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## Disclaimer



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## Interpretation of residential leases (service charges)

Alero Orimoloye  
Leasehold Advisory Service  
12 May 2015

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### What you will learn



- The basic principles
- Construing the lease
- Implying terms
- Important case law
- Rectification

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### A lease is a contract



- Literal interpretation or
- Business common sense

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### Literal interpretation



- *“To force upon the words a meaning which they cannot fairly bear is to substitute for the bargain actually made one which the court believes could better have been made. This is an illegitimate role for the court...”*
- Charter Reinsurance & Co. Ltd (In Liquidation) v Fagan [1997] A.C.313
  - Lord Mustill

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### Business common sense



- *"If detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business common sense"*
- Antaios Compania Naviera SA v Salen Rederierna AB
  - Lord Diplock
  - [1985] AC191

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### Over-riding objective



- Give effect to what a reasonable person would have understood the parties to mean
- In spite of linguistic problems if the meaning is clear it is that meaning which must prevail
- Jumbo King Limited v Faithful Properties Ltd [1999] 3 HKLRD 757, CFA
  - Lord Hoffman

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### The Investors Compensation judgment



- Investors Compensation Scheme v West Bromwich Building Society [1998] 1 WLR 896
- Lord Hoffmann
- Five principles

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### Five principles

- Ascertainment of meaning
- Matrix of fact
- Exclusion from admissible background
- Meaning of the document
- Words given natural and ordinary meaning



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### Ascertainment of meaning

- *Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract*



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### Matrix of fact

- *The background was famously referred to by Lord Wilberforce as the “matrix of fact,” but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man*



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### Exclusion of prior negotiations



- *The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear...*

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### Meaning of the document



- *The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean*

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### Meaning of the document



- *The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax (see *Mannai Investments Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] 2 WLR 945)*

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### Natural and ordinary meaning



- The “rule” that words should be given their “natural and ordinary meaning” reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had

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### A slight qualification to these principles



- “The overriding objective in construction is to give effect to what a reasonable person rather than a pedantic lawyer would have understood the parties to mean. Therefore, if in spite of linguistic problems the meaning is clear, it is that meaning which must prevail”
- Jumbo King v Faithful Properties Limited
- per Lord Hoffman

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### Correction as a matter of construction



- Error in written contract may be corrected as matter of construction without seeking rectification order
- Two conditions
  - Clear mistake on the face of the document
  - Must be clear what correction ought to be made in order to cure the error
- Kruger Trading Ltd v Global Network Holdings Ltd [2004] EWHC 1396 (Ch)

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### Interpretation against the landlord



- Contra proferentem rule
- Doubt about meaning of a clause
- Resolved against party who put forward the clause
- Usually the landlord

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### Interpretation against the landlord



- *Gilje v Charlegrove Securities Ltd* [2011] EWCA Civ 1777
- Liability of underlessee to pay service charges in respect of rental value of flat occupied by resident caretaker employed by lessor
- Did notional rent for caretaker's flat foregone by landlord fall within expression "expended by the lessor"?

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### *Gilje v Charlegrove Securities*



- *The landlord seeks to recover money from the tenant. On ordinary principles there must be clear terms in the contractual provisions said to entitle him to do so. The lease, moreover, was drafted or proffered by the landlord. It falls to be construed contra proferentum*

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### Gilje v Charrgrove Securities



- *At the end of the day, I do not consider that a reasonable tenant or prospective tenant, reading the under-lease which was proffered to him, would perceive that paragraph 4(2)(1) obliged him to contribute to the notional cost to the landlord of providing the caretaker's flat. Such a construction has to emerge clearly and plainly from the words that are used. It does not do so*
  - (Per LJ Laws)

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### Implication of terms



- Term must be
- Reasonable
- Necessary to give business efficacy to contract
- So obvious that it goes without saying
- Capable of clear expression
- Not contradicting any express term of contract

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### Implication of terms



- Finchbourne v Rodrigues
- [1976] 3 All E R 581
- Implied term as to reasonableness

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### Ejusdem Generis rule



- General words following a list
- Interpreted so as to be limited to items with the same characteristics as those on the list
- Assethold Limited v C Bell and others
  - LON/00AY/LSC/2009/0610

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### Examples



- Management costs
- Legal costs

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### Management costs



- Embassy Court Residents Association Limited v Lipman[1984] 2 EG 545 CA
- Lloyds Bank PLC v Bowker Orford [1992] 2 EGLR 44

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### Management costs



- London Borough of Brent v Hamilton LRX/51/2005
- Norwich City Council v Marshall LRX/114/2007

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### Embassy Court Residents Association Limited v Lipman



- "...it is perfectly clear that if an individual landlord wants to [employ managing agents] and to recover the costs from the lessee, he must include explicit provision in the lease"
- Cumming-Bruce LJ

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### Embassy Court Residents Association Limited v Lipman



- ECRA was residents company established to assume freeholder's obligations
- Freeholder leased whole of EC to ECRA for 99 year term for that purpose
- ECRA had no funds

