4221

FIRST - TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case Reference	:	LON/00BK/OLR/2011/1214
Property	:	Flat 124A, 4 Whitehall Court, London, SW1A 2EP
Applicant	:	Michael Rossman
Representative	:	In person
First Respondent	:	Crown Estate Commissioners
Representative	:	Jonathan Upton (Counsel)
Second Respondent	:	Whitehall Court London Limited
Representative	:	No appearance
Type of Application	:	Enfranchisement
Tribunal Members	:	Judge Robert Latham Richard Shaw FRICS
Date and venue of Hearing	:	24 and 25 May 2016 at 10 Alfred Place, London WC1E 7LR
Date of Decision	:	22 June 2016

DECISION

The Tribunal modifies clause 2.21 of the proposed lease by substituting for "0.8%" the following: "0.62% (calculated by reference to the formula in the voluntary abatement scheme described in the schedule annexed to the lease) or such other fair and reasonable proportion as the Lessors may reasonably determine from time to time".

Introduction

1. On 25 March 2011, by a notice of claim served under section 42 of the Leasehold Reform, Housing and Urban Development Act 1993 ("the 1993 Act"), Mr Rossman gave notice of his intention to acquire a new lease of Flat 124A, 4 Whitehall Court, London, SW1A 2EP ("the flat"). The Flat is in one of two blocks known as 3 and 4 Whitehall Court ("the development").

2. The sole issue which we are required to determine is the modification which must be made to clause 2.21 of the proposed new lease with regard to how Mr Rossman's service charge contribution should be formulated. Clause 3A of his current lease requires him to contribute a fixed 0.8% of the relevant service charge expenditure.

3. Initially, the aggregate of the fixed service charges amounted to 100% of the expenditure. That is no longer the position. Over time, as a result of additional flats being added to the development, the aggregate of the service charge contributions payable under the leases now amount to 129% of the expenditure. The landlord has adjusted the sum demanded under an extra-contractual scheme so that the service charge collected is only 100% of the expenditure. Under the scheme, the lessees are only required 0.775% of the sum that they are contractually obliged to pay.

4. Whilst it is correct to describe the adjusted scheme as "extra-contractual", statute does not permit a landlord to profit from the service charge account. Section 42 of the Landlord and Tenant Act 1987 provides that a landlord is obliged to hold any service charge funds on trust (a) to defray costs incurred in connection with the matters for which the relevant service charges were payable and (b) subject to that, on trust for the contributing tenants.

5. On 23 September 2013, a First-tier Tribunal (FTT) determined that the service charge provisions of the new lease should be granted on the same terms as the existing lease. The FTT found that Mr Rossman had not established a case for modifying the term under either section 57(6)(a) or (b) of the Act. On 25 May 2015, Mr Rossman successfully appealed this decision to the Upper Tribunal. The decision of the President, Sir Keith Lindblom, is reported at [2015] UKUT 288 (LC).

6. The President remitted the case to this Tribunal so that we 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.

The Hearing and Inspection

7. There are three parties to this application:

   (i) Mr Michael Rossman, the lessee, who appeared in person. He derives his interest from a lease dated 14 December 1969 (at C47 of the Bundle). On 4 August 1989, there was a surrender and regrant for a term of 99

years from 25 March 1987 (at C60). On 16 August 2006, Mr Rossman acquired the lease of the flat (C59).

(ii) The Crown Estate Commissioners ("CEC") are the freeholders and the "competent landlord" for the purpose of Chapter II of Part I of the 1993 Act. They were represented by Jonathan Upton, Counsel, who was instructed by Pemberton Greenish LLP. On 23 April 2007, the CEC were registered with the freehold title of Whitehall Court. The Office Copy entries indicate that there have been leasehold extensions under the 1993 Act in respect of some 33% of the flats. Neither party adduced any evidence in respect of these extensions. There is no evidence that the service charge contribution reserved in the leases caused any difficulties in negotiating the requisite 90 year extensions.

