FIRST-TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case reference	**:**	**LON/AF/LSC/2023/0294**
Property	**:**	**Flats at 97 Martins Road, Bromley BR2 0ED**
Applicant	**:**	**(1) Brian Engel (flat 2)** **(2) Rachael Osman (flat 4)** **(3) Laura Denton (flat 3)** **(4) Kim Grantham (flat 1)**
Representative	**:**	**Ms Laura Denton**
Respondent	**:**	**Southern Housing**
Representative	**:**	**Mr William Richardson, counsel**
Type of application	**:**	**Determination of the liability to pay and the reasonableness of service charges, section 27A Landlord & Tenant Act 1985**
Tribunal members	**:**	**Judge Mark Jones** **Mr Kevin Ridgeway MRICS**
Venue	**:**	**10 Alfred Place, London WC1E 7LR**
Date of hearing	**:**	**18 October 2024**
Date of decision	**:**	**11 November 2024**

DECISION

Decisions of the tribunal

(1) The Tribunal determines that the charges claimed by the Respondent as service charges in respect of Flats 1, 2, 3 and 4, 97 Martins Road, Bromley BR2 0ED for the service charge year 1 April 2022 to 31 March 2023 are payable by the Applicants.

(2) The Tribunal determines that the charges claimed by the Respondent as service charges in respect of Flats 1, 2, 3 and 4, 97 Martins Road, Bromley BR2 0ED for the service charge year 1 April 2022 to 31 March 2023 are payable by the Applicants, save for:

(2.1) The Sinking Fund (otherwise referred to as Reserve Fund) contributions are reduced by 50% in the case of each Applicant.

(2.2) The management fee is reduced by £68.88 *per annum* in the case of each Applicant.

(3) The Tribunal makes a s.20C Order under the provisions of the Landlord and Tenant Act 1985 that prevents the recovery from the tenants of costs incurred by the Respondent in these proceedings.

(4) The application and hearing costs totalling £300 incurred by the Applicants in bringing this application are to be reimbursed by the Respondent.

The Tribunal's Reasons

The application

1. The Applicant tenants seek a determination pursuant to s.27A of the Landlord and Tenant Act 1985 ("***the 1985 Act***") as to the amount of service charges payable by them in respect of the service charge years:

1.1 1 April 2022 to 31 March 2023, and

1.2 1 April 2023 to 31 March 2024.

2. The Applicants also sought an order under s.20C of the 1985 Act for the limitation of the landlord's costs of the proceedings.

The Hearing

3. The Applicants were represented at the hearing by one of their number, Ms Laura Denton. She conducted herself admirably and we are grateful for her cogent submissions, despite the fact that she has no apparent legal background.

4. The Respondent was represented by Mr William Richardson of counsel, to whom we are also grateful for his assistance.

5. Mr Sean Duncan, Service Charge Analyst employed by the Respondent attended the hearing and gave evidence, albeit briefly, for which we also express our gratitude.

Preliminary Matters

6. Directions in this matter were given by the Tribunal on 6 September 2023 and 23 January 2024. A mediation appointment was held on 8 February 2024, but the Respondent failed to attend, as later explained due to some difficulty in internal communications. Further directions were then given on 27 February 2024, and finally on 24 June 2024, following exchange by the parties of their respective Statements of Case. The matter was, finally set down for hearing on 18 October 2024 by notice to the parties dated 17 July 2024.

7. 3 days prior to the hearing, by application in Form Order 1, the Respondent applied for permission to rely upon the witness statement of Mr Duncan dated 15 October 2024.

8. As a preliminary matter, we heard Mr Richardson on that application, and then considered carefully the submissions of Ms Denton, who very reasonably informed the Tribunal that she had no objection to its admission save that she did take issue with the contents of the statement insofar as it asserted (in §A(iii)) that recent evidence suggested a rebuild value for the block at Martins Road was £293,235.00. This was new evidence that she had not had the opportunity to review, prior to service of the statement, and any underlying evidence of valuation had not been disclosed.

9. In considering and applying the broad discretion afforded to the Tribunal by Rule 6 of the Tribunal Procedure (First-tier Tribunal)(Property Chamber) Rules 2013, we were satisfied that it was correct to permit the application to rely upon Mr Duncan's evidence, but to allow Ms Denton the opportunity to put to him any questions she chose concerning that evidence, and so we directed.

The background

10. The building at 97 Martins Road which is the subject of this application is a purpose-built block of 6 two-bedroom flats across 3 floors. The common parts comprise the front door opening onto a hallway, and two flights of stairs permitting access to the upper floors.

11. The Applicant tenants each occupy one of the flats in the building. Three of the six flats (nos. 1, 3 and 5) are slightly larger than the other three, and pay a slightly higher service charge.

