LRX/3/2006

LANDS TRIBUNAL ACT 1949

LANDLORD AND TENANT – service charges– apportionment of charges between residential and commercial tenants – whether landlord was in manifest error under the terms of the residential leases by increasing the residential proportion – effect of previous LVT decision on the same issue – appeal allowed – Landlord and Tenant Act 1985 ss 19(1) and 27A

IN THE MATTER OF AN APPEAL FROM A DECISION OF THE LEASEHOLD VALUATION TRIBUNAL FOR THE SOUTHERN RENT ASSESSMENT PANEL

BY

ROWNER ESTATES LIMITED

Re: The Village,
Grange Road and Nimrod Drive,
Rowner, Gosport,
Hampshire,
PO13 8AE

Before: A J Trott FRICS

Sitting at: Southampton Combined Court Centre, London Road,
Southampton, Hampshire, SO15 2XQ
on 26 September 2007

Peggy Etiebet, instructed by Bramsdon & Childs, for the appellant
There was no respondent to the appeal

The following cases are referred to in this decision:

R v Brent LBC ex parte Bariise (1999) 31 HLR 50 CA
Schilling and Others v Canary Riverside Development PTD Limited (2005) Lands Tribunal LRX/26/2005 (unreported)
Longmint Limited v Marcus [2004] 3 EGLR 171

DECISION

Introduction

1. This is an appeal by Rowner Estates Limited (the appellant) against the decision of the Leasehold Valuation Tribunal for the Southern Rent Assessment Panel dated 15 July 2005. There were four applications before the LVT all of which related to the property known as The Village, Grange Road, Rowner, Gosport, Hampshire, PO13 8AE (the estate). Two of the applications were made by the appellant (as landlord) under section 27A of the Landlord and Tennant Act 1985 (the Act) to determine service charges for 2004 and 2005 respectively. The other two applications were made by Mr and Mrs H R Münch in respect of their flat at 34 Hillary Court, which forms part of the estate, for the determination of service charges for the years 2003 and 2004 and by Mr V Burt who applied for the appointment of a receiver and manager of the estate under Part II of the Landlord and Tenant Act 1987. The appellant responded to these two applications. The Lessees of The Village, Rowner, an association of 110 of the 301 tenants on the estate, responded to the two applications made by the appellant. The remaining tenants were not present nor represented at the hearing before the LVT.

2. The LVT refused the appellant leave to appeal on 21 November 2005. The main ground for appeal was that the LVT had been wrong to conclude that the due proportion of the service charges payable by the residential tenants was 86.3% rather than 95% of the total service charge budget for the estate. The appellant applied to this Tribunal for permission to appeal on 15 December 2005. His Honour Michael Rich QC made three orders for directions, the last of which was made on 19 May 2006. This stated that:

> "Permission to appeal should have been given ... only in respect of the cases in which the Applicants [the appellant] had been applicants to the LVT as there listed, and in respect therefore of the years 2004 and 2005.
>
> ... I hereby give permission to appeal in respect of the 'Due Proportion' for the years 2004 and 2005..."

This decision amended his previous directions and so the appellant was given until 2 June 2006 to add to or vary its statement of case. It did not do so. His Honour Michael Rich QC directed that the amended order dated 19 May 2006 should be served upon Mr and Mrs Münch and on the Lessees of The Village, Rowner who were given until 2 June 2006 to serve a notice of intention to respond. Only Mr and Mrs Münch served such a notice and so they were the sole respondents to the appeal. On 29 July 2007 Mr and Mrs Münch wrote to the Tribunal stating that they no longer wished to defend the appeal. Consequently the appeal proceeded unopposed. The hearing before this Tribunal was by way of a rehearing of the evidence relating to the due proportion of the service charge payable by the residential tenants.

3. Peggy Etiebet of counsel appeared for the appellant and called Mr Michael James Baker-Harber of Rowner Estates Limited and Mr Nicholas Alexander Faulkner FRICS of Labyrinth Properties Limited as witnesses of fact and Mr Charles John Dawson MRICS of Dawson and Associates as an expert witness.