(iii) Whitehall Court London Limited ("WCLL") are the intermediate landlord. WCLL was registered with their interest on 17 December 2013. They derive their interest from a lease dated 12 May 1987 (at C41) granted by the CEC to Whitehall Court (Holdings) Ltd. On 11 September 1989, the head lease was assigned to Whitehall Court (Investments) Ltd ("WCI" - see C421). WCLL provide the services at the block and operate the service charge account. On 18 June 2015, WCLL served a Notice to act independently from CEC (A87). Mr Rossman challenged their right to appear and this led to an application for permission to appeal to the Upper Tribunal (at A96). WCLL now support the terms of acquisition proposed by the competent landlord and did not appear before us.

8. Neither Mr Rossman nor Mr Upton adduced any evidence. Mr Rossman relied on a Skeleton Argument which largely repeated the material which he had filed on 30 March 2016 (at A1-57B). Mr Upton relied on this Statement of Case, dated 4 April 2016 (at A58-69). This attaches a schedule which indicates how the extra-contractual scheme has operated (at A68-69).

9. The Tribunal completed its hearing on 24 May. On 25 May, we inspected the flat and the development. We were accompanied by Mr Rossman and Mr Dyer from Savills on behalf of CEC. Paul Farrell, from Stiles Harold Williams ("SHW"), the managing agents employed by WCLL, was also present. The purpose of the inspection was not to receive any further evidence. It was rather to give the Tribunal a better understanding of the evidence and issues which had canvassed at the hearing.

The Submissions of the Parties

10. Mr Rossman asks us to consider three possible modifications to Clause 2.21:

(i) Clause 2.21 should be excluded so as to void the service charge contribution. He argues that as the CEC has failed to propose any modification that is capable of remedying the defect, the only remedy is to exclude it. Mr Rossman contended that this would cause no injustice to the landlord as it would still recover more than 100% of the sums

needed to cover the service charge expenditure. Further, it would not create any anomaly as the tenants of Flats 58 and 148 currently make no contribution. He complained that "for as long as Whitehall Court has existed, the landlord has cut special and unique deals with leaseholders, often to the detriment of others". By objecting to WCLL's right to appear, Mr Rossman denied the Tribunal with the opportunity to seek an explanation from WCLL who currently operate the service charge account, as to how the current situation has developed. Strictly, Mr Rossman's formulation would be an "exclusion" rather than a "modification" of the term.

(ii) Clause 2.21 should specify a fixed contribution of £3,755.86 which the landlord could increase in line with inflation. This would reduce his current contribution to 0.193% of the overall service charge expenditure compared with the fixed figure of 0.8% which is currently specified in his lease, and 0.6201% which is his net contribution under the extra-contractual scheme. Mr Rossman contends that this would be a "fair and reasonable" contribution for his flat. This figure is intended to reflect in real terms the contribution that the lessee was required to pay in 1969 when the original lease was granted. Mr Rossman complains that since 1969, the service charge expenditure has increased in real terms by three times more than inflation. He contends that since 1969, there have been a number of physical and ownership changes in Whitehall Court which have had a substantial and material effect on the operation of the service charge regime.

(iii) Clause 2.21 should be modified "to use a modern apportionment methodology based on current best industry practices". Mr Rossman's preferred apportionment would seem to be based on floor area of the respective flats, rather than a fixed percentage. Any apportionment should "have regard to physical size, benefit to and use by occupiers". He suggests that a weighted apportionment should be used as is common to shopping centres or mixed used developments. Mr Rossman argues that his contribution should be reduced to 0.287%.

11. Mr Upton proposes two options:

(i) Mr Upton argues that it is for the applicant to propose a modification that is capable of remedying the defect in the lease. Any modification must not merely ameliorate the defect, but must cure it. He contends that Mr Rossman has signally failed to propose such a modification and highlighted the manifest flaws in his three formulations. Where an applicant is unable to propose a solution, the default position is that the new lease should be granted on the same terms as the existing lease. The Tribunal should therefore include Clause 2.21 without modification.

