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THE RESIDENTIAL PROPERTY TRIBUNAL SERVICE

LANDLORD AND TENANT ACT 1987 SECTION 35

DECISION OF THE SOUTHERN LEASEHOLD VALUATION TRIBUNAL

156B AND 156C MILTON ROAD GRAVESEND DA12 2RG

Applicant: 1. Mr Mark Sugden (Flat B)

2. Mr Neil James (Flat C)

Represented by: In person

Respondent: Mr Irfan Erdogan (Landlord)

Represented by: In person

Date of application: 13 April 2010

Date of hearing: 9 August 2010

Members of the Leasehold Valuation Tribunal:

MA Loveday BA Hons MCI Arb

Ms H Bowers MRICS

INTRODUCTION

1. This is the hearing of an application for variation of a lease under s.35 of the Landlord & Tenant Act 1987. The application is made by Mr Mark Sugden and Mr Neil James, who are the lessees of Flats B and C, 156 Milton Road Gravesend. The landlord, Mr Irfan Erdogan is the freeholder. The application is dated 13 April 2010 and directions were given on 26 May 2010. A hearing was held on 9 August 2010, at which the three parties appeared in person.

THE STATUTORY PROVISIONS

2. The relevant statutory provisions under Part IV of the 1987 Act are:

Applications relating to flats
35 Application by party to lease for variation of lease

(1) Any party to a long lease of a flat may make an application to a leasehold valuation tribunal for an order varying the lease in such manner as is specified in the application.

(2) The grounds on which any such application may be made are that the lease fails to make satisfactory provision with respect to one or more of the following matters, namely—
...(f) the computation of a service charge payable under the lease.

... (4) For the purposes of subsection (2)(f) a lease fails to make satisfactory provision with respect to the computation of a service charge payable under it if—
(a) it provides for any such charge to be a proportion of expenditure incurred, or to be incurred, by or on behalf of the landlord or a superior landlord; and
(b) other tenants of the landlord are also liable under their leases to pay by way of service charges proportions of any such expenditure; and
(c) the aggregate of the amounts that would, in any particular case, be payable by reference to the proportions referred to in paragraphs (a) and (b) would either exceed or be less than the whole of any such expenditure.

38(6) A tribunal shall not make an order under this section effecting any variation of a lease if it appears to the tribunal —

(a) that the variation would be likely substantially to prejudice—

(i) any respondent to the application, or

(ii) any person who is not a party to the application,

and that an award under subsection (10) would not afford him adequate compensation, or

(b) that for any other reason it would not be reasonable in the circumstances for the variation to be effected.

(7) A tribunal shall not, on an application relating to the provision to be made by a lease with respect to insurance, make an order under this section effecting any variation of the lease—

(a) which terminates any existing right of the landlord under its terms to nominate an insurer for insurance purposes; or

(b) which requires the landlord to nominate a number of insurers from which the tenant would be entitled to select an insurer for those purposes; or

(c) which, in a case where the lease requires the tenant to effect insurance with a specified insurer, requires the tenant to effect insurance otherwise than with another specified insurer.

INSPECTION

3. The Tribunal inspected the common parts and exterior of the property before the hearing. Number 156 Milton Road is a period property in the commercial centre of Gravesend in a terrace of similar retail buildings. The building has retail use on the ground floor and basement and three upper floors of residential. The property abuts another building at the back in separate ownership and there is no rear garden or yard. Access to the residential common parts is through a street door between two shops on the left hand side of the subject premises and there is a separate access to the shop on the right hand side. The street door to the flats gives access to a short hallway and stairs to the upper floors. There is a self contained single flat on each floor, but the arrangement of each floor differs slightly:

   (a) 156c is on the third floor, with the entrance from the communal landing on the second floor to an internal staircase. When the lease was granted in 2002, the top floor flat was originally smaller than the others in the building and this is clear from the lease plan. However, the second respondent extended the flat to the rear by creating a rear mansard room with the pitched rear wall extending to a line slightly short of the main rear elevation. This flat is now therefore about the same size as the other two flats.

   (b) 156b is on the second floor and 156a is on the first floor. These flats each take up the whole of the floor of the building, and both flats extend up to the rear elevation of the building.