4. I made an unaccompanied site inspection of the estate on 25 September 2007.

Facts

5. The Village, Rowner is a former Ministry of Defence housing estate located in Grange Road to the north west of Gosport. It is believed to have been constructed in the early 1960s and comprises a total of 301 maisonettes with either two (189 units) or 3 (112 units) bedrooms. The estate comprises three main high rise (up to 8 storey) residential blocks around a precinct of 12 unit shops and several other commercial units. These comprise a supermarket and former Ministry of Defence stores and offices (both long vacant) and a doctor's surgery (now used as a security guard base). A community centre that was previously on site was demolished following constant vandalism. At one time the Spreadeagle public house (latterly renamed The Grange) formed part of the estate but the freehold interest in this property was sold circa 1995. No service charge was paid in respect of the public house. The remainder of the estate comprises lower rise residential blocks, service roads, car parking and landscaping. The area of the estate is approximately 4.45 hectares.

6. The Ministry of Defence sold the freehold interest in the estate to Aldersgate Developments Limited in the late 1980s. Aldersgate proceeded to sell all the residential units on standard long leases. New Horizons Management Limited was a party to the leases as the landlord's managing agent. However the residents wanted to manage the estate and so formed VMC1 (Village Management Company) to be responsible for day-to-day management. Subsequently, and following problems with this arrangement, the management company was incorporated as VMC2 Limited. By a headlease dated 13 July 1988 Aldersgate let all the commercial units to Caseacre Limited for a term of 125 years from 1 January 1987. These units were already let on a variety of occupational leases. Under the headlease Caseacre covenanted to pay the "Tenant's Proportion" of the service charge which was defined as 13.7% of the total service charge for the estate. Under the commercial subleases the lessees of each of the 12 unit shops covenanted to pay 0.364% of the total service charge for the estate, making a total of 4.368%. The balance of 9.332% was therefore payable by the lessees of the other commercially let properties such as the supermarket. For many years the residential tenants were charged 86.3% of the total service charge of the estate being the difference between 100% and the tenant's proportion under the commercial headlease of 13.7%. However the residential leases did not specify this proportion. The proportional division of the service charge between the residential and commercial properties was based upon their floor areas being 25,000 sqm and 4,000 sqm respectively.

7. In 1989 Focushawk Limited acquired the freehold interest in the estate. On 31 December 2000 Focushawk entered into a verbal agreement with Caseacre to vary the tenant's proportion of the service charge from 13.7% to 5%. At the same time Caseacre agreed to pay all the

outgoings in respect what the appellant said was the outlying commercial property other than the 12 unit shops. The reason the appellant gave for this change was the high vacancy rate among the unit shops and the continued vandalism of the other commercial units, making them virtually unlettable. The verbal agreement was made the subject of a Deed of Variation to the headlease dated 1 January 2003. Later that year both Focushawk and New Horizons Management went into liquidation. Before doing so Focushawk sold the freehold interest in the residential units to Rowner Estates Limited and the freehold interest in the commercial properties to Caseacre (although the headlease was not subsequently merged with the freehold interest). Rowner Estates Limited was the holding company of Focushawk, New Horizons Management and Caseacre. Labyrinth Properties Limited was appointed as the new (professional) managing agent.

8. Between 1995 and 2003 Focushawk entered into five leases/agreements with telecommunications companies for the erection of aerials on the roof of the high rise residential blocks. The total initial income from these lettings was £17,500 per annum. The leases/agreements did not require the payment of a service charge.

The residential leases

9. A copy of the lease of Flat 34 Hillary Court was included within the evidence before both the LVT and this Tribunal and this was accepted as being representative of the terms of the residential leases granted in respect of the estate as a whole.

10. Under paragraph 3 of the Fifth Schedule to the lease the tenant covenants with the Landlord and the Company (the managing agent):

> "To pay to the Company the Service Charge which shall be the Due Proportion applied to the Annual Cost being reasonably and properly incurred by the Company in each Accounting Period (including a reserve for any future expenditure)."