(ii) Alternatively, Clause 2.21 should be modified to incorporate the extra-contractual scheme which has been operated by the landlord. In Clause 2.21, the reference to "0.8" should be modified to read "0.62% (calculated by reference to the formula in the voluntary abatement

scheme currently operated by the landlord) or such other fair and reasonable proportion to be determined by the Lessor from time to time acting reasonably". Mr Upton contends that the current abatement scheme is adequately described in the table annexed to his Statement of Case (at A68-69). The President had considered this modification at [54] of his judgment. The Tribunal pointed out that it would have been open to the President not only to have allowed this appeal, but also to have made this modification. The President had rather concluded that he was not satisfied on the submissions made to him that it would be right to take this course. Mr Upton responded that at the Appeal, the CEC had not contended for this outcome. This was now their fallback position. The Tribunal further pointed out that the President had remitted the matter to us to determine how the service charge provision should be determined "in the light of full evidence" and "relevant expert evidence". Neither party had adduced evidence to explain how the original percentages were computed, the point of time at which the fixed percentage charges had amounted to 100%, or how the current situation had arisen. Mr Upton responded that the CEC did not operate the service charge account and had no knowledge as to how the situation has arisen. These were rather matters for the intermediate landlord.

The Law

12. 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 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 (emphasis added):

> "(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—
>
> > of the omission from the new lease of property included in the existing lease but not comprised in the flat;
> >
> > of alterations made to the property demised since the grant of the existing lease; or
> >
> > 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.
>
> .....

(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—

> it is necessary to do so in order to remedy a defect in the existing lease; or
>
> 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."

13. For the purposes of Sub-section 6(b):

    (i) the "date of commencement of the existing lease" is 4 August 1989, the date of the surrender and regrant of Mr Rossman's leasehold interest,

    (ii) the "relevant date" is 25 March 2011, the date of Mr Rossman's Notice of Claim to exercise his right to an extended lease.

The Background

14. Whitehall Court is one of two contiguous building which overlook the River Thames in Westminster. Nos. 1 and 2 are occupied by the Royal Horseguards Hotel. Nos. 3 and 4 ("the development") contains both residential accommodation and commercial uses, including the Farmers Club. The development has a basement, a ground floor, an upper ground floor and seven floors above, and further accommodation in the six towers and within the roof. It is Grade II* listed. It looks out onto Whitehall Gardens. It is in Prime Central London.

15. The development was built during the mid-1880s by Archer and Green, with finance provided by Jabez Balfour. It is an imposing neo-Gothic building with marble, alabaster, stained glass and other periodic features. There is a large boiler room which extends underneath the pavement. Originally, the development contained serviced apartments with communal facilities. These included the typical communal facilities for that era such as reading and living rooms, a restaurant and a service kitchen. The apartments did not have kitchens. There have been a number of illustrious residents, many involved in politics. The colourful story of the development is described by David McKie in "Jabez: The Rise and Fall of a Victorian Rogue".

16. In the 1960s and 70s many of the rooms and suites in the development were converted into self-contained flats and sold on long leases at a premium, with a ground rent and service charge. It would have been necessary to install kitchens in all the residential flats. As we saw in Mr Rossman's flat,

imaginative solutions have been required, given the listing attached to the building. His flat has been reconfigured to provide a large living room at the front, a small walk-in kitchen, and two small bedrooms in the rear.

17. Penthouse flats were added in the roof and six towers. These would afford superb views of the Thames and of the surrounding areas. We were told that the restaurant (in the adjoining building outside the development) was converted into a hotel in about 1968. There are now 115 residential flats let on long leases in the development. Our inspection confirmed a history of past neglect and botched works. In the common parts, the cast iron frame is corroding and dislodging the marble finishes. The original finishes in No.3 are of a somewhat higher quality that those in No.4. The process of change from office to development use is continuing. Our inspection confirmed that this is an expensive and unpredictable block to maintain. Attempts are now being made to restore the development to its former glory.

