Neutral Citation Number: [2020] EWCA Civ 1521

Case No: A3/2020/0803

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
PROPERTY, TRUSTS AND PROBATE LIST (Ch D)
KELYN BACON QC (sitting as a Deputy Judge of the High Court)
CH-2019-000345

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 13 November 2020

Before:

LORD JUSTICE DAVID RICHARDS
LORD JUSTICE NEWEY
and
LORD JUSTICE ARNOLD

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Between:

SARA & HOSSEIN ASSET HOLDINGS LIMITED	**Appellant**
- and -	
BLACKS OUTDOOR RETAIL LIMITED	**Respondent**

- -
- -

Richard Fowler (instructed by **Pinsent Masons LLP**) for the **Appellant**
Morayo Fagborun Bennett and **Usman Roohani** (instructed by **Gateley plc**) for the **Respondent**

Hearing dates: 28 July 2020

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Approved Judgment

Lord Justice David Richards :

1. This second appeal concerns the construction of a provision in a commercial lease under which the landlord's certificate of the total cost of services provided under the lease, and the service charge payable by the tenant, is conclusive in the absence of manifest or mathematical error or fraud. The courts below held that the certificate was conclusive as to the cost incurred in providing the services but not as to whether such services fell within the scope of services for which the landlord was entitled to charge under the lease. The landlord appeals with permission granted by Lewison LJ.

2. From 2012, the respondent Blacks Outdoor Retail Limited (Blacks) was the tenant of retail premises located at Chicago Buildings, Whitechapel and Stanley Street, Liverpool L1 6DS, the previous owner of the Blacks business having been the tenant since 2005. Other parts of Chicago Buildings were let to different tenants.

3. The appeal concerns two leases. The first was dated 15 May 2013, made between IVG Institutional Funds GmbH as landlord and Blacks as tenant, with a term of 10 years but with a break clause after 5 years (the 2013 lease). The freehold reversion was assigned to the appellant Sara & Hossein Asset Holdings Limited (S&H) in December 2016. Blacks exercised its rights under the break clause and entered into a further lease dated 23 April 2018 (the 2018 lease), with S&H as landlord, for a term of one year ending on 15 May 2019. Blacks vacated the premises at the expiry of the 2018 lease.

4. So far as the terms of the leases relevant to this appeal are concerned, the 2018 lease incorporated by reference the terms contained in the 2013 lease.

5. The relevant terms of the 2013 lease were as follows. Clause 2.3(d) provided for the payment by the tenant of "the Service Charge calculated and payable at the times and in accordance with Schedule 6". By clause 3.1(a), the tenant covenanted "not to exercise or seek to exercise any right or claim to withhold rent or any right or claim to legal or equitable set-off or counterclaim (save as required by law)". It is no longer in dispute that this provision applies to all sums due under the lease, including the service charge.

6. The relevant provisions of schedule 6 were:

> "1. There shall be calculated by the Landlord as soon as practicable after the 31st day of December in each year the total reasonable and proper cost to the Landlord during the calendar year ending on such 31st day of December of the services and expenses specified in Part II of this Schedule (excluding costs and expenses met by the insurers under the policy of insurance effected by the Landlord hereinbefore mentioned)
>
> 2. The further rent payable by the Tenant shall be a sum equal to a fair and reasonable proportion of such total cost of the service [*sic*] and expenses specified in Part II of this Schedule and in the event of the Term commencing or determining during the course of the calendar year in question a corresponding proportion of such sum

> 3. The Landlord shall on each occasion furnish to the Tenant as soon as practicable after such total cost and the sum payable by the Tenant shall have been ascertained a certificate as to the amount of the total cost and the sum payable by the Tenant and in the absence of manifest or mathematical error or fraud such certificate shall be conclusive
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> 6. The contribution payable by the Tenant of the total costs of the services and expenses incurred by the Landlord hereunder shall be the proportion which the net internal area of the Demised Premises bears to the net internal area of the aggregate of all areas of the Building which are let or intend to be let and any dispute between the parties as to the proportion shall be determined by Expert Determination"

7. The services and expenses for which the landlord was entitled to charge were set out in part IIA and part IIB respectively of schedule 6. The tenant was not required to pay service charges in respect of "Excluded Costs" which were defined in paragraph 10 of schedule 6.

8. The term "Expert Determination" used in paragraph 6 was defined in clause 1 of the 2013 lease, as involving determination "by an expert who shall be an independent valuer", to be appointed by the President of the Royal Institution of Chartered Surveyors in the absence of agreement by the parties.

9. On 14 January 2019, S&H's appointed surveyors served a service charge certificate for the year ended 30 September 2018 pursuant to paragraph 3 of schedule 6, certifying that over £400,000 was due. This was a very substantially larger sum than in previous years, the figure for 2016-17 having been some £55,000.

10. In April 2019, S&H issued proceedings, claiming (following a correction) a sum of £407,842.77 in respect of unpaid service charges for the years 2017-18 and 2018-19. In respect of the latter year, the amount claimed when the claim was issued was on account of the service charge, but subsequently a certificate was issued for that year.