"The Due Proportion" is defined in the First Schedule of the lease as:

> "a fair proportion of the Annual Cost (which proportion may vary for different categories of the Service Charge Works) attributable to the Flat together with such further categories as the Company shall from time to time determine such fair proportions to be determined by the Landlord's or the Company's Managing Agent or qualified surveyor or accountant whose decision save for manifest error shall be final and binding."

"The Annual Cost" means "the expenditure incurred by the Company in any Accounting Period in carrying out the Service Charge Works (including any sums which in the Accounting Period in question are set aside for future expenditure)."

"The Accounting Period" means the period of not more than twelve months commencing on 1 January and ending on 31 December each year."

"The Service Charge Works" are defined in the First Schedule as being "such services as specified in the Ninth Schedule as the Company shall from time to time in its discretion provide." These services include maintenance, repair, renewal, redecoration and cleaning of the estate as well as its insurance, security and management.

The LVT's decision

11. The LVT's decision is dated 15 July 2005. In paragraph 84 the LVT determined that:

> "The service charge schedules for each of the three years in issue are to be adjusted by taking into them the figures that the tribunal has determined in substitution for the amounts that have been varied. The charges are to be determined by reference to the apportionment between commercial and residential properties mentioned at paragraph 30, and by reference to the proportions payable by the two and three bedroom maisonettes respectively mentioned at paragraph 10."

12. Paragraph 30 is the last of five paragraphs under the heading "the Due Proportion" and states:

> "This tribunal is not bound by the decision of the previous tribunal, but sees no reason to depart from its findings upon the question of the division of the service charge between the residential and the commercial parts of the property. The evidence before it is that this was the division adopted apparently without any material dispute, for many years, and that it is only in the last two or three years that any attempt has been made to depart from that position. There has been no evidence adduced to suggest why such a departure may have been justified. Mr Faulkner [of Labyrinth Properties Limited] has not attempted to justify the change to the requirement for the commercial parts to pay 5% of the service charge only within the context of these proceedings. The tribunal has had the benefit of seeing the estate as a whole, and of satisfying itself from that inspection, as well as from the evidence before it, that the 86.3% – 13.7% split between residential and commercial appears to be reasonable and appropriate."

13. The previous decision of the LVT that is referred to is dated 19 December 2002. The decision relates to an application made by a residential tenant on the estate under the then section 19(2B) of the Act for a determination of the reasonableness of a service charge where costs were proposed to be incurred in the year 2002. Paragraph 161 of that decision states:

> "The total Service Charge which we are to determine as reasonable is applicable to both the residential and commercial premises. In evidence it became apparent that the lease to Caseacre Limited provides for a contribution of 13.7% of the Service Charge from that company in respect of the commercial properties. Mr Baker-Harber's reduction of this proportion to 5% was arbitrary and without any legal effect. Consequently only 86.3% of the total Service Charge we have determined as

> reasonable should be allocated to and payable by the tenants of the residential properties. The concessions offered by Mr Baker-Harber are not binding on him or his companies and could be withdrawn at any time. Any change, for whatever reason, in the relative proportions of the total Service Charge payable by the tenants of the residential properties and Caseacre Limited is a matter for agreement between the parties or determination by the Court and is not a matter for this Tribunal."

14. The proportions of the total service charge payable by the two and three bedroom maisonettes were specified in paragraph 10 of the 2005 LVT's decision as being 0.2987% and 0.3457% respectively.

