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Case No: LC-2024-38

IN THE UPPER TRIBUNAL (LANDS CHAMBER)
AN APPEAL AGAINST A DECISION OF THE FIRST-TIER TRIBUNAL (PROPERTY CHAMBER)
FTT REF: LON/00AE/LSC/2022/0332

16 July 2024

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007
AN APPEAL FROM A DECISION OF THE FIRST-TIER TRIBUNAL (PROPERTY CHAMBER)

LANDLORD AND TENANT – SERVICE CHARGES – recovery of legal and mediation expenses as service charges – construction of the lease

BETWEEN:

THANET LODGE (MAPESBURY ROAD) RTM COMPANY LIMITED

Appellants -

and-

ARUN MIRCHANDANI

Respondent

29 Thanet Lodge,
10 Mapesbury Road,
London, NW2 4JA

Upper Tribunal Judge Elizabeth Cooke
Decision on written representations

Streathers Highgate LLP for the appellants
Raphael Levy for the respondent

The following cases are referred to in this decision:

*Arnold v Britto*n [2015] UKSC 36
Assethold Ltd v Watts [2014] UKUT 537 (LC)
Holland Park Management Company Limited v Dell [2023] EWCA Civ 1460
Kensquare Ltd v Boakye [2021] EWCA Civ 1725
London Borough of Tower Hamlets v Lessees of Brewster House and Malting House [2024] UKUT 193 (LC)
No. 1 West India Quay (Residential) Ltd v East Tower Apartments Ltd [2021] EWCA Civ 1119
Sella House Ltd v Mears (1988) 21 HLR 147

Introduction

1. This is an appeal from a decision by the First-tier Tribunal ("the FTT") that certain legal fees and mediation costs were not recoverable by the appellant, which is a right to manage or "RTM" company, from the respondent leaseholder, Mr Mirchandani. It has been decided under the Tribunal's written representations procedure.

Background

2. The respondent holds a long lease of 29 Thanet Lodge, one of 43 flats in a five-storey block. The appellant RTM company was incorporated by the leaseholders in order to exercise the right to manage the block conferred by the Commonhold and Leasehold Reform Act 2002. The respondent is not a member of the appellant.

3. In October 2022 the respondent applied to the FTT for a determination under section 27A of the Landlord and Tenant Act 1985 as to whether certain service charges were payable. Some of the items charged were challenged by the respondent on the basis that costs were not reasonably incurred, in light of section 19 of the 1985 Act which provides that service charges are payable only insofar as the costs they represent were reasonably incurred. In respect of other charges the respondent argued that the terms of his lease did not permit the appellant to recover them.

4. The FTT's determination covered five different types or groups of charges. The appellant sought to appeal the decision in respect of just one group, and has permission from this Tribunal to do so. The charges in question are for legal fees incurred by the appellant. The FTT decided that the terms of the lease did not permit the appellant to recover them by way of service charges. There was no challenge on the basis that the costs were not reasonably incurred, and therefore the FTT's decision and this appeal are solely about the construction of the lease.

5. The costs claimed by the appellant were incurred in the period March 2020 and October 2019 and are as follows:

    a. Solicitors' costs for advice about the membership and constitution of the RTM company, and about a proposed EGM.

    b. Solicitors' costs in relation to a dispute with another leaseholder and the consequences of the settlement of a dispute about service charges.

    c. Legal costs incurred in relation to a compensation claim brought by the respondent.

    d. Legal costs (solicitors and barrister) for advice in connection with a mediation of the respondent's compensation claim.

    e. The appellant's share of the mediation fee.

6. The amounts claimed range from £960 to £1838; if I have understood correctly those figures represent the total cost, which was then apportioned between the leaseholders.

7. The respondent's lease, dated 15 June 1995, requires him to pay the Service Charge as provided in the Fifth Schedule; that schedule requires him to pay a specified percentage of the "Total Expenditure", defined as follows:

> "(1) "Total Expenditure" means the total expenditure incurred by the Lessors in any Accounting Period in carrying out their obligations under Clause 5(4) of this Lease and any other costs and expenses reasonably and properly incurred in connection with the Building including without prejudice to the generality of the foregoing (a) the cost of employing Managing Agents (b) the cost of any Accountant or surveyor employed to determine the Total Expenditure and the amount payable by the Tenant hereunder and (c) an annual sum equivalent to the fair rent of any accommodation owned by the Lessors and provided by them rent free to any of the persons referred to in Clause 5(4)(f) of this Lease and (d) interest charged upon Bank accounts maintained for the purposes of the Management of the Building"

8. Clause 5(4) of the lease, to which that definition refers, imposes obligations on the landlord (into whose shoes the appellant, as an RTM company, stands for these purposes) in sub-clauses (a) to (n) including the maintenance and repair of the structure of the building and of its common parts, and:

