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HM Courts and Tribunals Service
Leasehold Valuation Tribunal

Case No. CHI/00MW/LIS/2012/0004

DECISION OF THE LEASEHOLD VALUATION TRIBUNAL
SECTION 20C & 27A of the LANDLORD AND TENANT ACT 1985

Property:	Flat 6, Cliff House, Bonchurch Shute, Ventnor, Isle of Wight PO38 1NU
Applicant:	Mr B Acutt (Flat 6) (tenant)
Respondent	Cliff House (Bonchurch) Management Company Limited (landlord)
Date of Application:	03 January 2012
Directions:	11 January 2012
Consideration:	04 April 2012
Decision:	11 May 2012

Members of the Leasehold Valuation Tribunal

Ms J A Talbot MA
Mr N I Robinson FRICS

Application

1. This Application was made on 03/01/2012 by Mr B Acutt, tenant of Flat 6, Cliff House, Bonchurch Shute, Ventnor, Isle of Wight PO38 1NU, pursuant to Section 27A of the Landlord and Tenant Act 1985, for a determination on the payability of service charges for the years 2009, 2010 and 2011. There was also a s20C application.

Background

2. Directions were issued on 11/01/2012. Neither party objected to the application being determined without an oral hearing. Both parties provided Statements of Case and documentation relating to the issues in dispute, which were identified in the Directions as (a) the format and content of the service charge accounts and (b) an application under s20C to limit the costs of the Respondent (in relation to this application) recoverable as service charges.

Jurisdiction

3. The Tribunal has the power to decide about all aspects of liability to pay service charges and can interpret the lease where necessary to resolve disputes or uncertainties. Service charges are sums of money payable by a tenant to a landlord for the costs of services, repairs, some improvements, maintenance or insurance or the landlord's costs of management, under the terms of the lease (s18 LTA 1985). The Tribunal can decide by whom, to whom, how much and when service charge is payable. A service charge is only payable insofar as it is reasonably incurred, or the works to which it related are of a reasonable standard (s19 LTA 1985). The Tribunal therefore also determines the reasonableness of the charges.

Lease

4. The Tribunal had a copy of the lease of Flat 6. The lease is dated 15 July 1983 and is for a term of 99 years from 25 December 1979 at a ground rent of £30 rising thereafter. The property definitions refer to the flat as the Demised Premises, along with the Building, meaning the block of flats, the Common Parts, the Estate, meaning the land on which the building stands, and the Retained Property, meaning (inter alia) the gardens, footpaths, and parking areas.

5. The provisions relating to the calculation and payment of the service charges are to be found at the Fifth Schedule. The tenant's share of the "Service Charge" is one ninth of the lessor's "total expenditure relating to the building", with an additional "Retained Property Service Charge" in respect of "the total expenditure relating to the Retained Property and the Estate". The tenant's proportion of this latter charge is "the ratio borne by the rateable value of the demised premises to the aggregate rateable value of all those premises enjoying rights over the retained property".

6. The "total expenditure" means "expenditure incurred by the Lessor in any accounting period in carrying out their obligations under clause 5(5) of this Lease". Clause 5(5) requires the landlord, inter alia, to maintain, repair and insure the Building, Common Parts and Retained Property. It also entitles the landlord to employ managing agents and "accountants", and to set aside sums for anticipated expenditure, such sums

being "deemed to be an item of expenditure incurred by the Lessor". The accounting period runs from 25 December to 24 December each year, or any other period which the landlord may determine.

7. The landlord may demand an interim service charge on 24 June and 25 December each year, with any balance payable at the end of the accounting period, specifically (paragraph 5) "within twenty eight days of service upon the Lessees of the Certificate referred to in the following paragraph".

8. Paragraph 6 provides: "as soon as practicable after the expiration of each Accounting Period there shall be served on the Lessees by the Lessor or its Agents a certificate signed by the Auditors appointed by the Lessor containing the following information: (a) the amount of the Total Expenditure for that Accounting Period (b) the amount of the Interim Charge (apportioned as between the Service Charge and the Retained Property Service Charge) paid by the Lessees in respect of that Accounting Period together with any surplus carried forward from the previous Accounting Period (c) the amount of the Service Charge in respect of that Accounting Period and of any excess or deficiency of the Service Charge over the apportioned part Interim Charge (d) the amount of the Retained Property Service Charge in respect of that Accounting Period and of any excess or deficiency of the Retained Property Service Charge over the apportioned part of the Interim Charge".

