FIRST-TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case Reference	**:**	**MAN/30UH/LSC/2023/0081**
Property	**:**	**Apartment 3 Cinnabar House, Poulton Road, Morecambe, LA4 5BW**
Applicants	**:**	**Mark Jan Wach & Janet Eagleton**
Applicants' Representative	**:**	**BG Solicitors LLP**
Respondent	**:**	**MW Freeholds Limited**
Respondent's representative	**:**	**Paul Simon, In-house Solicitor**
Type of Application	**:**	**Landlord and Tenant Act 1985 – s 27A** **Landlord and Tenant Act 1985 – s 20C** **Commonhold and Leasehold Reform Act 2002-Schedule 11 Paragraph 5A**
Tribunal Members	**:**	**Judge J.M.Going** **S.D. Latham MRICS**
Date of decision	**:**	**1 October 2024**

DECISION

The Decision

The Tribunal has determined that the "section 20 sinking charge provision" totalling £3409.04 demanded by the Respondent from the Applicants was not reasonable nor payable.

Further, it makes Orders pursuant to section 20C of the Landlord and Tenant Act 1985 ("the 1985 Act") and under Paragraph 5A of Schedule 11 to the 2002 Act that any costs incurred by the Respondent in relation to the proceedings before the Tribunal shall not be included in the amount of any service charge payable by the Applicants and to extinguish any liability that the Applicants might have, outside of the service charges, to pay an administration charge in respect of litigation costs relating to the present proceedings.

Preliminary

1. By an application ("the Application") dated 6 October 2023 the Applicants applied to the First-Tier Tribunal Property Chamber (Residential Property) ("the Tribunal") under Section 27A of the Landlord and Tenant Act 1985 ("the 1985 Act") for a determination as to whether certain service charges demanded were payable and reasonable, and for separate orders under Section 20C of the 1985 Act and Paragraph 5A of Schedule 11 to the 2002 Act.

2. The Tribunal issued Directions on 16 April 2024 setting out how the parties should prepare and a timetable for provision of relevant documents. The Directions confirmed that the matter was considered suitable to be determined by way of a paper determination after an inspection, but also emphasising the parties' right to request an oral hearing. Neither party has requested an oral hearing.

3. The bundle of documents before the Tribunal include copies of the Application, the Directions, the Applicants lease ("the Lease") and registered title, their initial statement of case, the Respondent's statement of case, the Applicants' supplementary statement, various service charge accounts, budgets and demands, a specification of works, tenders, notices, correspondence, emails, previous determinations by the Tribunal relating to Cinnabar House, the first dated 30 September 2019 handed down on under case reference MAN/30UH/LSC/2018/0079 – 85 ("the Tribunal's 2019 determination") and the second dated 17 April 2020 handed down on 7 September 2020 under case reference MAN/30UH/LRM/2019/0006 ("the 2020 Right to Manage determination") as well as papers from to a claim issued by the Applicants against the Respondent in the County Court in April 2022 ("the CC claim").

4. The Tribunal inspected the property and Cinnabar House on 19 September 2024, with Mr Wach in attendance. No one representing the Respondent attended.

5. Later on the same day the Tribunal convened to consider and make its determination.

The factual background

6. The following matters confirmed or referred to in the papers are not disputed, except where mentioned. References to pages or paragraphs in the bundle or specific documents are contained in square brackets **[ ].**

7. Cinnabar House, built in 1922 as the Morecambe Art and Technical School, is a listed building. It was converted into 22 apartments between 2005 and 2014 **[149-150]**. The Respondent owns the freehold which it acquired in November 2014 **[150]**. Each apartment is owned and held under a long 150-year term beginning on 1 January 2008 lease containing the same or comparable provisions **[151].**

8. The property is one of those flats. The Applicants have owned it since 15 January 2013 **[72-73].** They, as with the other individual apartment owners, are due to pay 1/22nd of the Service Charges as set out in the Lease **[76].**

9. During the period in question Cinnabar House was managed by Moreland Estate Property Management Company ("Moreland"). Laurence Freilich is a director both of the Respondent and Moreland **[64 para 3 confirmed at 197 para 2].**

10. In May 2017 Lancaster City Council wrote to the Respondent stating that "the external appearance of the above-mentioned premises is a source of concern…" and attached a Schedule of required works warning that if the works were not progressed it would have the option of taking enforcement action **[150]**.

11. Mr Freilich prepared a specification of works in November 2017 **[213- 215]** in response to the Council's letter and began what was then referred to as the Section 20 Consultation.

