2092

Ref: LON/00AF/LSC/2005/0337

LEASEHOLD VALUATION TRIBUNAL

FOR

LONDON RENT ASSESSMENT PANEL

DETERMINATION IN RESPECT OF

25 BLAKE HOUSE, PORCHESTER MEAD, BECKENHAM, KENT

24 KEATS HOUSE, PORCHESTER MEAD, BECKENHAM KENT

Applicant: Mr. Abdul Karim

Respondent: Palgrave Estate Ltd

Hearing: 15 February 2006 (Inspection 24 February 2006)

Appearances: The applicant (in person)

Mr S Gallagher of counsel instructed by Messrs. Thackray Williams & Co (for respondent)

Members of the Leasehold Valuation Tribunal:

MR M LOVEDAY BA(Hons) MCIArb

MR. M MATHEWS FRICS

MR. A RING

INTRODUCTION

1. This is a determination in respect of liability to pay service charges under section 27A of the Landlord and Tenant Act 1985.

2. The matter relates to two flats on the Porchester Mead estate in Beckenham. The respondent is the freehold owner of the estate, and the applicant is the lessee of both flats. On 25 November 2005 the applicant applied to the Tribunal for a determination under section 27A of his liability to pay charges for the service charge years beginning 25 March 2004 and 25 March 2005. On 1 December 2005 the Tribunal gave directions. The hearing took place on 15 February 2006.

3. The flats are at 24 Keats House and 25 Blake House. The total amount of "on account" charges payable for each was £1,281 for the 2004/5 service charge year and £1,454.54 for the 2005/6 service charge year. At the outset of the hearing, the parties agreed that the Tribunal was being asked to consider whether the following relevant costs were limited by s.19 of the Landlord and Tenant Act 1985:

   (a) Insurance - £41,000 in the year 2004/5 and £46,771 in the year 2005/6, and;

   (b) General Maintenance/Sundries - £16,000 in the year 2004/5 and £20,000 in the year 2005/6.

The applicant expressly conceded that the costs were recoverable under the terms of the leases and that there was no other statutory bar to recovery of the relevant costs. In addition, the applicant applied under section 20C of the 1985 Act for an order that the costs incurred by the landlord in connection with proceedings before the Tribunal should not be regarded as relevant costs to be taken into account in determining the amount of service charges.

4. For the purpose of the application, the Tribunal was referred only to the provisions of the applicant's lease of 24 Keats House dated 30 April 1982 which it is agreed is in similar form to the lease of 25 Blake House. The material terms of the appear at clause 2, at paragraphs 29-31 of the Sixth Schedule and paragraphs 14-17 of the Seventh Schedule to the lease. The charges referred to above are all elements of "on account" service charges demanded in each of the two service charge accounting years. The provisions in the lease require the landlord to provide a certificate of expenditure within two months of the end of each accounting year (Seventh Schedule paragraph 17) and the "on account" charge for the following year is the same as that figure payable by equal quarterly instalments on the usual quarter days (Sixth Schedule paragraph 30(b)).

5. In this instance, the application was made after the end of the 2004/5 service charge year but before the applicant received the respondent's end of year accounts and certificate for that year. A copy of those accounts (dated 15 September 2005) were shown to the Tribunal. Save in one respect (which is dealt with below), the parties agreed that this should have no effect on the substance of the application.

INSPECTION

6. The Tribunal inspected the subject premises and the other properties referred to by the applicant for comparison purposes on 24 February 2006.

7. Porchester Mead is a large estate with two distinct elements. There is a small terrace of 2 storey houses built in about 1925 as accommodation for retired governesses. In about 1960, three 10-storey tower blocks were also built on the site surrounded by extensive garage blocks and parking. There are limited areas of

shrubs and trees at the edge of the site and on slopes. The blocks are of brick facing with flat roofs with a mix of timber framed/UPVC and double glazed window units. They are each served by two lifts and door entry systems. There is CCTV and a resident porter on site. The external condition of the blocks is reasonably good and the grounds are tidy. Internally, the common parts are neat but fairly basic, with carpeting only to the first floor. Although well-maintained, the estate has very much the "feel" of social housing of the period.

8. Copperfields is a four storey block of 28 flats in a quiet tree-lined avenue built in the 1970s. It is built of fair faced brick with timber windows. Each flat appears to have a balcony and there are penthouse apartments on the top floor. There are well kept lawns surrounding the block. Internally the common parts are tiled and carpeted and there are lifts. Each flat enjoys the use of a garage in a separate garage area well screened from the flats themselves. The whole of the development is very well maintained and has a much more upmarket "feel" than the subject premises.

