The marmalade sandwiches of Michael Bond’s bear and the electronic cool of the Pet Shop Boys’ 1986 hit spring irrepressibly to mind here.

The issue in this case however is neither literary nor musical: it is the liability of the lessees of flats in one part of the Paddington Basin development in London to pay service charges in respect of costs incurred in respect of the whole.

The legal value in the case is HHJ Karen Walden Smith’s review of the principles of interpreting contracts. For those inclined to curiosity about the running of one of London’s largest redevelopments of recent years, there is factual value in the lengthy history of ownership and management interests which precedes the legal argument.

The judgment runs to some twenty dense pages. I have condensed it as best I can without losing too much of the detail.
The Factual Background

Interests in Paddington Basin

On 05 December 1995, the British Waterways Board granted a lease of the Paddington Basin site to Paddington Basin Developments Limited (“PBDL”) for a term of 999 years from 25 March 1995.

On 02 August 1996, European Land and Property Developments Plc (“EL&PD”), which was the beneficial owner of PBDL’s lease, agreed to PBDL assigning part of the site to Frogmore Developments Limited. I will refer to this agreement as the “1996 agreement”.

Clause 13 of that agreement included:

- A promise by PBDL to put in place “detailed arrangements for the repair maintenance and renewal of all … common areas” of the development, and
- Provisions for an estate service charge scheme under which a future management company would be granted leases of the common areas of the development. In the event this scheme was never implemented.

The land to be assigned is known in the appeal as the West End Quay Land. The land retained by PBDL/EL&PD is known as the Retained Land. Hold on to these definitions: they are at the heart of this appeal.

On 24 December 1996, PBDL and EL&PD entered into an agreement for the purpose of transferring all of the former’s trade and undertakings to the latter.

On 29 December 1997:

- The West End Quay Land was assigned to Frogmore Developments Limited, and
- A deed of apportionment and variation was entered into. It apportioned the rent covenants and other provisions of PBDL’s lease 80/20 between the retained land and the West End Quay Land.

On 04 May 2000, Frogmore Developments assigned the West End Quay Land to West End Quay Limited.

The grant of the underleases

Between 2002 and 2004, West End Quay Limited granted underleases of all the flats for a term of 990 years commencing on 1 January 2001. Mr Gritz’s underlease was granted on 02 October 2002.

At the date of the appeal, West End Quay Limited had dropped out of the picture, having (I assume) assigned their lease of the West End Quay Land to Freehold Managers (Nominees) Ltd.
Management

On 04 January 2001, Paddington Basin Management Limited (“PBML”), was incorporated. Its objects were to carry on the business of the management company responsible for the maintenance and management of the Paddington Basin Estate. I imagine that this was in order to implement the estate service charge scheme envisaged in the 1996 agreement.

On 28 January 2002, WEQEM was incorporated. The sole subscriber to WEQEM was West End Quay Limited.

WEQEM’s objects were: “To undertake the management and administration of the communal parts including car parking of a development known as West End Quay, Paddington, London W2 the leasehold title to which is currently registered at HM Land Registry under Title No. NGL758149 and to provide such services for the owners and occupants thereof and to carry out such reconstruction, renewal, repairs, maintenance or renovations thereto ...” Only the West End Quay Land was registered under that title number.

On 05 September 2005, under an Estate Management Deed (“the EMD”) PBDL, EP&PD and WEQEM appointed PBML to provide estate services to the whole Paddington Basin Estate. WEQEM covenanted to pay a fair proportion of the cost incurred by PBML in providing those services.

On 04 November 2005, the lessees took control of WEQEM.

WEQEM paid the first two service charge demands made by PBML (29 September and 25 December 2005 quarters) under the EMD without demur. From March 2006 however, it challenged the extent of its liability.

Geography of the West End Quay Land

The West End Quay Land comprised 467 flats together with approximately 10 commercial units, divided into three blocks being block A (Westcliff Apartments), block B (Peninsular Apartments) and block C (Balmoral Apartments).

The underleases

The underleases of flats on the West End Quay Land, granted by Frogmore Developments, contained the following provisions:

The Estate was defined as “all that leasehold land and buildings to be erected thereon shown...and known as West End Quay Praed Street and South Wharf Road Paddington London W2 as registered at HM Land Registry under title number NGL758149 ...” Remember, only the West End Quay Land was registered under that title number.

The Estate Common Parts were defined as “all parts of the Estate available for the common use of the owners residents or occupiers of the apartment blocks within the Estate, but shall not include the Apartment Block nor the other two apartment blocks within the Estate nor the Parking Area.”
By clause E3 the underlessee covenanted to pay: “to the Estate Management Company a service charge (“the Estate Service Charge”) being [a] proportion … of all amounts sums costs expenses and outgoings … expended or incurred … by the relevant Management Company in relation to the Apartment Block and the Estate such service charges to be payable in accordance with the provisions of Clause … J”.

