UPPER TRIBUNAL (LANDS CHAMBER)

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TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

LEASEHOLD ENFRANCHISEMENT – Flat – Leasehold Reform, Housing and Urban Development Act 1993 – grant of new lease – section 57(6) – modification of term of existing lease – lessee's liability to service charge contribution on fixed percentage basis

IN THE MATTER OF AN APPEAL AGAINST A DECISION OF THE FIRST-TIER TRIBUNAL (PROPERTY CHAMBER)

BETWEEN:

MICHAEL ROSSMAN

Appellant

and

THE CROWN ESTATE COMMISSIONERS

Respondents

Re: Flat 124A
4 Whitehall Court
London S.W.1

Before: The President, Sir Keith Lindblom

Sitting at: Upper Tribunal (Lands Chamber), Royal Court of Justice, Strand, London WC2A 2LL
on 28 January 2015

The appellant in person
Mr Jonathan Upton, instructed by Pemberton Greenish LLP, for the respondents

The following cases were referred to in this decision:

Morgan v Fletcher [2009] UKUT 186 (LC)
Rossman and others v Crown Estate Commissioners, LON/00BK/LVL/2011/0013, unreported
Kilmartin SCI (Hutton House) Limited v Safeway Stores Plc [2006] EWHC 60 (Ch)
Lucie M. v Worcestershire County Council and Evans [2002] EWHC 1292 (Admin)
Havering London Borough Council v MacDonald [2012] UKUT 1454 (LC)
Howard de Walden v Aggio [2009] 1 A.C. 39
Gordon v Church Commissioners for England LRA/110/2006, 25 May 2007, unreported
Director General of Fair Trading v First National Bank [2001] UKHL 52
Davies v Howard de Walden Estates Ltd., 14 October 1998, unreported
Cadogan v Chelsea Properties Ltd., 25 June 2008, unreported
Waitt v Morris [1994] 2 E.G.L.R. 224
Burchell v Raj Properties Ltd. [2013] UKUT 0443 (LC)
R. (on the application of Khatun) v Newham London Borough Council [2005] Q.B. 37

DECISION

Introduction

1. The main issue in this appeal is whether, under section 57 of the Leasehold Reform, Housing and Urban Development Act 1993, the term of an existing lease which apportions the lessee's liability to a service charge contribution on a fixed percentage basis ought to have been modified in his new lease to what he contends would be a fair proportion based on the floor space of his flat, given that the aggregate of service charge contributions for which the lessees are liable is now well in excess of 100% of expenditure.

2. The appellant, Mr Michael Rossman, is the lessee of Flat 124A at 4 Whitehall Court, London S.W.1. The respondents, the Crown Estate Commissioners, are the freehold owners of the building. Mr Rossman appeals against the decision of the First-tier Tribunal (Property Chamber), dated 23 September 2013, by which it decided the terms of acquisition of a new lease of Flat 124A under section 48(1) of the 1993 Act.

3. Permission to appeal against the First-tier Tribunal's decision was granted by the Deputy President on 26 February 2014.

4. At the hearing Mr Rossman presented his appeal himself. The Crown Estate Commissioners were represented by Mr Jonathan Upton.

Section 57 of the 1993 Act

5. Chapter II of Part I of the 1993 Act gives the tenant of a flat the right, subject to paying a premium, to be granted a new lease of the flat in substitution for the existing lease, for a term expiring 90 years after the term date of the existing lease. Section 57, "Terms on which new lease is to be granted", provides:

> "(1) Subject to the provisions of this Chapter (and in particular to the provisions as to rent and duration contained in section 56(1)), the new lease to be granted to a tenant under section 56 shall be a lease on the same terms as those of the existing lease, as they apply on the relevant date, but with such modifications as may be required or appropriate to take account –
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> (a) of the omission from the new lease of property included in the existing lease but not comprised in the flat;
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> (b) of alterations made to the property demised since the grant of the existing lease; or
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> (c) in a case where the existing lease derives (in accordance with section 7(6) as it applies in accordance with section 39(3)) from more than one separate leases, of their combined effect and of the differences (if any) in their terms.
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> …
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> (6) Subsections (1) to (5) shall have effect subject to any agreement between the landlord and tenant as to the terms of the new lease or any agreement collateral thereto; and either of them may require that for the purposes of the new lease any term of the existing lease shall be excluded or modified in so far as –

(a) it is necessary to do so in order to remedy a defect in the existing lease; or

(b) it would be unreasonable in the circumstances to include, or include without modification, the term in question in view of changes occurring since the date of commencement of the existing lease which affect the suitability on the relevant date of the provisions of that lease."

The facts

6. The essential facts are set out in the Crown Estate Commissioners' statement of case. They are not in dispute.

7. 4 Whitehall Court is one of two blocks on the south side of a late Victorian development of several buildings overlooking the River Thames in Westminster. The buildings in the development now contain both residential accommodation and commercial uses. They have a basement, a ground floor, an upper ground floor and seven floors above, and further accommodation in towers and within the roof. Originally they contained serviced apartments, with communal facilities. In the 1960s and 70s many of the rooms and suites in the buildings were converted into self-contained flats and sold on long leases at a premium, with a ground rent and service charge. Initially, the aggregate of the fixed percentage service charge contributions amounted to 100%. Neither party to this appeal knows how the fixed percentages were calculated. Other space in the development, including the towers, was later adapted to provide more flats. These were also sold on long leases, with a ground rent and service charge. Some of the flats have since been combined to form larger dwellings, others re-arranged or sub-divided or enlarged to incorporate areas formerly within the common parts, sometimes – though not always – with an adjustment of the service charge contributions payable by the lessees.

