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HM Courts
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Residential
Property
TRIBUNAL SERVICE

Case reference: LON/00BK/LSC/2011/0620 and LAM/2011/0019

**DECISION OF THE LONDON LEASEHOLD VALUATION TRIBUNAL ON
APPLICATIONS UNDER SECTION 27A OF THE LANDLORD AND TENANT
ACT 1985 AND 24 OF THE LANDLORD AND TENANT ACT 1987**

Property: Dorset House, Gloucester Place, London NW1

Application under section 27A of the 1985 Act:

Applicant: Dorset House Residential Limited

Respondents: The leaseholders of the flats in Dorset House

Joined party: The liquidators of Bellnorth Limited

Application under section 24 of the 1987 Act:

Applicants: Ipe Jacob and others

Respondent: Dorset House Residential Limited

Date heard: 23, 24, 25 and 26 April 2012

Appearances: Sol Unsorfer, Parkgate Aspen, for Dorset House Residential Limited

Greville Healey, counsel, instructed by Trowers & Hamlins, solicitors, for the 53 leaseholders who are applicants in the application under the 1987 Act and, for 138 leaseholders who are members of the Dorset

House Tenants' Association and are respondents in the application under the 1985 Act

Susan Brown and Timothy Sampson, counsel, instructed by Ian Robert, Kingston Smith & Partners LLP, insolvency practitioners, for the liquidators of Bellnorth Limited

Tribunal:

Margaret Wilson
Luis Jarero FRICS
Owen Miller BSc

Date of decision:

16 July 2012

Introduction

1. There are two applications before the tribunal. One is an application by Dorset House Residential Ltd ("DHRL"), the landlord, under section 27A of the Landlord and Tenant Act 1985 ("the 1985 Act") to determine the liability of the leaseholders ("the tenants") of the 199 flats in Dorset House ("the block") to pay service charges for the years ended 29 September 2009, 2010 and 2011. The other is an application by the tenants of some 53 of the flats under section 24 of the Landlord and Tenant Act 1987 ("the 1987 Act") for the appointment of a manager to manage the block.

2. The application under the 1987 Act was heard by the tribunal as presently constituted at a five day hearing on 5, 6, 7, 8 and 9 December 2011 at which those of the tenants who had made or been joined as applicants were represented by Greville Healey, counsel, instructed by Trowers & Hamlins, solicitors, and DHRL was represented by Howard Lederman, counsel, instructed by Osbornes, solicitors. The liquidators of Bellnorth Ltd ("Bellnorth"), which was the landlord before it went into liquidation, had been given permission, with the consent of the other parties, to be heard in relation to matters which concerned them, and were represented by Susan Brown and Timothy Sampson, counsel, instructed by Ian Robert of Kingston Smith and Partners, insolvency practitioners. At the hearing it became clear, and was accepted by the tenants, that the manager whom they had proposed was unsuitable. It was also agreed that the application under the 1987 Act should be adjourned, on undertakings from DHRL which were recorded in an order dated 18 December 2011, and that it would be considered further at the hearing of DHRL's application under the 1985 Act which was then fixed to take place over five days commencing on 19 March 2012 but was later adjourned by consent to commence on 23 April 2012, as it did.

3. At the present hearing DHRL was represented by Sol Unsdofer of Parkgate Aspen Ltd which has been the managing agent of successive landlords since 2000 or thereabouts. The 138 tenants who are members of the Dorset House

Tenants' Association ("DHTA") were represented by Mr Healey, instructed by Trowers & Hamlins. The liquidators of Bellnorth, who, with the consent of the other parties, had been joined as parties to the application under the 1985 Act, were represented by Ms Brown and Mr Sampson, instructed by the liquidators. None of the tenants who were not represented by Mr Healey took any active part in the proceedings.

Background

4. Dorset House is a large block occupying a prominent site in Gloucester Place NW1 with an underground NCP car park, commercial units, including shops and a restaurant, on the ground floor, and 199 flats or thereabouts (opinions as to the numbers of flats differed) on the nine storeys above the ground floor. The block was built in the 1930s in the art deco style. In March 1998 it was listed Grade II.

5. In the early years it is understood that the flats were let on short underleases. In the 1970s, when the long underleases were granted, the freehold interest in the entire block was owned by MEPC Ltd and the residential parts of the block, together with all the structural walls and drains, including those at ground floor and basement level, were the subject of a headlease to Buckingham Properties Ltd. The freehold of the block was in due course acquired by Benesco Charity Ltd and in 1978 Bellnorth acquired the headlease from Buckingham Properties Ltd. Bellnorth was and is a wholly owned subsidiary of Orro Ltd, which is part of a group of companies owned by Equiom Trust Company Ltd, which is based in the Isle of Man. On 11 December 2003 Orro Ltd purchased the freehold of the entire block from Benesco Charity Ltd for the sum of £11,350,000. By deeds of surrender between Orro Ltd and Bellnorth made in 2008 and 2009 Bellnorth surrendered to Orro Ltd parts of its interest in the residential parts of the block, including the roof. Over time, Winllan (Dorset) Ltd and Nome Ltd, two companies owned by Orro Ltd, acquired the underleases of, respectively, 12 and 5 flats. On 25 December 2010 Bellnorth transferred its head leasehold interest to Winllan

(Environmental) Limited, an associated company, for the sum of £25,000 and on the same day Winllan (Environmental) Ltd transferred the head leasehold interest to DHRL, also in the ownership of Orro Ltd, also for a consideration of £25,000. It is understood that shortly after the transfer Winllan Environmental Ltd changed its name to DHRL.