11. Blacks served a defence and counterclaim, helpfully summarised by Kelyn Bacon QC (now Bacon J), sitting as a Deputy High Court Judge, in her judgment on the first appeal at [11]:

> "Blacks served a Defence and Counterclaim on 14 May 2019, mounting a number of challenges to the sums claimed. Some of those were characterised as challenges to the charges themselves. These included complaints that some of the works were unnecessary or were not repair works within the meaning of the relevant repairing covenants, and that the cost of the work was increased by past failures to keep the premises in good repair. In addition, Blacks alleged various breaches that were relied on by way of set-off or counterclaim, including some of the same matters giving rise to its challenges to liability, as well as additional complaints such as failure to

> progress the works with reasonable speed and failure to remove scaffolding promptly when the works were completed."

12. S&H issued an application for summary judgment, contending that, by virtue of paragraph 3 of schedule 6, the certificates were conclusive and precluded reliance by way of defence on any of the matters pleaded by Blacks. S&H further contended that Blacks was precluded by clause 3.1(a) from withholding payment on the grounds of the matters pleaded in the counterclaim. Blacks did not allege that there had been any mathematical or manifest error or fraud in the certificates.

13. The application was dismissed by Deputy Master Bartlett, who held that paragraph 3 of schedule 6 did not preclude Blacks from relying on the matters pleaded by it as a defence to S&H's claim.

14. On appeal by S&H, Kelyn Bacon QC (the judge) dismissed the appeal.

15. The judge began her discussion of the issue by reference to authorities on contractual terms providing for binding determination of an issue by an independent expert. Mr Fowler, then as now appearing for S&H, had submitted that these authorities could be applied by analogy to the present case. As to this, the judge said:

> "24. That is, at its inception, a difficult proposition. There is to my mind a fundamental distinction between a contractual provision that assigns matters that might potentially be disputed to an independent expert, and a provision that is said to confer on one of the parties to the contract the power to determine conclusively (subject to limited exceptions for obvious errors and fraud) the question of whether that party has complied with its obligations under the contract. In this case, the lease provided a clear example of the former, in paragraph 6 of Schedule 6 which provided for an expert determination of the proportion of the total costs that were payable by the tenant. On S&H's case, however, the landlord has the power to decide conclusively all of the issues that might arise in determining whether certain costs were properly claimed as service charges under the lease at all, including issues of law and principle as to the correct construction of the lease.
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> 25. As the Deputy Master noted, that would make the landlord judge in his own cause. Notwithstanding the express provisions in Schedule 6 excluding from the service charges matters such as (for example) costs caused or necessitated by the negligence of the landlord, or the cost of improvement or modernisation the premises, the tenant would be precluded from enforcing those provisions against the landlord, absent obvious errors or fraud. Mr Fowler was not able to identify any precedent authority that supported his position on this point."

16. As to the terms of paragraph 3 of schedule 6, the judge said at [28]:

> "In the present case, the Certification Provision provided for the landlord's certificate to set out "the amount of the total cost and the sum payable by the Tenant". The natural and obvious construction of that provision is that the certificate is conclusive as to "the amount of the total cost" of the services said to be comprised within the service charge. There is, however, a clear distinction between a certificate establishing "the amount" of a cost, and the question of whether that cost should properly have been incurred in the first place, within the scope of the obligations in the lease. As to that latter question, Schedule 6 makes no provision for any conclusive determination by the landlord or indeed anyone else. It follows that, in the ordinary way, that must be a matter which the tenant can put in issue and which is capable of determination by the court in the event of a dispute between the parties."

17. The judge considered that this construction was supported by the provision for an expert determination, after representations from each party, of the proportion of the total costs to be borne by each tenant under paragraph 6 of schedule 6. It would be "inconsistent with that carefully-defined dispute mechanism if the (potentially far more significant) question of the headline figure of the total costs and services was construed as falling to be determined conclusively by the landlord": see [29].

18. The judge's conclusion, echoing what she said at [28], was:

> "30….The certificate is conclusive as to the amount of the costs incurred, absent manifest or mathematical error, or fraud, but is not conclusive as to the question of whether those costs as a matter of principle fall within the scope of the service charge payable by the tenant under the lease. The Deputy Master's example of a routine accounting matter is one example of a matter on which the certificate might be conclusive. It is, as the Deputy Master noted, not necessary to define exhaustively the circumstances in which a certificate would or might be conclusive; rather it is sufficient for the purposes of this appeal to find that the landlord's certificate is not conclusive as to the various matters relied upon by Blacks which the Deputy Master considered were properly characterised as defences to liability."

19. In summary, therefore, the judge held that Blacks' construction of paragraph 3 represented its natural and obvious meaning, in a context where (i) the determination was to be made not by an independent expert but by the landlord and (ii) there was the contrasting provision for an expert determination, following representations by the parties, in paragraph 6.