8. As I have said, the freehold of the building is now owned by the Crown Estate Commissioners. The intermediate landlord is Whitehall Court (Investments) Ltd., under a headlease dated 12 May 1987, made between (1) the Crown Estate Commissioners and (2) Whitehall Court (Holdings) Ltd. for a term from 5 January 1981 to 4 April 2086. The headlease was assigned to Whitehall Court (Investments) Ltd., which is a company associated with Whitehall Court (Holdings) Ltd., in September 1989. Whitehall Court (Investments) Ltd. is responsible for providing the services in the building, and it collects the service charge.

9. Flat 124A is one of 115 flats at Whitehall Court now let on long leases. It was originally demised by an underlease dated 14 February 1969, made between (1) Clabon Developments Ltd. as "the Lessors", (2) Molton Builders Ltd. as "the Lessees", and (3) Whitehall Court (Holdings) Ltd. as "the Managers", for a term of 61 years beginning on 24 December 1967. Clause 3(A) of the 1969 lease provided:

> "The Lessees HEREBY COVENANT with the Managers that they the Lessees will in manner hereinafter provided pay to the Managers 0.8 per centum (hereinafter called "the Contribution") of the reasonable costs and expenses incurred by the Managers in compliance with their obligations under Clause 5 hereof together with all other costs and expenses incurred in the management of the building and other … property of which the Flat forms a part (hereinafter called "the Expenditure")".

Clause 3(B) provided that the contribution had been "pre-estimated" at £248 per annum. Clause 5 provided for the services which were to be performed by Whitehall Court (Holdings) Ltd.. By a

deed of re-grant and variation dated 4 August 1989, made between (1) Whitehall Court (Holdings) Ltd. as "the Lessors" and (2) Glen Richard Moreno and Cheryl Eschbach Moreno as "the Lessees", Flat 124A was demised for a term of 99 years from 25 March 1987 on terms similar to those of the 1969 lease. Under clause 7 of the deed of re-grant and variation clauses 3(A), 3(B) and 5 of the 1969 lease remained "in full force and effect".

10. Mr Rossman took an assignment of the lease of Flat 124A on 16 August 2006.

11. The aggregate of the service charge contributions payable under the leases at Whitehall Court is now 129% of expenditure. However, the liability to pay a service charge contribution at the level specified in each lease is adjusted in an extra-contractual scheme, so that the total service charge collected is 100% of what is actually spent. The effect of this abatement is that none of the lessees pays more than he has contractually agreed to pay, and most of them, including Mr Rossman, pay less.

12. On 25 March 2011, by a notice of claim served under section 42 of the 1993 Act, Mr Rossman gave notice of his intention to acquire a new lease of Flat 124A. The notice of claim proposed a premium of £9,319.50 for the freeholder and £7,030.50 for the intermediate leaseholder. The proposed terms, in paragraph 7 of the notice, were "[a] term expiring 90 years from the date of expiry of the existing lease, at peppercorn ground rent, and otherwise on similar terms with appropriate updating and as agreed in DRAFT form with the Crown Estate as of January 2009". Clause 2.21 of the draft new lease was in terms similar to clause 3(A) of the 1969 lease. On 16 May 2011, by a counter-notice under section 45 of the 1993 Act, the Crown Estate Commissioners as the landlord for the purpose of Chapter II of Part I of the 1993 Act admitted Mr Rossman's right to acquire a new lease. Paragraph 4 of the counter-notice stated that "[save] as specified in paragraph 5 below the proposals contained in the Tenant's Notice are acceptable". Paragraph 5 proposed a premium of £68,228 for the freeholder and £2,947 for the intermediate leaseholder. On 14 November 2011 Mr Rossman applied under section 48(1) of the 1993 Act for the Leasehold Valuation Tribunal to determine the premium to be paid and the other terms of acquisition which remained in dispute.

The proceedings under section 35 of the Landlord and Tenant Act 1987

13. By the time Mr Rossman made his application under section 48(1) of the 1993 Act, he and 36 other lessees in Whitehall Court were also engaged in proceedings before the Leasehold Valuation Tribunal under section 35 of the Landlord and Tenant Act 1987, seeking to vary the service charge provisions in their leases. The section 35 application was made in August 2011. Cross-applications under section 36 of the 1987 Act were made by the Crown Estate Commissioners in March 2012, and by Whitehall Court (Investments) Ltd. in April 2012. A number of other lessees of flats in Whitehall Court became respondents to the section 36 proceedings.

14. Section 35(1) of the 1987 Act, as amended, provides that "[any] party to a long lease of a flat may make an application to the appropriate tribunal for an order varying the lease in such manner as is specified in the application". Section 35(2) provides that the grounds on which a party to a long lease may apply for an order varying the lease "are that the lease fails to make satisfactory provision with respect to" one or more of seven matters, which include, under subsection (2)(f), "the computation of a service charge payable under the lease". Section 35(4) provides that "[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" (see *Morgan v Fletcher* [2009] UKUT 186 (LC)).

15. Section 36(1) provides that where an application is made under section 35 by any party to a lease, "any other party to the lease may make an application to the tribunal asking it … to make an order which effects a corresponding variation of each of such one or more other leases as are specified in the application". Under section 36(3) the grounds on which such an application may be made are "(a) that each of the leases specified in the application fails to make satisfactory provision with respect to the matter or matters specified in the original application", and "(b) that, if any variation is effected in pursuance of the original application, it would be in the interests of the person making the application under this section, or in the interests of the other persons who are parties to the leases specified in that application, to have all of the leases in question … varied to the same effect."

16. The section 35 application in this case was made on the grounds that the aggregate of the fixed percentage service charge contributions of the leases of flats in Whitehall Court was about 130%, and that the apportionment ought to be varied from the fixed percentages originally agreed to different percentages based on floor area.