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**Embassy Court Residents Association Limited v Lipman**



- Court held term should be implied that ECRA could recover proper expenditure to carry out imposed functions
  - Business efficacy
- Expenditure includes cost of employing managing agents

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**Lloyds Bank PLC v Bowker Orford**



- Landlord relied on two provisions of service charge schedule
  - Provision that leaseholder could not object to service charge on ground that managing agents were employed "to carry out and provide on the lessor's behalf services under this Part of the Schedule"
  - Covenant by leaseholder to pay "the total cost of providing the services specified in section 2 of this Part of the Schedule"

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**Lloyds Bank PLC v Bowker Orford**



- Court held agents fees not recoverable under first provisions
- However recoverable under second provision as it included the cost of employing managing agents to organise and supervise provision of services specified in Section 2
- Limited to cost of employing agents to organise/supervise such services and did not extend to say cost of employing agents to collect rent

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*London Borough of Brent v Hamilton*



- Right to Buy lease
- Liability to pay a reasonable part of “the expenditure incurred by the Council during the Council’s financial year in fulfilling the obligations and functions set out in Clause 6 hereto”
- Upper Tribunal held that a “management fee” raised in respect of work carried out by the council in fulfilling the obligations and functions set out in Clause 6 was recoverable

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*London Borough of Brent v Hamilton*



- “To the extent that expenditure is so incurred it is recoverable, and, whether it is so incurred is a question of fact... Clause 6 includes the usual landlord’s covenants, of which the provision of services is one, and... they will require expenditure to be incurred by the council in their performance

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*London Borough of Brent v Hamilton*



- *“If repairs are to be carried out or windows painted or staircases cleaned someone will have to be paid for doing the work and someone will have to arrange for the work to be done, supervise it, check that it has been done and arrange for payment to be made*

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**London Borough of Brent v Hamilton**



- *Since the council can only act in these respects through employees or agents it will have to incur expenditure on all these tasks. If it does incur such expenditure, the lessee will be liable to pay a reasonable part of it*

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**London Borough of Brent v Hamilton**



- *"It seems improbable that a housing authority forced in 1986 to sell part of its housing stock at a substantial discount and at a nominal ground rent would have chosen to subsidise the purchasing tenant by including in the lease a provision that made her liable for part only of the council's costs in performing its covenants under the lease"*

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**Norwich City Council v Marshall**



- The costs of management reasonably incurred for the specific services which the landlord was obliged to provide under the terms of the lease were recoverable as service charges but not the costs of dealing with breaches of covenants, enforcements action, repair orders and permission applications

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### Legal costs



- Sella House Ltd v Mears [1989] 21 HLR
- St. Mary's Mansions Ltd v Limegate Investment Co Ltd [2002] EWCA Civ 1491

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### Legal costs



- Morgan v Stainer
  - [1992] 2 EG 162
- Staghold Limited v Takeda
  - [2005] 47 EG 146
- Assethold Ltd v Watts
  - [2015] UKUT 0537

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### Sella House Ltd v Mears



- Whether landlord could recover legal expenses incurred in recovering rent from other leaseholders as part of the service charge
- Service charge based on expenditure incurred by landlord in carrying out obligations

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### Sella House Ltd v Mears



- “ To employ managing agents and chartered accountants to manage the building and to discharge all proper fees and expenses payable to such agents or other person who may be managing the building including the cost of computing and collecting the rent...in respect of the building”

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### Sella House Ltd v Mears



- Fees of solicitors and counsel outside contemplation of the provisions
- Absence from those provisions of any specific mention of lawyers, proceedings or legal costs was noted
- Scope of provisions concerned with management, maintenance, safety and administration

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### Sella House Ltd v Mears



- On the landlord's argument a tenant paying his rent and service charge regularly would be liable by the service charge to subsidise the Landlord's legal costs of suing his co-tenants, if they were all defaulters. For my part I should require to see a clause in clear and unambiguous terms before being persuaded that the result was intended by the parties”

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**St Mary's Mansions Limited v Limegate Company Limited**



- *"The cost of all other services which the Lessor may at its absolute discretion provide or install... for the comfort and convenience of the lessees; (b) the reasonable and proper fees of the Lessors managing agents for the collection of rents of the flats in the said Buildings and for the general management thereof"*

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**St Mary's Mansions Limited v Limegate Company Limited**



- The Court of Appeal held that such provision did not permit recovery of:
  - proceedings to recover service charges
  - proceedings to recover ground rent, and
  - obtaining general legal advice in relation to obligation under the leases

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**Morgan v Stainer**



- Leaseholders required to contribute to specified sum for carrying out maintenance
- Under lease obliged to "pay all legal and other costs that may be incurred by the landlord in obtaining the payment of the maintenance contribution from any tenant of the building"

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*Morgan v Stainer*



- Leaseholders had issued proceedings against landlord on related matter
- Settled on terms including that landlord pay leaseholders' costs
- Landlord sought to recover cost incurred in relation to the proceedings under service charge clause