12. The Applicants' complaint, in summary, derives from Southern Housing having taken over management of the building in January 2023, following a form of restructuring were Southern Housing merged with their previously identified landlord, Optivo.

13. The Applicants initially appointed Mr Brian Engel to represent them, but he has been suffering from very poor health, is undergoing treatment for cancer and was too unwell to attend the hearing. As indicated in the directions of 24 June 2024, Ms Denton replaced Mr Engel to represent the Applicants. Ms Denton confirmed that Mr Harvey Bailey, who was formerly an applicant, had vacated his flat (flat 5) and she had lost contact with him, so that the number of Applicants is (now) the four named parties.

14. Neither party requested an inspection, and the tribunal did not consider that one was necessary, nor would it have been proportionate to the issues in dispute.

The Lease Provisions

15. The Applicants are each the long lessees for flats within the building.

16. The bundle contains a sample lease, specifically that of Ms Denton's flat, Flat 3 (pp. 40-64). We understand that all leases are in virtually identical terms, *mutatis mutandis*.

17. The landlord's obligations by way of provision of services, including maintenance, repair and so on, are defined in clause 5 of the lease, and the sub-clauses thereunder. Clause 5(2) contains the landlord's insuring obligations for the building.

18. Clause 3.2(b) obliges the tenants to pay the Service Charge (as defined) in accordance with Clause 7, by way of further or additional rent.

19. Clause 7 sets out the tenants' obligations regarding the payment of service charges. Clause 7(5) defines such expenditure to be included in computation of such service charges as comprising all expenditure reasonably incurred by the landlord in connection with the repair, management, maintenance and provision of services for the building, and is followed by a non-exhaustive series of identified elements.

20. Clause 7(4)(a) enables the landlord to levy interim charges, based upon anticipated annual expenditure, and requires the tenants to pay on

account in each year. Clause 7(6)(a) provides for any excess paid by the tenants to be retained and applied against their liability for the succeeding year, and for any shortfall at the end of each accounting period to be made up by the tenants, upon certification by the landlord.

21. Clauses 7(4)(b) and (c) relate to the establishment and maintenance of what was referred to during the proceedings as a *Sinking Fund*, by defining the Service Provision (against which the individual service charges are to be calculated) as comprising, *inter alia*:

"...an appropriate amount as a reserve for or towards such of the matters specified in clause (5) hereof as are likely to give rise to expenditure after such Account Year being matters which are likely to arise either only once during the then unexpired term of this Lease or at intervals of more than one year including (without prejudice to the generality of the foregoing) such matters as the decoration of the exterior parts of the Building (the said amount to be computed in such manner as to ensure as far as is reasonably foreseeable that the Service Provision shall not fluctuate unduly from year to year) but

"...reduced by any unexpended reserve already made pursuant to paragraph (b) of this sub-clause in respect of such expenditure as aforesaid..."

The Scope of the Tribunal's Jurisdiction on the Application

22. As was clarified by Ms Denton for the Applicants at the commencement of the hearing, and agreed by Mr Richardson, the Tribunal is asked to determine the reasonableness under s.19 of the 1985 Act, and liability to pay under section 27A of the 1985 Act of service charges for the years 1 April 2022 to 31 March 2023, and 1 April 2023 to 31 March 2024. The Tribunal has only considered those service charges and other charges that are mentioned in the application. The Tribunal has not considered whether other charges that may have been levied against the Applicants are payable.

23. The Tribunal has considered whether individual service charge costs were reasonably incurred, or services provided to a reasonable standard under section 19 of the 1985 Act. It also has power to determine whether sums are payable under section 27A of the 1985 Act, whether under the terms of the lease or by another law.

24. Of particular relevance to the issue of the Sinking Fund, where a service charge is demanded before the relevant costs were incurred, the Tribunal is also permitted to consider whether the amount charged in advance is reasonable.

The Law

25. Section 18 of the 1985 Act defines *"service charges"* and *"relevant costs"*:

> *(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 a 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.*

26. S.19 of the 1985 Act deals with limitation of service charges:

> *(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.*

27. S.27A of the 1985 Act addresses questions of liability to pay service charges:

> *(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.*
>
> *(2) Subsection (1) applies whether or not any payment has been made.*

The Issues

28. The specific aspects of the service charges in dispute were identified by Ms Denton for the Applicants, and confirmed by Mr Richardson for the two years in question as the following:

28.1 Insurance charges;

28.2 Management fees; and

28.3 Sinking Fund contributions.

29. At the hearing the above identified issues were effectively deployed as an agenda, with each item addressed sequentially following Mr Duncan's evidence. For each disputed item Ms Denton for the Applicants provided an explanation of their challenge and, where she was able, made proposals of an alternative reasonable sum. Mr Richardson then responded in respect of each item, and Ms Denton was afforded the opportunity to respond, in turn, to his submissions regarding each item.