17. On 11 February 2013 the Leasehold Valuation Tribunal issued its decision refusing to order any variation (*Rossman and others v Crown Estate Commissioners*, LON/00BK/LVL/2011/0013, unreported). It discussed the issues in the section 35 application in paragraphs 122 to 141. It acknowledged that its discretion was wide (paragraph 123). But it went on to say this (in paragraph 127):

> "In our judgment on an application to vary the terms of a lease under section 35 or section 36 of the [1987] Act we should adopt a minimalist approach. We should resist the temptation to re-write the agreement or impose what might be termed a fairer but different agreement. On the contrary, we should strive to try and keep as closely as possible to the original contractual scheme; to try and keep the nature and extent of the variations to the absolute minimum consistent with the objective of the promoters of the Act and the intentions of Parliament in ensuring the policy objectives. In particular if there is to be an intervention it should be one [that] will not only improve upon the current position but actually cure, or at least substantially cure, the defect and have a real effect on the upkeep of the building and fitness for habitation of the flats within it."

The Leasehold Valuation Tribunal accepted that it had "to consider not only the contractual scheme but also the manner in which the contractual scheme has been operated and then to consider whether intervention is appropriate"; and that "if a block were not being properly maintained or if the flats within it were not fit for habitation intervention would be justified but not otherwise" (paragraph 128). It saw nothing to suggest that Whitehall Court was not being properly maintained (paragraph 129). And in paragraph 130 of its decision it said this:

> "None of the parties pretended that the current scheme was perfect. It patently is not and it is not a scheme that will be put in place if one were starting from scratch. [Whitehall Court (Investments) Ltd.] has put in [place] a voluntary abatement scheme so that it only recovers 100% of expenditure. We accept that the abatement scheme is not itself perfect and it has some anomalies. Nevertheless it was put to us and we accept that it works in that the block is

maintained and the landlord does not over recover. It is also self-evident that each lessee pays less than the contractual contribution set out in their respective leases save perhaps for the commercial tenant of 3A which evidently pays 1.10% instead of a fixed £100 per year."

This, therefore, was not an appropriate case for intervention to disturb "the contractual scheme as adjusted and operated by [Whitehall Court (Investments) Ltd.]" (paragraph 131).

18. The Leasehold Valuation Tribunal went further. In paragraphs 132 to 135 it said:

> "132. Even if we were minded to intervene we were far from satisfied that the variation proposed by the Applicants would be appropriate and bring about any material improvement. The Applicants propose changing a fixed percentage in the lease to a different percentage; one based on floor area. Floor area is one of several different ways in which the proportion of service charge contributions can be determined. There are several different methods by which such proportions can be determined. It is debateable whether any of them is fair to all of the lessees concerned. In our experience each method available has some benefits and some dis-benefits to one or more lessees. There was no evidence put to us that floor area was a fair method or the fairest method; it is simply one of several methods that might be deployed.
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> 133. It has been said that sometimes floor area is appropriate for a mixed use development. Such schemes often separate out the commercial element from the residential; where, for example[,] there are commercial retail units on the ground floor and flats on upper floors. The subject development is far more complex than this in that the commercial units and those to which Part II [of the Landlord and Tenant Act] 1954 apply are very much intermingled with the pure residential leases throughout the development. For example[,] many of the units occupied by the Farmers Club are on upper floors.
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> 134. We find that a move to a floor areas basis would be expensive for both the landlord and the lessees. Even with the benefit of the RICS Code of Measuring Practice there is significant scope for dispute over precise measurements. It is not a simply a question of [Whitehall Court (Investments) Ltd.] engaging a firm to carry out a measurement exercise … . It cannot be certain that all lessees would agree the measurements [put] forward. It was demonstrated in *Kilmartin SCI (Hutton House) Limited v Safeway Stores Plc* [2006] EWHC 60 [(Ch)] that there is scope for complex and expensive litigation over the proper measurement of quite small areas of space.
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> 135. In our judgment a floor area basis of determining service charge contributions is not what any of the lessees contracted for. It would be expensive to implement. It would undo and undermine specific contractual arrangements, for example those affecting flats 148 and 148a and it cannot be applied to any of the units to which Part II LTA 1954 [applies]. For these reasons alone we would reject a variation to a floor area basis of determining the fixed contributions payable by the residential lessees."

19. In paragraph 136 of its decision the Leasehold Valuation Tribunal said that "[even] if floor areas could be agreed it would still be necessary to insert a figure in the Applicants' proposed form of variation to separate out the commercial element or what might be regarded as the commercial element, as to which there are some uncertainties". The applicants preferred an arrangement in which there would be "no rebate to any of the commercial lessees". But the Leasehold Valuation Tribunal said that this would "give rise to a step change to a practice in operation for in excess of ten years", that there could be "no certainty that the commercial lessees would accept it", that there might be "estoppel issues if leases have been granted, renewed or assigned on the basis of a scheme

that has been in operation for so long", and that, if there were successful challenges to this new arrangement, there would be "an under-recovery and the risk that the development might not be properly maintained, a mischief the Act was designed to avoid". The parties could not agree the form of such a variation (paragraph 137). The Leasehold Valuation Tribunal was "far from satisfied that the Applicants' proposed variation [was] workable" (paragraph 138). It identified several practical problems in the implementation of such arrangements (paragraphs 139 to 140). And it concluded, in paragraph 141:

> "Given the matters set out above and, in particular[,] that we are not satisfied that the [Applicants'] proposed variation is workable and an improvement over the current scheme as operated by [Whitehall Court (Investments) Ltd.], and also bearing in mind the disproportionate cost and risks inherent in the implementation of the Applicants' proposed variation we conclude that it would not be reasonable in the circumstances for the variation to be effected."