9. Paragraph 7 provides that the certificate is conclusive but the lessees are entitled to inspect the vouchers and receipts relating to the landlord's expenditure by request within one month of service of the certificate. The only other reference to the certificate is in paragraph 1(i)(d) which further defines the costs which the landlord is entitled to include in the total expenditure: "the cost of any Accountant or Surveyor employed to determine the Total Expenditure and the amount payable by the Lessees ... including the provision of certificates prepared pursuant thereto".

Consideration

Background to Application

10. We determined the application by carefully considering the papers. We did not inspect the property, but are aware from the documentation that Cliff House comprises a block of flats set in grounds with communal gardens and parking spaces. The estate contains another smaller block, Cliff Mansions. It appears that Cliff House is in need of maintenance, whereas Cliff Mansions is well maintained.

11. The Respondent landlord, Cliff House (Bonchurch) Management Company Limited, is a tenant-owned management company (referred to herein as the Company). It purchased the freehold of Cliff House in May 2009 by collective enfranchisement. The previous freeholder was Cliff Investment Properties Ltd, a company controlled by the applicant tenant, Mr Acutt. He is not a member of the Company. The property was managed from 2003 to 2009 by an LVT appointed Manager. The current managing agent is David Orlik of John Rowell Estate Management (JREM), instructed by the Company in August 2010. He is also the Company Secretary.

12. The factual background in relation to the service charges and accounts is as follows. No accounts were served for the year ending 24 December 2008 (when Mr Acutt's

company owned the freehold). No service charge demands were sent to the lessees during 2009, but it seems that the lessees, apart from Mr Acutt, were making monthly payments, presumably by prior agreement. Mr Acutt paid ground rent but no service charges, in the absence of any demands.

13. In 2010 two service charge demands were sent to Mr Acutt by JREM, both dated 27 September 2010. The first was for service charges of £560.00 "due 25.12.2009 & 24.06.2009 for period 22.5.09 to 24.12.09" plus apportioned ground rent of £18.33, total £578.33. The second was for "half-yearly service charge due 25.12.2009" of £480.00, and "half-yearly service charge due 24.06.2010", also for £480.00. The total amount demanded was £1,568.33. A further demand dated 26 January 2011 was for £600.00 due in advance on 25/12/2010 plus ground rent of £30.00 and "interest on arrears" of £120. The covering letter states that the service charge for the year 2011 was to be £1,200, or £100 per month for lessees paying by standing order.

14. All the demands refer to an "enclosed Notice" which was not in the papers. Mr Acutt confirmed that the demands had the "required Statutory Notices attached" so this is presumably the summary of rights and obligations in the prescribed form (under s21B LTA 1985). He has not argued that the demands are invalid on this ground.

15. Also on 26 January 2011, JREM issued two "Statements of Income and Expenditure", headed "Cliff House Bonchurch Service Charge Trust", both dated 24 December 2010, for the periods 22 May to 24 December 2009, and year ending 24 December 2010. The accounts showed expenditure on insurance, management fees, electricity, fire alarms, waste disposal, cleaning and gardening. Mr Acutt has not challenged the reasonableness of the costs or standard of works or services. The accounts also showed income received from the other lessees of flats 1-9.

16. The accounts contained an "Accountants' Certificate" with the wording: "we have examined the above statement of income and expenditure, debtors and creditors of the is [*sic*] in accordance with the underlying books and records and transactions, invoices and receipts to prove expenditure are available for inspection". The accounts were signed by David Orlik, but not by the accountant, David Hilliam. Mr Hilliam confirmed on 4 February 2011 that he had not seen the accounts. Following correspondence between Mr Acutt and JREM, the accounts were re-served in the same form on 11 May 2011, this time signed by Elizabeth Dack FCCA (senior statutory auditor) of accountants Harrison Black Ltd.

