cornerstone barristers

Service Charge Update

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Selected Developments

- Decision-making on repairs
- Whether costs of repairs are reasonably incurred – the test clarified
- Presumption against double recovery
- Service charge issues arising from:
  - The replacement of non FD30 Front Entrance Doors
  - Retro-fitting of Sprinkler Systems

Decisions to Repair Costs Reasonably Incurred

The Landlord's covenant to repair – General Points

- The concept of repair takes as its starting point the proposition that that which is to be repaired is in a physical condition worse than that in which it was at some earlier time
- Where the deterioration is the product of an inherent defect in the design or construction of the building the carrying out of works to eradicate that defect may be works of repair
- General measures taken to avoid the recurrence of the deterioration may also be repair

The Landlord's covenant to repair (2)

- In principle, where there is a choice of methods of carrying out repair, the choice is that of the covenantor provided that the choice is a reasonable one -*Plough Investments Ltd v Manchester City Council* [1989] 1 EGLR 244

- At common law there is no bright line division between what is a repair and what is an improvement

- The use of better materials or the carrying out of additional work required by building regulations or in order to conform with good practice does not preclude works from being works of repair - *Postel Properties Ltd v Boots the Chemist* [1996] 2 EGLR 60.

- Where a defect in a building needs to be rectified, the scheme of works carried out to rectify it may be partly repair and partly improvement -*Wates v Rowland* [1952] 2 QB 12.

Costs Reasonably incurred – *Waaler (1)*

- ***Hounslow LBC v Waale*r** [2017] EWCA Civ 45

- Ivybrook Estate constructed in 1960s on a landfill site
- Subject building is originally constructed of concrete load bearing frames, floor and flat roof, with double glazed painted timber windows

- Under W's lease, H covenants to keep the structure and exterior of the building in repair

- W also covenants to pay a service charge which includes a proportion of H's costs both of carrying out repairs and also improvements

Costs Reasonably incurred – *Waaler (2)*

- H carries out works to the building, including replacing flat roofs with pitched roofs and replacing the wooden-framed windows with metal-framed units
- As a consequence of the window replacement, H also has to replace the external cladding
- W's service charge contribution is £55,195.95
- W applies to FTT under section 27A, contending that the windows should have been repaired instead of being replaced, which would also render the cladding replacement unnecessary
- FTT rejects W's case. Holds that H's decision to replace the windows is not unreasonable and that the costs of replacing them are reasonably incurred

Costs Reasonably incurred – *Waaler (3)*

- UT allows W's appeal:
  - The window replacement and cladding works are ones of improvement, not repair
  - In deciding whether costs have been reasonably incurred, H should have taken into account the length of the leases of the flats, the leaseholders' views on the works and the financial impact of the works on them
- H appeals to CoA, arguing that:
  - In considering whether costs have been reasonably incurred, the views of leaseholders are immaterial
  - FTT should focus on whether the landlord has acted reasonably in reaching the decision to carry out the works, i.e. did it act rationally

Costs Reasonably incurred – *Waaler (4)*

- CoA rejects H's appeal and holds that UT did not err in law
- The contractual dimension
  - A rationality test applies to H's decisions under the leases as to (i) choices between different methods of repair and (ii) deciding to carry out optional improvements
- The statutory requirement that costs must be reasonably incurred
  - The test is not the same
  - Whether costs have been reasonably incurred is not simply a question of process but also of outcome

Waaler on the ‘margin of appreciation’

- But there is a *margin of appreciation* under section 19
  - Where a landlord is faced with a choice between different methods of dealing with a problem to the fabric of a building, there may be many outcomes each of which is reasonable
  - If a landlord chooses a course of action which leads to a reasonable outcome, the costs of pursuing that course will have been reasonably incurred even if there was another cheaper, reasonable outcome

Waaler on works of improvement

- What about works of improvement and section 19
- Although this legal test is the same for all categories of work, the legal and factual context applicable to different categories of works cannot be ignored
- there is a real difference between works of repair which a landlord is obliged to carry out and works of improvement which are optional

- The relevance of leaseholders' views and the financial impact on them depends on the nature of the improvements
  - Those which are undertaken to prevent the future failure of a part of a building caused by a defect in its original design
  - Those involving new systems which may benefit all leaseholders (e.g. CCTV or keypad locks)
  - Those which benefit only some (e.g. creation of a children's play area)
  - Those which are aesthetic only (e.g. installation of a water feature)

Waaler on works of improvement (2)