6. Clause 8 of the agreement for the transfer of the head leasehold interest is concerned with service charges and reserve funds. It provides that the seller, Bellnorth, shall on completion assign to the buyer (effectively DHRL) the right to all arrears of advance payments and service charges. By clause 8.4.2 DHRL is to use all reasonable endeavours at the earliest possible time to collect service charges from the tenants but, by clause 8.4.3:

if any such sum remains outstanding for more than four months after the earliest due date for payment by the tenant, [DHRL] will on written notice from [Bellnorth] execute ... an assignment with full title guarantee to [Bellnorth] in a form reasonably acceptable to [Bellnorth] of any sums then outstanding which [DHRL] is to collect pursuant to clause 8.4.2 and from the date of such assignment [DHRL's] obligation to collect any such sum ceases.

7. On 26 January 2011 Bellnorth went into creditors' voluntary liquidation. At the date of the hearing the liquidators had not called for an assignment of the duty to collect outstanding service charges although they had indicated that they might do so.

8. By a letter dated 24 April 2012 from Aldan Davin, a director of, presumably, one or more of the Equiom group of companies, faxed to the tribunal during the course of the hearing, we were informed that Winllan Ltd is the legal and beneficial owner of DHRL and that the freehold interest in Dorset House has been sold to Winllan Ltd, which is controlled by Soberano Ltd "as General Partner of Mebco LP". The letter said that the legal and beneficial ownership of Winllan Ltd remained as it was at the time of the last tribunal hearing, that there

had been no change in the legal or beneficial ownership of Winllan Ltd in the last two years, and that on the sale of the freehold interest in the block to Orro Ltd, Winllan's balance sheet and cash reserves increased substantially and were in excess of £7 million.

The leases

9. Some of the residential underleases have been extended under the Leasehold Reform, Housing and Urban Development Act 1993, but all the residential underleases and leases are essentially in common form. So far as is relevant they provide that the tenant is to pay a proportionate part of:

the cost of maintaining repairing ... and renewing the structure of the building and ... the cost of maintaining repairing and where necessary replacing the whole of any heating and hot water systems serving the building; and such sums as the lessor shall reasonably consider necessary from time to time to put to reserve to meet the future liability of carrying out major works to the building ... with the object as far as possible of ensuring that the contribution shall not fluctuate substantially from time to time.

The tenant is required on 25 March and 29 September in each year to pay one half of the amount payable for the preceding year with the balance, if any, payable on demand after certification by the managing agent after the end of the accounting year on 29 September. An effect of these provisions is that, other than by way of reserve fund contributions, it is difficult for the landlord to collect in advance the money required for major works. That is a particular problem because the infrastructure of the block has required massive expenditure in recent years.

The issues

10. Before the hearing DHRL and the tenants were able to agree a number of issues raised in the application under the 1985 Act. At the start of the hearing Mr Healey said that the tenants no longer disputed further issues raised in that application, and at the end of the hearing he said that the tenants were content that the application to appoint a manager should be dismissed provided that Mr Unsdorfer and Parkgate Aspen agreed to continue to abide by the undertakings recorded in the tribunal's order dated 18 December 2011. Mr Unsdorfer agreed that he and Parkgate Aspen would do so and on that basis the application under the 1987 Act was dismissed by consent.

11. Accordingly there remained few issues which required determination. The most contentious issue, which occupied most of the hearing, was the tenants' liability to contribute to sums which have been adjudicated to be due to Argent FM Ltd ("Argent") in respect of the replacement of the pipework in the block. In addition there was an issue between the tenants and the liquidators, but not between the tenants and DHRL, as to whether contributions to the reserve fund demanded by Bellnorth in respect of the years ended 29 September 2009, 2010 and 2011 were reasonable. There was also initially argument as to whether the tenants were entitled to credits, by way of set off, in respect of sums disallowed by a tribunal in an earlier decision, but at the end of the hearing Mr Healey said that he was no longer pursuing that issue.

The Argent award

Background

12. In the late 1980s it became evident that much of the infrastructure of the block had come to the end of its useful life and that it would have to be renewed. In about 2000 the managing agents published a programme of works, agreed with the DHTA, which included the replacement of the pipework. In September

2004 Bellnorth applied to the tribunal for a determination of the reasonableness of the reserve fund contributions it proposed to collect to cover the cost of the pipework replacement programme ("PRP"). CD Associates, consulting engineers ("CDA"), produced a statement of the objectives of the PRP and its likely cost, which they estimated to be £6,019,818 including fees and VAT, and on 12 April 2005 a tribunal decided that the proposed programme for the works was reasonable, that £6,000,000 was a reasonable estimate of its cost, and that reserve fund contributions of £500,000 for the year ended 29 September 2004 and of £750,000 for the years ended 29 September 2005, 2006 and 2007 would be reasonable.

