

**Daejan Investments –v- Benson (28/1/2011)- failure to consult over service charges leaves landlord substantially out of pocket.**

**The Message:** Landlords may not recover service charges for major works if they fail to consult properly with tenants.

**The Case:** The Court of Appeal has held that landlords may suffer severe financial consequences if they undertake major works to residential properties without first complying with the statutory consultation procedure. The Landlord and Tenant Act 1985 provides substantial protection for residential tenants who are liable to pay service charges to their landlords for the costs of running and repairing their buildings. Such service charges have to be reasonable in amount and any works have to be undertaken to a reasonable standard.

There is also a detailed consultation procedure that has to be followed where works are proposed which will result in any tenant having to contribute more than £250. A landlord who fails to follow this procedure cannot recover more than this amount from each tenant unless it obtains retrospective dispensation from the Leasehold Valuation Tribunal to do so. The consultation requirements are intended to ensure a degree of transparency and accountability and to permit tenants to participate in determining the works to be undertaken and who they are undertaken by.

Daejan is the landlord of a block of flats called Queens Mansions in Muswell Hill, London. Of the 7 flats in the block, 5 contribute to the maintenance costs by way of service charges. As Daejan had materially failed to comply with the consultation requirements, the tenants of these 5 flats challenged their liability to contribute more than £250 each to the total costs of £270,000 incurred on major works.

The consultation process involves 2 stages. The first stage involves serving notice on the tenants of the nature of the proposed works and the reasons for them so the tenants can make any observations and nominate contractors from whom estimates should be sought. The second stage involves providing details of estimates obtained and observations received on the proposed works and the landlord's responses thereto. The landlord has to allow the tenants 30 days to inspect and comment upon the estimates before a contractor is selected. The landlord must then have regard to the tenant's further observations before choosing the contractor.

In relation to the second stage, Daejan failed to comply with the consultation requirements in a number of respects. It did not detail the observations received in response to the first stage and its answers thereto. More importantly, it only made the estimate it preferred available for inspection and it made a decision in relation to select this contractor before the consultation period had ended, thereby making futile any further representations by the tenants. However, the 2 most competitive estimates were about the same level and Daejan did select one of these.

Both the Leasehold Valuation Tribunal and then the Upper Tribunal held that Daejan's failures were so serious that dispensation would not be granted, even though Daejan offered a discount of £50,000. Daejan appealed further to the Court of Appeal on the basis that the punishment did not fit the crime. It argued that the tenants had suffered no real prejudice and that it was totally disproportionate to only allow it to recover £1,250 out of the £270,000.

Daejan argued that the financial consequences for the landlord should be taken into account when deciding whether to grant dispensation. It pointed out that dispensation was wholly discretionary and could be granted even where the landlord had acted unreasonably. However, the Court considered the financial consequences to be irrelevant. It noted that the legislation was focused on compliance with the procedure and not on granting relief from the consequences of non-compliance. Dispensation was not to be readily granted and would generally be restricted to minor breaches or emergency situations or works where only one specialist contractor could have undertaken them.

The Court then considered whether the nature of the landlord should affect the approach to granting dispensation? Daejan had argued that it was being treated more severely as it was a corporate landlord. The Court did not consider that a more rigorous approach had been taken although it indicated that a more lenient approach may be taken to tenant owned landlords who are, in effect, spending their own money.

Finally, the Court considered whether the tenants had actually suffered any prejudice? It accepted that the extent of any prejudice suffered was of the first importance in deciding whether to grant dispensation. Daejan argued with some force that the result would have been no different if there had been complete compliance but the Court took a very serious view of the premature curtailment of the consultation. It felt the whole procedure would be undermined and made far more complicated if landlords could readily argue that further consultation would have made no difference.

Accordingly, the Court held that Daejan could not recover anything more than £250 from each tenant. Clearly, landlords need to be aware that the integrity of the consultation procedure is sacrosanct and dispensation will only be granted where there is a good excuse for failing to follow it.