Case Commentary

The Meaning of Qualifying Works—The Sets Approach

Francis v Philips [2014] EWCA Civ 1395

Holiday accommodation; Landlords' duties; Management; Service charges

This is an important case on the meaning of "qualifying works" in s.20 and s.20ZA of the Landlord and Tenant Act 1985. The case decides that the "aggregating approach" preferred by the High Court ([2012] EWHC 3650 (Ch D)) is wrong. The correct approach is to identify whether works are part of a set of works. The lessee's service charge contribution towards a set of qualifying works is capped at £250 unless the consultation requirements have been complied with in respect of that set of qualifying works.

Introduction

The right to recover, and the requirement to pay, a service charge is governed by the terms of the lease, subject to ss.18–30 of the Landlord and Tenant Act 1985 (the Act), and the Service Charges (Consultation Requirements) (England) Regulations 2003 (the Regulations).

Under s.20 of the Act, there is a statutory maximum that the leaseholder has to pay by way of a contribution to "qualifying works" or a "qualifying long term agreement" (QLTA) unless consultation requirements have either been complied with or dispensed with by, or on appeal from, an LVT. Under s.20ZA(2) of the Act, "qualifying works" means works on a building or any other premises.

Under the Regulations, s.20 of the Act applies to qualifying works when the relevant costs incurred on carrying out the works exceed an amount which results in the service charge contribution by any tenant to the cost of the works being more than £250, and applies to QLTAs when the relevant costs incurred under the agreement in a 12 month period exceed an amount which results in the service charge contribution of any tenant, in respect of that period, being more than £100. Unless the consultation requirements have either been complied with or dispensed with, the statutory maximum the landlord can recover in respect of relevant costs is limited to these amounts.

In *Philips v Francis* [2012] EWHC 3650 (ChD); [2013] 1 W.L.R. 2343, the Chancellor held that the common approach of considering whether a particular *set of works* are "qualifying works" was wrong. The decision was deeply unpopular with those working in the property management industry and severely criticised as being unworkable in practice. The Secretary of State for Communities and Local Government intervened in the appeal because the point raised a question of statutory construction of public importance with the potential to affect a large number of residential landlords and tenants throughout the country. The Court of Appeal ([2014] EWCA Civ 1395) reversed the Chancellor's decision on this issue. (The Chancellor's decision on the proper construction of the lease was upheld, albeit for different reasons, but that issue is not of general importance and will not be discussed in this commentary).

Facts

The case relates to long leases of chalets on a holiday site. The chalets were held to be dwellings within the meaning of s.38 of the Act, so that ss.18–30 applied. The freehold of the holiday site was purchased by the defendants (the lessors). In a letter sent to all lessees in May 2008, the lessors indicated their intention to bring the site up to a first class standard and proceeded to carry out works without consulting in accordance with the Regulations. The lessees welcomed the plans for improvement, but not the increase in service charge liability and sought declarations as to the true construction of the leases and injunctions preventing forfeiture.

At first instance, one of the issues was which items of expenditure amounted individually or collectively as "qualifying works" for the purposes of s.20 and s.20ZA of the 1985 Act. The trial judge applied the three stage test derived from the judgment of Walker LJ in *Martin v Maryland Estates* [1999] L. & T.R. 541; [1999] 2 E.G.L.R. 53, namely:

(1) which of the works fell within the definition of "qualifying works" contained in s.20ZA(2)?
(2) Did those works constitute one or more "sets of qualifying works"?
(3) Did any of those sets fall below the triviality threshold set by the limit on the cost of those works?

This has become known as the "sets approach". The trial judge rejected the lessees' submission that that the works were one scheme planned in advance, instead finding that there were many disparate pieces of work. As such, no consultation was required.

On appeal to the High Court, the appellant lessees argued that the judge was wrong not to recognise all the qualifying works as being a single set originally designed by the lessors, as stated in the May 2008 letter to lessees. Those works generated individual service charges for lessees greatly in excess of the limit prescribed by the Regulations and, as there had been no compliance with the consultation requirements, the excess over £250 was irrecoverable.

The lessors submitted that the mechanics for consultation set out in Pt 2 of Sch.4 to the Regulations necessarily required a pre-defined set of works. Counsel contended that whether there were one or more sets of qualifying works was a question of fact in respect of which the trial judge was in the best position to judge, having had the benefit of a site visit.

The Chancellor (Sir Andrew Morritt) held that the "sets approach" was wrong. There is no "triviality threshold" in relation to qualifying works: *all works* that are "qualifying works" should be brought into the account for computing the lessee's contribution. In other words, once the limit for contributions has been reached (£250 per tenant), the landlord must consult the tenants on any service charge items, however small they may be. This became known as the "aggregating approach". The decision was curious given that neither party argued that a landlord was required to consult on a distinct set of qualifying works if a lessee's contribution to the cost of those particular works would not exceed £250: the lessees' case was that the qualifying works were all part of the same set of works.

It was widely recognised that the "aggregating approach" was not sensible and gave rise to serious practical problems. It is instructive to compare the different approaches using a worked example.