13. It was intended that the PRP would be undertaken in three consecutive phases, designed to minimise disruption to the occupants of the block. The first phase was the decommissioning of the artesian well which had previously supplied water to the block and the connection of a mains water supply. The decommissioning works were carried out by Argent, the lowest tenderer, in 2005/2006. The second phase, known as Phase 1, comprised upgrading works within the boiler room and tank room and the routing of new pipework through the basement and ground floors. The third phase, Phase 2, comprised the stripping out of the existing hot water, cold water, rainwater and soil pipes, the installation of new pipework in the riser ducts, the provision of new heating risers within the airing cupboards, the installation of new radiators and heating controls within the flats, and the stripping out of redundant plant and pipework at roof level. According to the evidence of Dennis Daly of CDA, which we accept, the design of the new system was intended to minimise disruption to the residents and to be the quickest, least invasive and most cost-effective solution, which avoided the need to lift floorboards and provided a time frame which would enable residents to remain living in their flats while the works proceeded. It was accordingly envisaged that the pipework within the flats would be surface-mounted at skirting level and the tenants would be able if they wished to box in the pipework when they refurbished their flats.

14. The DHTA appointed a surveyor to represent their interests in connection with the PRP and he attended most of the pre-contract design meetings. The proposed scheme was accepted by him and the DHTA raised no objections to it at the pre-contract stage. The specification for the PRP was prepared by CDA in collaboration with a surveyor instructed by the DHTA, and the first consultation notice in respect of the works was given to the tenants on 16 March 2006.

15. Three contractors tendered for the works in Phases 1 and 2. The tenders were of £4,751,200, £4,316,999 and £3,728,501 and Argent's tender was the lowest. A statement of estimates was given to the tenants on 22 August 2006, and Argent was in due course appointed to carry out the works. The landlord organised various meetings and residents' clinics, and drawings and models showing the proposed surface-run pipework were made available for inspection by the residents. After the consultation period had expired, a letter of intent was issued to Argent to undertake the Phase 1 works for the sum of £1,173,136, with a programme of some 30 weeks. It was intended that during this phase Argent would survey the flats to confirm the locations of the existing risers and establish pipework routes.

16. In August 2006 Bellnorth applied to Westminster City Council for listed building consent for the PRP in order to ensure that some of the alterations to the block which it entailed would not be subject to VAT. A representative of the Listed Buildings Department visited the block and raised no objection at that time to the proposal to run the central heating pipework above the skirting boards of the flats.

17. In October 2006, Christopher Hill, a leaseholder and former chairman of the DHTA, wrote on his own behalf to the Council's Listed Building Department objecting to the proposal to route the pipework above the skirting boards. Much to the surprise and dismay of Bellnorth's advisers his objection was upheld and the Council required the pipework to be run underneath the floorboards in the flats. This came as a surprise to the landlord not only because neither Mr Hill,

nor the DHTA, nor the Listed Building Department, had previously made any objection to the proposal for surface-run pipework but also because the listing included: "the interiors of the flats are not of special interest". An effect of Council's decision was that the PRP became very significantly more disruptive to the residents, who had to remove furniture and floor coverings so that floorboards could be raised, and many of the residents decided that they preferred to move out of the block while the works proceeded. It also became necessary for each flat to be surveyed for a second time, and it became impossible for Phase 2 to follow seamlessly after Phase 1 as had been intended.

18. The contract was entered into on or about 31 January 2007, the contract sum for Phase 1 being £1,173,136. The Phase 1 works started on 1 February 2007 and finished on 7 September 2007. During that period the programme for the Phase 2 works was amended to comply with the requirements of Westminster City Council, and an increased contract sum £3,879,523 and delayed completion date of 31 July 2009 was renegotiated with Argent, which could not be instructed to start Phase 2 until February 2008, some four months later than intended. The original contingency sum of £742,000 was applied at the outset of Phase 2 to the additional costs of running the pipework under the floors, and a VAT refund of some £355,000 was applied to contingencies.

19. Although the majority of the residents decided to move out while the Phase 2 works proceeded, a number did not, and some of those who remained chose to be obstructive and court action against some of them was required to enable access to be given to the contractor. The design of the block is such that delayed access by just one resident would be likely to delay works to all the flats above and below, and delay in one work zone would tend to cause consequential delays in others. Further serious delays arose when asbestos was discovered under the floorboards in the flats.

20. In the course of the Phase 2 works a number of leaseholders refused to pay service charges on the due date in September 2008 and Argent issued a

preliminary notice under the contract that it would suspend works until the stage payments were made. After negotiations with the landlord Argent agreed to continue the works on the basis of part payments, and, by allocating additional labour to the project, the works were completed on 31 July 2009 as planned.

21. On 10 June 2009 Bellnorth applied to the tribunal under section 27A of the 1985 Act for a determination of the tenants' liability to pay service charges for the years ended 29 September 2005 to 2009, the application later enlarged to include the year to 29 September 2004. At the date of the application service charges of some £1 million were unpaid. The application, together with a number of county court claims for arrears of service charges, was heard by a tribunal in April 2010, the disputes relating mainly to the PRP.

22. The tribunal's determination dated 14 July 2010 included the following:

i. that an agreement between Bellnorth and Vision Building Services Ltd ("VBS") was a qualifying long term agreement which required, but had not received, consultation with the tenants in accordance with the 1985 Act and the relevant regulations, and that dispensation from the statutory consultation requirements should not be dispensed with so that the maximum which could be recovered from each tenant was £100 per flat per year, equivalent to a sum which was significantly less than the the fee which the landlord had paid to VBS;

ii. that although in principle Bellnorth ought to have re-consulted the tenants in accordance with section 20 of the 1985 Act when the scope of the PRP changed following the requirement of Westminster City Council that the pipework be run underneath the floorboards, it was reasonable in the circumstances to dispense with further consultation;

iii. that payments made to Argent up to September 2008 amounted in total to £4,437,159 and that sum, together with the unpaid £1,463,218 due under the contract, was reasonably incurred and payable by the tenants, but that any payment to Argent in excess of those amounts, including all amounts payable in

2010, would, if not agreed, have to be subject of further proceedings because they had not been the subject of evidence before the tribunal;

iv. that legal fees, and a rent charged for premises in the block used by the design team site works manager and tenant liaison officer for the purpose of the PRP, were not recoverable as service charges under the lease.