(c) The shop is on the ground floor and basement and it is used as an off licence. To the left hand side, the shop excluded the corridor and it was therefore much narrower than the flats above. The rear areas of the ground floor were not easy to compare to the upper floors, but the respondent accepted that the shop projected slightly beyond the main rear elevation wall of the building at ground floor level. The Tribunal was unable to inspect the basement because the stairs from the shop was full of stock, but the respondent stated that the basement was about the same area as the floor of the shop. In short, the shop was about the same size as the floors above, but included substantial basement storage.

THE LEASES AND THE PROPOSED VARIATIONS

4. The lease of flat 156b is dated 21 November 2002 and the lease of flat 156c is dated 24 June 2002. Both are in similar form, but for sake of clarity we have quoted from the lease of 156c Milton Road. The material covenants are as follows:

   (a) By clause 2(c), the lessee covenanted:

   "(i) to contribute and pay one third of the costs expenses and outgoings and matters mentioned in the Fourth Schedule hereto (herein referred to as 'the Service Charge')."

   (b) The First Schedule described the 'demised premises' as "The top floor flat known as 156c Milton Road Gravesend Kent which is shown edged red on the plan annexed hereto and forms part of the building known as 156 Milton Road Gravesend Kent (herein called 'the building') of which the Lessor is registered as proprietor with absolute title under the above title number ..."

   (c) The Fourth Schedule paragraph 1 included as service charge relevant costs "the expenses incurred by the Lessor in carrying out his obligations under this lease."

   (d) The Fourth Schedule paragraph 2 included as service charge relevant costs "Keeping in repair and renewing the roof foundations main structure and exterior of the Building and the curtilage thereof".

5. The variations proposed by the applicants are set out in their undated statement of case. The proposal was that clause 2(c)(i) should be amended to:

"(i) to contribute and pay one ***quarter*** *of the costs expenses and outgoings* ***including buildings insurance*** *and matters mentioned in the Fourth Schedule hereto (herein referred to as 'the Service Charge')* ***with the following exception: When repair, maintenance, refurbishment or cleaning works are undertaken only in the communal area servicing the three flats, namely 156a, 156b and 156c Milton Road, then the costs for each tenant should be fixed at one-third."***

THE APPLICANTS' SUBMISSIONS

6. The applicants relied on their undated statement of case and expanded on these submissions at the hearing. The shop and first floor flat were retained by the landlord, who ran the off licence and used the first floor flat for his relations. The applicants submitted that it would be fairer if flats 156b and 156c paid one quarter of the cost of building insurance and repairs to the building (e.g. repairs to the roof or the external walls) since the flats were subsidising the landlord. However, it was appropriate to make some distinction between the building costs and the service charges which related to the common parts for the flats (such as cleaning). It was fair to divide these three ways between the flats.

7. At the hearing, the applicants submitted that it seemed strange that in a block with three flats and a shop (on two levels), the two upper flats together paid two thirds of the entire costs for the building. The leases "fail to make satisfactory provision" in section 35 because the percentages were unfair. They accepted that a lease could "make satisfactory provision" in a number of ways, for example by allocating the percentage service charges according to the rateable value of each unit, by allocating them according to the floor areas or by an equal division according to the number of units in the building etc. However, in this case the one third liability of the two flats was not obviously based on any of these. Furthermore, the respondent had in the past let the shop out and collected one third of the service charge costs from the business tenant – which mean that he paid nothing at all for the first floor flat which he retained for his family. The applicants did not consider they should pay anything in compensation under section 38(10) since the present situation was obviously unfair. The applicants wished to sort things out in case they had to sell their flats.

THE RESPONDENT'S SUBMISSIONS

8. The respondent relied on a statement of case dated 26 July 2010, which had been drawn up by his solicitors. He stated that the ground floor shop and first floor flat were retained by him as one unit. The shop has a separate entrance and he had never demanded a service charge contribution from the applicants for any costs associated with the shop. The applicants had in any event been independently advised when they acquired their leases and never raised any issue with the service charge. He submitted that the leases did make "satisfactory provision" within then meaning of s.35. The question of whether the applicants find the division fair (which he disputed) was not a ground for varying the lease. It was established that a lease does not make satisfactory provision simply because it could have been better or more expertly drafted. If the lease terms were varied, he sought compensation under s.38(10) of the Act.

9. At the hearing, the respondent denied he had recovered 100% of the costs from the two applicants and the former leaseholder of the shop. He explained that the one third allocated in the leases was based on the fact that there were three flats – he understood that the leases did not allow him to recover costs which related to the ground floor of the building, the basement or the foundations. In practice, he paid one third of the outgoings for the building such as the insurance – whilst the shop had its own insurance policy. As to compensation, he agreed that this would ordinarily require some valuation evidence and agreed that in the event that the Tribunal ordered a variation, further directions would have to be given for valuation evidence to be provided by the parties on this point.