12. In December 2017 Moreland included within its service charge demand sent to the Applicants the first of what was referred to as the "section 20 works sinking charge provision (quarterly charge)" in the sum of £852.26 for the quarter beginning on 1 January 2018, and in addition its general service charges **[106-107]**. This was followed in February, May, and August 2018 by 3 further similar service charge demands for the remaining 3 quarters of 2018 **[108-113]**. The total sum that was demanded from the Applicants under this particular provision was therefore £3409.04. Assuming all 22 apartment owners were charged the same the total sum demanded was almost exactly £75,000.

13. The Tribunal's 2019 Determination found that "The Section 20 Consultation clearly did not properly comply with the Regulations and most significantly was fraudulent and included reference to fictitious estimates**." [160 para 51(11)]**. It also found that the monies that had been demanded under the heading "section 20 works sinking charge provision" were neither reasonable nor payable and that such as had been paid must be recredited in accordance with the terms of the lease **[147 sub para (3) of the Decision & 164 paras 62-74].**

14. It was ordered in the Tribunal's 2019 determination that the Respondent should send a full copy of the determination to each flat owner **[147 sub para (7) of the Decision]**. The Applicants state they were not sent one **[66].** The Respondent states a belief that it instructed Moreland to do so **[198]**.

15. The notes to Moreland's service charge budget on page **[172]** confirmed (inter alia) "The costs of the major works were demanded, on account, in parallel to the general budget for 2018 but no work was done in 2018 so those leaseholders who paid are entitled to a credit on their account…".

16. The Respondent states that "the sums were demanded on account, in anticipation of completing a section 20 consultation that started in November 2017… However, the consultation was not completed and the work was not done. The reason that the work was not completed was after delaying service of the second statutory notice to give the leaseholders the opportunity to nominate a contractor, after the first notice had expired,.. the Respondent was served notice claiming the right to manage, by Cinnabar House RTM Ltd dated 16 April 2018…and upon receipt of that Claim Notice, the Respondent decided not complete the consultation" **[197-198]**.

17. Cinnabar House RTM Ltd acquired the right to manage Cinnabar House on 8 July 2019 as confirmed in the 2020 Right to Manage determination **[178]**.

18. The parties dispute whether any uncommitted service charges were subsequently passed from Moreland to the RTM company **[199 para 12 contradicted at 230 para 6].**

19. As part of its defence to the CC claim the Respondent submitted: –
"…. it is denied that the Claimants were party to any application in the First-tier Tribunal. Accordingly, they are not entitled, in law, to rely on the Learned Tribunal's determination in that matter ….

a. It is admitted that, for the benefit of the applicants in the Application, the Learned Tribunal ruled that:

b. 3.3.1. the sums relating to the "S.20 sinking fund" were inappropriate; …

c. 3.4. The Determination only binds the parties to the case". **[226-227]**

The Inspection

20. Sadly, the Tribunal when making its external inspection found Cinnabar House to be in much the same state as it had been when inspected as part of the 2019 determination. The exterior remains, as was then stated, "poorly maintained with the vast majority of the wooden windows, soffits and all of the ironwork railings needing painting". Whilst there had been some cleaning of the gutters, tidying of the rear, and improvements to the car parking area it was abundantly clear that the gutters and soffits are in increasingly urgent need of replacement. The passage of time has only made the necessary remedial works more pressing, and undoubtedly more expensive. Mr Wach commented that the RTM company and its managing agents have in hand major repair works with an anticipated start date in the next months.

The relevant legislation

21. Section 27A of the 1985 Act provides that:-

> "(1) An application may be made to the appropriate Tribunal for a determination whether a service charge is payable and, if it is, as to -
>
> (a) the person by whom it is payable,
>
> (b) the person to whom it is payable,
>
> (c) the amount which is payable,
>
> (d) the date at or by which it is payable, and
>
> (e) the manner in which it is payable.
>
> .....
>
> (4) No application under subsection (1).. may be made in respect of a matter which –
>
> (a) has been agreed or admitted by the tenant,
>
> .....
>
> (5) But the tenant is not to be taken to have agreed or admitted any matter by reason only of having made any payment."

22. Section 18 states that: –

> "(1) In the following provisions of this Act "service charge" means an amount payable by a tenant of a dwelling as part of or in addition to the rent –
>
> (a) which is payable, directly or indirectly for services, repairs, maintenance, improvements or insurance or the landlord's costs of management, and
>
> (b) the whole or part of which varies or may vary according to the relevant costs.
>
> (2) The relevant costs are the costs or estimated costs incurred or to be incurred by or on behalf of the landlord, or a superior landlord, in connection with the matters for which the service charge is payable.