23. Those tenants who were represented at the tribunal hearing applied for but were refused permission to appeal.

24. Many of the tenants declined to pay the service charges which they had been held liable to pay and by the end of 2010 the service charge arrears had risen to about £2 million.

25. Argent, represented by Knowles Ltd ("Knowles"), construction and engineering consultants, submitted a substantial claim to Bellnorth, largely for disruption during the Phase 2 works. Bellnorth contested the claim and instructed Heasmans, quantity surveyors, to negotiate with Knowles in order to reach a settlement. Negotiations were still in progress when Bellnorth went into creditors' voluntary liquidation on 26 January 2011.

26. On or about 24 and 26 January 2011 Argent served on Bellnorth and on Parkgate Aspen (which, surprisingly, had signed the contracts with Argent) notices of adjudication in respect of, respectively, the sums which it alleged to be due and unpaid in respect of the Phase 2 and Phase 1 works. Parkgate Aspen wrote to the adjudicator, Mr Anthony Bingham, to say that it was not a party to the contracts, but neither Bellnorth nor Parkgate Aspen took any other active part in the adjudication. Argent's case was presented in writing by Knowles. On 28 February 2011 the adjudicator issued his decisions in relation to Phases 1 and 2. In relation to both phases he determined that Parkgate Aspen was a party to the contract. In relation to Phase 1 he determined that the total sum payable for the contract works and agreed variations was £1,360,000 of which £148,418.85 was unpaid and payable forthwith, with interest of £18,930.99 to the date of the award

and continuing at £40.61 per day, plus VAT and plus the adjudicator's fees. In relation to Phase 2 he determined that the following sums were due and payable forthwith: £391,500.10 plus VAT under the contract, £296,075.26 plus VAT in respect of variations, £2,644,000.30 plus VAT in respect of disruption, £304,098.81 in respect of interest to the date of the award, and Mr Bingham's fees.

27. It is agreed that, although the awards are binding and enforceable, it would in principle be open to Bellnorth to refer to arbitration the questions determined by the adjudicator and that an arbitrator's award would supersede the adjudicator's awards. There will, however, be no arbitration because Bellnorth is in liquidation and the companies which lie behind it will not fund an arbitration. The liquidators' only source of funds for litigation is Argent itself, which has, indeed, paid the liquidators' costs of the present proceedings before the tribunal. Argent has agreed not to enforce the award against Parkgate Aspen.

28. In the circumstances summarised above we have to decide what amount owed to Argent was reasonably incurred and recoverable from the tenants as service charges.

The evidence and arguments

29. It was agreed that 12.6% of the costs occasioned by disrupted labour, plant and preliminary costs was attributable to the commercial element in the block and is not recoverable from the residential tenants.

30. A summary of the amounts claimed by Argent, as revised by Knowles since the adjudicator's award, is set out in a table at paragraph 25 of the second witness statement, dated 5 April 2012, of Andrew Rainsberry, a chartered civil engineer and the managing director of Knowles, who gave evidence. The table is a convenient starting point. It shows, in each case excluding VAT and interest

which continues to accrue at a rate of some £800 per day, assuming it continues to be payable after the date of the liquidation:

| | |
|---|-----------------------------|
| Contract sum | £3,879,523 |
| Variations | £297,501.69 |
| Disrupted labour | £1,444,946.32 |
| Additional claim for disrupted labour | £126,624.40 |
| Plant and preliminary costs | £87,737.08 |
| Knowles's costs | £487,196.43 |
| <u>Less 12.6% reduction for commercial</u> | - £270,459.53 |
| Overheads @ 9.4% | £201,126.07 |
| Profit @ 12.4% | £291,272.10 |
| Interest | <u>£273,565.95</u> |
| SUBTOTAL | £6,819,033.51 |
| Less previous payments | <u>£3,488,022.94</u> |
| TOTAL | £3,331,010.57 |

31. The contract sum and cost of variations were agreed, and it was agreed that these sums were reasonably incurred and payable as service charges. After allowance for VAT refunds paid to Argent Mr Unschorfer said, and it was not disputed, that the sum of £570,879.16 was due to Argent by way of amounts unpaid for the contract sums relating to Phases 1 and 2 and variations and that this sum was reasonably incurred and payable as service charges.

32. The disputes related to Argent's claims in respect of disruption, to interest, and to the fees which it was liable to pay to Knowles for preparing its case for submission to the adjudicator. We will consider them separately.