30. While the service charges for the flats varied slightly, the majority of submissions focussed on Flat 2, Mr Engel's demise, with focus upon the service charge statement for 2022-3 at p.79 of the bundle, which was by its terms generated on or after 31 March 2023, and the (anonymised) service charge demand dated 24 February 2023 for the year 2023-4, at pp.84-95.

Disputed Insurance Charges

31. Ms Denton referred the Tribunal to the service charge account for 2022-3, and the demand for 2023-4, emphasising the key points she wished to make in respect of:

    31.1 the insurance charges per flat of £157.08, against a total charge for the building of £1,249.21, for 1 April 2022 to 31 March 2023, and

    31.2 the insurance charge of £30.97 per month, or £371.64 per annum, per flat, a total of £2,229.84 per annum for the building as a whole, for the year 1 April 2023 to 31 March 2024.

32. Ms Denton (rightly) conceded that insurance is an obligation of the landlord, properly chargeable to the tenants under the leases, from which the tenants derive the not inconsiderable benefit of living in an insured building.

33. The Applicants' complaint was that the charges were unreasonably high, year on year, as against insurance for the building in the year 2021-2, in the sum of £770.40.

34. Ms Denton stated, as was agreed by the Respondent, that this was an apportioned sum each year, where the Respondent in fact obtained a composite insurance policy for a large number of buildings within its portfolio. Despite directions having been given by the Tribunal on 27 February 2024 requiring details of the apportionment process of the consequential costs between premises owned by the Respondent, this had not been provided.

35. This led, Ms Denton submitted, to the prospect that the insurance charge apportioned to the building, and then divided between the tenants, was artificially high, where the total premium may well be substantially inflated in consequence of other properties within the portfolio bearing substantially increased risk factors, and/or with deleterious claims histories, as against the building being comprised of (just) six flats, where the Respondent's evidence was that (just) one claim had been made on the insurance policy in the last 5 years, details undisclosed.

36. Ms Denton referred to clause 5(2) of the lease, submitting that this required the provision of a receipt for the policy premium, which had never been provided by the Respondent: the clause requires provision of details of the policy and evidence of payment, albeit not a *receipt*.

37. Ms Denton also made an ambitious submission based upon an asserted valuation of the Respondent's portfolio of some £9 billion, as against estimated rebuild value of the building as contained in Mr Duncan's

statement of £293,235, to the effect that the building therefore represented (just) 0.000326% of the Respondent's total holdings. She then referred to recent correspondence from the Respondent dated 3 October 2024 (that was not before us, but the summary of which was not contested by Mr Richardson, and which we accept) that insurance quotations for the entire portfolio[1] had been obtained in the sums of £7.7 million, £10.6 million and £11.4 million. Applying the 0.000326% percentage to the lower of the quotations suggested that a reasonable insurance premium for the building would be (just) £252.

38. There was no direct, mathematical evidence before us as to the apportionment process, or indeed that the Respondent had sought alternative quotes in the market.

39. The Respondent's case was to the effect that there was a (very) limited pool of insurers prepared to offer cover to the property in issue, and to its portfolio more generally. It had conducted a competitive tender process 4 years ago, and had accepted the best value response for a commitment of 5 years from Zurich Municipal, expiring on 31 October 2024, the actual terms to be negotiated annually based upon the risk to be insured and the claims history.

40. Mr Richardson submitted that the increase in premiums was a regrettable consequence of inflation increasing rebuilding costs, and consequently insurance premiums as a product of the appreciation of risks. Essentially, the increased premiums are a natural, if regrettable consequence of what is frequently referred to as the *cost of living crisis*.

41. As to the question of apportionment, the Respondent's case is that this is based upon property size, where the added costs (which would be recoverable from tenants) of engaging staff to calculate individual insurance premiums make the current approach far more cost-effective. It was Mr Duncan's evidence that it is standard practice within the housing industry to seek comprehensive portfolio policies, this being cost-effective and efficient to ensure provision of comprehensive cover at an effective rate.

42. Mr Richardson urged caution upon us in relation to any anticipated reliance upon the arithmetical approach summarised in §37, above, based upon figures and dates with which the Tribunal is not directly concerned on this application, in contrast to the actual insurance costs incurred by the Respondent.