Statutory provisions

15. The statutory provisions by reference to which the LVT reached its conclusions are set out in paragraph 23 of its 2005 decision:

> "The service charge applications made by Mr Münch in respect of the years 2003 and 2004, and by Rowner for the years 2004 and 2005, require the tribunal to determine, in accordance with section 27A of 1985 Act (as amended) whether a service charge is payable, the person to whom it is payable, the amount which is payable, the date at which it is payable, and the manner in which it is payable. Section 18 of 1985 Act defines the elements that are included in a service charge, namely costs for maintenance, improvement, insurance, or management of any specified description. Section 19 provides that service charges are only payable to the extent that they are reasonably incurred and, where they are incurred for the provision of services or the carrying out of works, only if the services or works are of a reasonable standard. The provisions of these sections govern the tribunal's consideration of those applications."

The case for the appellant

16. Ms Etiebet submitted that the LVT had erred in considering the apportionment of the service charge for five reasons. Firstly, it was irrational in principle for the LVT to have considered the issue at all when some of the parties affected by its decision were neither present at the hearing nor given the opportunity to make representations, ie Labyrinth Properties Limited (the managing agent who set the Due Proportion) and Caseacre (the commercial headlessee who was a party to the Deed of Variation to reduce the commercial proportion of the service charge to 5%).

17. Secondly, the LVT had not used the appropriate test to decide whether it was able to adjudicate upon the apportionment of the service charge. It had not considered whether the managing agents had made a "manifest error" by increasing the Due Proportion of the service charge attributable to the residential tenants to 95% of the total. The LVT was bound to consider the matter by reference to the residential lease. But it made no mention of manifest error in its decision and Mr Faulkner's evidence was that the LVT had not considered the

definition of the Due Proportion contained in the residential lease, preferring instead to focus upon the proportion payable by Caseacre under the headlease (13.7%). The LVT's failure to address such an important issue meant that it was reasonable to infer that it had not received any or sufficient consideration, as per *R v Brent LBC ex parte Bariise* (1999) 31 HLR 50 CA. Furthermore, and in any event, the LVT was not able to conclude that there had been a manifest error because it had found that "there has been no evidence adduced to suggest why such a departure [from the previous apportionment of 86.3% - 13.7%] may have been justified." Ms Etiebet submitted that the proper course for the LVT to have taken in the absence of such evidence was to make a direction calling for its production. In fact the 2005 LVT had taken account of the 2002 LVT decision which itself recorded the reasons why the departure was considered justified by the appellant. Consequently there was evidence before the 2005 LVT in support of the adjustment to the service charge apportionment.

18. Thirdly, even if the LVT had properly considered that there had been a manifest error, it had been irrational to determine that there was no reason to depart from the 2002 LVT's findings. Those findings were flawed because the relevant terms of the commercial headlease had not been consulted and the LVT had been wrong to conclude that the reduction of the tenant's proportion from 13.7% to 5% "was arbitrary and without any legal effect." The definition of the "Tenant's Proportion" in the headlease was 13.7% of the total service charge for the estate or "if the landlord shall hereafter so determine such other proportion as to the landlord shall seem fair and equitable." The reduction was therefore in accordance with the terms of the headlease which did not require that a reason be given for exercising the right to vary the Tenant's Proportion. Nor was it an arbitrary reduction; Mr Baker-Harber had given unchallenged evidence before the 2002 LVT explaining why the reduction had been made.

19. Fourthly, the LVT used the wrong test when deciding the appropriate figure for the Due Proportion to be paid by the residential tenants. The lease required the determination of a fair proportion whereas the LVT determined a figure that it considered to be "reasonable and appropriate".

20. Fifthly, the LVT failed to take account of a number of relevant factors. It knew that the commercial properties other than the unit shops had been taken out of the service charge regime because they were derelict, were no longer covered by insurance and received no services. It was therefore irrational to conclude that the remaining 12 shops should take up the shortfall of 8.7%. The Deed of Variation signed in January 2003, which reduced the Tenant's Proportion under the headlease to 5%, was known to the LVT but not under challenge. Neither was the question of whether that 5% was a fair and equitable proportion under the terms of the headlease. It was therefore irrational and beyond its jurisdiction for the LVT to assign 13.7% to the commercial element. The LVT failed to take account of the fact that the landlord would have to make up any shortfall between the 13.7% commercial apportionment determined by the LVT and the 5% provided for in the Deed of Variation. That was irrational since it was the tenants, whether residential or commercial, that benefited from the services and who should therefore pay for them. The residential tenants would benefit disproportionately from the LVT's decision.