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*Morgan v Stainer*



- Court held costs were not costs incurred in obtaining the payment of the maintenance contribution
- Costs incurred in resisting the leaseholders' proceedings
- Agreement reached was also clear that landlord to pay leaseholders' costs and could not then be liable to pay in another way

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*Staghold Ltd v Takeda*



- Service charge included proportion of landlord's expenses incurred in "providing the several services and amenities specified in the seventh schedule hereto"
- List included costs of employing legal professional advisers concerning such matters as "the collection of rents" and carrying out of "the landlord's rights and obligations"

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### Staghold Ltd v Takeda



- Service charges included landlord's costs of defending proceedings brought by tenants in Leasehold Valuation Tribunal challenging amount of service charges
- Proceedings successfully defended by landlord
- Court decided landlord entitled to recover its costs of LVT proceedings through the service charge provisions

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### Assethold Limited v Watts (Upper Tribunal)



- Appeal against a decision of the LVT made on 21 January 2013
- LVT decided that landlord not entitled to recover costs of employing solicitors and counsel in a boundary dispute per lease terms

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### Assethold Limited v Watts (Upper Tribunal)



- Question for the Upper Tribunal was recoverability of legal costs in accordance with lease terms?
- Para 6 of First Schedule
  - "To do or cause to be done all works installations acts matters and things as in the reasonable discretion of the Landlord may be considered necessary or desirable for the proper maintenance safety amenity and administration of the Development"

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### Assethold Limited v Watts (Upper Tribunal)



- Upper Tribunal considered proper approach to construction of service charge provisions
- Relied on Court of Appeal decisions in Arnold v Britton and Francis v Phillips
  - There are no special rules of construction for service charge provisions

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### Assethold Limited v Watts (Upper Tribunal)



- Davis LJ in the Court of Appeal decision of Arnold v Britton agreed with Morgan J's approach in the High Court
  - "That a service charge clause in a lease is not subject to any special principle... but ultimately it all depends on the meaning of the language, set in context and having regard to the commercial purpose..."

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### Assethold Limited v Watts (Upper Tribunal)



- Satisfied that the language of para 6, though general, is sufficiently clear to entitle appellant to recoup through the service charge costs of engaging solicitors to take steps to ensure the protection afforded by a Party Wall Act award would not be lost
- Those steps can be described as having been taken for the proper maintenance, safety, amenity and administration of the building

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*Arnold v Britton*



- EWCA Civ 902
- Court of Appeal judgment dated 22 July 2013
- Long leaseholders of 91 holiday chalets
- Oxwich leisure park near Swansea

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*Arnold v Britton*



- Fixed service charge clause
- Annual service charge of £90 pa for first three years of 99 year term **plus**
- Ten pounds per hundred for every subsequent year thereafter
- 1975 - RPI was 16%
- Projected annual service charge in last year of 99 year term - **£1,025,004.00**

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*Arnold v Britton*



- Court of Appeal held that cannot introduce new or other terms to repair a "bad bargain"
- Section 18 of LTA 1985 did not apply

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**Arnold v Britton**



- *“As Morgan J put it in his judgment at paragraph 43: I do not see why a service charge clause in a lease should be subject to a special principle... I consider that what is required is that the court must examine the wording of the charging provision. In its context and against all the admissible background and in the light of the apparent commercial purpose of the clause and then decide what the provision means and how it operates”. I agree with that statement”*

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**Arnold v Britton**



- Permission to appeal to the Supreme Court granted
- Awaiting Supreme Court judgement
- Lord Justices Neuberger, Carnwath and Toulson

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**Rectification - four conditions**



- Parties had a continuing common intention, whether or not amounting to an agreement, in respect of a particular matter in the instrument to be rectified
- Outwards expression of accord
- Intention continued at the time of execution of the instrument sought to be rectified
- By mistake the instrument did not reflect that common intention
- Swainland Builders Ltd Freehold Properties Ltd [2002] 2 EGLR 71

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## Questions?

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## Upcoming LEASE courses

<b>13 May 2015 – London</b> <b>20 May 2015 – Manchester</b>	<b>23 June 2015</b>
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<b>Classroom training</b> <b>Service charges</b> <ul style="list-style-type: none"><li>• What is a lease?</li><li>• What is a service charge?</li><li>• Contents of the demand</li><li>• Timing the demand</li><li>• Recovery of service charges</li><li>• Section 20 consultation, including dispensation</li><li>• First-tier Tribunal (Property Chamber) procedure</li></ul>	<b>Webinar</b> <b>Introduction to lease extensions for flats</b> <ul style="list-style-type: none"><li>• Advice on entitlement to a lease extension</li><li>• Draft and serve the initial notice</li><li>• Anticipate opposition</li><li>• Argue which new terms can be inserted into the extended lease</li><li>• Deal with the conveyancing procedure</li></ul>
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