(3) For this purpose –

(a) "costs" includes overheads, and

(b) costs are relevant costs in relation to the service charge whether they are incurred, or to be incurred, in the period for which the service charge is payable or in an earlier or later period."

23. Section 19 of the 1985 Act confirms that :-

"(1) Relevant costs shall be taken into account in determining the amount of a service charge payable for a period -

(a) only to the extent that they are reasonably incurred, and

(b) where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a reasonable standard;

and the amount payable shall be limited accordingly.

(2) where a service charge is payable before the relevant costs are incurred, no greater amount than is reasonable, is so payable, and after the relevant costs have been incurred any necessary adjustment shall be made by repayment, reduction or subsequent charges or otherwise."

24. Section 20C states that: –

"(1) A tenant may make an application for an order that all or any of the costs incurred, or to be incurred by the landlord in connection with proceedings before… the First-tier Tribunal… are not to be regarded as relevant costs to be taken into account in determining the amount of any service charge payable by the tenant or any other person or persons specified in the application.

… (3) The court or Tribunal to which the application is made may make such order on the application as it considers just and equitable in the circumstances."

25. Paragraph 5A of Schedule 11 to the 2002 Act states that: –

"(1) A tenant of a dwelling in England may apply to the relevant court or Tribunal for an order reducing or extinguishing the tenant's liability to pay a particular administration charge in respect of litigation costs.

(2) The relevant court or Tribunal may make whatever order on the application it considers just and equitable."

The Tribunal's Reasons and Conclusions

26. The Tribunal began with a general review of the papers, to decide whether the case could be dealt with properly without holding an oral hearing. Rule 31 of its procedural rules permits this provided that the parties give their consent (or do not object when a paper determination is proposed).

27. Neither party has requested an oral hearing and having reviewed the papers, the Tribunal is satisfied that this matter is suitable to be determined without a

hearing. The documentation provides clear and obvious evidence of the contents and the relevant facts, allowing conclusions to be properly reached in respect of the issues to be determined.

The Section 27A Application

28. The question for the Tribunal to decide is whether the section 20 works sinking charge provision demanded of the Applicants totalling £3409.04 was reasonable and payable.

29. The short answer is no.

30. The reasons set out in the Tribunal's 2019 determination are equally applicable now to the parties to this case as they were in 2019 to the parties to the Tribunal's 2019 determination.

31. For ease of reference, the relevant paragraphs in that determination are now reproduced, but with the references to the "respondent" and "applicant" transposed because of the Respondent being referred to as the Applicant in the Tribunal's 2019 determination).

"*Section 20 Sinking Charge Provision*

62. The Tribunal has no hesitation in agreeing with the RICS's "Service charge Residential Management Code-3rd edition" stating that "it is … considered good practice to hold reserve funds where the Lease permits". Tribunal is also absolutely clear that Cinnabar House, a Listed Building on a constricted site, requires strategic management and an ongoing rolling plan of maintenance and repair to sustain its unique structure, roof and infrastructure.

63. There is no statutory requirement for Consultation prior to levying an "on account" service charge if the Lease in question allows for it. Section 19 (2) of the 1985 Act makes it quite clear that it is perfectly possible for service charges to be payable before the relevant costs are incurred, but it also states that "no greater amount than is reasonable is… payable".

64. In this case the authority to collect certain monies in before they are expended starts with paragraph 10.1.11 of the Lease.

65. Paragraph 10.1.11 imposes its own constraints and makes explicit that the monies that can be set aside are limited to "such sums … as the Management Company shall reasonably require to meet such future costs as the Management Company shall reasonably expect to incur…". It also confirms "such setting aside being deemed an item of expenditure by the Management company" which brings it within the costs which can be included in the service charges. Those costs are however themselves also limited by the wording of the first line of part 2 of the 7th schedule to those which are "properly incurred".

66. *Taking those requirements together, for advance payments to be collected, and payable, they must be: –*

1. *for future costs that are reasonably expected,*
2. *for costs that are reasonably required,*
3. *properly incurred, and*
4. *reasonable.*

67. *The Tribunal had no doubt looking at Cinnabar House that costs to pay for the works referred to by the Council and in the {Respondent's} specification could be both reasonably expected and would be reasonably required, if funds were not already available. The mismatch between the amounts previously demanded under the general service charges, and the management company's actual expenditure as shown in the audited accounts should have ensured that there were adequate balances to be able to proceed with at least some (but not necessarily all) of the {Respondent's} specified works forthwith.*

68. *The Tribunal then went on to consider whether the costs demanded for the "section 20 sinking fund provision" were properly incurred and, when looked at in the round, reasonable.*