9. Sandringham Court is situated in an unmade private road. It was constructed in about 1980 and comprises a four storey block of 16 flats of fair faced brick walls and tiled roof with UPVC windows. There is a small neat garden to the rear. Internally, there is a lift and the common parts are carpeted and painted. The internal and external decorations were in need of renewal.

10. Glenthorne Lodge was built in about 1980 and comprises two three storey blocks with balconies to the front. There are 12 flats and 14 garages surrounded by neat lawns. Internally there is no lift, but the property is carpeted. Decorations and maintenance appear good.

INSURANCE

11. The evidence. The buildings insurance for 2004/5 and 2005/6 appear respectively in the respondent's budgets for those years dated 25 March 2004 and 15 March 2005.

12. The applicant stated that he runs a property investment firm called AK Management Group. He produced the 2005/6 service charge accounts for another block at Sandringham Court, Beckenham. This included a figure of £4,170 for building insurance. The insurance certificate showed the sum insured to be £1,805,351. He also produced details for the insurance of another block known as Copperfields. The reinstatement value was £3,400,456 for a premium of £5,846.44. In cross examination, the applicant accepted he had not sought any estimates for insurance of Porchester Mead itself. In cross examination, the applicant accepted that a bad claims history could have an adverse effect on insurance premiums. He had placed building insurance policies himself.

13. The respondent relied on the evidence of Mr. Richard Mason, Director of managing agents Goodacre Property Services. Mr. Mason stated that he had been involved in property management in Beckenham since 1985 and he was a fully bonded member of the NAEA. His firm was an agent for the insurance company Royal & Sun Alliance. He described the procedure for preparing the budget in each year. About 10 months into each service charge year, he prepared an estimated budget based on actual expenditure for the first nine months of the year. This was then submitted to the budget meeting of the respondent's board. In the case of the insurance premium, the premium would have already been paid for the calendar year in January of each year, so the budget figure for insurance was partly the premium already paid, and partly the estimated figure payable the following year. Thus, the 2004/5 budget figure was based on the actual premium paid for the first 9 months of 2003/4 with an estimate for the premium for the next year. For 2003/4 the board had decided at the budget meeting to take out separate

terrorism cover. Mr. Mason produced a copy of the renewal schedule for the insurance for the year beginning 21 January 2005. The total premium payable to Royal & Sun Alliance was £43,361.96 (including a terrorism premium of £8,301.71) for a total reinstatement value of £17 million. One difficulty here was that the estate had a poor claims history. When he had taken over management, the blocks had serious structural defects, and works were completed in 1991. This had to be declared. In the 1990s, he had looked at alternative insurers, but he had been informed that no other insurer was interested in insuring the risk. He understood that such major claims had to be disclosed for a period of 10 years. Mr. Mason had not submitted a formal request for an alternative quote since if insurance was declined by an insurer, this could have had a big impact on the premium payable. A schedule of minor claims over the past 5 years was produced, which suggested there had been 14 claims over this period. Once the 10 years had expired for the structural claims in 2005/6, he had asked the specialist broker Deacon Insurance to test the market. Deacon informed him that there were a very limited number of insurers prepared to insure a 10 storey tower block. They obtained a lower estimate for a premium from Zurich Insurance, but the Royal & Sun Alliance matched this quote. Mr. Mason was familiar with both Sandringham Court and Copperfields. They were very different properties. He gave a rough analysis of the premiums payable for both these properties which suggested that the Porchester Mead premium was competitive. In cross examination Mr. Mason did not accept he should have tried more insurers. The board had been partly influenced by the good relationship with the existing insurer – which had paid out claims without protest. An alternative insurer might not have paid out so easily – and may also have raised premiums in subsequent years after making a competitive bid for the new business in the first year.

14. Submissions. The applicant relied on paragraph 10 of his response to the respondent's statement of case and briefly supplemented this in his closing submissions. He submitted that the agent should have gone to more than one insurer. Even where it had tested the market in 2005/6, the landlord had failed to

produce evidence of alternative quotations from other insurers. The increase in premiums over the years had been astronomical. There was a conflict of interest between Goodacre Property as agent for Royal and Sun Alliance and its position as managing agent.