17. Following further objections from Mr Acutt on the format and contents of the accounts, on 20 July 2011 JREM served amended accounts. These were now headed "Annual Certificate & Summary of Expenditure & Application to Individual Flats". These accounts distinguished between expenditure on the "house, all flats" 1/9th share" and "rateable value (house & mansions)", and separated the items of expenditure accordingly. They also included "contribution to future maintenance" which did not appear on the previous version.

18. Mr Acutt continued to challenge the accounts. On 8 December 2011 Mr Orlik served a further version of the accounts for 2009 and 2010, with the same expenditure figures, endorsed with a "managing agents certificate" signed by him, together with a separate "accountants report of factual findings" signed by Harrison Black, dated 20 September 2011. This document confirmed that the figures in the accounts were

extracted correctly from the records, that the accountants had checked the receipts and other supporting documentation, and that service charge monies were held in a separate designated account.

19. On 1 February 2012, JREM served accounts for the year ending 24 December 2011, not yet certified by the accountants. These accounts give a breakdown of service charge income from all flats, and expenditure identifying service charge and retained property charge. The covering letter referred to the Company AGM held in September 2011 at which it was confirmed that service charge contributions would remain at £1,200 for the year from 25 December 2011.

The Applicant's case

20. Mr Acutt set out his objections to the accounts and service charge demands in voluminous correspondence. In summary, he contended that the accounts did not comply with Schedule 5 of the lease, initially because they did not show the apportionment between the Service Charge and Retained Property Service Charge. Even after the accounts were amended, he argued that the certification by both the managing agent and accountant was inadequate, because the lease required an Auditor's Certificate, which was not the same as a report of factual findings. He argued that the certificates ran counter to various accountancy "best practice guidance" such as TECH 01/10 and TECH 03/11 (professional guidance on accounting in relation to service charge accounts prepared by various accountancy, property management and chartered surveyors professional organisations).

21. Mr Acutt argued that the certificate in paragraph 6 should be personal to the individual lessee, and not contain information on alleged arrears designed to embarrass lessees in arrears. He alleged that the landlord was in breach of the lease by failing to provide any accounts or demands for the year 2008 or 2009, whilst the accounts for 2009 and 2010 did not comply. He challenged the reserve fund figures in the revised accounts, which he contended had been retrospectively added, rather than crediting lessees with any surplus. He contended that the rateable value figures used in the revised accounts were incorrect and supplied RV figures which he had applied in the 1990's since the last domestic rates change on 1 April 1990.

22. Mr Acutt did not dispute any of the expenditure items in terms of reasonableness of cost or standard of works provided, but he did submit that ground rent and the Company's administration costs in the 2011 accounts were not service charge items. He further argued that in the absence of any valid demands or accounts, there was no entitlement to charge interest on any alleged arrears of service charges.

The Respondent's case

23. Mr. Orlik provided a statement of case responding to Mr Acutt's submissions. In summary, he accepted that the initial accounts did not comply with the requirements in the fifth schedule to the lease, although he contended that they were factually correct. He argued that the revised accounts were compliant, fit for purpose, produced by his firm and independently reviewed by chartered accountants to an acceptable professional standard. It would be unnecessary and disproportionate for fully audited accounts to be produced.

24. Mr Orlik contended that the lease provided for a contribution for future maintenance, such sums to be "set aside" at the landlord's discretion and deemed to be a service charge item. Cliff House was in need of maintenance which had been hindered by lack of resources, and the Company sought to put in place a planned maintenance programme to avoid further deterioration to the property. He objected to Mr Acutt's suggestion that the revised accounts had been retrospectively altered. The format had been changed to comply with the fifth schedule in response to Mr Acutt's correspondence, and reconciled the previous cash-based statement with the amount of interim service chares invoiced but not necessarily received. The difference reflected the contribution to future maintenance. As for rateable value, his firm had no information from the previous managing agents, so had carried out a calculation using council tax banding information. Mr Orlik accepted that the Company's annual return fee for Companies House should not have been included but argued that other expenses of director's insurance were valid service charge items.