- Where a landlord is considering undertaking improvements it must take into account:
  - The extent of the interests of the leaseholders (measured by the length of the unexpired terms of their leases)
  - The views expressed by leaseholders (as expressed in response to the statutory consultation) – save that as the landlord is exercising a discretionary power to improve, the views of leaseholders should be “more influential” than in a case where the landlord is simply complying with his obligation to repair
  - The financial impact of the works (in general terms on the class of leaseholder – Knightsbridge vs Isleworth)

Waaler on section 20

- On the contents of the statutory obligation to consult:

- “38. … the landlord must conscientiously consider the lessees’ observations and give them due weight, depending on the nature and cogency of the observations. In the light of this statutory obligation to consult, it is impossible to say that the tenants’ views are ever immaterial. They will have to be considered in every case. This does not of course mean that the lessees have any kind of veto over what the landlord does; nor that they are entitled to insist upon the cheapest possible means of fulfilling the landlord’s objective. But a duty to consult and to "have regard" to the lessees’ observations entails more than simply telling them what is going to happen.”

The margin of appreciation in practice

- ***Dehavilland Studios Ltd v Peries*** [2017] UKUT 322 (LC)

- Windows in large block of 41 flats are defective
- D proposes to repair the windows at a cost of about £100,000
- P applies to FTT arguing that these costs would not be reasonably incurred because D should replace the windows instead
- Cost of replacement significantly more than cost of repair
- Experts agree that replacement is the best solution but do not rule out repair as unreasonable even though windows nearing end of life and repair would not cure all problems

The margin of appreciation in practice (2)

- FTT determines that “the replacement of the windows was the most reasonable option” and disallows cost of repairs
- On appeal to UT: appeal allowed
- Decision to repair was a reasonable even if not (in the FTT’s opinion) the best option
- FTT applied the wrong test

No double recovery

No double recovery

- ***Sheffield City Council v Oliver*** [2017] EWCA Civ 225

- S undertakes major works (insulation, re-cladding and new boilers) to various properties, including O's building
- S receives a contribution to the costs of these works from the Community Energy Savings Programme (CESP), which is calculated by reference to the number of properties which are the subject of the major works, including this building
- S does not credit O with the sum of money attributable to their flat (although it does decide not to charge for certain of the other works)

No double recovery (2)

- O unsuccessfully challenges the service charge demand in the FTT
- UT allows her appeal: holds that the authority has not "incurred" the costs which are the subject of the CESP grant
- S then appeals:
  - There was nothing unfair about the apportionment adopted
  - In any event the lease gives the decision about apportionment to the authority, whose decision should ordinarily be respected.

No double recovery (3)

- CA dismisses S's appeal:
- When interpreting the service charge provision in the lease, the starting point is that the parties would not have intended the landlord to make a profit through the service charge
- Where the landlord has received money from a third party to fund the cost of works (such as grant assistance or payments from an insurer) those sums should be taken into account so as to prevent double recovery
- Although the lease gives the decision on apportionment to the landlord, this is also within FTT's section 27A jurisdiction (and the provision does not have a contractually determinative effect: ss(6))

Front Entrance Door Replacement

Initial questions

- Is the FED demised to the leaseholder or retained by the landlord
- Who is liable to keep the FED in repair
  - Express terms of lease
  - RTB leases implied covenant that the landlord will “keep in repair the structure and exterior of the dwelling-house”: paragraph 14 to Schedule 6 Housing Act 1985)
  - ***Sheffield CC v Oliver*** [2007] (Lands Tr) - external windows are part of the structure and/or the exterior of a maisonette

Is the FED in disrepair

- Is the FED in a state of disrepair triggering the obligation to repair
- ***Quick v Taff Ely BC*** [1986] QB 809 - no breach of the repairing covenant where there is no physical deterioration
- ***Alker v Collingwood HA*** [2007] 2 EGLR 43 – FED glass panel is not safety glass but ordinary annealed glass

The St Saviours Case

- ***Southwark LBC v Various*** [2017] UKUT 10 (LC)

- St Saviours Estate built in the 1960s with FEDs being rated to FD20 standard
- Lease includes covenant to repair but no entitlement to improve
- S's surveyor conducts a visual inspection
- Notes that some leaseholders have replaced their FEDs, or installed new locks or letterboxes within the existing doors (enlarging existing apertures or drilling in)
- Takes view that any FED which has been replaced or altered is no longer FD20-compliant and therefore in disrepair
- Places no weight on its own fire safety assessments
- S undertakes programme of replacement FEDs