15. Mr. Gallagher drew the Tribunal's attention to the fact that the "on account" costs of insurance in question included partly premiums already paid and partly premiums to be incurred. He submitted that they were therefore covered by both s.19(1) and s.19(2) of the Act. However, for these purposes it made no difference, there was a "bracket of reasonableness" within which the landlord had a discretion. He referred to the decision of the Lands Tribunal in ***Forcelux v Sweetman*** [2001] 2 EGLR 173. There was a two stage test: (1) whether the landlord behaved reasonably in selecting the insurance and (2) whether the premium paid was reasonable. As to (1) the respondent's directors employed a competent managing agent. The respondent submitted that this was not the ideal property for insurance purposes. There was a history of structural defects and a poor claims record. The estate had 10 storey tower blocks built about 45 years ago. The estate was not really comparable with the other blocks referred to by the applicant – and the insurance for these blocks included other risks not covered by the insurers of Porchester Mead. Bearing in mind these factors and the other matters referred to by Mr. Mason, the landlord had acted reasonably in not formally testing the market. As to (2), the usual way a lessee challenged insurance costs was to produce evidence of an estimate for cover for the subject premises. Here, the lessee relied instead on evidence of cover at other premises. If a cross check was needed, it had been seen that the present insurer had matched the alternative quote from Zurich Insurance. If a further cross-check was needed, the premium at Porchester Mead was still competitive compared to the cover at the other two blocks. The premium here was about £2.44 per £1,000 of cover. This compared favourably to the premium at Sandringham Court which was equivalent to £2.72 per £1,000 of cover (which included terrorism cover) or the premium at

Copperfield which was £2.43 per £1,000 of cover (excluding terrorism cover). The premium here was within the broad bracket of reasonableness.

16. The determination. This application relates to "on account" service charges – but on the evidence of Mr. Mason, these were payable only partly before the relevant costs (i.e. the insurance premiums) were incurred. The Tribunal must therefore consider whether both the relevant costs are limited by both s.19(1) and s.19(2) of the Act. The wording of s.19(1) differs from that of s.19(2) - the former has tests of costs "*reasonably incurred*" and services of a "*reasonable standard*" whereas the latter simply uses the word "*reasonable*". However, the Tribunal considers it would be an artificial exercise to apply different tests to the component parts of the insurance costs element of "on account" charges for the two years in question. The Tribunal therefore adopts the two-stage test suggested by the Lands Tribunal in ***Forcelux*** for all parts of the relevant costs relating to insurance.

17. As far as the first stage is concerned, the Tribunal must consider whether the landlord's actions were appropriate, in the light of the provisions in the lease which reserve the choice of insurer to the landlord. The Tribunal is satisfied on the evidence that the insurance costs element of the "on account" charges were appropriate in the circumstances of this property. The Tribunal takes into consideration the fact that the landlord relied on the advice of a professional managing agent, the history of longer term structural problems with the blocks, the poor recent claims history, the risk that formal market testing of the premiums might result in refusal of cover and the good relationship with the insurer as to claims. Taken together, these are factors which would reasonably persuade a prudent landlord spending its own money to place the insurance with the Royal & Sun Alliance without formally market testing those premiums. The Tribunal would have preferred to have heard the evidence of a broker, although it considers that the landlord's actions are within the "broad bracket of reasonableness" described by Mr. Gallagher.

18. As far as the second stage is concerned, the Tribunal notes that the applicant has not adduced any direct evidence that the premium charged by the Royal & Sun Alliance for this property is excessive. The evidence entirely related to premiums charged for Sandringham Court and Copperfields (both situated in the Avenue Beckenham). The Tribunal considers that such an approach will seldom be of much assistance in assessing whether a premium is reasonable under section 19 of the Act – particularly without expert evidence to assist with comparing the rates charged for the different buildings. In this instance, the Tribunal's inspection showed the two blocks relied upon by the applicant were wholly different to the Porchester Mead estate. No information was given about factors which might have influenced the premiums at the other two blocks – such as the claims history or the terms of the policies. Moreover, even the crude exercise undertaken by Mr. Gallagher suggested that the premium charged for Porchester Mead was not demonstrably excessive when compared to the rates charged at the two other blocks.

19. Finally, the Tribunal rejects the applicant's suggestion that an excessive premium was paid as a result of a conflict of interest between Goodacre Property as the landlord's agent, and its position as an agent for Royal & Sun Alliance. Such arrangements are common in the property management sector. Absent any evidence that this resulted in an excessive premium, the allegation amounts to little more than a speculative attack on the managing agent.