> "(4)(g)(i) To employ at the Lessors' discretion a firm of Managing Agents and Chartered Accountants to manage the Building and discharge all proper fees salaries charges and expenses payable to such agents or such other person who may be managing the Building including the cost of computing and collecting the rents and service charges in respect of the Building or any parts thereof
> (ii) To employ all such surveyors builders architects engineers tradesmen accountants or other professional persons as may be necessary or desirable for the proper maintenance safety and administration of the Building
> …"

9. The appellant argued in the FTT, and on appeal, that the use of legal professionals and the incurring of legal fees falls within the expenditure described at clause 5(4)(g), and in any event with the definition of Total Expenditure and the words "any other costs and expenses reasonably and properly incurred in connection with the Building."

The FTT's decision

10. The FTT set out the costs claimed and the relevant provisions of the lease, and referred to the principles of contractual construction set out in *Arnold v Britto*n [2015] UKSC 36 and in particular to Lord Neuberger's judgment at paragraph 15 where he said that the court must identify the intention of the parties by reference to:

> ""what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean", ... And it does so by focussing on the meaning of the relevant words … in their documentary, factual and commercial context. That meaning has to be assessed in the light of
> (i) the natural and ordinary meaning of the clause,

(ii) any other relevant provisions of the lease,
(iii) the overall purpose of the clause and the lease,
(iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and
(v) commercial common sense, but
(vi) disregarding subjective evidence of any party's intentions."

11. The FTT the referred to *Sella House Ltd v Mears* (1988) 21 HLR 147 and said:

> "41. …in *Sella*, the Court of Appeal were considering the payability of service charges arising from legal fees and pointed out that the lease did not contain any specific mention of lawyers, proceedings or legal costs. They held that liability would require a clause in clear and unambiguous terms.
>
> 42. Clause 5(4)(g)(i) is clear. This particular clause does not create obligationsrather than specify the means by which obligations spelled out elsewhere may be achieved.
>
> 43. Paragraph 1 of the Fifth Schedule refers to "any other costs and expensesreasonably and properly incurred in connection with the Building". Taken in isolation, these words could cover anything and everything but they must be read in context. When creating the contract, the parties sought to identify their respective liabilities. All certainty would disappear with an interpretation of these words which was too wide, giving rise to unknown future liabilities of unknown size. The Tribunal has concluded that the lease in this case has the same issue as that in *Sella* – the absence of any specific mention of lawyers, proceedings or legal costs suggests that the general words of paragraph 1 of the Fifth Schedule are not meant to be read as covering such matters.
>
> 44. Therefore, the service charges arising from the bills for legal fees are notpayable."

12. The FTT's decision on this point was understandably brief, because the hearing and written decision were for the most part concerned with much larger amounts charged for work done to the building and with the provisions of the Building Safety Act 2022. For the reasons explained below I agree with the FTT about the outcome, but for the appellant the ability to recover legal costs from leaseholders is an important issue that may well recur in the future and so I take the opportunity to explain it in more detail.

The appeal

13. The appellant's primary argument is that taking legal advice falls within the scope of clause 5(4)(g). It relies on the FTT's observation that the clause gives the landlord a discretion to employ professionals in connection with the meeting of its obligations, and says that all the fees concerned with one exception (item (a) in paragraph 5 above) related to claims in respect of damage to two flats in the building (the respondent's and another leaseholder's) which were said to be the responsibility of the appellant as a result of the landlord's repairing covenants. The cost of the repairs was recoverable and equally, says the appellant, legal fees incurred in connection with them were recoverable.

14. Turning to the definition of Total Expenditure in the Fifth Schedule, the appellant argues that the wording is deliberately wide, and that the inclusion of legal fees of this kind would make commercial sense, given the proviso that costs have to be reasonably and properly incurred in connection with the building. The appellant says that there is nothing in *Sella* to compel a construction that it cannot recover legal fees, and that the FTT's conclusion was contrary to the natural and ordinary meaning of the words in clause 5(4)(g) and the Fifth Schedule and contrary to the overall purpose of those provisions. Moreover the FTT's conclusion fails to make commercial sense, because it leaves the original lessor, and the appellant as an RTM company, unable to get legal assistance or obliged to raise funds for it by way of voluntary contribution from its members.

15. The respondent relies on the reasoning in the FTT, and argues that the appellant's construction of the relevant clauses would make them so wide as to be meaningless. He observes that the landlord, as a sophisticated property company, would have had legal advice when the lease was drafted, and if it was the intention that legal fees were to be recoverable the lease would have said so explicitly.