Clause J, which was critical from the Appellants’ point of view, provided:

“It is agreed and declared that there shall be included in the Service Charges

4. Any payments to be made by the Landlord and/or by the relevant Management Company to the Superior Landlords and/or to the company authority or body which manages and maintains the whole area known as the Paddington Basin of which the Estate forms part whether under the provisions in the Headlease or otherwise including the maintenance of the Basin as set out in the Headlease.”

**The High Court proceedings**

The Paddington Basin development has already been the subject of High Court proceedings. In Paddington Basin Developments Ltd v West End Quay Ltd [2010] 1 WLR 2735, Lewison J (as he then was) held that the EMD was a Qualifying Long Term Agreement for the purposes of the Service Charges (Consultation Requirements) (England) Regulations 2003.

**Proceedings before the Leasehold Valuation Tribunal**

In 2008, Mr Gritz, one of the underlessees, applied to the LVT for a determination of the liability to pay the service charge pursuant to the terms of the EMD. His flat was located in a block on the West End Quay Land.

At a hearing of preliminary issues, the LVT was asked to determine whether the provisions of Mr Gritz’s underlease required him to contribute to the costs of maintaining the Retained Land.

The LVT determined, at paragraph 40 of its Decision, that“… there is no provision in the underleases that would oblige the lessees to make contributions towards WEQEM’s liability under the Sept 2005 Estate Management Deed.”

**The application for permission to appeal**

The appellants applied to the LVT for permission to appeal, and included the ground that paragraph 40 of the Decision effectively meant that the underlessees had no liability for pay any service charge, whether in relation to the West End Quay Land or the Retained Land. This was a “question which … formed no part of the pleaded case of the Applicant nor was it a question upon which the Tribunal heard argument”.

© Amanda Gourlay, 2013. Not to be reproduced without the author’s written permission.
The LVT:

- Refused permission to appeal;
- Accepted that paragraph 40 of its Decision may have been misleading, but
- Asserted that its decision was actually contained in paragraph 21: “… the provisions of the Applicant’s underlease dated 2 October 2002 do not entitle [WEQEM] to recover the costs of maintaining the land and premises which were the retained land under the Assignment of Part dated 29 December 1997 …”.

A Correction Certificate was issued.

The application for permission to appeal was renewed to the Lands Chamber on the ground that the LVT erred in concluding that the underleases did not entitle WEQEM to recover the costs of maintaining the retained land. The LVT’s conclusion, the offending paragraph 40 having been removed, was unjustifiable.

Permission to appeal was granted. The appeal was to be by way of review. Therefore the only evidence that could be considered on appeal was the evidence that had been presented to the LVT.

The Law: construing a contract

The parties are agreed that the starting point in construing documents was the speech of Lord Hoffman in Investment Compensation Scheme Limited v West Bromwich Building Society [1998] 1 WLR 896 pp 912H-913E.

In Rainy Sky SA v Kookmin Bank [2011] 1 WLR 2900, Lord Clarke said (at paragraph 21):

“The language used by the parties will often have more than one potential meaning. I would accept the submission made on behalf of the appellants that the exercise of construction is essentially one unitary exercise in which the court must consider the language used and ascertain what a reasonable person, that is a person who has 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, would have understood the parties to have meant. In doing so, the court must have regard to all the relevant surrounding circumstances. If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other.”

The appellants also relied upon the decision of Munby LJ in Universities Superannuation Scheme Limited v Marks and Spencer [1999] 1 EGLR 13, 14M:

“The purpose of the service charge provisions is relevant to their meaning and effect. So far as the scheme, context and language of those provisions allows, the service charge provisions should be given an effect that fulfils rather than defeats their evident purpose. The service charge provisions have a clear purpose: the landlord that reasonably incurs liability for expenditure in maintaining (the premises) for the benefit of all its tenants there should be entitled to recover the full costs of doing so from those tenants and each tenant should reimburse the landlord a proper proportion of those service charges.”
The Respondents relied on *Earl Cadogan and Anr v 27/29 Sloane Gardens Ltd & Anr* [2006] 2 EGLR 89. In that case, HHJ Michael Rich QC sitting in the Lands Tribunal, held that it is for the landlord to show that a reasonable tenant would perceive that the underlease obliged it to make the payment sought; such a conclusion must emerge clearly and plainly from the words used.

The Respondents therefore relied upon Earl Cadogan as supporting the basic proposition that in order to establish liability the landlord must discharge the onus upon it that the words used in the lease clearly and plainly establish that liability.