GENERAL MAINTENANCE/SUNDRIES

20. <u>The evidence</u>. These items also appear respectively in the respondent's budgets dated 25 March 2004 and 15 March 2005.

21. The applicant relied on paragraph 7 of his response to the respondent's statement of case. He stated that the 2004/5 figure for repairs and maintenance had been underestimated and that the landlord had had to increase this by 25% in 2005/6. Management on the estate was incompetent. Part of the costs arose from defects to the water mains in 2004 – and this was also due to poor maintenance over the years. However, even those works were carried out poorly, since contractors had to return again on 18 and 26 February 2005. In evidence, the applicant stated that he had experienced a lot of problems with general maintenance. He referred to a letter from Goodacre management dated 1 July 2004 which suggested that certain electrical faults were the responsibility of the lessees. He relied on a statement from Mr. James Callaghan, the lessee of 1 Blake House to the effect that there was disrepair. The applicant produced a petition from residents on the estate supporting the applicant's case suggesting that costs of proposed works were unreasonable. He further relied on five short statements from lessees. In each case, Mr. Gallagher did not object to these statements.

22. Mr. Mason referred to the reports prepared for the budget meeting and to spreadsheets which included a more detailed breakdown of the sundry repairs and maintenance items. The report for the budget meeting on 5 February 2004 advised that the sum of £15,000 in the 2003/4 budget should be retained because although there had been an overspend in the previous year, it was hoped that a number of non-recurring items would not appear the following year. In 2004/5 there had been an overspend compared to the budget – largely as a result of roof parapet works which had been required. The 2004/5 audited accounts showed actual expenditure of £22,424 for that year and £17,139 for 2003/4. In fact, each year the respondent had under budgeted for repairs – which is why the figure was increased each year in the budget. In cross examination, Mr. Mason accepted that some of the costs of repairing leaks came from the contingency fund. Water had appeared on one of the roadways in 2004. The respondents excavated down and found that the underlying clay was saturated – suggesting a long term problem. Because of access problems, excavation had to be done by hand. It emerged that

the pipes were fractured in 6 places and that a range of copper, cast steel and iron pipes had been used. The works took 6 weeks to complete. The later fracture outside Keats House was an unconnected problem – namely a massive 1ft fracture in a main high pressure supply pipe. The cause was not known. The insurers denied liability but made an *ex gratia* contribution to avoid a claim. When this main was replaced, the increased pressure burst a valve.

23. Submissions. In his succinct closing submissions, the applicant relied on the underestimate for 2004/5 which showed the incompetence of the respondents. The cost of the water mains works had increased due to defective installation for which the respondents were liable.

24. Mr. Gallagher submitted that the respondent's board acted on the advice of the agent. The repairs and maintenance element of the budget dealt with the unexpected - a subsidiary part of the works budget once capital costs and the reserve fund were excluded. The only way to deal with minor recurring repairs was the way dealt with by Mr. Mason – namely taking the previous years costs and at the end of the day making an estimate. There was a rolling budget and in each year he undershot. One could derive from that that each year the board made a careful and conservative estimate. The amounts in question were not only reasonable, but they were conservative.

25. Determination. The Tribunal considers that the general approach of the landlord is acceptable – an estimate based on previous year's expenditure adjusted for foreseen contingencies is the only way of budgeting for such costs. The respondent relied not on mere guesswork, but plainly required detailed evidence from Mr. Mason of what was to be spent in each year – as evidenced by the spreadsheets provided to the Tribunal. As far as the second limb of ***Forcelux*** is concerned, there is no suggestion that the cost of these works was not reasonable

in themselves. On inspection, the Tribunal found the Porchester Mead Estate to be in a good state of repair for an estate of this kind and it had the appearance of being well-managed.

26. The thrust of the applicant's complaints are really twofold. First, that the "on account" charges made insufficient provision for the cost of repair works. The Tribunal considers that this cannot be a valid argument to limit the relevant cost on grounds of reasonableness – since (if sustained) it is really an argument that the relevant costs should be more than that provided for in the "on account" charges. Secondly, that the costs had been increased due to previous want of repair by the respondents. On this issue, the applicant produced no evidence at all to show that the repairs to the pipes and mains during the period in question were as a result of any default by the respondent. Mr. Mason's detailed evidence on this was both unchallenged and persuasive.