20. On 29 May 2013 the Leasehold Valuation Tribunal refused permission to appeal against its decision, as did the Tribunal on 9 September 2013.

The decision of the First-tier Tribunal

21. Before the hearing of Mr Rossman' application under section 48(1) of the 1993 Act the parties had agreed the premium payable to the freeholder, the amount payable to the intermediate leaseholder, and all the other terms of the new lease, except the service charge contribution.

22. At the hearing before the First-tier Tribunal on 2 July 2013 Mr Rossman argued that because Whitehall Court (Investments) Ltd. was now able to recover more than 100% of service charge expenditure, clause 2.21 of the draft new lease should be modified under section 57(6) of the 1993 Act, so that the service charge contribution would be a fair proportion based on square footage – namely 0.287230%. He made three main submissions: first, that the existing terms of the lease relating to service charges contravened the Unfair Terms in Consumer Contracts Regulations 1999, and that, for this reason and others, clause 2.21 should be regarded as a "defect" in the lease; secondly, that it was unconscionable for a landlord to have absolute discretion in setting the tenants' liability for service charges extra-contractually; and thirdly, that the existing arrangements for setting service charges at Whitehall Court breached the guidelines issued by the R.I.C.S.. The Crown Estate Commissioners argued that the service charge provisions of the new lease should be in the same terms as the existing lease, unless the parties agreed different terms. They contended for the rate of 0.8%.

23. In its decision the First-tier Tribunal determined that the service charge provisions of the new lease should be the same as in the existing lease unless the parties agreed different terms. In paragraph 11 it referred to the decision of the Leasehold Valuation Tribunal on the application under section 35 of the 1987 Act, and in paragraph 12 it said this:

> "On that occasion, the Applicant had proposed the same service charge variation he seeks in these proceedings and as part of his case had advanced the same argument as set out at point (b) above [i.e. "that the service charge provisions operated extra contractually, that is, the landlord has an absolute discretion in relation to the lessees' service charge liability"]. The reasons given by the Tribunal in dismissing are to be found at paragraphs 122 to 141. Essentially, the Tribunal held that whilst the present regime was not perfect, it did not amount to [a] defect that warranted the terms of the leases being varied. As part of the earlier

decision, the Tribunal also considered the extra contractual arrangements that formed part of the service charge regime. In addition the Tribunal was satisfied that the Applicant's proposed variation was not workable and an improvement on the current scheme operated by [Whitehall Court (Holdings) Ltd.]."

The First-tier Tribunal went on to say, in paragraphs 13 to 18:

"13. Whilst the earlier decision is not strictly binding on this Tribunal, it is nevertheless highly persuasive, as Mr Sheftel correctly submitted. Indeed, this Tribunal repeats and relies on the same reasoning set out in the earlier decision to find that the existing service charge terms in the Applicant's lease do not amount to a sufficiently serious defect within the meaning of section 57(6)(a) of the Act. In addition, the Applicant had not referred to any physical or legal changes since the grant of the lease as a result of which it would be unreasonable to include in the Respondent's proposed clause without modification in accordance with section 57(6)(b).

14. The Tribunal then turned to consider the arguments made by the Applicant in relation to the Unfair Contract Terms Regulations 1999 [sic] ("the Regulations") and, specifically, whether existing service charge terms infringed one or more [of] the Regulations and could be regarded as a "defect". This was not an argument that the Applicant had specifically advanced in the previous proceedings.

15. The Tribunal concluded that the service charge terms did not breach any of the Regulations and could not, therefore, be regarded as a defect within the meaning of section 57(6)(a) of the Act. Paragraph 1 of Schedule 2 of the Regulations sets out a non-exhaustive list of contractual terms that could amount to an unfair term. The Tribunal concluded that the service charge provisions in the Applicant's lease did not breach any of the terms set out in paragraph 1 of Schedule 2 of the Regulations. Mr Sheftel correctly submitted that the service charge provisions are not ambiguous or unfair to the tenant. They do not allow the landlord to unilaterally vary the tenant's liability, for example, in breach of paragraph 1(k) of Schedule 2 of the Regulations and the terms are absolute.

16. The Applicant's service charge liability was not affected by the extra contractual arrangements in place and do not, in any event, form part of the terms of the Applicant's lease. They are, therefore, not caught by the Regulations. Indeed, at paragraph 130 of the earlier decision, the Tribunal stated that the lessees in fact paid less than the contractual contribution stipulated in their leases as a consequence of this arrangement. They could not, therefore, either be regarded as being an unfair term within the meaning of the Regulations or a "defect" requiring remedying under section 57(6)(a) or being unreasonable and thereby requiring modification under section 57(6)(b) of the Act.

17. As to whether the service charge terms breached one or more of the RICS Management Code, the Tribunal had little difficulty in concluding that the provisions of the Code cannot form the basis on which the contractual terms of a lease can be varied. The RICS describe the Management Code as "guidance on best practice to practitioners" with none of the provisions mandatory. They are intended to be no more than a guide in the practice of good management and no more.

18. Accordingly, the Tribunal was satisfied that none of the exceptions set out in section 57, and in particular in subsection (6), of the Act had been met by the Applicant and it

determined that the service charge provisions of [a] new lease should be granted on the same terms as the Applicant's existing lease unless the parties agree on different terms."