21. In his evidence Mr Faulkner explained that the number of commercial units receiving services from the estate had been reduced. The NAAFI supermarket and former Ministry of Defence stores and offices had required considerable monies spent on them, notably in respect of boarding up, dealing with fires and other acts of vandalism. These units posed a considerable insurance risk and had been removed from the insurance cover. Under the December 2000 verbal agreement, that subsequently formed the subject of the 2003 Deed of Variation, Caseacre, as headlessee, agreed to pay for all of the outgoings on these buildings. Mr Faulkner said that to take them back into insurance cover would increase the premium for the estate from £129,000 per annum to just over £220,000 per annum. He estimated that the additional costs would be between £200,000 to £230,000 per annum if the total costs of including these buildings back into the service charge regime were taken into account including security, repairs, the cost of boarding up the premises and the increased insurance premium.

22. Mr Baker-Harber acknowledged that the commercial headlease contained separate covenants by the tenant to pay additional rent to the landlord in respect of insurance (clause 6.3.1) and to pay additional rent in respect of the services provided by the landlord which included insurance (clause 3.5 and the Fourth Schedule). The occupational subleases also made such a double provision for insurance and the sublessees had apparently been charged twice for the insurance premium until Labyrinth Properties Limited identified the overcharging. Thereafter the commercial sublessees paid additional rent for insurance only through the service charge.

23. Mr Dawson considered the reduced commercial contribution of 5% of the service charge to be fair and equitable under the circumstances. Ms Etiebet submitted that treating the outlying commercial property as though it did not exist for the purposes of the service charge apportionment was fair because, in absolute terms, the tenants of the shops and residential units would pay less. The arrangement was fair and equitable to Caseacre because, although its service charge contribution had been reduced, it was liable for any expenditure required in respect of the outlying commercial properties. Those properties received no benefit from the services provided to the other tenants. The apportionment of 5% of the service charge to the unit shops was fair and equitable because it was close to the historic contribution of 4.368%.

24. It was decided by the appellant in 2003 that it would be fair to assign the 8.7% shortfall in the service charge to the residential tenants. Ms Etiebet gave a number of reasons why this was justified and why the revised apportionment could not be considered a manifest error. Firstly, if the appellant had to pick up the shortfall then it would be unable to do so given its limited rental income from the residential ground rents and would probably follow Focushawk into liquidation. The residents would be left to manage the estate against the known background of their having done so poorly previously.

25. Secondly, it was not fair for the unit shops to make up the shortfall on their own. There were only 12 of them compared with 301 residential units and their contribution under the revised apportionment had increased from 4.368% to 5%, a percentage increase of 14.5%. By contrast the residential tenants faced an increase in their service charge contribution from 86.3% to 95% a percentage increase of 10.1%. The proportionate allocation of the service charge to the

residential units, having removed the outlying commercial property from the charging regime, would be 86.3/90.668 x 100 which equals 95.2%. Even after this increase the average contribution of a residential unit (0.32%) remained less than that of each unit shop (0.42%).

26. Thirdly, as described above, to bring the outlying commercial units back into the service charge regime would lead to a significant increase in the absolute amount of that charge.

27. Fourthly, the residential units would benefit disproportionately were the apportionment of the service charge to remain in the historic ratio of 86.3% - 13.7%. Mr Faulkner explained that the great majority of the cleaning services were for the benefit of the residential units with 16 stairwells and a quarter of a mile of walkways having to be cleaned. The unit shops meanwhile were serviced from the precinct. They did not use the lifts. In 2002 a five-year plan had been prepared to remedy the disrepair on the estate most of which related to the residential units, eg replacing the lifts, electrical repairs to the residential blocks and redecorating the residential communal areas.