GENERAL ARGUMENTS

27. The applicant raised a further argument to support the contention that the relevant costs of insurance and repairs/maintenance should be limited by section 19 of the Act. This was that the service charges as a whole were excessive when compared to other parts of Beckenham.

28. <u>The argument</u>. For this argument, the applicant relied on evidence of other 2 bedroom flats which he owned elsewhere in Beckenham:

(a) 7 Sandringham Court. The total budgeted service costs for 2005/6 for the former were £14,766.

(b) 5 Copperfields. The total certified expenditure for 2005/6 was £28,963 for which the applicant was liable for £1,136.

(c) 7 Glenmore Lodge, The Avenue Beckenham. In 2005, the service charge liability was £1,000. The flat was let in March 2005 on an assured shorthold tenancy for £950 per month.

By contrast, 25 Blake House had been let on an assured shorthold tenancy in October 2004 at a monthly rent of £750, and 24 Keats House had been let at £800 per month (although tenants had vacated early due to the respondent's failure to repair). The evidence showed that rental values on the Porchester Mead Estate were much lower than for other parts of Beckenham although the service charges were much higher. The applicant suggested that the service charges at the other properties were broadly the same as the monthly rental value. By contrast, the service costs at Porchester Mead were 40% higher than the monthly rental value. This showed the service costs at the subject premises were 40% higher than elsewhere.

29. Mr. Gallagher did not dispute the evidence as presented. However, in cross-examination, he put to the applicant that there were very real differences between the various blocks, and that there was no relationship between the rental values achievable for a flat and the service charges payable.

30. Determination. The Tribunal has no hesitation in rejecting the applicant's argument. The mere fact that gross service charges may be higher in one property than in another is of little or no assistance. Plainly, properties vary according to the amount of maintenance, costs of insurance, staff, costs of lighting and heating, porterage and so on. Even the most cursory inspection of the other properties relied on by the applicant showed them to be so different from Porchester Mead that the Tribunal must disregard them as providing any evidence of costs. Furthermore, given that only two elements of the "on account" costs are challenged, the Tribunal cannot safely find that these elements are excessive by reference to the cost of providing the whole range of services included in the charge.

31. As to the suggestion that there is an arithmetical relationship between rack rental value and the level of service costs, the Tribunal has no hesitation in rejecting this. Service charges vary according to cost – whereas rental values are largely a result of supply and demand. There is no necessary or even likely relationship between the two, and the applicant has not adduced any valuation evidence to suggest that there might be.

SECTION 20C

32. The applicant applied for an order under section 20C of the Act. The Tribunal must consider this in the light of what is just and equitable in the circumstances, i.e. in accordance with section 20C(3) of the Act. The Tribunal takes into account the guidance of the Lands Tribunal in ***Tenants of Langford Court v Doren Ltd*** [2001] LT LRX/37/2000.

33. Mr. Gallagher conceded that he could not identify any readily apparent provision in the lease which would entitle the respondent to recover the costs of the proceedings before the Tribunal. However, he submitted that this was not a matter for the Tribunal at this stage when considering a possible s.20C order.

34. The Tribunal accepts that the recoverability of any such costs is solely a matter for any future application under s.27A of the Act – but cautions the respondent that the Tribunal shares Mr. Gallagher's doubts that such costs are recoverable under the terms of the lease provided.

35. The Tribunal refuses an order under s.20C. In this instance, the applicant has failed in its application. The conduct of the respondent before and during the application does not appear to have been unreasonable. It gave detailed accounts

and explanations to lessees about service costs at meetings and in writing. Its expenditure on legal costs to meet a multi faceted complaint was not a disproportionate response. The Tribunal notes that the applicant's complaints at the hearing were far narrower than at the date of the witness statements.

CONCLUSIONS

36. The Tribunal determines that the following relevant costs are not limited by section 19 of the Act, namely:

(a) Insurance - £41,000 in the year 2004/5 and £46,771 in the year 2005/6, and;

(b) General Maintenance/Sundries - £16,000 in the year 2004/5 and £20,000 in the year 2005/6.

The Tribunal therefore determines under s.27A that the above sums are payable as part of the service charges. The extent to which they may have been overtaken by balancing charges under the leases is not a matter before the Tribunal.

37. The Tribunal further refuses the application for an order under section 20C of the Landlord and Tenant Act 1985.

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Mark Loveday BA(Hons) MCI Arb
Chairman

Dated: 13 April 2006