Mr Rossman's grounds of appeal

24. When he granted permission to appeal the Deputy President identified "the nub" of Mr Rossman's complaint as being "whether, in considering under section 57(6) of the 1993 Act whether the terms of the new lease should be varied from those of the original lease, [the First-tier Tribunal] was entitled simply to adopt the reasons of [the Leasehold Valuation Tribunal] which had dismissed an application to vary the terms of the existing lease under section 35 [of the 1987 Act]". He added that it was "arguable that a different and more flexible approach is justified in the case of a new lease, particularly where either the factual or legal context is said to have changed since the grant of the original lease". He required Mr Rossman to file a further notice of appeal identifying the propositions of fact or law he was inviting the Tribunal to accept.

25. On 1 April 2014 Mr Rossman filed a second notice of appeal, which identified a number of "key considerations" in the appeal. These were refined in the skeleton argument he produced for the hearing of his appeal. In that skeleton argument he identified a series of questions for the Tribunal to consider, which seem to encompass all but three of the points raised in the second notice of appeal. They are, in effect: (1) whether the First-tier Tribunal misinterpreted and misapplied section 57(6) of the 1993 Act; (2) whether its decision is consistent with the relevant jurisprudence; (3) whether it took into account all of the relevant physical and legislative changes since the date of the commencement of the existing lease; and (4) whether the proposed modification of the service charge provision in the lease of Flat 124A was fair, reasonable and rational. As will be clear, these questions all go to the main issue in the appeal – whether, under section 57 of the 1993 Act, the term in the existing lease which sets the lessee's service charge contribution at 0.8% ought to have been modified in the new lease (see paragraph 1 above).

26. The other three questions were: (1) whether the First-tier Tribunal ought to have adjourned its own hearing until the application for permission to appeal against the Leasehold Valuation Tribunal's decision in the proceedings under sections 35 and 36 of the 1987 Act had been determined; (2) whether the reasons it gave for its decision were adequate; and (3) whether it was wrong to rely upon and adopt the reasoning and conclusions of the Leasehold Valuation Tribunal. I shall consider those questions briefly before turning to the main issue.

Adjournment

27. I cannot accept that the First-tier Tribunal ought to have adjourned the hearing until the parties knew whether permission would be granted for an appeal against the Leasehold Valuation Tribunal's decision. The proceedings before the First-tier Tribunal under section 57 of the 1993 Act were a quite separate process. It had to make its own decision on the application before it. There was nothing in any way unfair to the parties in its holding the hearing into Mr Rossman's application when it did and making its decision without needless delay. And in any event no prejudice arose, because permission to appeal was refused in the section 35 proceedings.

The adequacy of the First-tier Tribunal's reasons

28. The First-tier Tribunal's reasons are succinct. But they are not in my view so succinct as to be inadequate. They show that the First-tier Tribunal had identified and addressed the main issues arising under section 57. They expressly adopt the very full reasoning of the Leasehold Valuation Tribunal in its decision on the section 35 application. They address, in short form, both limbs of section 57 of the 1993 Act, and the main considerations bearing on each of those limbs. In my view they do not fall short of the standard of reasons expected of a tribunal exercising a jurisdiction of this kind (see, for example, the judgment of Laurence Collins J., as he then was, in *Lucie M. v Worcestershire County Council and Evans* [2002] EWHC 1292 (Admin), at paragraphs 10 and 11 – cited by the Tribunal (H.H.J. Walden-Smith) in *Havering London Borough Council v MacDonald* [2012] UKUT 1454 (LC), at paragraph 31).

The Leasehold Valuation Tribunal's reasoning

29. In making its decision under section 57 of the 1993 Act the First-tier Tribunal exercised its own judgment on the facts and argument before it. It did not simply echo the reasons given by the Leasehold Valuation Tribunal for refusing the section 35 application. It sought to apply that reasoning within the statutory context for its own decision. It was not bound by the Leasehold Valuation Tribunal's analysis. It was free to differ. But it found support for its own conclusions in that analysis. In principle, I cannot see anything wrong with that approach. Whether the First-tier Tribunal's conclusions were correct is, of course, another question.

Was the First-tier Tribunal wrong to reject Mr Rossman's proposed modification to the lease?

30. Section 57(6) provides the opportunity to ensure that defects in the existing lease are remedied when a new lease is granted (see the decision of the House of Lords in *Howard de Walden v Aggio* [2009] 1 A.C. 39, and the decision of the Tribunal (H.H.J. Huskinson) in *Gordon v Church Commissioners for England* LRA/110/2006, 25 May 2007, unreported). Mr Rossman pointed, in particular, to what Lord Neuberger of Abbotsbury said about the wide ambit of section 57 in *Aggio*. In paragraph 49 of his speech – with which Lord Hoffmann, Lord Scott of Foscote, Lord Walker of Gestingthorpe and Baroness Hale of Richmond all agreed – Lord Neuberger said that "[section] 57(6) … indicates that the LVT was intended to have relatively wide powers, often involving sophisticated judgment". In paragraph 62 he observed that "[a] wide discretion has been accorded to the LVT by the legislature under provisions such as section 57 …".

31. Mr Rossman argued that the term specifying the service charge contribution in his existing lease was now manifestly defective and in need of modification, that there have been a number of changes in circumstances which should have caused the First-tier Tribunal to accept that this term ought to be changed in his new lease, and that the modified term he had formulated was both appropriate and necessary.

32. He pointed to several physical and practical changes in, or affecting, Whitehall Court, and a single change in legislation – the coming into force of the Unfair Terms in Consumer Contracts Regulations 1999 – which he says are significant. The changes he described as "material changes in the building" were:

> (1) In real terms, it costs three times more to provide the necessary services for Whitehall Court today than it did in 1969, when the original lease of Flat 124A was entered into. Even since 2006 costs have risen by 37% in real terms.