69. *Whilst compliance with the Regulations and the Consultation requirements are not a necessary prerequisite to an estimated on account demand for service charges, compliance is certainly required in respect of qualifying works. The Regulations and the Consultation requirements also provide a template by which to judge whether advance payments are properly incurred and reasonable. Any deliberate deviation or avoidance must draw in to question the reasonableness of the end result. Significantly the Consultation requirements make it abundantly clear that at least one estimate must be from a person "wholly unconnected with the landlord". The purpose of the Consultation requirements has been confirmed by the Supreme Court in Daejan Investments Ltd v Benson and others (2013) UK SC 14 (the leading case on the proper way to deal with applications for dispensation) as being to ensure that leaseholders are not put at risk of having to pay for inappropriate works or paying more than would be appropriate. The Tribunal is clearly of the view that the same benchmark should be applied when considering whether the costs demanded in this case were properly incurred and reasonable.*

70. *Sadly, the Tribunal has had no difficulty in concluding that the {Respondent} has shown in its dealings with the {Applicants} a wholesale disregard for both the purpose and the detailed provisions of the Consultation requirements, and by its actions put the {Applicants} at risk of having to pay for inappropriate works or paying more than would be appropriate. As such, it has concluded that*

the costs demanded under the heading "Section 20 sinking fund provision" were not properly incurred and not reasonable.

71. It also follows, from the Tribunal's finding that the Consultation requirements were not properly complied with, that the service charge contributions due from each of the Leaseholders for any actual works included within the {Respondent's} proposed works would be limited to £250 as a consequence of Section 20 of the 1985 Act, unless and until there has been a properly compliant consultation or until any dispensation is granted.

72. It further follows that, as soon as it became apparent that the Consultation requirements were not being properly complied with, the {Applicants} became immediately entitled (in the knowledge that their maximum individual contributions were then limited by statute to £250) to conclude that no more than £250 should or could be charged to each for the {Respondent's} proposed works. As was put in the {Applicants} submissions "if works are required, genuine estimates will need to be obtained and the statutory consultation process will need to be undertaken again."

73. In all the circumstances, the Tribunal has concluded that the {Respondent} was not entitled to any of the sums described as the Section 20 sinking charge provision".

32. It was recognised in Tribunal's 2019 determination that all of the leaseholders who had contributed the Section 20 sinking charge provision should have such monies credited back to them **[166 para 74].** As was clearly stated in subparagraph (7) of the Decision, it was because the case gave rise to common issues applicable to all the flat owners that the Respondent was ordered to send a full copy of the determination to each one. The Applicants state that this was not done. Whilst little now turns on the point, the Tribunal finds that the Respondent's assertion that it instructed Moreland (with all its close connections to the Respondent) to comply with that part of the order, but without now providing any proof of postage or other service, less than convincing. The Tribunal would expect any experienced and professional management company to routinely keep comprehensive records of correspondence.

33. The Respondent does admit that it never proceeded with the specified works, and made the decision not to do so, for whatever reason, over six years ago. (The reason stated within the papers to this case, being the receipt of a notice of a right to manage application in April 2018 **[198 para 2]**, is not necessarily consistent with that stated in the 2019 case, being a change in the Council's requirements **[155 para 34]**, and quite possibly there were multiple reasons beyond those stated.) In any event, the Respondent had demanded monies for specific works, which it then decided not to proceed with. Once that decision had been made it became even clearer that the Section 20 sinking charge provision was neither reasonable nor payable.

The general service charges for the years 2015 – 2017 as referred to in the Tribunal's 2019 determination

34. For the avoidance of any future doubt and, noting that the Applicants have owned the property since 2013, the Tribunal reaffirms that they, as with the flat owners who were parties to the 2019 case, and all the other flat owners who were overcharged for those items identified in paragraph 59 of the Tribunal's 2019 determination, are entitled to have the overcharged amounts recredited as referred to in that determination, or repaid.

The Section 20C and Paragraph 5A Applications

35. The Tribunal went on to consider the Applicants' separate applications, that it make orders both under section 20C of the 1985 Act so that the Respondent be precluded from including within the service charges the costs incurred by the Respondent in connection with the present proceedings before the Tribunal, and under Paragraph 5A of Schedule 11 of the 2002 Act to reduce or extinguish any liability that the Applicants might have under the Lease in respect of the Respondent's costs.

36. In each instance, the Tribunal having regard to what is just and equitable in all the circumstances, and in the light of its foregoing decisions, determined that Orders should be made precluding the Respondent from seeking to recover any of its costs incurred in relation to the proceedings before the Tribunal from the Applicants either as part of the service charges or as an administration charge.