25. Mr Orlik argued that there was no requirement under the lease for individual certificates to be served on each lessee. The accounts produced gave a full breakdown of income and expenditure to give all lessees an informed view. Interest on arrears was due from Mr Acutt, because it related to non-payment of interim charges, and he had not made any payments since May 2009. Whilst it was correct that no demands had been served in 2009, his firm only took over management in August 2010 and was not in a position to serve demands before that. The absence of accounts for 2008 was the responsibility of the previous freeholder, i.e. the company controlled by Mr Acutt.

Determination

26. The main issue in this application was the format and contents of the accounts, specifically whether they complied with the fifth schedule to the lease. It was not in dispute that the initial form of accounts for 2009 and 2010 as served on 26 January 2011 did not comply, specifically with the requirements of paragraph 6. They were cash accounts showing income and expenditure only. It was perhaps unwise of JREM to serve these accounts signed only by Mr Orlik and not by the then accountant Mr Hilliam.

27. However, we accepted that the revised version of the accounts for 2009, 2010 and 2011 – as eventually served on 8 December 2011 and 1 February 2012 – did comply in format. They contained the necessary apportionment between the Service Charge for the building and the Retained Property Service Charge for the retained property. We accepted Mr Orlik's explanation for the contribution of future maintenance and it is quite clear that the lease allows the landlord at Clause 5(5) to set aside such sums, which are defined as service charges.

28. We further accepted that it was not necessary under the terms of the lease for the landlord to prepare and serve separate certificates of account for individual lessees. From our own knowledge and experience, we find that it is usual and good practice to provide a single account showing all expenditure incurred and income received and due to the landlord, in the interests of transparency and giving full information to all lessees. This may mean that any unpaid service charges will be evident, but that is not a reason for issuing separate certificates.

29. On the question of the accountant's certification, paragraph 6 provides for the certificate to be "signed by the Auditor appointed by the Lessor". In our view, this does not mean that accounts should be subject to a full formal audit. There is no reference in the lease to audited accounts. This is the only use of the word "auditor" whereas the word "certificate" appears four times in the fifth schedule (sometimes with a capital C and sometimes without). The landlord is entitled to recover the costs of any "accountant" to determine the total expenditure and prepare the certificate. The use of the term "auditor" rather than "accountant" in paragraph 6 seems to be rather loose drafting – as with the inconsistent use of capital and lower case letters. Therefore, we consider a certificate signed by an accountant will be sufficient, although we note that Elizabeth Dack refers to herself as a qualified auditor.

30. There is also no requirement in the lease that the accounts must comply with any particular professional or technical guidance, although this would be good practice. We note the technical release giving such guidance in relation to residential service charges. The signed "report of factual findings" from Harrison Black records that they have checked and found that (a) the figures in the account have been extracted correctly from the accounting records, (b) that the account entries were supported by receipts or other inspected documentation, and (c) that the service charge monies were held in a separate designated account and that the balances reconciled. The accounts are also signed by the managing agent. We are satisfied that this taken together constitutes sufficient certification in accordance with the lease.

31. We saw the force of Mr Acutt's objection on the rateable value (RV) issue. It was not possible for us to make a clear finding on what the correct RV figures should be, but we consider both RJEM's calculations and Mr Acutt's figures to be incorrect. There is no co-relation between RV and council tax – they are entirely separate regimes. Mr. Acutt's figures derived from the last domestic rate change on 1 April 1990. However, the lease is dated 15 July 1983, and the apportionment is "the ratio borne by the rateable value of the demised premises to the aggregate rateable value of all those premises enjoying rights over the retained property". There is no reference to the RV "from time to time" or anything similar. Therefore, in our view, the correct RV must be that which was in force when the lease was granted. This is a question of fact, which in our experience can be easily ascertained by direct enquiry to the local authority where records are kept.

32. Our conclusion therefore is that the final version of the accounts for 2009 and 2010 served on 8 December 2011, albeit late for 2009, are compliant with the fifth schedule in terms of the format, content and certification, subject to clarification on the RV apportionment for the retained property charge.