(2) There have been a number of physical and ownership changes in Whitehall Court since 1969, which have had a "substantial and material" effect on the operation of the service charge regime. As a result of these changes the total amount of service charge contributions for which the lessees are liable each year under their leases has gradually increased so that it is now far more than the annual expenditure on services.

(3) The apportionment of service charge contributions from the lessees in Whitehall Court does not today operate in the same way as it did when the original lease was entered into in 1969. The basis for apportionment is now extra-contractual. The 0.8% contribution stipulated in the 1969 lease of Flat 124A has long since been abandoned.

(4) The abatement scheme itself is neither fair nor reasonable. It has created a two-tier method of apportioning the service charge – "one for the big commercial and/or residential tenants and one for the others". It was introduced as a "blunt extra-contractual instrument", and "without any prior negotiation or agreement with leaseholders via variation of leases", to enable the collection of only 100% of the service charge expenditure rather than the "contractual entitlement" of 129%. In the case of Flat 124A, the percentage under the abatement scheme is 0.62% rather than 0.8%. That is still 198% higher in real terms than the service charge contribution to which the lessee of Flat 124A was liable when the 1969 lease was entered into. This arrangement discriminates against the leaseholder of Flat 124A, who is now "subsidizing the discounts and special deals negotiated in the extra-contractual framework that currently operates in Whitehall Court".

33. Mr Rossman also contended that the Unfair Terms in Consumer Contracts Regulations are relevant in this case because the current service charge regime in Whitehall Court discriminates between "commercial leaseholders" and "individual leaseholders". Individual leaseholders are not able to negotiate exclusions and discounts or "extra-contractual relief". In support of this contention Mr Rossman relied on the decision of the House of Lords in *Director General of Fair Trading v First National Bank* [2001] UKHL 52 – in particular the speech of Lord Steyn at paragraph 36, and the speech of Lord Millett, at paragraph 54.

34. Finally, Mr Rossman submitted that his proposal for the modification of his lease is "fair, reasonable and rational". An apportionment of the total service charge on the basis of square footage is transparent, complies with the recommendations of the R.I.C.S. in its relevant guidance on managing mixed use developments, and is likely to endure. It is not subject to the anomalies and inconsistencies of the extra-contractual abatement scheme.

35. Countering that argument, Mr Upton submitted that the general presumption in section 57(1) of the 1993 Act is that a new lease will be in the same terms as those of the existing lease. I accept that. The general presumption is subject to the other provisions of Chapter II of Part I of the 1993 Act, in particular those relating to rent and duration in section 56(1), and to the need to modify the terms of the lease to take account of the considerations specified in subsection (1)(a), (b) and (c). As the Tribunal emphasized in paragraph 39 of its decision in *Gordon*, "the starting point is firmly based in the terms of the existing lease". The Tribunal thought this was "unsurprising bearing in mind that at the date when the new lease falls to be granted there may well be a substantial number of years … still unexpired on the existing lease …". The Tribunal also observed in *Gordon* (at paragraph 40) that the power to alter terms of the existing lease under subsections (1) and (2) of section 57 is "notably wider" than the scope for effecting changes under subsection (6). It went on to state (at paragraph 41):

> "It is one thing to exclude or modify a term or terms of the existing lease where a good reason ([i.e.] within paragraph (a) or (b) of section 57(6)) can be shown. It is another thing to permit a party to seek a rewriting of the lease by the introduction of new provisions."

36. Mr Upton submitted that it is clearly implicit in section 57(6) that the party contending for the change in question has to show the need for the disputed term in the existing lease to be excluded from the new lease, or modified. There is no burden on the other party to show the contrary. Again, I agree. This proposition has been accepted in at least two decisions of the Leasehold Valuation Tribunal (see *Davies v Howard de Walden Estates Ltd.*, 14 October 1998, unreported, at p.5; and *Cadogan v Chelsea Properties Ltd.*, 25 June 2008, unreported, at paragraph 22). It is also accepted in Hague on "Leasehold Enfranchisement" (at paragraph 32-10(b)), which states that "[the] onus is on the person proposing the change to show that there are grounds for deleting or modifying the term in question".

37. In paragraph 47 of its decision in *Gordon* the Tribunal noted that there is no definition of a "defect" in the 1993 Act, but adopted the definition of that word in the New Shorter Oxford English Dictionary (fourth edition) – as "[a] shortcoming, a failing, a fault, an imperfection". It went on to say:

> "… [A] lease can only properly be described as containing a defect (in the sense of shortcoming, fault, flaw or, perhaps even, imperfection) if it can objectively be said to contain such a defect when reasonably viewed from the standpoint of both a reasonable landlord and a reasonable tenant. It may be noted that once a defect is shown to exist in the existing lease then a party may "require" that for the purposes of the new lease any term of the existing lease "shall" be excluded or modified in so far as it is necessary to do so in order to remedy the defect. This mandatory language indicates that the concept of a defect is a shortcoming below an objectively measured satisfactory standard. It is not sufficient for a provision to be a defect only when viewed from the standpoint of one or other party."

Hague comments (at paragraph 32-10(a)) that "[the] word "defect" is not defined, but given the use of the word "necessary" a strict or narrow interpretation seems the proper one", and therefore that "the use of [section 57(6)(a)] to attempt to modernise the terms generally in the face of opposition from the other party would not be permissible" .

38. The task of the First-tier Tribunal under section 57(6)(a) is to establish whether, in its judgment, there is a proper basis for regarding the disputed term as defective. Otherwise, it must leave the term in place. The same goes for the question that arises under section 57(6)(b). It is for the First-tier Tribunal to ascertain whether, in the light of any relevant changes in circumstances since the existing lease was entered into, it would be unreasonable in the circumstances not to interfere with the term that is now contentious. In either case the question for the First-tier Tribunal is a wholly objective one, which it must deal with by exercising its own judgment on the relevant facts and circumstances of the case before it, as it finds them to be.