43. In the course of examining the historical service charge accounts for the years 2020-1, 2021-2, and 2022-3, the Tribunal raised of Mr Richardson the query that the sums for insurance apparently charged to the

[1] Said to be in the region of some 77,000 dwellings, upon merger of Optiva and the Respondent,

individual lessees of, at least, flats 1, 2, 3 and 4 appeared to have been recorded as just £2 per annum, as against actual costs of £770.40 for 2021-2 and £1,249.21 for 2022-3, divided between each flat. This had., it seems, resulted in refunds to the leaseholders against sums paid by them for those years.

44. Having allowed Mr Richardson the opportunity to take instructions, he informed the Tribunal that for those years Optivo (in 2020-1) and Southern Housing (in 2022-3) had, in error, only charged each leaseholder £2 per annum by way of contributions through service charges for buildings insurance, against the significantly more substantial sums expended by the Respondent. The error had not been observed until the issue was raised during the hearing. Ms Denton did not disagree. Mr Richardson informed the Tribunal that the Respondent did not propose, now, to seek to recover the erroneous shortfall from the Applicants.

45. We accept this explanation, as against the accounts provided, and consider that the substantial increase in service charge demands complained of by the Applicants is in large part attributable (now) to the inclusion of insurance costs as actually incurred by the Respondent in the demands for the year from 1 April 2023.

46. We consequently find that for the service charge year 2022-3 the four Applicants were each charged the extremely modest sum of £2 apiece by way of service charges in respect of the element of buildings insurance. We make no finding in respect of the other leaseholders in the building, against a submission by Ms Denton that they may or may not have been charged substantially more, where no application from or evidence relating to those persons are before us.

Decision

47. For the service charge year 2022-3, the Applicants were each charged just £2 for buildings insurance: albeit that the charge was made in error, we find that this was (extremely) reasonable, the error having substantially benefitted each of the Applicants,

48. As to the year 2023-4, the Tribunal notes the judgment in *Cos Services v Nicholson & Williams* [2017] UKUT 382 (LC) in which the Upper Tribunal held that in considering the reasonableness of insurance charged by way of service charge:

> *"It will require the landlord to explain the process by which the particular policy and premium have been selected, with reference to the steps taken to assess the current market."*

49. *Forcelux v Sweetman* [2001] 2 EGLR 173 established that insurance charges reasonably incurred:

"…cannot be a licence to charge a figure that is out of line with the market norm…"

50. Mindful of such guidance, the Tribunal concludes from the evidence presented that the insurance cover obtained was the product of a competitive tendering process. The fact that it was a composite, portfolio-wide policy is standard industry practice, conferring the benefit of cost-efficiency, securing appropriate cover at the most competitive rate available, which we find to have been entirely reasonable.

51. The Tribunal has experience and knowledge of these matters, and we determine that the significant increases in premiums, year on year, are an unfortunate consequence of prevailing economic trends. There is no evidence to suggest that alternative cover was available to the Respondent at a cheaper rate, not least because the Respondent was contractually bound to take cover from Zurich until October 2024, as a consequence of the tendering process, which we found to have been reasonable to have engaged in. We also accept the evidence of the Respondent as to the apportionment of the far larger composite premium between buildings, based upon size and location.

52. With respect to her, we reject Ms Denton's arguments based upon the percentage approach to the Respondent's portfolio, summarised in §37, above. While certainly ingenious, this appeared to us to be an artificial mathematical construct that bears no relation to the practical realities of securing insurance cover faced by the Respondent, the actual sums incurred in defraying the premium, and the complex exercise of ensuring a fair attribution of fractions of a far larger policy premium between the multiple properties within its portfolio.

53. In conclusion, where the costs charged had clearly been incurred by the Respondent, we cannot conclude that they were unreasonably incurred or in sums falling far outside a reasonable range of charges for buildings insurance provision.

54. Accordingly, we conclude that the charges rendered, of £30.97 per month, or £371.64 per annum as set out in the specimen demand at pages 85-88, or any slightly adjusted sum attributed to other flats based upon the same policy premium, are reasonable, and are therefore payable.

Sinking Fund

55. Contributions to the Sinking Fund (referred to in the disclosed accounts for 2022-3 as the 'Reserve Fund') totalled £5,210.64 in 2021-2, and £5,466.24 in 2022-3. This broke down to an individual contribution by Mr Engel of Flat 2 of £820.06 for the former year and £860.28 in the latter.

56. The monthly demand for 2023-4 for this item was for £76.56, amounting to £918.72 per annum. Albeit that this might be subject to very slight variation as between the larger and smaller flats, this suggests a total demand for around £5,512.32 across the 6 flats in the building, for the year.

57. Notably, the Reserve Fund (as referred to in the account) contained a closing balance of some £74,293.13 as at 31 March 2023, including some £1,471.86 in interest earned in the preceding year, a happier consequence of rising interest rates. By contrast, the sum held as at 1 April 2022 was £67,355.03. The fund is held with Federated Hermes Cash Management, in an interest-bearing account.