28. Fifthly, Ms Etiebet made a qualitative distinction between the shops and the residential units. Mr Faulkner explained that the estate was run down and that it was difficult to let the shops. Indeed there had been no increase in rent since 1989. Some of the units had been occupied by charities whose charitable purposes had been of direct help to the residents. It was beneficial to the estate as a whole that as many shops as possible were occupied. To place a higher burden of apportionment upon the commercial units would not be justified and would risk the further deterioration of the important social function provided by the shops.

29. Ms Etiebet submitted that this Tribunal should:

(i) quash the decision of the LVT that the residential tenants should pay 86.3% of the total service charge; and

(ii) find that the decision of the managing agent to assign the 8.7% shortfall to the residential units was fair and not in manifest error; and

(iii) determine that the residential tenants should pay 95% of the total service charge for 2003, 2004 and 2005.

Conclusions: the extent of the appeal

30. The appellant seeks a determination of the service charge apportionment for the three years 2003, 2004 and 2005. In his order dated 19 May 2006 His Honour Michael Rich QC granted permission to appeal only in respect of the Due Proportion for the years 2004 and 2005. The decision of the LVT regarding the service charge payable for the year 2003 had been reached in respect of an application made by Mr and Mrs Münch and not by the appellant. The Member acknowledged that, in his previous orders, he should only have granted

permission to appeal in respect of those cases where the appellant had been applicants before the LVT, namely in respect of the years 2004 and 2005.

31. At the hearing Ms Etiebet invited me to reconsider this decision but I declined to do so for two reasons. Firstly, in his order dated 19 May 2006, and in the light of the amendments that he had made to his previous ruling about the extent of the appeal, His Honour Michael Rich QC granted permission to the appellant to add to or vary its statement of case by 2 June 2006. The appellant did not do so. Secondly, although Mr and Mrs Münch withdrew their response to the appeal before the hearing they did so in the knowledge of the order. To allow the appellant to re-open the issue of the 2003 service charge before the Tribunal would, in my opinion, have unfairly disadvantaged Mr and Mrs Münch.

Conclusions: the LVT's consideration of apportionment

32. I do not accept Ms Etiebet's first ground for challenging the jurisdiction of the LVT to determine the apportionment of the service charge, namely that it was irrational in principle to do so. Mr Faulkner represented the appellant at the 2005 LVT and gave evidence in his capacity as a director of Labyrinth Properties Limited, the managing agent that set the Due Proportion under the residential leases at 95% of the total service charge. It was not procedurally improper for Mr Faulkner to speak about apportionment as Ms Etiebet suggested. I also note from Mr Baker-Harber's evidence before this Tribunal that the appellant company, Rowner Estates Limited, owned Caseacre Limited. It seems to me that, contrary to Ms Etiebet's submission, all relevant parties had the opportunity to make representations at the 2005 LVT hearing.

33. I consider that Mr and Mrs Münch's application, relating as it did to one particular residential unit, could not have been determined as to the amount of the service charge payable by them without consideration of the Due Proportion under their lease. Furthermore the respondents to the two applications made by the appellant were 110 out of a total of 301 residential tenants. The issue of apportionment was relevant to the amount which they as individuals would be required to pay. I therefore believe that the LVT was correct to have considered the issue of the Due Proportion payable by the residential tenants even if this was not requested explicitly in the applications.

Conclusions: the LVT's assessment of the Due Proportion

34. The LVT concluded that an 86.3% (residential) – 13.7% (commercial) split of the service charge was "reasonable and appropriate". The LVT apparently interpreted section 19 of the Act as requiring a reasonable apportionment of costs that had been reasonably incurred. But that is not what that section provides. As His Honour Michael Rich QC said in *Schilling and Others v Canary Riverside Development PTD Limited* (2005) Lands Tribunal LRX/26/2005 (unreported) at paragraph 19:

> "Costs are to be taken into account 'only to the extent that they are reasonably incurred', but if reasonably incurred they fall to be apportioned in accordance with the terms of the lease, except if excluded by a failure to consult or otherwise under for example ss20B and 20C."