THE TRIBUNAL'S DECISION

10. The central issue in this application is the meaning of the words "fails to make satisfactory provision" with respect to the computation of the service charges. The applicants submitted that these words confer a wide discretion on the Tribunal. The respondent contends that the words have a restricted meaning and that the Tribunal has only a limited discretion.

11. Plainly, the phrase cannot involve a subjective test. Almost any provision in a lease is not "satisfactory" from the point of view of a party with the burden of that covenant whilst being "satisfactory" from the point of view of the party with the benefit of that covenant. The test must be an objective one, namely whether the lease fails to make "satisfactory provision" from the point of view of both parties (and indeed from the point of view of any other lessees and persons with an interest in the building).

12. Some assistance is given by looking at other statutory provisions. One can compare and contrast the phrase used in s.35 with paragraph 3 of Schedule 11 of the Commonhold and Leasehold Reform Act 2002. In the 2002 Act, variations are permitted to administration charge provisions where the "*charge specified in the lease is unreasonable*" or "*any formula specified in the lease ... is unreasonable*"). This tends to suggest that there is a distinction between a provision which is not "satisfactory" and one which is "unreasonable". More significantly, it should be noted that s.35 is only the first of at least two stages which the Tribunal must go through before making any variation. Section 35 only deals with the grounds for making a variation. The discretion given to the Tribunal is exercised under s.38, and it is at that stage that parliament directs that matters such as prejudice to the parties is to be considered: see s.38(6) and (7). Some assistance is also given by s.35(4), which deals with whether a service charge scheme is 'workable', rather than the merits of the provision.

13. Typically, variations are made by Tribunals under s.35 where the wording of the lease was always unworkable or impractical or the relevant provision subsequently became unsatisfactory as a result of developments since the grant of the lease (e.g. the construction of new parts of the building or the destruction of parts of the building). The Tribunal also accepts that a lease could in some circumstances fail to make "satisfactory provision" for something if it was grossly unfair to one or other of the parties. However, the above considerations tend to suggest that the phrase "fails to make satisfactory provision" is construed narrowly and that the Tribunal has no general discretion under s.35 to vary a lease simply because its provisions could be better or more expertly drafted or they are merely unfair.

14. The Tribunal takes into account that the percentages in the leases do not reflect the floor areas of the units within the building, and that this 'favours' the landlord. Moreover, the explanation given by the landlord for the allocation of one third of the service charge costs to each of the applicants is plainly wrong. The First Schedule to each lease plainly defines the "building" as including the whole of the property – including the foundations and external walls of the shop. The applicants are contractually liable to contribute towards insurance and repairs to the exterior of the shop and the ground floor. Indeed, there was no real explanation offered as to why the costs were divided three ways between the lessees and the landlord – other than the fact that there were three flats.

15. The Tribunal does not consider the costs actually charged by the landlord under clause 2 of the lease to be relevant. This applies to the lessees' contention that the respondent has previously arranged matters so that it recovered 100% of the costs from residential and business lessees (thereby avoiding any liability attaching to the first floor flat). It also applies to the respondent's argument that he has never asked for a contribution towards the costs of the ground floor and basement. Section 35 deals with the terms of the lease, not sums paid by way of service charges.

16. However, on balance, the Tribunal ultimately agrees with the arguments advanced by the respondent in his statement of case. The landlord has not arranged matters in such a way that the leases engage section 35(4) of the Act. The leases of flats 156b and 156c are not unworkable as currently drafted. They have not become anachronistic as a result of some change – indeed the only real change in the premises since the grant of any of the leases was the extension in the floor area of the top floor flat. The division of service charge liability into thirds which was adopted by the draftsman of the lease in this case was a simple one, but that does not mean it fails to make satisfactory provision. Even if clause 2(c) as currently worded can be said to be objectively unfair, the allocation is not so disproportionate as to make it grossly unfair.

17. The Tribunal therefore finds that the applicants' leases, as currently worded, make satisfactory provision for the computation of service charges. It therefore rejects the

application to vary the leases of flats 156b and 156c under section 35 of the Landlord and Tenant Act 1987.

Signed

Mark Loveday BA(Hons) MCIArb
Chairman
10 August 2010