their contention that a valid demand had not been served within the 18-month time limit. In dismissing the appeal the President did not accept that Shulem B was comparable as it was concerned was a contractual invalidity, and was not one which was capable of retrospective correction. It was held that the service of the later demands had the effect of validating those served within 18 months of the charges being incurred.

Section 21(B) LTA 1985 provides that a demand for the payment of a service charge must also be accompanied by a summary of the rights and obligations of tenants of dwellings in relation to service charges. In *Tingdene Holiday Parks Ltd v Cox* [2011] UKUT 310 it was held that a summary sent separately a few days later will not suffice.

The effect of this decision appears to be that, while a landlord can retrospectively correct a failure to serve the summary,

when doing so it must be accompanied by the demand. Furthermore, although the effect of section 20B (1) LTA 1985 is not specifically covered in this decision, it would appear that, as the tenant was notified in writing that the costs had been incurred within 18 months by the first demand, the saving provision in section 20B (2) LTA 1985 will apply.

Complying with time limits

A key problem that landlords have faced to date is how to determine when costs are 'incurred' for the purposes of Section 20B. The case of *OM Property Management v Burr* [2013] EWCA Civ 479 has been widely credited as resolving this issue. The tenant was required under his lease to pay service charges which included a share of the costs of fuel supply to common parts. The management company's gas supplier presented them with a bill for fuel supplied many years earlier and they sought to recover that bill through the service charges. The tenant argued that as the costs had been 'incurred' more than 18 months before the service charges were claimed they were irrecoverable. The LVT agreed with him and held that the costs were incurred when the gas was supplied, not when the gas company invoiced the landlord or the landlord paid the bill.

The management company appealed to the Upper Tribunal who found in their favour and when the tenant appealed to the Court of Appeal, the Master of the Rolls agreed with the Upper Tribunal and confirmed that costs are 'incurred' for the purposes of section 20B when an invoice is served or payment is made.

Consultation before qualifying works

Section 20 LTA 1985 provides that tenants paying variable service charges must be consulted before a landlord carries out qualifying works where any tenant is required to contribute more than £250. Qualifying works are defined in Section 20ZA (2) as "works on a building or other premises".

Had this update been written pre *Phillips v Francis* [2012] EWHC 3650 (Ch D), it is unlikely that there would have been any reference to "qualifying" works, as generally practitioners would discuss "major" works to reference the fact that a project or set of works would have to be substantial to exceed the £250 threshold. However, in *Phillips v Francis* the High Court (on appeal) decided that the common sense approach adopted since *Martin v Maryland Estates* [1999] 2 EGLR 53 of considering whether a particular set of works are "qualifying works" is incorrect. The Chancellor instead held that there is no triviality threshold in relation to qualifying works as all works which are "qualifying works" should be brought into the account for computing the lessee's contribution.

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In allowing the landlord's appeal, the Chancellor moved away from previous thinking in a radical way. In many cases, a lessee's contribution to the cost of qualifying works in an accounting period will exceed £250, even if no major works projects are planned for that year, simply because the definition will cover basic and unexpected maintenance.

The case of *Daejan Investments Limited v Benson & Ors* [2013] UKSC 14 came as a welcome relief for landlords following *Phillips v Francis*.

At first instance the LVT had held that the landlord had not complied with the statutory consultation requirements by failing to provide a summary of the observations received from the tenants and by not making all of the estimates available for inspection. The landlord appealed and when the case got to the Supreme Court, three questions of principle were considered:

1) the proper approach to be adopted when considering an application to dispense with the consultation requirements;
2) whether the LVT can grant dispensation subject to conditions; and
3) the approach to be adopted where prejudice is alleged by the tenants.

On the first question they found that the LVT should look at the extent, if any, to which the tenants' protection from paying for unreasonable works, or paying more than necessary, has been prejudiced. If there is no prejudice dispensation should be granted.

On the second question, they held that the LVT has the power to grant dispensation on such appropriate terms as it thinks fit. This means that the LVT can grant dispensation but only if certain conditions are met. As a result, the landlord's dispensation was conditional upon it paying the tenants' reasonable costs, and the cost of the works that it was entitled to recover was reduced by £50,000.

Finally, on the third issue they decided that the factual burden of establishing prejudice was the tenants' responsibility, and only when a credible case for prejudice was established should the LVT look to the landlord to rebut it.

As a result of *Daejan*, the LVT will be able to interpret the statutory consultation requirements in a more commercial and flexible manner. However, the fact that tribunals can impose conditions means that landlords will still face potentially significant financial disadvantages if they fail to consult properly.

Ascertaining development value

Finally, the case of *Kutchukian v The Free Grammar School of John Lyon* [2013] EWCA Civ 90 which was decided in February this year is causing quite a stir. The case concerned the issue of development value and how it should be assessed. It was accepted that the building was much more valuable as a house rather than flats. One issue was whether it would be possible to terminate the sub-leases in order to carry out the development under section 61 of the 1993 Act.

The Upper Tribunal had deducted 30 per cent from the development value to reflect legal uncertainties relating to section 61. The Court of Appeal decided that this was wrong. They said that a valuation must proceed by taking a view on what the legal position is, not treating it as an uncertainty by applying a discount. This means that tribunals will now have to reach a decision on legal issues rather than just applying a percentage reduction to reflect risk.

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