58. Against the Respondent's case, that the reserve fund contribution demands are based on calculations using the anticipated lifespan of certain items, estimated inflation and replacement costs and future planned works and contingencies, based in turn upon a stock condition survey, working out projected replacement costs and life cycles based on the *Hunter Report* and RICS guidance, the Applicants point to the fact that no disclosure has been given of the stock condition survey or of the calculations employed.

59. This is augmented by the evidence of Mr Duncan which, while providing comfort in relation to the interest-bearing nature of the fund in which the monies are held, candidly concedes that he was unable to say whether or not there were any anticipated major works. In response to questions, he reiterated that he was unable to say whether any major works were in the offing.

60. Ms Denton told us, and we accept, that the building had recently been painted, albeit that again we have no evidence from the Respondent of this very relevant issue, and in particular of the cost associated with it, and whether this was an item paid for as part of annual maintenance, or as an item to be attributed to the sinking/reserve fund.

61. The Applicants' case, as expressed in their Statement of Case, is to the effect that the building is a block of just 6 flats. Rough estimates had been sought as to likely costs of redecoration of around £15,000, and for a new roof of around £35 – 30,000 plus VAT. While a roof's lifespan was said to be around 25 years, as against the building's completion in 2002, the sums retained very comfortably exceeded what would be required. If some catastrophic event were to occur and a claim needed to be made on the insurance policy for an entire rebuild, the excess is £40,000: an entire rebuild paid for by insurance and a replacement roof would, logically, never occur at the same time, as the former presupposes replacement of the latter.

62. In short, the Applicants contend, the existing fund appears substantially to exceed anything that might be anticipated to be reasonably required

by way of future works, none apparently being planned in any event (albeit that roof overhaul may be necessary in the near future). Analysis of the sums claimed for the sinking/reserve fund showed that these amounted to more than 50% of the total service charges demanded in the years in question. These were sums that the leaseholders could ill afford: against recent and well-publicised costs of living difficulties, Ms Denton works on a teacher's salary, while other Applicants were described as, variously, elderly, in poor health, and in one case dependent on food banks for nutrition.

63. Ms Denton made it clear that the Applicants were not seeking a pause in contributing to the fund altogether: she was well aware that retention of such a fund was desirable as a buffer against large future costs, but against all the above circumstances argued that it should reasonably be but a proportion of what was claimed: she suggested 50% of the sums being demanded would adequately protect the fund against inflation and other increasing costs.

64. The Respondent identifies the sinking fund as a product of future anticipated costs, spread over time to seek to make the payments more manageable for lessees. It contends that the amounts collected are based on professional assessment of future maintenance and repair requirements, albeit that no disclosure was made of such assessments, or of any financial projections. We repeat that Mr Duncan was unable to point to any anticipated major works, albeit we do take note of the recent redecoration.

65. Mr Richardson characterised some of the Applicants' financial observations as being based upon *'back of a fag packet calculations'*, to which the Tribunal takes the view that the Applicants could be expected to do little more, against the wholesale failure of the Respondent to disclose *any* of the underlying financial information. He suggested that it was for the Applicants to prove that the demands were unreasonable, and that a substantial reduction might well leave the fund insufficient to absorb future capital expenditure.

66. The obvious problems of cash-flow for a landlord obliged to carry out works under the terms of a lease can clearly be ameliorated by the use of a lease's provisions a suitably drafted clause providing for the accumulation of capital in "*reserve*" and/or "*sinking*" funds, avoiding dramatic fluctuation in service charge demands from year to year. Although the terms are frequently used interchangeably, traditionally the term "*reserve fund*" is used in relation to a fund created for the purposes of equalising across accounting periods demands made on the tenant in respect of items of expenditure which, whilst recurring on a regular basis, tend to vary in amount from period to period (for example, internal cleaning and decorating. A "sinking fund", on the other hand, is a fund accumulated to pay for major repairs (e.g. to roofs) or for the repair or renewal of major items of plant and equipment (e.g. lifts, air

conditioning plant, etc). Such items may only require renewal or repair once or twice, or possibly not at all, during the term of a lease. The distinction may be more or less academic in the circumstances of the present case, and we shall refer to the fund hereafter as *"the **Sinking Fund**"*.

67. The lease clearly provides for the accumulation of such a fund, by clause 7(4)(b), subject to clause 7(4)(c).

68. Where, as here, the Applicants' flats are each dwellings, demands for contributions to the Sinking Fund must, in addition to complying with the terms of the lease, have to satisfy the test of reasonableness set out in s.19(2) of the 1985 Act.