The St Saviours Case (2)

- V challenge their liability for service charges on the grounds that the FED replacements amount to improvements
- FTT not satisfied that all the FEDs were in disrepair
- UT dismisses S's appeal
  - Common ground that an FED door will be in disrepair if it falls below the "as-built" FD20 standard of the original doors, i.e. if it has deteriorated from that pre-existing state
  - It does not follow that because an FED has been replaced or altered, that it is no longer FD20-compliant
  - There is a need for an appropriate assessment of each FED by someone with expertise in fire safety

The proper approach

- The approach to be taken when considering FED replacement in discharge of the landlord's obligation to repair:
  - An FED is not in a state of disrepair simply because it fails to meet current standards
  - Before determining whether any FED is in a state of disrepair, so as to trigger any obligation to repair, it is necessary to identify its original (i.e. as built) fire-resistance standard
  - Each FED needs to be assessed by a fire safety expert to determine whether it has deteriorated to a condition where it no longer meets the original fire-resistance standard
  - If it has so deteriorated, then the FED will be in disrepair
  - If it has not, then the FED will not be in disrepair

The proper approach (2)

- Retro-fitting of letterboxes, key drops, or other ‘invasions’ into the door structure which have the effect of compromising its pre-existing standard (whatever that was) may be sufficient deterioration
- If an FED is found to be in disrepair, and the landlord has covenanted to repair it, its replacement will likely be a repair as a matter of law (and even though it will be an ‘improvement’ on the existing FED)
- Ordinarily, albeit depending on the particular lease, the replacement of FEDs will be service charge costs, and not ones directly levied against the individual whose FED has been replaced

Other routes to recovery?

- Where a non FD30 FED is not in disrepair, are there other covenants the landlord can rely on to justify replacement and recover a service charge
- Obligation to keep in “good condition”?
  - Credit Suisse v Beegas Nominees Ltd [1994] 1 EGLR 76 - this covenant is broken once the condition of the premises falls short of such condition as, having regard to the age, character and locality of the premises, would make them reasonably fit for the occupation of a reasonably minded tenant of the class likely to take them, even though there may have been no physical damage or deterioration in the subject matter.
- Landlord’s contractual entitlement to improve (but consider cases where the FED is demised to the leaseholder)

But please note …

- Other possible means of ensuring the replacement of FEDs?

- Other covenants in leases
- Powers to make regulations
- Insurance covenants (i.e. not doing acts etc which may have the effect of rendering insurance policies void or voidable)
- Compliance with notices served on landlord
- Regulatory Reform (Fire Safety) Order 2005
- Part I Housing Act 2004

Sprinkler Systems

Sprinkler systems

- Where a landlord wishes to install fire alarms or sprinkler systems in the common parts of blocks, (not requiring access to individual flats)
- It is doubtful that any lease would prevent it from doing so

- But a service charge would only be payable if
  - There is a contractual entitlement to improve or to add to the existing installations or services (always depending on the precise terms of the lease), and
  - The landlord has adopted a ***Waaler*** compliant approach

Sprinkler systems (2)

- Where the landlord wishes to install a sprinkler system or hardwire alarm system into each flat in a block, *very difficult* questions arise as to the landlord's entitlement to do so (and, logically, then to recover a service charge)

- Even if the lease contains an entitlement to improve, there are substantial arguments that such an entitlement does not extend to a right to improve the demised premises themselves (towards which the leaseholder is bound to contribute)

Sprinkler systems (3)

- Other options
  - Agree lease variations. (Any varied lease would need to be found reasonable by the County Court under paragraph 14(4), Schedule 6 Housing Act 1985 – but that endorsement would be bound to be given).
  - For LAs CANNOT seek a variation of the leases under section 35 Landlord and Tenant Act 1987 on the basis that the running costs of the common parts are not recoverable because this is implied into the lease by paragraph 16A(1), Schedule 6 Housing Act 1985.

Sprinkler systems (4)

- Grenfell Tower Public Inquiry
  - (14 of the flats were on long leases – 2 Housing Association owned)
  - The Regulatory Reform (Fire Safety) Order 2005 could be amended to require freeholders to fit sprinklers throughout blocks regardless of tenure.
  - Schedule 6 of the Housing Act 1985 could then be amended to include a new implied term across all right to buy leases that the lessee contributes towards the freeholder fire safety statutory obligations.

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Questions?

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