39. Under section 57(6)(a), not only must a defect be clearly identified in the existing lease; the party seeking the exclusion or modification of the term in question must also be able to show that the exclusion or modification contended for will indeed remedy that defect. That, in my view, is the effect of the statutory formula – "necessary to do so in order to remedy a defect in the existing lease".

40. The concept of necessity here is a demanding one. I agree with what the Leasehold Valuation Tribunal said to that effect in *Waitt v Morris* [1994] 2 E.G.L.R. 224 – where the tenant failed in his

request for a term requiring the landlord to give his, the tenant's, mortgagee 21 days' notice of forfeiture proceedings. The Leasehold Valuation Tribunal said (at p.226C) that the proposed term "may be "convenient" but it is not "necessary" to remedy a defect in the existing lease …". The distinction between convenience and necessity is important. It is emphasized in Hague (at paragraph 32-10(a)). The crucial question is not whether it is necessary to remedy the defect in the existing lease, but whether, given that there is a defect which must be remedied, it is necessary to make the exclusion or modification to achieve that.

41. The need for the modification or exclusion to be demonstrably capable of remedying the defect is also plain. Section 57(6)(a) does not allow for the exclusion or modification of a term in the existing lease unless that change will result in the identified defect being put right. The statutory language – "to remedy a defect" – indicates that the change proposed must not merely ameliorate the defect, but actually cure it. In this respect, as Mr Upton submitted, section 57(6) is to similar effect as section 35 of the 1987 Act. As the Leasehold Valuation Tribunal said in paragraph 127 of its decision, "if there is to be an intervention it should be one [that] will not only improve upon the current position but actually cure, or at least substantially cure, the defect …".

42. Mr Upton submitted that a reasonable landlord and a reasonable tenant would not consider the existing service charge provision in the lease of Flat 124A to be defective. When Mr Rossman took an assignment of his lease in August 2006 he was prepared to be bound by the requirement to pay a service charge contribution on the basis of a fixed percentage of expenditure, and to accept the term specifying that percentage for Flat 124A as 0.8%. The lease originally entered into in 1969 contained a term by which the parties deliberately provided for the tenant's service charge contribution to be 0.8% of expenditure. The parties to the deed of re-grant and variation of the lease in 1989 agreed that this provision should remain, and in the same terms. In neither case was it inserted in error. Its insertion in the lease was seen as appropriate and necessary. This is not the kind of situation envisaged by the Tribunal (Martin Rodger Q.C., Deputy President) in *Burchell v Raj Properties Ltd.* [2013] UKUT 0443 (LC) (at paragraph 43): the existence of "a "defect" in the sense of a mistake which neither party can have intended to be included in the Lease as originally granted".

43. Mr Upton did not attempt to justify the level of the fixed percentage contribution in the existing lease – the figure of 0.8%. But he submitted that the voluntary abatement scheme overcomes any potential unfairness arising from the disputed term – as the First-tier Tribunal held – and that there is therefore no need to change it. In the section 35 proceedings the lessees of the flats in Whitehall Court had the chance to promote a new regime for service charge contributions, which, in their collective view, was both acceptable and fair to them all. Yet their proposal failed. Modifying the service charge provision in one lease, and only one, would disrupt the voluntary abatement scheme for service charges in Whitehall Court, and might encourage other lessees to apply to vary their service charge contribution when they claim for new leases. The regime which would result from that would be inconsistent and difficult to operate. In the circumstances it is neither necessary nor sensible to modify this term in the new lease of Flat 124A.

44. I cannot accept that argument.

45. Both the Leasehold Valuation Tribunal in the section 35 proceedings and the First-tier Tribunal in determining Mr Rossman's application under the 1993 Act seem to have accepted that the existing lease is defective in the particular respect Mr Rossman has identified both in those proceedings and in these.

46. The Leasehold Valuation Tribunal said in paragraph 130 of its decision that "the current scheme" for service charge contributions in Whitehall Court was "patently not [perfect]". That is clearly right. In paragraph 13 of its decision the First-tier Tribunal said the "existing service charge terms in [Mr Rossman's] lease do not amount to a sufficiently serious defect within the meaning of section 57(6) (a) of the [1993] Act" (my emphasis). I disagree.

47. In my view, there is clearly a defect in the existing lease of Flat 124A, and it is a sufficiently serious defect to require a remedy. To include in the new lease a term replicating the provision for a fixed 0.8% service charge contribution in the existing lease would be wrong. No justification for setting the contribution at that level in the new lease has been put forward. It is, in truth, indefensible, and demonstrably so. If the existing lease of Flat 124A, and others, were sound in this respect there would be no need for the voluntary abatement scheme, which currently operates, without the force of contract, to reduce Mr Rossman's liability for service charge contributions to a percentage figure materially below the figure in his lease, and has a similar effect on the corresponding provisions in the other leases too. Whitehall Court (Investments) Ltd., as landlord, is currently entitled to collect from the tenants of Whitehall Court almost 30% more by way of service charges than it is actually spending on services, which is an obvious disparity. But for a voluntary abatement scheme which might be altered or even withdrawn altogether, either by Whitehall Court (Investments) Ltd. or by another landlord who was not minded to make the same concession, the full amount for which the lessees are liable under their leases could be collected. There is, of course, nothing to indicate that the voluntary scheme is likely to be altered or withdrawn in the foreseeable future. I also acknowledge that the abatement is effective, because it ensures that the total service charge collected does not exceed, or fall short of, 100% of expenditure in any particular year. None of the lessees pays more than he is bound under the terms of his lease to pay, and most, if not all, pay less. And no doubt a good deal of evidence could be given about the history and rationale of the voluntary abatement scheme. In my view, however, the existence of that voluntary scheme, and the fact that it is obviously regarded as a necessary means of mitigating the effect of the service charge provisions in the leases at Whitehall Court, serves to confirm that those provisions, including the one in Mr Rossman's lease, are unrealistic and out of date. I do not think it can be right for a defect of this nature to be incorporated into the new lease of Flat 124A. To do that would be inimical to Parliament's evident intention in section 57(6) of the 1993 Act.