69. This in turn requires of a landlord demonstration of some rational basis for the sums demanded. This should, of course, be based upon analysis involving consideration of the life expectancy of relevant items, projected costs of replacement or repair, and inflation.

70. We do not accept Mr Richardson's submission that it is for the tenants to prove that the demands were unreasonable: there is good authority for the proposition that, upon a challenge being made to the reasonableness of sums demanded, the onus is on the landlord to justify that the item in question satisfies the test in s.19(2). Thus, in *Balkhi v Southern Land Securities Ltd*. [2016] UKUT 239 (LC), the Upper Tribunal observed, in relation to a s.19(2) challenge to sinking fund contributions: *"In a case where a tenant raises a question regarding the reasonableness of the amount claimed and where the tenant (as here) produces material suggesting the amount claimed may not be reasonable, then it will be for the landlord to justify the reasonableness of what is claimed."*

71. This requires the Tribunal to adopt a two-stage approach, of asking firstly whether the decision-making process was reasonable and secondly whether the sum to be charged is reasonable in light of the evidence: see *Southall Court (Residents) v Tiwari* [2011] UKUT 218 (LC) at §11, *Carey Morgan v De Walden* [2013] UKUT 0134 (LC) at §§22, 33, 35, *23 Dollis Avenue (1998) Ltd v Vejdani* [2016] UKUT 0365, §33, and Knapper v Francis [2017] UKUT 3 (LC), §39.

72. In *Hyde Housing Assoc Ltd v Lane* [2009] UKUT 180 (LC) the Upper Tribunal considered sums claimed for *'miscellaneous'* items of anticipated future expenditure for the purposes of building up a reserve fund, as against a report prepared by independent consultants as to anticipated future expenditure for the following 60 years for the purpose of establishing a reserve fund. The aim was to set the service charge at a rate which would ensure that there were no additional charges for major works because these could be met from the reserve fund. The Lands Tribunal accepted that this methodology was reasonable in principle, but where it could discern no explicable reason for the sums actually

demanded , it determined that it was not possible to be satisfied that the sums demanded were reasonable within s.19(2), and in the event determined that half the total cost claimed would be a reasonable amount to be paid by the lessees.

73. In this case, the Respondent has produced no evidence whatsoever in the form of detailed analysis of projected future costs, relying solely upon the generalisations contained within its Statement of Case and (with respect to him) Mr Duncan's witness statement.

74. As Her Honour Judge Robinson observed in *Hyde Housing*, *"To require a service charge payment of an estimated sum to reflect likely future expenditure for a reserve fund without any supporting evidence as to likely works, the date when they may have to be carried out and their cost is bound to result in a challenge from the lessee(s). In the absence of such evidence there is no basis on which a tribunal can find that the amount is reasonable for the purposes of section 19(2) of the 1985 Act..."*

75. In this case the Respondent appears to have established a mechanism whereby a Sinking Fund contribution is demanded, year on year, subject to a small inflationary increase, so that the sums demanded over the period in question were as identified in §§55-6, above.

76. We accept that this methodology is reasonable *in principle*, but we can discern no explicable reason for the sums actually demanded, particularly in 2023-4. It is not apparent to the Tribunal that the mechanism and the specific sums have been the subject of any review or detailed consideration in recent years, most particularly for the year 2023-4 against the substantial accrued capital balance of £74,293.13 as at 31 March 2023.

77. We also take into account the Applicants' submissions as to their means, noting that such matters can be material considerations in determining whether service charges levied are reasonable, following the decisions in *Marie Garside & Michael Anson -v- RFYC Limited & B R Maunder Taylor* [2011] UKUT 367 (LC), and in *LB Hounslow v Waaler* [2017] EWCA Civ 45. While liability to pay service charges cannot be avoided simply on the grounds of hardship even if extreme, and while a lessee cannot escape liability to pay by pleading poverty if repair work is reasonably required at a particular time, we cannot conclude that it is reasonable to continue to demand slowly increasing sums without periodic detailed consideration or review, informed by a substantial capital balance that has accrued, augmented by rising interest rates, and as against the economic difficulties clearly faced by some if not all of the Applicants.

78. While clause 7(4)(b) of the lease entirely sensibly seeks to ensure that service provision (as defined) shall not fluctuate unreasonably year to year, we also note in particular the effect of clause 7(4)(c), that the

accumulations to the Sinking Fund should be reduced by any unexpended reserve already paid by lessees. This does not, we think, mean that no further demands may be made in the event that a capital balance is held, but rather serves to require moderation of future demands as against consideration what may already have been paid and retained in respect of anticipated future liabilities.