The different approaches: an example

Imagine a residential block of flats with four tenants: the annual regulatory limit is 4 x £250: £1000. Three lots of minor works on a building each costing £75 are carried out in the first half

of the year. The landlord has spent £225 on service charge items. There has been no consultation. Unexpectedly, in September the outer door of the block breaks and a new door frame is required which would cost £800. A storm in November causes window damage that would cost £400 to repair.

Applying the "sets approach", the landlord would not need to consult on any of these items. They are all distinct sets of qualifying works none of which costs more than £1,000. The landlord could respond immediately and repair the damage to the door and the window. The tenants are still protected because they have the after-the-event protection afforded by s.19 of the 1985 Act that the costs are only relevant costs to the extent that they are reasonably incurred and of a reasonable standard.

By contrast, applying the "aggregating approach", the annual limit is exceeded by the broken door. The landlord is obliged to consult on it. This process takes time and costs money. If instead he replaces the door immediately, he has no right to recover the full amount without dispensation. Seeking dispensation has attendant legal and administrative costs as well as the risk of non-recovery and delay. But if he does not replace the door, the flats are unsafe and he is likely to have irate tenants.

The Court of Appeal's decision

Allowing the landlord's appeal (in part), the Court of Appeal held that the consultation requirements place significant administrative burdens on the landlord: if this were required for every piece of minor repair work that a landlord wished to carry out over a year, it was likely that there would have to be perpetual consultation. To apply the landlord's obligation to have regard to the observations of the tenants in each consultation to every item of maintenance and repair would, in many cases, be unworkable. It would increase costs for landlords and, if recoverable under the terms of the lease, the tenants would have to pay for the protection of consultation even on minor matters. This cannot have been Parliament's intention. Accordingly, the trial judge was correct to apply the sets approach and entitled to find that the work planned and carried out until 2009 was not all part of a single set of works.

Identifying a set of works

It is a question of fact and degree whether the work carried out is all part of one planned single set of works or a series of disparate pieces of work. In most cases, it should be obvious whether works comprise one or more sets but relevant factors are likely to include:

(1) where the items of work are to be carried out (whether they are contiguous to or physically far removed from each other);
(2) whether they are the subject of the same contract;
(3) whether they are to be done at more or less the same time or at different times;
(4) whether the items of work are different in character from, or have no connection with, each other.

What are "qualifying works"?

In *Paddington Walk Management Ltd v Peabody Trust* [2010] L. & T.R. 6, Judge Marshall QC considered whether window cleaning was "qualifying works". At [90], she said:

> "'Qualifying works' means, 'works on a building or any other premises'. That is not a very illuminating definition. [Counsel for L] reminds me of the history where, of course, the Act originally provided protection in relation to works on a building. She says that window cleaning is not 'works on a building' or 'building works' because it falls more naturally in the category of 'services'. By definition, it is 'cleaning', which itself is part of 'services' and not 'works' … [Counsel for T] says it is 'works' and it is works being done 'on a building'. Window cleaning is not that different from stone cleaning, which itself is not that different from maintenance work on stone surfaces. There is really no ground for distinguishing any form of such works that are being done, and window cleaning works, therefore, fall within the definition."

The learned judge concluded, at [92]:

> "It is again a short point and a matter of impression. I prefer [Counsel for L's] argument. Window cleaning may be 'work' and even 'work on a building' but it is not, in my judgment, 'works on a building'. Works on a building comprise matters that one would naturally regard as being 'building works' and it does not seem to me that window cleaning naturally falls within that concept."

In *Philips v Francis*, having referred to *Paddington*, the trial judge said at [341]:

> "a commonsense approach to construction needs to be taken and in view of the fact that it acts as a trigger for the protection afforded by consultation. If the threshold were too low and all minor or on non permanent works covered the result would be commercially unmanageable to the detriment of both lessor and lessee. The phrase building works is used to describe significant works with a permanent effect by way of modification of what there was before. Whether works are indeed qualifying works, is a question of fact having regard to the nature and extent of the works in question."

The writer's case commentary on the Chancellor's decision in an earlier issue of the *Review* (see, (2013) 17 L. & T. Rev. 60) criticised this interpretation of building works: there is no basis for requiring work to be "significant", "permanent" and "modify" what was there before and such a test is an illegitimate gloss upon s.20ZA(2). The Court of Appeal agreed. It held that qualifying works will often be significant or substantial as opposed to minor and insignificant, but it is not necessary to have a permanent effect modifying what was there before. For example, a substantial programme of redecoration or repair would not have a permanent effect modifying what was there before but such a programme would still be qualifying works.

Commentary

This decision restores the law to as it was understood in December 2012. It will be an enormous relief to landlords and managing agents who did not know on which works they should consult tenants. It should also come as a relief to tenants. Sensible tenants do not want to be bombarded with notices asking for their views on small items of expenditure and they do not want to pay the landlord's costs of complying with the consultation requirements. In future, the consultation requirements will only apply to individual sets of works.

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