18. We also inspected externally 1 Horseguards Avenue, a commercial unit to the south of the development and part of the block. This is currently in commercial use. Mr Rossman complains of the contribution that this unit makes to the service charge expenditure.

19. At some unspecified date, the aggregate of the fixed percentage service charge contributions amounted to 100%. Neither party was able to explain 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.

20. The Tribunal has been provided with the Service Charge Budget for the Year ending 24 December 2016 (at A38). We note the contributions by the Farmers Club to the staff costs and by the Hotel to the supply of heating and hot water. There is a reception area which is staffed. We inspected the boiler room which provides heating and hot water to all the buildings. Lifts serve the flats. Repairs are currently being executed to the common parts. The landlord cleans the common parts. It is not for this Tribunal to determine the reasonableness of the service charges but rather the contribution that Mr Rossman should be required to make towards the service charge expenditure under the terms of his new lease.

21. The Notice of Claim, dated 25 March 2011 (at C17) 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 a 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.

22. By a Counter-Notice, dated 16 May 2011 (at C21), the CEC, the freeholder and "competent landlord" for the purpose 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.

23. On 14 November 2011 (at C1), Mr Rossman applied to this Tribunal to determine the premium to be paid and the other terms of acquisition which remained in dispute. The premium and terms of the new lease have been agreed, save for clause 2.21, in respect of the service charge contribution payable by the lessee.

24. The current term proposed by the CEC reads as follows:

> "2.21 That the Lessee in the manner hereinafter provided pay to the Lessors 0.8% (zero decimal point eight per centum) (hereinafter called "the contribution") of the reasonable costs and expenses incurred by the Lessors in compliance with their obligations under Clause 3 hereof together with all other costs and expenses incurred in the management of the Building and other the property of which the Flat forms a part together with the cost of maintaining servicing overhauling repairing and when necessary rebuilding renewing and reinstating such premises furnishing and equipment and of providing all normal utilities outgoings and services to such premises on the expiration or sooner determination of the headlease including without prejudice to the generality of the foregoing where accommodation is provided for the use occupation or residence of any staff (either within the Building or elsewhere) a sum equivalent to the market rent of such accommodation (hereinafter called "the expenditure)."
>
> This reflects Clause 3(A) in the lease dated 14 February 1969.

25. On 25 August 2011, Mr Rossman, together with 36 other lesees at the development, made a separate application under section 35 of the Landlord and Tenant Act 1987, seeking to vary the service charge provisions in their leases. Cross-applications under section 36 were made by the CEC and by WCI. A number of other lessees became respondents to the proceedings.

26. Section 35(1) of the 1987 Act 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".

27. 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."

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

29. On 11 February 2013 the Leasehold Valuation Tribunal ("LVT") issued its decision refusing to order any variation (LON/00BK/LVL/2011/0013). The hearing had been conducted over two days on 15 and 16 January. Four Counsel were involved: Mr Mark Loveday appeared for Mr Rossman and 36 other lessees; Mr Tim Hammond for the lessees of Flats 3, 96B and 154; Mr James Sandham for the lessee of Flat 148; and Mr Upton for the CEC. WCI were represented by Mr Nicholas Faulkner, from SHW. There was no consensus as to how the service charges should be apportioned.

30. The LVT discussed the issues in the section 35 application at [122] to [141]. It acknowledged that its discretion was wide ([123]), but concluded (at [127]):

> "In our judgment on an application to vary the terms of a lease under section 35 or section 36 of the 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."

31. The LVT 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" ([128]). It saw nothing to suggest that the development was not being properly maintained ([129]). At [130] the LVT observed:

> "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. WCI 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."

32. The LVT concluded (at [131]) that this was not an appropriate case for intervention to disturb "the contractual scheme as adjusted and operated by WCI". The LVT summarised its reasons for this decision at [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 WCI, 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."