35. Ms Etiebet submitted that the LVT should have determined the Due Proportion solely by reference to the residential leases. The LVT appears to have relied upon the decision of the 2002 LVT at paragraph 161 which states that:

> "Any change, for whatever reason, in the relative proportions of the total Service Charge payable by the tenants of the residential properties and Caseacre Limited is a matter for agreement between the parties or determination by the Court and is not a matter for this Tribunal."

I believe that the LVT was wrong to have accepted this reasoning, which it does implicitly in paragraph 30 of its decision, and that it had jurisdiction to interpret the residential leases on this point. As His Honour Judge Rich QC said in *Longmint Limited v Marcus* [2004] 3 EGLR 171 at 172C:

> "It is, in my judgment, however quite wrong for the LVT to decline jurisdiction to construe a lease if its true construction is determinative of a matter that the LVT has to decide. It may, as a matter of discretion, decline to determine a point of construction because it is better determined by other means. If however, no provision has been made or accepted by the parties for such other determination, the LVT, in my judgment, not only has jurisdiction but has a duty to construe the lease in so far as is necessary in order either to determine its own jurisdiction to determine an application, made to the LVT under section 19 of the Act, or to determine how it should exercise such jurisdiction as it decides that it has."

The application in 2002 was made under section 19(2A) of the Act whereas the applications that are the subject of this appeal were made under section 27A of the Act which replaced the relevant subsections of section 19. However the same principle still applies. In the absence of provision to the contrary the jurisdiction of the LVT to make its determination depends not only upon the proper construction of the statutory provisions but also upon the proper construction of the residential lease.

36. Unlike the commercial headlease and subleases the residential leases do not specify a fixed service charge proportion. The historic allocation of 86.3% of the service charge to the residential units was based upon the ratio of the areas of residential to commercial floor space. The Due Proportion determined under the residential leases must be a fair proportion of the Annual Cost as determined by the appellant's managing agent and whose decision shall be binding and final save for manifest error. There is nothing in the residential leases to suggest that 86.3% is immutable and that an apportionment based upon floor areas is necessarily the only one that is fair.

37. It was open to the appellant under the residential leases to vary the apportionment of the service charge payable by the residential tenants provided this led to a fair result and avoided manifest error. I do not believe that it is possible, given that the residential and commercial units share commonly provided services, to determine the fairness of the residential Due Proportion of the service charge without regard to the service charge proportion determined, or varied, under the commercial headlease. The appellant decided, given the physical deterioration of the outlying commercial units and their persistent unlettability, that an apportionment made on the basis of floor areas was no longer fair, despite the established historical precedent of such a method. The alternative that the appellant adopted was to remove the outlying commercial units from the service charge regime and to make the headlessee, Caseacre, responsible for paying all of the outgoings on such property. This was put into effect by means of a verbal agreement between Focushawk and Caseacre reached in December 2000 that was subsequently incorporated into a Deed of Variation dated 1 January 2003.

38. It was this agreement, reducing the Tenant's Proportion under the headlease from 13.7% to 5%, that the 2002 LVT described as being arbitrary and without any legal effect, a conclusion implicitly adopted by the 2005 LVT. I assume that this statement was based upon the 2002 LVT's acceptance of the applicant's case that:

> "Mr Baker-Harber's evidence as to whether Caseacre's lease was formally amended was initially unsatisfactory, but he did eventually admit that it had not been" (paragraph 57).