48. I therefore accept Mr Rossman's submission that the term in the existing lease of Flat 124A which requires of the lessee a fixed service charge contribution of 0.8% is a defect of the kind contemplated in section 57(6)(a) of the 1993 Act, and that a modification of this term is required in the new lease. I also see force in his contention that, in view of changes which have occurred since the commencement of the existing lease, the inclusion of this term unmodified in the new lease would be unreasonable in the sense of section 57(6)(b). It follows that the disputed term must now be modified.

49. This conclusion does not require me to accept Mr Rossman's submission that the existing lease also offends the provisions of the Unfair Terms in Contracts Clauses Regulations 1999. It is not necessary for that point to be decided in this appeal. And I express no view about it, beyond noting that the 1999 regulations are, or may be, capable of applying to a service charge provision in a lease (see *R. (on the application of Khatun) v Newham London Borough Council* [2005] Q.B. 37, in particular paragraphs 52 to 83 of the judgment of Laws L.J.; and the helpful discussion in Chapter 37 of "Commercial and Residential Service Charges" by Rosenthal, Fitzgerald, Duckworth, Radley-Gardner and Sissons).

50. What should follow from my conclusion that a modified term for the service charge contribution should be incorporated in the new lease?

51. In paragraphs 132 to 141 of its decision in the section 35 proceedings the Leasehold Valuation Tribunal concluded that the variation proposed by the applicants had flaws of its own. As it said in paragraph 141, it was not satisfied that the modification put forward was workable, or an improvement on the scheme operated by Whitehall Court (Investments) Ltd.. The last sentence of paragraph 12 of the First-tier Tribunal's decision makes clear that it found this part of the Leasehold Valuation Tribunal's analysis cogent and relied on it when making its own decision. The Leasehold Valuation Tribunal was not persuaded that the use of a percentage of total floor space as the basis for fixing each lessee's contribution to the service charge was necessarily fair to all of the lessees, let alone that it was the fairest possible basis (see paragraph 132 of the Leasehold Valuation Tribunal's decision). Neither am I.

52. As Mr Upton submitted, in a mixed use building the use of floor area is only one of several possible methods of apportioning service charges. Others include the use of a fixed amount, a fixed percentage, a weighted floor area apportionment, a fair and reasonable proportion, and a rateable value apportionment. These are briefly described in the R.I.C.S. information paper "Apportionment of service charges in mixed use developments", published in August 2009, Appendix 2 of which is an extract of section D4 of the R.I.C.S. "Service charges in commercial property code of practice". I note the salutary comments made in section 11 of the information paper, "Alternative apportionment strategies": that in "mixed use property" it is "necessary to apportion costs, initially per the specific lease requirements and if there is discretion then based on the benefit and use of the services received", but that "the increase of mixed use development and the clarification that residential law applies means more transparency is advised and that process and timeliness are essential". Each of the several possible methods of apportionment of a "mixed use service charge" will have its advantages and disadvantages, depending on the particular characteristics and circumstances of the development in question. It is not my task in deciding this appeal to explore the relative merits of the various approaches, either in general or in their application to the particular, perhaps unique, circumstances of Whitehall Court. Indeed, I think it would be impossible to do that with any confidence in the absence of relevant expert evidence to guide me. But in any case I find Mr Rossman's suggested approach unconvincing. It has the attraction of mathematical precision. But it is not supported in this appeal by evidence on the practicalities of managing a large and complex mixed use development such as Whitehall Court, in which, as the Leasehold Valuation Tribunal said in paragraph 133 of its decision, "the commercial units and those to which Part II [of the Landlord and Tenant Act] 1954 apply are very much intermingled with the pure residential leases throughout the development".

53. The Leasehold Valuation Tribunal's observation in paragraph 127 of its decision that any intervention in the terms of a lease must "actually cure, or at least substantially cure, the defect" was of course made in the context of a determination under section 35 of the 1987 Act. But it is also germane to section 57(6) of the 1993 Act. If the First-tier Tribunal had decided that the term proposed by Mr Rossman should be included in the new lease, it would, in my view, have been accepting that the existing term should be replaced with another provision which was itself unsuitable. Section 57(6) does not allow that. It does not permit the substitution of one defective or inappropriate term for another.

54. It would be possible, I accept, simply to substitute for the fixed percentage figure in the service charge provision in the existing lease of Flat 124A the percentage which has been applied in the voluntary abatement scheme. But neither party contended for this outcome, and I am not satisfied on the submissions made to me in this appeal that it would be right to take that course.

55. In my view, therefore, the case should go back to the First-tier Tribunal so that it can determine, in the light of full evidence and submissions from the parties, how the service charge provision in Mr Rossman's new lease should be formulated.

Conclusion

56. For the reasons I have given, this appeal is allowed to the extent I have indicated. The First-tier Tribunal's decision that the service charge provision in the existing lease of Flat 124A should be included in the new lease must be set aside. This term must be modified. The case will therefore be remitted to the First-tier Tribunal for it to determine what that modification should be. Within 21 days of the date of this decision Mr Rossman must apply to the First-tier Tribunal for directions for the further conduct of the case.

Dated: 29 May 2015

Sir Keith Lindblom, President