79. It is of some significance, we find, that the sums demanded by way of Sinking Fund contributions exceed all other items for which service charges are required. This appears to this Tribunal to provide an obvious imbalance, for which an explanation is warranted from the Respondent, but none has been forthcoming (besides the generalisations adverted to).

Decision

80. We hold that where, as here, the lessees challenge the reasonableness of the amount claimed, it is for the landlord to justify that it is reasonable, by producing cogent evidence to justify the nature and calculation of the sums claimed.

81. We consider the lack of detail or particularisation of the Respondent's case on this issue to be regrettable. It is most opaque how the sums claimed by way of Sinking Fund contributions have been calculated, and as discussed above, there is no evidence whatsoever to demonstrate that the sums claimed have been the subject of consideration or review, particularly against the substantial capital balance that has accrued, on the one hand, and the absence of any programme of proposed works on the other. In this regard we do note the recent decorative works at the building, but we have no details of any costings for the same.

82. In our view, the Respondent has failed to satisfy us that the contributions demanded for the Sinking Fund for the year 2023-4 are reasonable. This decision is in large part predicated upon the substantial capital balance accrued by 31 March 2023 (as stated above, and with accrued interest, £74,293.13), which, we find, substantially exceeds anything that might be anticipated to be needed to be paid for in respect of the building for the foreseeable future.

83. Doing the best we can upon the unsatisfactory evidence provided, and not without some reservations, we consider that the demands made for contributions to the Sinking Fund for the year 2022-3 were reasonable, *inter alia* serving to reach the accumulated balance as at 31/3/23 that has informed our decision. That capital balance at that date marks, however, a significant line in the sand.

84. Thereafter, we consider that the reasonable amount that the Respondent was entitled to seek from the Applicants by way of contributions to the Sinking Fund for the year 1 April 2023 to 31 March 2024, and that the

Applicants were required to pay, was one half of what was actually demanded during that period.

85. In the case of the anonymised, specimen demand at pp.84-8 of the bundle, the reasonable sums would thus be £76.56 / 2 = £38.28 per month, or £459.36 per annum. This may require slight adjustment in the case of the individual Applicants' own demands, of which we have not had sight, but our firm conclusion is that in each case the appropriate, reasonable proportion in accordance with s.19(2) is 50% of what was demanded.

86. We should stress that this is not intended to limit recovery of larger sums in future years, if the sums sought are justified, taking account of accrued capital balance in the Sinking Fund, anticipated expenditure and so on.

Management Fees

87. We have left determination of this head to the last because in our view it is properly informed by our determination on the other matters in issue.

88. The management fees for the year 2022-3 were charged in the total sum of £1,504.08, amounting to approximately £250.68 per flat, or £20.89 per flat, per month.

89. For 2023-4, the discernible management fee for one flat from the specimen demand is £23.83 per month, £285.96 per annum.

90. The Respondent's Statement of Case asserted that "*The guidance provided by home ownership is that the management charge for leaseholders is 15% of the service charge.*" Some time was spent in the hearing analysing that assertion, where as against other items in the service charge accounts the management element could (at least superficially) be discerned as exceeding 17%, or even reaching 18%.

91. The Applicants make the point that a fee of 15% is specified nowhere in the lease, and that it must be justified.

92. The Applicants also contend that there is little to manage: the building is a small, simple block, part brick and part rendered and painted, externally and in the internal common parts. Those common parts are modest in their extent, consisting of the entrance, a small hall, and staircase containing 3 lighting units.

93. Ms Denton made the point that even when refunds were made to tenants, as happened in 2021-2 and 2022-3, apparently in consequence (at least in part) of the error regarding insurance premiums, no concomitant refund was made in respect of management charges that had been levied.

94. The other, key point made by the Applicants is that they are being charged 15% for managing the sums held in the Sinking Fund, which is, they assert, demonstrably excessive for a task requiring of the Respondent next to no work whatsoever. This is particularly so, they submit, if – as we have found – the Sinking Fund was itself demanded in unreasonably excessive amounts.

95. As to the question of percentage, we accept Mr Richardson's contention that management fees are a species of service charge properly to be included within the global whole, so that the actual percentage transpires to be but a small fraction over 15% in each case. That is, we find, using our own knowledge and experience of such matters, within a reasonable range of management fees, calculated as a product of the various costs of the matters being managed.

96. We also accept Mr Richardson's point that such a reasonable percentage admits of a small margin of fluctuation, so that if individual items may transpire to have attracted a discernible management charge of, say, 17%, that too is within a reasonable range. Thus, even if we are wrong in our conclusion at §95 that management fees are properly to be included in service charge demands as an element of those service charges, we nevertheless do not find that the percentage rates applied by the Respondent for calculation of their management charges were unreasonable.

