Limitation on recovery

Natasha Rees assesses the outcome of a case that highlights the intricacies of the notices required to recover service charges effectively

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Recovery of residential service charges is a minefield for landlords generally, and particularly for unwary landlords who do not demand or give details of sums due by way of service charge within the time limits set by the Landlord and Tenant Act 1985. Section 20B of the 1985 Act essentially provides that a landlord has 18 months from when he incurs a service charge expense to:

- demand it as a service charge or;
- notify the leaseholders that they will, at a subsequent date, be required to pay this amount.

If a landlord falls foul of this limitation period they will be prevented from recovering any sums incurred outside the time limit, notwithstanding that such expenditure was reasonably incurred and the tenants have benefitted from it. As a result there have been a number of cases concerning the construction of s20B and what constitutes a valid demand for the purposes of complying with it.

The leading decision on this issue, until now, was a case called *Gilje & ors v Charlgrove Securities Ltd & anor* [2003] where it was decided in the landlord's favour that s20B did not apply to account charges, but only to balancing charges once the expenditure had been incurred. At the end of June, the High Court gave judgment in another appeal concerning s20B, but this time relating to recovering the costs of major works in arrears rather than in advance. In *Brent Borough Council v Shulem B Association Ltd* [2011] the High Court decided that a freeholder's letter, which notified tenants of the estimated, rather than the actual, cost of major works, did not constitute a valid demand or a relevant notification for the purposes of s20B.

Facts

Brent Council owned five blocks of residential flats in Willesden. The appellant, Shulem B Association Limited, was a company that leased 15 flats within these blocks. Under the terms of its leases it was required to pay a due proportion of the various expenses incurred in respect of the flats. The key clause that came under some scrutiny in the appeal was Clause 2(6). This clause provided as follows:

> At all times during the said term to pay and contribute a rateable or due proportion of the expenses of making, repairing, maintaining rebuilding and cleansing and lighting the exterior of the flat and the building of which it forms part... such proportion in the case of difference to be settled by the Surveyor for the time being of the Lessor whose decision shall be final and to be paid to the Lessor on demand.

The local authority decided that extensive works were required to the blocks, which would involve costs being incurred in relation to 'qualifying works' within s20 of the 1985 Act and also relevant costs that were potentially within s20B.

In March 2004, Brent Council served their tenants with a section 20 notice of intended major works together with details of the proportion of the estimated cost of the works each tenant was liable for. The works were completed by March 2005 at a total cost of some £640,000. In February 2006 Brent Council sent out a letter together with an invoice for major works carried out between 2003 and 2004. It was this letter that was at the heart of the dispute. The letter and invoice were based on the estimated costs that were set out in the original March 2004 section 20 notice. The sums set out in the original section 20 notice were the sums demanded in the invoice. The wording of the letter was as follows:

> This is the invoice for the major works carried out to your property during the financial year 200 (sic). The estimated costs for these works were sent to you on 12 March 2004, as required under Section 20 of the Landlord and Tenant Act 1985.
>
> The actual costs have not been calculated as yet therefore this invoice is based on estimated costs that you were sent with the Section 20 Notice. When we receive the actual costs, a further invoice will be sent to you detailing these and the adjustment required as the actual costs may vary from the estimated costs. If the actual costs are less than the estimated costs then we will refund the difference to each leaseholder. The estimated costs and the details of works are shown below. Payment or proposal for payment is required within 28 working days of the date of this invoice. Methods of payment are enclosed.

Clause 2(6) entitled the landlord to charge the tenant with a proportion of its expenses. The judge felt that the word 'expenses' referred to money that the landlord had spent and that it did not include anticipated future expenditure.

It was not until December 2006 that an invoice based on the actual

costs was served on the tenants. Shulem B refused to pay the sums demanded on the grounds that they had been incurred more than 18 months before December 2006.

County court proceedings

Brent Council issued proceedings to recover the service charges and, in response, Shulem B applied for the proceedings to be struck out on the basis that the local authority was barred from recovering the sums due by virtue of s20B(2). The local authority therefore tried to rely on the letter and invoice it had sent out in February 2006 seeking payment of the likely costs as being the necessary demand or notification served within 18 months of the costs being incurred. At first instance, HHJ Cowell refused to strike out the local authority's claim on the basis that the letter of 26 February was a relevant notification for the purposes of s20B(2). Shulem B appealed and the appeal was heard by HHJ Morgan in the High Court.

On appeal

The first issue that the judge considered was whether the letter of 23 February 2006 was a valid demand for the purposes of clause 2(6). Clause 2(6) entitled the landlord to charge the tenant with a proportion of its expenses. The judge felt that the word 'expenses' referred to money that the landlord had spent and that it did not include anticipated future expenditure. In view of this, he stated that the February 2006 letter and invoice was not a valid demand under the leases because clause 2(6) required the landlord to demand a proportion of 'actual' expenditure that had been incurred, and the letter was unclear as to whether the works had been carried out. He referred specifically to the fact that the figures used in the February letter and invoice were exactly the same as the figures used in the section 20 notice.

The second issue that he considered was whether the February 2006 letter was a demand for payment of service charge for the purposes of s20B(1). He held that since the February 2006 letter was not a valid demand under the terms of the lease it was not a demand for payment of service charge under s20B(1).

Finally, he considered whether the February 2006 letter was a written notification for the purposes of s20B(2). He held that the February 2006 letter was not a notification within s20B of a future charge based on costs that had been 'incurred' because the letter made it clear that the sum claimed was estimated and not based on actual costs. As a result, because the leases did not provide for advance payments, and the landlord had failed to serve any valid demand or notification based on the 'actual' cost incurred, the landlord was unable to recover any of the cost. A very substantial penalty for what was a purely technical fault.

Because the leases did not provide for advance payments, and the landlord had failed to serve any valid demand or notification based on the 'actual' cost incurred, the landlord was unable to recover any of the cost. A very substantial penalty for what was a purely technical fault.

Brent Borough Council v Shulem B Association Ltd [2011] EWHC 1663 (Ch)

Gilje & ors v Charlegrove Securities Ltd & anor [2003] All ER(D)162

Conclusion

This case highlights how important it is to ensure that service charges are demanded in accordance with the terms of the lease, or notified within 18 months of the costs being incurred. If costs have been incurred on major works, but a final figure has not been ascertained, then, in order to protect its position under s20B, a landlord must ensure that its demand is based on the actual costs as far as they are able to then calculate them. It will not matter if the actual costs are overstated as the judge made clear that it is open to landlords to correct the figures later. ■

Section 20B of the Landlord and Tenant Act 1985

Limitation of service charges: time limit on making demands

(1) If any relevant costs taken into account in determining the amount of any service charge were incurred more than 18 months before a demand for payment of the service charge is served on the tenant, then (subject to subsection (2)), the tenant shall not be liable to pay so much of the service charge as reflects the costs so incurred.

(2) Subsection (1) shall not apply if, within the period of 18 months beginning with the date when the relevant costs in question were incurred, the tenants were notified in writing that those costs had been incurred and that he would subsequently be required under the terms of his lease to contribute to them by the payment of a service charge.