The claim for disruption

33. The liquidators relied on the evidence of John Eleftheraki and Mr Rainsberry.

34. Mr Eleftheraki is a director of PBSS Ltd. He was and is employed by Argent as contracts manager in relation to the PRP and other projects, and he provided a witness statement for use in Mr Bingham's adjudication. In his statement prepared for the adjudication he had said that Argent had been hampered in its performance of the contract by Bellnorth's default in providing access to the flats and commercial premises and its failure to provide Argent with accurate drawings, but in the evidence he gave to us he said that Bellnorth did all it could to afford Argent access to the flats and that the inaccurate drawings were relevant to variations but not to the disruption claim. He gave a graphic and convincing description of the massive disruption caused mainly by the unexpected discovery of asbestos in risers and under floorboards, difficulties in shutting down risers, and changes of mind and obstructive behaviour on the part of some of the residents. Of the disruption he said generally: "sometimes it was our fault and sometimes it was [the tenants'] fault". Asked why he had put the facts somewhat differently in his statement to the adjudicator he said "we have to blame people so that we can get the money". Asked for his estimate of the percentage of Argent's claim which arose from the landlord's default he said 10 per cent. He said that representatives of the tenants, who included Mr Hill, had come to see Argent's representatives in January 2011 after the liquidation of Bellnorth. They had said that they were happy with Argent's work and wanted Argent to be paid and they had made an offer to settle but it was inadequate. He said that Argent's tender was not too low for the work itself, but if Argent had

known of the previous difficulties between landlord and tenants in Dorset House the tender would have been £2 million higher. He said that if Argent had to go to arbitration it would, but that he would be happy to reach any reasonable compromise. He said that if Argent was not paid soon it would have to go into liquidation, and that he believed that some of the tenants were cynically hoping that, by refusing to pay, they would cause Argent to go out of business.

35. Mr Rainsberry explained the methodology which Knowles had used to formulate Argent's claim for disruption, which was the subject of a detailed report dated 12 August 2010 ("the Knowles Report") submitted to the adjudicator. He said that to complete the PRP on time Argent had used approximately twice the workforce it had planned to use. In order to determine whether the increased labour was due to disruption or to under-tendering in the first place, Paul Lomas Clarke FRICS (and also a qualified plumber) of Knowles Ltd, had analysed a sample of the disruptive events (collated in Appendix 28 to the Knowles Report) in order to determine whether the three categories of labour (builders, plumbers and carpenters) allowed for in Argent's tender had been adequate. He had done this by calculating the labour which should have been allowed for, by reference to *Spon's Mechanical and Electrical Services Price Book*, of the man-days needed to carry out the pipeworks in four sample zones and comparing the result with the actual timesheets, and had concluded that the level of productivity which Argent had allowed for in its tender was, on average, 6% less than was necessary to complete the works on time. The actual productivity was then modified to take account of variations, absenteeism and Argent's own disruption. All disruptive events for each of the three types of labour he then plotted against actual productivity, and the cost of lost productivity was calculated according to a mathematical formula set out in paragraph 73 of the Knowles Report.

36. Mr Rainsberry said that in preparation for the present hearing he had had two meetings with Matthew Molloy MSc FRICS FCIOB FCIArb, the quantity surveyor instructed by the tenants to give expert evidence, and Russell Gillespie, a quantity surveyor and the managing director of Heasmans, whom Bellnorth had

instructed to negotiate with Argent, and, in the light of their discussions and further information which had been provided, Argent's claim had changed marginally from that which it had put before Mr Bingham, and, in particular, the claim for disrupted labour had been increased by £126,624.40 (the additional claim for disrupted labour listed in paragraph 30 above) based on actual finish times given on work invoices. He said that any deficiency in the drawings which the landlord had supplied to Argent would be reflected not in the disruption claim but in the variations, which were not disputed.

37. Cross-examined by Mr Healey, Mr Rainsberry denied that Argent's claim was global and liable, if disputed, to be rejected for that reason. He said that Knowles's approach had been based on the contemporaneous records, which were unusually comprehensive. He said that he disagreed with Mr Molloy's approach in a number of respects which included what he considered to be excessive adjustments to the labour which should have been tendered for in respect of time for fixing flexible pipes under floorboards and for starting and finishing work each day. He said that Mr Gillespie's approach could be regarded as "ultra-global" because he had based his productivity analysis on invoiced labour and, if an invoice was missing, he had ignored the labour. He said that he was not saying that Argent would get every penny it claimed in a contested negotiation or arbitration, and he agreed that if Bellnorth had not gone into liquidation there would in all probability have been a successful negotiation in which a compromise figure would have been agreed.

38. Mr Molloy gave evidence. His preliminary opinion as expressed in his report and in his evidence in chief was that the disruption claim was unreasonable because it was based on an unrealistic assessment of the time which Argent should have taken to complete the works and because Knowles's assessment was based on a theoretical methodology which artificially inflated the claim. He said that the maximum which ought to be allowed for disrupted labour, based on a maximum of some £676 per disruptive event, was £124,457.50, but that bearing in mind the circumstances, which included design team errors and the

failure to obtain listed building consent before starting the works, Bellnorth had not established that the tenants were liable to pay any more than had already been determined to have been reasonably incurred in the tribunal's decision of 31 July 2010. He said that the level of variations was as he would expect in a contract of this nature and he did not take issue with that aspect of the claim. He did not take issue with Mr Rainsberry's proposed amounts for overheads and profit but did not agree that they were recoverable.

39. As the hearing proceeded Mr Molloy revised his opinion. He said that he considered that Argent had under-tendered by some £370,000 but he accepted that if the events relied on in support of the claim were factually correct they would have caused disruption and he concluded that in a contested adjudication or arbitration Argent would have been awarded £741,043 for disrupted labour, overheads and profit and about £50,000 for plant and preliminaries, less an allowance for the commercial element but plus VAT, resulting in a total award of £1,491,044.75, plus interest, and plus, possibly, Knowles's fees, and plus VAT. He, like Mr Rainsberry, agreed that, if Bellnorth had not gone into liquidation, it was probable that a deal would have been done between Argent and Bellnorth.