The failure of the appellant to regularise the verbal agreement reached in 2000 was explained before the 2002 hearing:

> "As a Director of both companies [Focushawk and Caseacre], Mr Baker-Harber could have attended to this formality but this would only be a cosmetic exercise reflecting what has now long been the position on site" (paragraph 93e)

39. Nevertheless the appellant hurriedly entered into a formal Deed of Variation on 1 January 2003 following the LVT's decision on 19 December 2002. The deed refers to a lease made between Aldersgate Developments Limited and Caseacre dated 18 April 1989. At the hearing before me Mr Baker-Harber acknowledged that there was no such lease and that the reference should have been to the headlease dated 13 July 1988. Furthermore the deed failed to identify specifically the property that it sought to exclude from the service charge regime. It stated at clause 2.3:

> "By agreement reached between the Landlord [Focushawk] and the Tenant [Caseacre] on 31 December 2000 the Landlord agreed to reduce [to 5%] the service charge proportion payable by the Tenant under the Lease following the Tenant's agreement to pay all the outgoings on certain properties demised by the Lease."

These "certain properties" were said in evidence before me to comprise the outlying commercial units other than the 12 unit shops. The close connection between Focushawk and Caseacre is evident from the fact that the Deed of Variation was signed by Mr Baker-Harber as a director, and by Diane Baker-Harber as the Secretary, of both companies.

40. The Deed of Variation is a poorly drafted document between connected persons. However, from the totality of the evidence I am satisfied that it reflected an agreement between Focushawk and Caseacre about a variation in the Tenant's Proportion under the commercial headlease that both parties considered fair and equitable. The Deed of Variation was known to the 2005 LVT (see for instance paragraph 27 of the 2005 decision). It did not, in the light of this knowledge, disagree with the earlier LVT's decision that the variation was without legal effect. The circumstances had materially changed between the two hearings and in my opinion the LVT was wrong not to recognise this. I do not accept that the variation of the Tenant's Proportion was without any legal effect by the time of the 2005 hearing.

41. The 2002 LVT also found that the variation in the commercial apportionment of the service charge was arbitrary. The 2005 LVT concluded at paragraph 30 that:

> "There has been no evidence adduced to suggest why such a departure [from 13.7% to 5%] may have been justified. Mr Faulkner has not attempted to justify the change to the requirement for the commercial parts to pay 5% of the service charge only within the context of these proceedings."

Mr Baker-Harber raised the main points of the appellant's argument about the apportionment before the 2002 LVT. Mr Faulkner's evidence before the 2005 LVT is reported in its decision to be limited to making the point (accepted by the LVT) that the LVT's jurisdiction did not extend to determining who should pay the 13.7% of the service charge specified under the headlease.

42. I have had the benefit of hearing the evidence of Mr Faulkner and Mr Baker-Harber on this issue, such evidence having been admitted in accordance with His Honour Michael Rich QC's order dated 19 May 2006. I also heard the expert evidence of Mr Dawson. The justification for the change in the percentage of the service charge paid by the commercial units has been explained in detail in paragraphs 21 to 23 above. The appellant's explanation of why it was fair to assign the resulting shortfall of 8.7% of the service charge to the residential units appears at paragraphs 24 to 28 above. I do not agree with the LVT that this variation was arbitrary. Its provenance was explained and I found the appellant's evidence on this point to be persuasive.

43. In my opinion, and upon the evidence presented to this Tribunal, the assessment of the Due Proportion of the total estate service charge on the basis of 95% (residential) – 5% (12 commercial shops) is fair and in accordance with the terms of the residential leases provided the outlying commercial units are not brought back within the service charge regime.

44. The apportionment in respect of the two and three bedroom maisonettes was stated in paragraph 10 of the 2005 LVT decision as being 0.2987% and 0.3457% respectively. The LVT determined that these proportions should apply to the apportionment of the service charge referred to in paragraph 30 of its decision, namely 86.3% - 13.7%. I believe that it was wrong to have done so because these proportions appear to reflect the appellant's apportionment of 95% - 5%. In any event I calculate that the proportions are slightly too high and I believe that

they should be assessed as 0.2982% and 0.3451% for two and three bedroom maisonettes respectively.

45. I therefore allow the appeals in respect of the years 2004 and 2005 and determine the Due Proportion payable in these years under the residential leases as being 0.2982% and 0.3451% for each two and three bedroom maisonette respectively.

Dated 18 October 2007

A J Trott FRICS