33. On 29 May 2013 the LVT refused the lessees permission to appeal its decision. On 9 September 2013, the Upper Tribunal refused permission to appeal. The President considered this decision at some length, with apparent approval.

34. The LVT gave the most careful consideration to the various modifications proposed by the parties. We highlight the following:

    (i) The LVT considered Mr Rossman's proposal for the service charge to be apportioned by reference to the floor area of each flat. The lessees considered a number of different variations (see [33] to [38]). The reasons for rejecting this proposed variation are set out in detail at [132] to [135]. The LVT was not satisfied that floor area was a fair method of apportionment. The LVT noted the difficulties presented by the mixed uses, namely residential, commercial and the Farmers Club. All these units were intermingled. Moving to a floor area basis

would be expensive and it was far from clear that an appropriate methodology could be agreed. Further, it would undo and undermine the specific contractual arrangement for the apportionment of the service charges which was based on a fixed percentage.

(ii) The LVT considered the apparent anomaly in respect of Flat 58 at [40]. Prior to the grant of the headlease, this flat had been demised with the adjacent hotel and had been used as a meeting room. It now enjoyed heating and lighting but paid for these services on a meter.

(iii) The LVT considered the apparent anomaly in respect of Flats 148 and 148a at [43] to [50]. It is apparent that no service charge is payable by Flat 148 because it is rather charged to Flat 148A. Thus it is the lessee of Flat 148A who has a grievance, rather than the other lessees.

35. Even though these matters had been considered in detail by the LVT, Mr Rossman still asked us to revisit them. We see no reason to depart from the careful findings made by the LVT. We remind ourselves that we are concerned only with the contribution that should be made by Mr Rossman. We have no jurisdiction to vary the service charge contributions of the other lessees. However, any decision that we make in respect of Mr Rossman's lease, potentially has implications for other lessees.

36. On 2 July 2013, the current application for a lease extension under the 1993 Act was first considered by a FTT. Mr Rossman argued that clause 2.21 of the draft new lease should be modified so that the service charge contribution in the new lease should be a fair proportion based on square footage. The CEC 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). On 23 September 2013, the Tribunal published its decision and determined that the service charge provisions of the new lease should be the same as in the exiting lease (unless the parties agreed different terms).

37. On 25 May 2015, Mr Rossman successfully appealed this decision to the Upper Tribunal. The President (at [48]) accepted his submission that the term in the existing lease which required of the lessee to pay a fixed service charge contribution of 0.8% was 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. He also saw 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).

38. The President found (at [7]) that "initially, the aggregate of the fixed percentage service charge contributions amounted to 100%". Neither party to the appeal knew how the fixed percentages had been calculated. Over time, as a result of additional flats being added to the development, the aggregate of the service charge contributions payable under the leases at Whitehall Court now amounted to 129% of the expenditure. The landlord adjusted the sum demanded under an extra-contractual scheme so that the service charge

collected was 100% of actual expenditure. This was not found to be sufficient to remedy the defect.

39. The parties have referred us to various passages of the President's judgment. We have added our own emphasis:

> "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 .... 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 ...".
>
> .....

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.

.....

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."

40. The CEC sought permission to appeal this decision. On 19 June 2015, the President refused permission in robust terms (at A88). He described the 8% fixed figure as "anachronistic and indefensible, and demonstrably so". He added that "it would be hard to imagine a clearer case of a term defective within the meaning of section 57(6)(a), and whose inclusion in the new lease would be unreasonable within the meaning of section 57(b) in view of changes that have occurred since the commencement of the existing lease". He concluded in these terms:

> "If the Crown Estate Commissioners really cannot agree with Mr Rossman how the flawed term should now be amended, each side will have the opportunity, in an adversarial hearing, to present evidence to support the provision for which it contends. If that is what happens, the First-tier Tribunal will be well able to decide how the service charge provision in the new lease ought to be framed".