40. When Mr Molloy was cross-examined by Mr Unsdorfer it emerged that Mr Molloy had unwittingly made a number of incorrect assumptions about the works. Most significantly he had wrongly assumed in his calculations that it had been for the plumbers to put notches in the underfloor joists to accommodate the flexible pipes, whereas that work had been carried out by the carpenters. That incorrect assumption had significantly affected Mr Molloy's proposed allowance for undertendering, and, mainly for that reason, Mr Healey in his final submissions invited us to accept Mr Gillespie's proposed deduction of 10 per cent for undertendering and thus his quantification of the claim for disrupted labour.

41. Mr Gillespie gave evidence. He said that he had been personally involved the early stages of Bellnorth's negotiations with Argent, and had spent many days in reviewing the documents at that time and had had a number of meetings

relating to the negotiations. He said that in August 2010 legal advice had been given to Bellnorth to the effect that Argent's claim was weak in several respects, namely that it was arguable that the claim was "global" and liable to be struck out for that reason, that the employment of PBSS was in breach of contract, and that profit, interest and Knowles's costs could not be recovered as a matter of law.

42. Mr Gillespie said in his written report, attached to Mr Rainsberry's witness statement (marked "without prejudice" but put before us and read without objection), that if profit on the claim, interest and costs were recoverable, Argent's total claim could be in the order of £2,000,000, excluding liability for interest after January 2011. He said that if Parkgate Aspen were in a position to challenge Argent's claim in an arbitration it would have to obtain legal advice, instruct a costs consultant, programme expert and expert witnesses and the costs which it would incur could be in the order of £500,000, excluding the costs which would have to be paid to Argent if it won. His conclusion was that, while there remained some doubt about whether Argent could fully substantiate its claim in the event of a contest, it was clear that Argent's claim for disruption was strong, and it would be sensible to settle the whole claim for in the order of £1,600,000 to £2,000,000.

43. In his oral evidence Mr Gillespie said that Knowles's approach to evaluating the disruption claim was complex and difficult to follow, and was based on theory and not on fact. His own approach had been to seek to establish the actual loss which Argent had suffered, which he had abstracted from the invoices, and, if invoices were not available, from the timesheets, and then to compare the result with the cost allowed for carrying out the work. He had concluded that the actual cost of disrupted labour, additional disrupted labour, and associated plant and preliminaries was £1,143,361, a sum which included disruption attributable to the commercial element. He said that he considered Mr Molloy's figures to be wrong, in particular because his allowance of 27 per cent for under-tendering was excessive, and he believed that his own approach was preferable to that of Mr Rainsberry because it was based on actual costs and not on theory. He said

that if there were to be a commercial settlement it would be likely to be at a figure between his and Mr Rainsberry's.

44. Ms Brown submitted that Argent possessed all the merits and deserved to be paid every penny it claimed and to be paid forthwith by the companies which stood behind Bellnorth and DHRL. She said that Argent had entered into a contract with a company of no substance but had not insisted, as it could have done, on guarantees of payment because those who spoke for Bellnorth promised that it would be paid. She invited us to accept Mr Rainsberry's evidence.

45. Mr Healey, while inviting us to accept Mr Gillespie's approach to the quantum of the claim for disruption, submitted that that should not lead us to the conclusion that the whole of the claim was recoverable from the tenants. Such recovery depended, he submitted, on whether the heads of the claim were recoverable under the lease and whether the costs were reasonably incurred. He submitted that the noise and the mess caused by the works under the floorboards could not of itself justify a claim for disruption because those factors were, or ought to have been, allowed for in the revised contract price for Phase 2 which was re-negotiated when the requirements of Westminster City Council became known. Moreover, he submitted, the costs occasioned by the fact that Bellnorth did not defend the adjudication were not reasonably incurred and therefore not recoverable, and costs occasioned disruption such as that described by Mr Eleftheraki in paragraph 26 of his witness statement, which arose from the landlord's failure to provide access to the flats at the proper time ought not to be passed to the tenants because they were due either to Bellnorth's default in providing access which it was contractually obliged to provide, or to Argent's failure to allow for such difficulties in its tender. He submitted that if individual tenants had caused disruption it was for the landlord to sue those tenants to recover the loss, which ought not to be passed to the tenants in general.

46. Mr Healey submitted that in order to determine what part of the sum attributable to disrupted labour was recoverable from the tenants as a whole it was necessary for the tribunal to decide what would have been the result if the landlord had funded the contract with Argent and if the adjudication had been properly contested. He submitted that Mr Rainsberry's method of quantifying the claim was not based on fact but on theory, was designed to get the best possible result, and should be rejected. He submitted that both Mr Molloy's and Mr Gillespie's methods produced meaningful results but he accepted that Mr Gillespie's suggested allowance of 10 per cent for undertendering was more realistic than that of Mr Molloy and invited us to accept it. He therefore submitted that £1,143,361, suggested by Mr Gillespie, was the amount which would have been agreed in negotiations if, in the absence of the liquidation, they had proceeded. He accepted that such a figure would have taken account of any default by Argent, but he submitted that a "broad brush" deduction of 10 per cent should be applied to reflect the inherent likelihood that some of the disruption was caused by the landlord's default. He accepted that such default did not include the landlord's failure to obtain listed building consent before it entered into the contract with Argent, because the contrary conclusion would be inconsistent with the tribunal's decision of July 2010.