97. As to Ms Denton's point that a rate of 15% for managing the Sinking Fund was demonstrably unreasonable, we also accept Mr Richardson's submission that this is but one element of the various matters that the Respondent needs to attend to, summarised in §B(i) of Mr Duncan's statement, and as can be discerned by considering the individual service charge accounts. To paraphrase, there is something of a swings and roundabouts principle in the application of a percentage rate to the whole, where some items – e.g. the recruitment and engagement of contractors to effect works – are likely to involve far more work than others, including the management of the Sinking Fund account.

Decision

98. Having accepted that the service charges demanded for the year 2022-3 were reasonable, having accepted reasonableness of the blanket percentage method of calculating management fees, and having accepted the reasonableness of the actual percentage applied, we also conclude that the management fees charged by the Respondent for the year 2022-3 were reasonable, and were and are payable by the Applicants.

99. Conversely, having concluded that the *'swings and roundabouts'* principle summarised at §97, above, is a reasonable means of calculation of management fees, we are driven to the conclusion that an element of the management fees for the year 1 April 2023 to 31 March 2024 was

unreasonable, insofar as it related to collection and administration of 50% of the Sinking Fund contributions that we have determined were not reasonably demanded and were consequently not payable.

100. Based upon the Respondent's assertion that a blanket 15% is applied to all items of expenditure demanded, we conclude that the proper course is to reduce the management charges levied against the Sinking Fund demands by 50%.

101. While the figures are a little difficult to reconcile, particularly where we have only the one specimen demand for 2023-4, in the case of the anonymised, specimen demand at pp.84-8 of the bundle, the management charge levied at the rate of 15% would have been £76.56 x 15% = £11.48 per month, or £137.76 per annum. Having concluded that 50% of that element of the management charge was unreasonable and therefore not payable, we determine that £5.74 of the monthly management charge, or £68.88 per annum, was unreasonably demanded and is not payable by the Applicants.

102. While this might in principle require slight adjustment against small variations in relation to the individual Applicants' own demands, we consider that the exercise in seeking to differentiate the precise sums would be entirely disproportionate to the modest sums in issue, most particularly where the Tribunal does not have the specific figures before it, and we therefore decline to do so.

103. Accordingly, we determine that an element of the management fees claimed was not reasonably incurred, amounting to £68.88 per annum in respect of each of the Applicants.

104. For the avoidance of doubt, the remainder of the management fees claimed by the Respondent were reasonable, and are payable.

Applications under s.20C and paragraph 5A

105. The Applicants have applied for an order under section 20C of the 1985 Act.

106. A Section 20C application is for an order that the whole or part of the costs incurred by the Respondent in connection with these proceedings cannot be added to the service charge of the Applicants.

107. In this case the Applicants have been successful in relation to two specific issues.

108. Taking into account our determinations above, the Tribunal determines that it is just and equitable in the circumstances for an order to be made

under section 20C of the 1985 Act. The Tribunal therefore makes an order in favour of the Applicants that none of the costs incurred by the Respondent in connection with these proceedings shall be added to their service charges.

109. The Applicants have not made an application and under paragraph 5A of Schedule 11 to the Commonhold and Leasehold Reform Act 2002. We therefore make no order under that section.

Reimbursement of Tribunal Fees

110. The Applicants have also applied under paragraph 13(2) of the Tribunal Procedure (First-tier Tribunal) (Property Chamber) Rules 2013 for an order that the Respondent reimburse their application fee of £100.00 and the hearing fee of £200.00.

111. As the Applicants' claim has been successful to a considerable degree, we are satisfied that it is appropriate in the circumstances to order the Respondent to reimburse these fees.

Name: Judge Mark Jones **Date:** 11 November 2024

Rights of appeal

By rule 36(2) of the Tribunal Procedure (First-tier Tribunal) (Property Chamber) Rules 2013, the tribunal is required to notify the parties about any right of appeal they may have.

If a party wishes to appeal this decision to the Upper Tribunal (Lands Chamber), then a written application for permission must be made to the First-tier Tribunal at the regional office which has been dealing with the case.

The application for permission to appeal must arrive at the regional office within 28 days after the tribunal sends written reasons for the decision to the person making the application.

If the application is not made within the 28-day time limit, such application must include a request for an extension of time and the reason for not complying with the 28-day time limit; the tribunal will then look at such reason(s) and decide whether to allow the application for permission to appeal to proceed, despite not being within the time limit.

The application for permission to appeal must identify the decision of the tribunal to which it relates (i.e. give the date, the property and the case number), state the grounds of appeal and state the result the party making the application is seeking.

If the tribunal refuses to grant permission to appeal, a further application for permission may be made to the Upper Tribunal (Lands Chamber).