41. The CEC subsequently sought permission to appeal from the Court of Appeal. On 27 October, Lady Justice Glossop refused permission to appeal (at A90). She was satisfied not only did the proposed appeal fail to meet the high threshold for a second appeal, but also that there was no reasonable prospect of successfully arguing that the Upper Tribunal was wrong in law to hold that the lease was "defective" for the purposes of section 57(6)(a) of the 1993 Act.

42. On 24 November 2015, the Tribunal gave Directions for the hearing (at A91). Each party was required to serve the following:

(i) a statement of case, with any legal submissions, dealing only with the question posed by the UT;

(ii) a list of proposed outcomes, marked clearly as being the parties' first, second and third (or more) preferences, with reasons why;

(iii) any witness statements of fact.

43. Neither party has served any witness statements. "No relevant expert evidence" has been adduced by either party as was contemplated by the President (at [52]). Both parties have filed their Statements of Case and their proposed modifications.

Our Determination

44. The President has made an express finding that there is a defect in the existing lease and that it is necessary for this to be modified for the purposes of section 57(6)(a) (see [48] of his decision). We are therefore required to determine what that modification should be (see [56]).

45. The President left open the separate issue as to whether the lease should be modified for the purposes of section 57(6)(b) (see [38]). We must be satisfied that "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 (namely 4 August 1989) which affect the suitability on the relevant date (namely 25 March 2011) of the provisions of that lease." Neither party has adduced any evidence as to the aggregate of the service charge contributions on either of these dates or whether there had been any significant change during this period. Neither has any evidence been adduced as to the date on which the aggregate of the fixed percentage contributions amounted to 100%. The significant conversation and additions seem to have been made in the 1960s and 1970s. Indeed, there is no evidence that the aggregate of the fixed percentage contributions amounted to 100% when the original lease was granted on 14 February 1969. We conclude that we are not entitled to either exclude or modify the lease under section 57(6)(b), as we are not satisfied that there has been any significant change of circumstances occurring between 4 August 1989 and 25 March 2011.

46. We must therefore consider what modification should be made for the purposes of section 57(6)(a). We reject the primary submissions made by both Mr Rossman and Mr Upton. We find them both equally unrealistic.

47. Mr Upton asks us to include Clause 2.21 without any modification. He argues that it is for the applicant to propose a modification that cures the defect and that Mr Rossman has failed to do so. The default position is that the new lease should be granted on the same terms. This is a correct recital of the law. However, it overlooks one critical fact. The President made express findings (i) that there is a defect in the lease sufficiently serious to require a remedy and (ii) that it would be wrong to replicate the existing 8% contribution in the new lease (at [47]). He has directed this Tribunal to determine what modification should be made (at [56]). In the light of this direction, all the parties, whether the tenant, the competent landlord, and the intermediary landlord, have been under a duty to assist this Tribunal to determine what modification should be made.

48. Mr Rossman's proposal that Clause 2.21 should be excluded is equally unrealistic. First, the Upper Tribunal have directed us to "modify" this clause; there has been no suggestion that it should be "excluded". Secondly, any contract specifies the respective rights and obligations of the parties. If a landlord is to be required to provide services from which the tenant is to benefit, the tenant must reasonably expect to contribute to the cost of those services. Were we to exclude Clause 2.21, we would also exclude all of the

covenants by the landlord in Clause 3 to repair and maintain the block and to provide services. It would not be in the interests of any of the parties were we to do this. Mr Rossman has suggested that there are a number of anomalies as to what some lessees contribute towards the service charge. These were addressed by the LVT which considered the section 35 application to vary the leases. The fact that an anomaly has arisen whereby the lessee of Flat 148 makes no contribution to the service charge, cannot justify Mr Rossman being put in the same position. If a landlord is to provide services, the tenants must pay for them.

49. We find Mr Rossman's alternative modifications to be equally unrealistic. We can see no justification for a fixed contribution of £3,755.68 to be increased in line with inflation. Any service charge contribution is intended to reflect the reasonable cost of currently providing services. The cost of providing services in 1969 is a matter of history. Our inspection confirmed a history of neglect that is now being addressed. If Mr Rossman wishes to challenge the reasonableness of the current service charges, that is a matter for a separate application under Section 27A of the Landlord and Tenant Act 1985.