Discussion and conclusions

16. Although there appears to be one issue in the appeal, namely the recovery of legal costs, the first item in the list at paragraph 5 above is different from the rest and merits separate consideration.

Costs of advice about the constitution of the appellant RTM company

17. The first item in the list of costs sought to be recovered was not incurred in connection with a dispute with a leaseholder. Instead it was about the membership of the appellant and about the convening of meetings (I take that description from the copy of the solicitors' invoice in the bundle).

18. Such costs were not contemplated by the original parties to the lease, because in 1995 the right to manage legislation had not yet been enacted. It was not part of "the facts and circumstances known or assumed by the parties at the time the document was executed", nor part of the "overall purpose of the clause or the lease" (see *Arnold v Britton* paragraph 10 above). Moreover, such costs benefit the RTM company, whose membership is a proportion – probably a majority, but in the present case not all – of the leaseholders, and there is no reason why the cost of the running of a company of which not all are members should be an expense charged to all.

19. Accordingly the appellant's claim to be able to charge the first item in the list at paragraph 5 above clearly fails.

Dispute resolution costs

20. The rest of the items at paragraph 5 can be grouped together as "dispute resolution costs", although they cover a number of different types of costs: advice about the settlement of a compensation claim by another leaseholder, advice about mediation of a claim by the respondent, and the appellant's share of the mediation fee. The clauses on which the appellant relies make no express mention of legal advice, nor of legal professionals or mediators, and the question therefore arises as it has done in a number of other cases: are

such costs nevertheless within the scope of clause 5(4)(g) or of the definition of "Total Expenditure" in the Fifth Schedule? It is convenient to look at those two provisions separately since slightly different legal considerations arise in respect of each.

Dispute resolution costs: clause 5(4)(g)

21. The provisions of clause 5(4)(g) are set out at paragraph 8 above. The FTT said that it is "aimed at the employment of professionals for the purpose of implementing other obligations under the lease. It is wide enough to include lawyers but there has to be an obligation elsewhere in the lease for which such lawyers may be used." The appellant therefore argues that the clause authorises the use of legal professionals in the implementation of its repairing covenant.

22. I do not agree that that is what the clause says or is "aimed at." Clause 5(4)(g)(i) enables the landlord to employ managing agents and accountants in order to manage the building and collect the rent and service charges. It is not a licence to use professionals in order to carry out any other obligations and it is not about repairs or maintenance. Clause 5(4)(g)(ii) is in broader terms and authorises the employment of professional persons for the "maintenance safety and administration" of the building. Taken literally that might be said to encompass the taking of legal advice, but does it really go that far in the absence of a specific mention of legal professionals?

23. A number of authorities have considered the same issue in construing similar clauses. It is worth saying at the outset that the absence of a specific mention of legal advice is not fatal to the appellant's construction; in *Assethold Ltd v Watts* [2014] UKUT 537 (LC) it was held that the landlord's obligation to do "all works installations acts matters and things as in the reasonable discretion of the Landlord may be considered necessary or desirable for the proper maintenance safety amenity and administration of the Development" included the taking of legal advice about a neighbouring development which posed a threat to the structure of the building, serving notices under the Party Wall Act 1966 and obtaining an injunction. The Tribunal (the Deputy President, Martin Rodger QC) said at paragraph 58:

> "It seems to me to be wrong in principle to start from the proposition that, with certain types of expenditure, including the cost of legal services, unless specific words are employed no amount of general language will be sufficient to demonstrate an intention to include that expenditure within the scope of a service charge. Language may be clear, even though it is not specific."

24. However, the purpose and context of the clause in question are critical. In *Sella House* the landlord sought to recover by way of service charge legal expenses incurred in pursuing other tenants for rent and service charges. The landlord argued that the expenditure arose from its fulfilling its obligations under clause 5(4)(j) of the lease, which required it:

> "(i) To employ at the Lessors' discretion a firm of Managing Agents and Chartered Accountants to manage the Building and discharge all proper fees salaries charges and expenses payable to such agents or such other person who may be managing the Building including the cost of computing and collecting

> the rents and service charges in respect of the Building or any parts thereof (ii) To employ all such surveyors builders architects engineers tradesmen accountants or other professional persons as may be necessary or desirable for the proper maintenance safety and administration of the Building."

25. That wording is identical to that of clause 5(4)(g) in the respondent's lease.

26. Dillon LJ concluded that legal costs were "outside the contemplation of either limb of Clause 5(4)(j) of the lease". Taylor LJ, said at 156:

> " Nowhere in Clause 5(4)(j) is there any specific mention of lawyers, proceedings or legal costs. The scope of (j)(i) is concerned with management. In (j)(ii) it is with maintenance, safety and administration. On the respondent's argument a tenant, paying his rent and service charge regularly, would be liable via the service charge to subsidise the landlord's legal costs of suing his cotenants, if they were all defaulters. For my part, I should require to see a clause in clear and unambiguous terms before being persuaded that that result was intended by the parties. Accordingly, I agree with my Lord that the terms of paragraph (j) of clause 5(4) do not extend to cover legal costs in the service charge."