33. Turning to the question of service charge demands, it seems to us that the service of demands on 27 September 2010 requiring payment of "interim charges" for 2009 was an attempt by RJEM to rectify the lack of any demands made during that year. Whilst this is understandable, we consider that it is not possible to create a retrospective liability for interim charges in this way. The whole point of interim charges is that they are payable "by equal instalments *in advance*" [our emphasis] on 24 June and 25 December each year. They are essentially payments on account, with any balance due from the lessee within 28 days of the issue of the certificate.

34. Therefore, as Mr Acutt paid no interim service charges, in our view he became liable to pay his full contribution 28 days after the service of the certificate of account, which we have determined was done on 8 December 2011 for the years 2009 and 2010, subject to a valid demand being made for the correct amount. The same will apply for 2011 once the duly signed certificate has been served (which was not the case when this application was made).

35. However, with regard to expenditure incurred by the landlord in 2009, we considered whether the landlord is precluded from recovering those costs under s20B of the 1985 Act, which provides that service charges must be demanded within 18 months of the costs being incurred, i.e. when they were payable by the landlord. In our view, s20B does apply in respect of the costs incurred in 2009. The absence of any interim service charge demands during that year, coupled with the considerable delay in providing accounts in the correct form for 2009 until 8 December 2011, means that Mr Acutt is not liable to pay service charges for costs incurred before 8 June 2009.

36. Mr Acutt is liable to pay the interim charge demanded correctly on 27 September 2010 for the sum due in advance on 24 June 2010, and on 26 January 2011 for the sum due in advance from 25 December 2010. We have not seen any later demands, but if these comply with the lease dates and contain all the required statutory information, then all further interim charges will be payable. We are satisfied that the sums demanded are reasonable and indeed have been agreed by the Company on advice from RJEM.

37. Regarding interest on arrears, the lease provides for interest to be charged at 4% above base rate, which is highly unlikely to have been 10% at the material time. Moreover, it is settled law that service charges are not lawfully due unless validly demanded, so without a valid demand there can be no service charge arrears. The interest as calculated is therefore not recoverable.

38. Mr Acutt did not dispute any items of expenditure apart from the Company's expenses in the 2011 accounts. Mr Orlik correctly conceded that the £14 annual return fee should not have been included. This also applies to the other costs. Directors' expenses are not service charge items under the terms of the lease. The Company is expected to cover its costs from its income or assets, such as ground rent income. Accountant's fees are, however, recoverable under the lease terms.

39. We note that the demands we have seen do not contain a statement of the landlord's address for service of notices, as required by s48 of the Landlord and Tenant Act 1985. A notice under s48 only has to be served once, and this may have been done separately at some time in the past, but in any event any defect is easily remedied and has retrospective effect (because a tenant is only entitled to withhold payment until the notice is served). Demands must also be accompanied by the statutory summary of rights and responsibilities, which we assume was done, as Mr Acutt confirmed he received the correct statutory notice.

Determination

40. Mr Acutt is liable to pay his service charge contribution towards the landlord's total expenditure for the year 2009 but only for costs incurred by the landlord after 8 June

2009. He is liable to pay in full for the years 2010 and 2011. For 2011, the total expenditure must exclude all Company expenses.

41. He is liable to pay interim service charges as demanded from 27 September 2010.

42. His liability is subject to adjustment of apportionment for the correct rateable value, once this is ascertained, in respect of the retained property service charge element.

43. He is not liable to pay the interest on arrears as currently calculated.

Section 20C

44. Mr Acutt sought an order pursuant to Section 20C of the 1985 Act that the costs incurred by the landlord in connection with the proceedings before the tribunal should not be regarded as relevant costs to be taken into account in determining the amount of the service charge payable by the tenant. The Act provides that the Tribunal may make such order on the application as it considers just and equitable in the circumstances. The tribunal is concerned with the merits rather than the quantum of these legal costs.

45. We considered that although Mr Acutt's has not yet paid any service charges there was some merit in his challenge to the format and content of the initial accounts. The accounts for 2009 were extremely late and no valid demands were served until September 2010. Had the landlord and its agents ensured at a much earlier stage that the property was being managed in accordance with the terms of the lease, the issues which are the subject of this application could have been avoided.

46. Therefore we make the order sought.

Dated 11 May 2012

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Chairman

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