50. Neither are we persuaded that Mr Rossman's service charge contribution should be changed from a fixed percentage to one based floor area. Mr Rossman failed to persuade the LVT that the service charges of all lessees should be varied to a new formula based on floor area. The LVT gave a number of reasons for rejecting this proposal. Neither was the President persuaded that such a formula was fair (see [51] of his decision). The Tribunal notes that Mr Rossman is now proposing a more sophisticated formula whereby any apportionment should "have regard to physical size, benefit to and use by occupiers". It is not for this Tribunal to devise such a scheme. Neither party has adduced the "relevant expert evidence" which we would require were we to contemplate such a scheme. It would be extremely costly for the parties to implement a new scheme. A more fundamental objection is that this is not the basis upon which either the landlord or any of the lessees have entered their contracts. It is not the role of this Tribunal to rewrite the contracts, freely entered into by the parties.

51. We finally turn to the alternative proposition proposed by Mr Upton. We are satisfied that this is the only realistic option. This is the modification which the President was minded to contemplate (see [54] of is judgement). This was not an outcome for which either party contended at the appeal. The situation has now changed. It is a modification proposed by the CEC. It ensures that no lessee pays more than the percentage specified in their leases. The President was willing to afford the parties the opportunity either to agree or to propose a better alternative. The parties have failed to do so. We are satisfied that this puts on a contractual basis, the statutory adjustment that section 42 of the Landlord and Tenant Act 1987 would require the landlord to make in any event.

52. We were told that under the current rebate scheme all lesees have their contribution reduced by 0.775%. We are satisfied that the Schedule attached

to the CEC's Statement of Case (at A68-69) adequately describes the operation of the current scheme. It should therefore be annexed to the new lease. The situation at the development continues to be fluid. There are likely to be further changes within the development which may increase the number of lessees that contribute to the service charge expenses. Such changes are likely to further reduce the percentage that Flat 124A is required to contribute. The formula in the lease must be flexible enough to reflect this.

53. The CEC propose that the reference to "0.8" should be modified to read "0.62% (calculated by reference to the formula in the voluntary abatement scheme currently operated by the landlord) or such other fair and reasonable proportion to be determined by the Lessor (sic) from time to time acting reasonably".

54. We have made some minor amendments to this formulation, and propose to modify Clause 2.21 of the lease by substituting for "0.8%" the following: "0.62% (calculated by reference to the formula in the voluntary abatement scheme described in the schedule annexed to the lease) or such other fair and reasonable proportion as the Lessors may reasonably determine from time to time".

55. Mr Rossman addressed us at some length about the impact of the Unfair Terms in Consumer Contracts Regulation 1999 which give effect to EU Council Directive 93/13/EEC. The President did not consider that this point added anything to Mr Rossman's case (see [49]). We agree. We noted that the Regulations have been repealed by the Consumer Rights Act 2015. We are required to modify the terms of the existing lease. Were our proposed modification to be unfair, Mr Rossman's remedy would be an appeal to the Upper Tribunal.

Judge Robert Latham
22 June 2016

RIGHTS OF APPEAL

1. If a party wishes to appeal this decision to the Upper Tribunal (Lands Chamber) then a written application for permission must be made to the First-tier Tribunal at the Regional office which has been dealing with the case.

2. The application for permission to appeal must arrive at the Regional office within 28 days after the Tribunal sends written reasons for the decision to the person making the application.

3. If the application is not made within the 28 day time limit, such application must include a request for an extension of time and the reason for not complying with the 28 day time limit; the Tribunal will

then look at such reason(s) and decide whether to allow the application for permission to appeal to proceed despite not being within the time limit.

4. The application for permission to appeal must identify the decision of the Tribunal to which it relates (i.e. give the date, the property and the case number), state the grounds of appeal, and state the result the party making the application is seeking.