27. Identically worded clauses do not necessarily generate identical outcomes, but there is nothing in the facts of the present appeal to permit a different conclusion about identical words.

28. What is different is that items (c) to (e) of the list at paragraph 5 above are legal costs incurred by the appellant in disputes with this respondent. Does that make a difference? In both *No. 1 West India Quay (Residential) Ltd v East Tower Apartments Ltd* [2021] EWCA Civ 1119 and in *Kensquare Ltd v Boakye* [2021] EWCA Civ 1725 the Court of Appeal had to decide whether a similarly worded clause encompassed a charge for legal costs incurred in a dispute with the tenant who contested the charges, and came to the same conclusion: a clause concerned with management, or with the provision of services, does not enable the landlord to recover through the service charge its legal costs in a dispute with any of its tenants.

Dispute resolution costs: the definition of Total Expenditure

29. It will be recalled that the Fifth Schedule defines the "Total Expenditure" that determines the amount of the service charge; the text is set out at paragraph 7 above. The appellants rely in particular upon the words "and any other costs and expenses reasonably and properly incurred in connection with the Building".

30. Exactly the same words were considered by the Court of Appeal in *Holland Park Management Company Limited v Dell* [2023] EWCA Civ 1460, where the issue was whether the management company could recover through the service charge the costs of litigation against a third party in a dispute about a restrictive covenant and planning – obviously rather different costs from those in issue in this appeal, but again the Court of Appeal had to consider how far the definition of "Total Expenditure" could extend the

leaseholders' liability beyond what was contemplated in the rest of the lease (which did not enable the landlord to make that charge). Falk LJ at paragraph 64 said this:

> "The relevant context includes not only the list of items that follows the words relied on but clause 4(4) itself (to which reference is made in the first part of the definition) and the other provisions of the Lease to which I have referred. The factual matrix also remains the same. Further, the wording is contained within a definition rather than forming part of what might be considered to be the substantive provisions of the Lease. It is inherently unlikely that the parties would have intended to include an obligation to fund uncertain but potentially significant costs of a planning-related dispute with a neighbour within general wording in a definition in circumstances where extensive and specific provision is made for the types of costs that may be included in the service charge both by the preceding words that cross-refer to clause 4(4) and by the list of items that follows."

31. Clause 4(4) in that lease set out the landlord's covenants, as does clause 5(4) in the present appeal. Obviously the charge in issue here is a different one, as it relates to litigation costs incurred against leaseholders rather than third parties, and the amounts likely to be at stake are probably smaller. Nevertheless the relevant considerations are the same: the definition has to be looked at in the context of the rest of the lease and of the landlord's obligations set out in clause 5(4); it is unlikely that the parties to the lease would have contemplated the extension of the service charge by this definition to include something quite different, namely legal and mediation costs, from what had already been specified.

32. A similar point arose in the Tribunal's decision in *London Borough of Tower Hamlets v Lessees of Brewster House and Malting House* [2024] UKUT 193 (LC), where again the need to look at the definition clause in its context was emphasised.

33. I am mindful of the appellant's concern that if legal costs are not recoverable through the service charge it will be deprived of legal advice, or will have to seek contributions from its members. That is the result of the absence on the lease of any clause enabling the recovery of such costs, and the members will indeed have to discuss whether they wish to take, and pay for, legal advice whenever the question arises. The landlords in *Sella House*, in *No. 1 West India Quay (Residential) Ltd v East Tower Apartments Ltd* and in *Kensquare Ltd v Boakye* faced the same difficulty.

Conclusion

34. Accordingly I conclude that the appeal fails, none of the legal costs that the appellant wanted to charge to the service charge are so chargeable.

Upper Tribunal Judge Elizabeth Cooke

16 July 2024

Right of appeal

Any party has a right of appeal to the Court of Appeal on any point of law arising from this decision. The right of appeal may be exercised only with permission. An application for permission to appeal to the Court of Appeal must be sent or delivered to the Tribunal so that it is received within 1 month after the date on which this decision is sent to the parties (unless an application for costs is made within 14 days of the decision being sent to the parties, in which case an application for permission to appeal must be made within 1 month of the date on which the Tribunal's decision on costs is sent to the parties). An application for permission to appeal must identify the decision of the Tribunal to which it relates, identify the alleged error or errors of law in the decision, and state the result the party making the application is seeking. If the Tribunal refuses permission to appeal a further application may then be made to the Court of Appeal for permission.

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