47. Mr Unsdorfer had said in evidence during the hearing relating to the application to appoint a manager that he had been very angry, and, indeed, had temporarily resigned as managing agent, when he heard that Bellnorth was to go into liquidation. Nonetheless, he now submitted, the suggestion that the liquidation was Bellnorth's fault, or the fault of those who controlled it, was wrong. He said that Bellnorth owned no flats in the block and had virtually no commercial interest in the block, but that Philip Wallis (who gave extensive evidence at the hearing of the application to appoint manager) had put enormous effort into refurbishing the block because he believed in the project. He said that Bellnorth had applied to the tribunal for approval of the PRP in advance and had received such approval, and the idea that Bellnorth ought to have underwritten the project was ludicrous. He said that the situation was stable when Argent entered into

the contract. There was a clear covenant on the part of the leaseholders to pay for the works which had been approved by the tribunal, and Argent was entitled to believe that it was working for the tenants, who would pay for the works. The problems, he submitted, had arisen wholly from the unforeseen consequences of Mr Hill's inexplicable letter to Westminster City Council. Without it, he submitted the disruption would not have arisen.

48. Mr Unsdorfer invited us to accept Mr Gillespie's evidence that Argent had under-tendered by about 10 per cent, but he submitted that in other respects Argent could not be criticised. He said that the record of disruptive events illustrated that Argent had employed labour wisely and had learned to improvise in the face of disruption as the works proceeded. He said that the disruption claim did not arise from the need to run the pipework under floorboards, which had been allowed for in the revised contract price, and that all the disruption arose either from denial of access by residents or from the unexpected discovery of asbestos in risers and under floorboards. In relation to access, he said that the landlord had appointed a tenant liaison officer, had done everything that could possibly have been done to arrange access to the flats, and could not properly be criticised in any respect.

49. Mr Unsdorfer accepted that the tribunal's approach should be to seek to determine the result of a hypothetical negotiation between Bellnorth and Argent, but he submitted that the result would not have been an equalsplit between the amount proposed by Knowles and that proposed by Heasmans but about two thirds to one third in Argent's favour because Bellnorth would have taken account of the fact that the lease probably does not permit recovery of legal fees as a service charge. He therefore invited us to conclude that the negotiated figure for disruption would have been in the order of £1,428,000, all of it, he submitted, recoverable from the tenants with the exception of the agreed 12.6 per cent attributable to the commercial element.

Decision

50. We accept Mr Unsdorfer's submission. It was not, in the end, disputed that the disruption claim was part of *the cost of the works* which fell within the landlord's covenant and was in principle recoverable as a service charge. The only question was the extent to which the disruption claim was reasonably incurred. We accept and adopt the approach advocated by Mr Healey and Mr Unsdorfer, and conclude that we have to decide, on the basis of the evidence given to us, what would have been the likely result of a negotiation between Argent and Bellnorth. We accept that Mr Gillespie's approach, based on Argent's actual loss, is realistic and we prefer his approach to that of Mr Rainsberry which, while impressively detailed, is theoretical. We also accept Mr Unsdorfer's submission that Bellnorth, even if had not been in liquidation, would have been in a weak negotiating position because of the deficiencies of the lease which make recovery of legal fees doubtful. We accept that the figure which would have been arrived at in negotiation for disrupted labour, plant and preliminaries would have been between the £1,143,361 with no allowance for overheads and profit proposed by Mr Gillespie and the £1,659,307 plus overheads and profit proposed by Mr Rainsberry. Our assessment is that the sum which would have been agreed in negotiation as appropriate in respect of the disruption claim is £1,500,000 plus, say £150,000 overheads and profit. From this sum must be deducted the agreed 12.6 per cent for the commercial element, but other elements fall to be added and are also payable as a service charge.

51. Insofar as any of the costs of disruption were attributable to default by Argent, and Mr Eleftheraki agreed that Argent was not wholly free from blame, in our view that any element of blame is be fully accounted for in the hypothetical negotiated figure which we have determined. We do not accept that any of the disruption claim can properly be attributed to the landlord's default in relation to the works. We agree with Mr Healey's realistic concession that to blame the landlord for its failure to obtain listed building consent before entering into the contract would be inconsistent with the decision of the previous tribunal, and,

indeed, we respectfully agree with that aspect of the decision because we are satisfied that the landlord could not reasonably have been expected the events which followed upon Mr Hill's letter to Westminster. We are satisfied that Bellnorth and its managing agents did all they reasonably could to provide access to the flats, and we do not consider that it would be realistic and proportionate to expect the landlord now to take action against individual tenants or occupiers for failing to give access to their flats at the proper time. We do not consider such default as there may have been on the part of Bellnorth in providing accurate drawings to Argent is of any relevance to the disruption claim, notwithstanding what Mr Eleftheraki said in his written statement to the adjudicator. The relevance of the drawings, as the quantity surveyors agreed, was to variations, and variations were agreed. Nor do we accept that Bellnorth was at fault in failing to foresee that there might be asbestos hidden under the floorboards, because to establish that would have caused similar disruption to that occasioned by the PRP itself. We therefore reject Mr Healey's suggested deduction of 10 per cent for landlord's default.

Interest and costs

52. These elements may be considered together. Both arise only because Argent was not paid when it should have been paid. A large proportion of both have arisen because of the liquidation.