20. Appearing for Blacks, Ms Fagborun Bennett supported the judge's reasoning.

21. I part company from the judge at the first step of her reasoning, that Blacks' construction represents the natural meaning of the crucial words in paragraph 3 of

schedule 6. The landlord's certificate is conclusive "as to the amount of the total cost and the sum payable by the Tenant". On any basis, this comprises at least two elements: (i) the amount of the total cost and (ii) the sum payable by the tenant. The latter is, if not agreed, subject to binding expert determination to the extent provided under paragraph 6, that is to say, as to the proportion of the total cost payable by the tenant. The judge reads the former as itself divided into two elements: (i) the identification of the services and expenses properly falling within part II of schedule 6 and not constituting Excluded Costs under paragraph 10 and (ii) the total costs incurred in respect of those services and expenses. It is, of course, correct that these elements make up the "total cost" certified by the landlord, as paragraph 1 makes clear. But, I am unable to see how, as a matter of the ordinary meaning of the language used in paragraphs 1 and 3, those two elements can be separated, with the certificate being conclusive only as regards the second element. Paragraph 3, as I read it, renders the certificate conclusive as regards the single figure of "such total cost", which necessarily involves both elements going to make up that single figure. Treating the categorisation of the relevant services and expenses as not being conclusively determined by the landlord's certificate (subject to mathematical or manifest error or fraud) would require express words to that effect or a necessary implication. There are no such express words, and, in my judgment, there are no grounds for a necessary implication to that effect.

22. An analogous point arose in *Dobbs v National Bank of Australasia Ltd* (1935) 53 CLR 643, where it was argued that a certificate by the creditor of the amount of a guarantor's indebtedness did not make the certificate conclusive of the legal existence of the debt but only of its amount. In a passage from the leading judgment in the High Court of Australia, cited with approval by Tomlinson LJ in *North Shore Ventures Ltd v Anstead Holdings Inc* [2011] EWCA Civ 230, [2012] Ch 31, it was said at p.651:

> "It is not easy to see how the amount can be certified unless the certifier forms some conclusion as to what items ought to be taken into account, and such a conclusion goes to the existence of the indebtedness. Perhaps such a clause should not be interpreted as covering all grounds which go to the validity of a debt; for instance illegality…But the manifest object of the clause was to provide a ready means of establishing the existence and amount of the guaranteed debt and avoiding an inquiry upon legal evidence into the debits going to make up the indebtedness. The clause means what it says…"

23. In my view, the position is further illuminated by the fact that the certificate is, under paragraph 3, also binding as to the sum payable by the individual tenant. How, it may be asked, can it be binding as to that amount if it is not also binding as to all elements going into "the total cost"?

24. The judge was clearly, and understandably, influenced by the consideration that she set out at [24]-[25], that S&H's construction would make the landlord judge in his own cause. That is undoubtedly a matter which a tenant would be well advised to consider very carefully before agreeing a lease in these terms, particularly where the amount of the service charge is not capped by the terms of the lease. But, it is not the function of contractual construction to save a party from an imprudent term, as Lord Neuberger said in *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619 at [20], a case

concerning service charge provisions in leases. He there observed that "The purpose of interpretation is to identify what the parties have agreed, not what the court thinks that they should have agreed".

25. Paragraph 3 of schedule 6, construed in this way, does not produce a result that neither party could rationally agree. On the contrary, it makes sense for the landlord, by avoiding what could be protracted and very detailed arguments about whether particular pieces of work and expenses did or did not fall within part II of schedule 6. The potential for such disputes is apparent from reading the categories of works and services envisaged by part II, even before getting to the open-textured terms of paragraph 13 of part IIA: "Providing all and any other services by the Landlord acting reasonably in the interests of good estate management".

26. The judge was also influenced by the provision for expert determination in paragraph 6. She took the view that this provided a basis for concluding that the potentially more important issue of whether particular services or expenses fell within part II, or were Excluded Costs as itemised in paragraph 10 of part I, was to be left to the court, in the absence of an equivalent provision for expert determination. In my judgment, this seeks to prove too much. The presence of the provision in paragraph 6 for an expert determination of the appropriate proportion, which feeds directly into the certified sum payable by the tenant, does not carry with it a basis for saying that, in the absence of such a provision applicable to the services and expenses provided and incurred by the landlord, their correct categorisation must have been intended to be a matter for the court. In the absence of any language in the provisions to suggest that result, of which there is none, the more natural inference is that it was a matter for the landlord's certificate.

27. I therefore respectfully find myself unable to agree with the judge's construction of paragraph 3 and with her conclusion as to the effect of the landlord's certificate.

28. Accordingly, I would allow the appeal and hold that S&H is entitled to summary judgment for the service charges claimed in these proceedings.

29. What was not explored in any detail before us is whether Blacks' counterclaim can, in whole or part, proceed in the light of this decision. If the parties are not able to agree this issue, I would remit it for determination by the Chancery Division.

Lord Justice Newey:

30. I agree.

Lord Justice Arnold:

31. I also agree.