53. Mr Rainsberry produced a paper prepared by Peter Giles of Knowles on the subject of whether costs incurred by Argent in instructing Knowles to represent it in the adjudication are recoverable under the apparently somewhat unusual form of building contract between Argent and Bellnorth, and also whether such costs are in principle recoverable as a service charge from the tenants under their leases. It was not seriously disputed that Mr Giles was correct in his conclusion on the first question, and we accept his opinion that Argent is entitled under its contract with Bellnorth to recover its costs of presenting the claim to the

adjudicator. It is not, of course, entitled to recover its costs referable to the hearing before the tribunal. The second question asked of Mr Giles is, we think, a matter for us. It is not in doubt that Argent is entitled as against Bellnorth to interest at the contractual rate on whatever sum is due to it between the date when payment should have been made and, at least, the date when Bellnorth went into liquidation.

54. On the question whether costs and interest are recoverable from the tenants as a service charge, Mr Healey submitted that neither element was recoverable under the lease. He said such elements were not costs of providing a service, but costs of not paying for a service, and that to say that such costs were recoverable would be stretching the language of the lease much too far. He submitted that Knowles's fees would have been taken into account in the negotiation between Argent and Bellnorth and that in any event would be wholly inappropriate to permit Argent to recover the whole of the fees payable to Knowles.

55. Mr Unsdorfer submitted that costs and interest were part of the costs of the works and were accordingly recoverable under the lease. He said that the amounts certified to be due to Argent would have been paid on time but for the service charge strike organised by the tenants' association, and that interest was paid to Argent to keep its team on the site to avoid what he called "the terrible scenario" which would have followed if Argent had walked off the site as it was quite entitled to do. Mr Healey submitted in reply that it was not open to us on the evidence to find that the primary or any cause of the failure to pay Argent was a service charge strike by the tenants, although he did not disagree with Mr Unsdorfer's evidence that some £2,000,000 of service charges were unpaid at the time when Argent ought to have been paid.

Decision

56. We are satisfied that both Argent's costs and contractual interest would have been taken into account in the hypothetical negotiations which would have taken place if Bellnorth had not gone into liquidation. Argent's costs would have been much less than they in fact were if there had been no need for an adjudication, but it would have expected a contribution towards its costs of preparing its claim and interest to the date of settlement and our best estimate of what those costs would have been is in the order of £100,000, and they would have settled at around £50,000. In our view this figure is part of the cost of the works and is recoverable as a service charge under the lease. It is inevitable that a contractor who is not paid will incur costs in recovering what he is owed and that interest will accrue on the debt, and, certainly if these elements are covered by the contract, they are, in our view, properly regarded as part of the cost of the works.

57. The position in respect of costs incurred and interest arising after the liquidation is, we consider, different from costs and interest which arose earlier.

58. It is clear to us from the evidence that there were several factors in the decision which Philip Wallis took to allow Bellnorth to go into liquidation without paying Argent.

59. One was that many, although not all, the tenants had refused to pay their service charges. We do not have the information we would need to enable us to decide whether there was an organised service charge strike, and, if so, who organised it, who refused to pay, and who paid. It would be disproportionate to conduct such an enquiry even if it were necessary. It is sufficient to say that we are satisfied that a large number of tenants failed to pay their service charges, resulting in massive arrears, and we are satisfied that that was a very significant factor in Mr Wallis's decision to allow Bellnorth to go into liquidation. It is relevant, however, to observe that those who controlled Winllan (Dorset) Ltd and Nome Ltd, two companies in the same group as Bellnorth, which owned, between them, some 17 flats in the block, had also decided not to pay their

debt to Argent since the liquidation, are too remote from the costs of the works which are recoverable under the lease.

Conclusions in respect of the costs of the pipework replacement programme

63. It thus appears to us that the position is as follows.

64. Mr Unsdorfer said, and we accept, that the amount owed to Argent under the contracts and for variations but less a set-off in respect of the VAT refund which Argent received, is **£570,879.16**. Our understanding is that this is not subject to a deduction for the commercial element. In addition, we have determined that the amount which would have been agreed in negotiations with Argent in respect of disruption to the Phase 2 works is £1,650,000 including overheads and profit, from which 12.6 per cent, or £207,900, falls to be deducted for the commercial element, leaving a balance of **£1,442,100**. To this we add **£50,000** in respect of the amount which would have been agreed in negotiation in respect of costs and interest. The total, which we determine to be payable by the tenants as service charges, is **£2,062,979.16, say £2,062,980**.

The second issue: reserve fund contributions

65. DHRL had in its application asked for a determination that the reserve fund contributions demanded of the tenants in respect of the years ended 29 September 2009, 2010 and 2011 were reasonable in amount, but before the hearing DHRL and the tenants reached agreement that DHRL would for the time being not demand any reserve fund contributions but would raise funds on a project-by-project basis as and when it was necessary to do so and accordingly it was agreed that DHRL would not seek a determination on this issue. Ms Brown, however, asked us to determine the question.

66. In our view the liquidators whom Ms Brown represents have no right to be heard on this issue because they have no interest to protect. Any reserve funds would be held on statutory trusts for the tenants and the liquidators would have no claim on them. We accept that the agreement of DHRL and the tenants deprives us of jurisdiction on this issue, or, alternatively, that there is no need for the issue to be determined.

CHAIRMAN.....

DATE: 16 July 2012