*Gilje & Ors v Charlgrove Securities Ltd* [2002] 1 EGLR 41, provided further authority that there must be clear terms to create a contractual liability. Laws LJ said that on ordinary principles when a landlord seeks to recover money from the tenant “there must be clear terms in the contractual provisions said to entitle him to do so…”

The Respondents also referred to Lewison LJ in *Cherry Tree Investments Ltd v Landmain Ltd* [2012] EWCA Civ 736 in which, at para 124, he made the distinction between “the use of background material in the interpretation of what I might call “ordinary” commercial contracts on the one hand, and the interpretation of negotiable and registrable contract or public documents on the other.”

In other words, when there are contracts which can be registered, for example at HM Land Registry, documentation which is a matter of registered record will form part of the background material.

**The Appeal**

At the appeal hearing, the appellants were represented by Katharine Holland QC and the first respondent was represented by Mr Daniel Dovar. The second respondent was represented by Mr James Fieldsend and the fourth to eighth respondents, some of the long leasehold owners of the flats in the West End Quay Land, were represented by the fourth respondent, Mr D Mosselson.

Freehold Managers (Nominees) Limited took no part in the proceedings.

**The Appellants’ arguments**

In (highly truncated) summary, the appellants argued that

- The EMD was entered into by the second respondent (WEQEM) in a deal which delegated most of their functions: it was a cost sharing exercise with one body dealing with all the maintenance.
- Clause J4 was worded deliberately widely as at the time the underleases were entered into there was no final conclusion as to how the maintenance of the Paddington Basin Estate was to be dealt with.
- The words “any payments to be made” and the phrase “or otherwise” give this clause exceptional breadth.
Clause J4 was sufficiently broad to allow the appellants to recover the works carried out in accordance with the EMD and as the management company had no assets other than the management fund, the tribunal should interpret the service charge clause on the basis of full recoupment of the cost of those services which the company is obliged or entitled to provide.

The words of clause J4 were absolutely clear and allowed that the recoverable service charge may include payments made in respect of the maintenance of the whole of the Paddington Basin Estate including West End Quay. Therefore, the service charge included payments for the maintenance of the retained land.

In the context of the totality of the documentation, the underlessees would have anticipated and understood that they would be paying for the whole of the Paddington Basin.

Were the Respondents arguing new points?

The Appellants also argued that, once the LVT had removed paragraph 40 from its decision, its decision could not be justified.

If that was correct, the respondents could not seek to have the decision of the LVT justified on alternative grounds because there was no cross appeal setting out that the Decision of the LVT should be upheld but on different grounds. In other words, the Respondents could not rely on the new arguments that they put before the Lands Chamber.

HHJ Walden Smith was not keen on this submission. She accepted that the only evidence that can be considered on an appeal by review is evidence that was presented to the lower tribunal and the arguments put before the LVT.

However:

- The further directions for the appeal, including directions for further disclosure, were given in May 2012;
- By section 175 of the Commonhold and Leasehold Reform Act 2002, the Lands Chamber may exercise any power available to the LVT, and
- The duty of the Lands Chamber on appeal is to construe the provisions for service charge in the underlease, particularly clause J4, in light of all the evidence and arguments that were before the LVT.

HHJ Walden Smith considered the effect of the Appellants’ argument. It was unpalatable: it meant that if the Lands Chamber agreed with the LVT’s decision, but determined that there had been a mistake in the LVT’s reasoning, it could not uphold the LVT’s decision, even though it was in agreement with it, because the Respondent to the appeal had not cross-appealed and introduced correct reasoning.

Rather pithily, she added: “The appellants know well the arguments that the respondents raised in seeking to support the LVT’s decision and it would plainly be wrong for the Tribunal to be bound to accept a construction that they did not agree with because the LVT had come to the right construction but expressing it for the wrong reasons”.

© Amanda Gourlay, 2013. Not to be reproduced without the author’s written permission.
The Respondents’ arguments

The Respondents submitted that the LVT was correct in its construction of clause J4:

- The EMD was not entered into as part of the overall plan for the provision of services. WEQEM entered into the EMD in order to obtain rights of way over an adjacent road for access/egress to commercial units on the West End Quay land. This was supported by correspondence exchanged in the lead up to the execution of the EMD.
- Clause J4 does not extend to the retained land. There was nothing in the lease or headlease which would have alerted the tenant to the argument that they would have to contribute towards costs incurred with respect to work and services carried out on and for the retained land.
- The clause has to be read in the context of the entirety of the underlease and that, further, the relevant documents that properly form the factual matrix do not extend the obligation of the lessees to pay for the retained land in addition to the estate.
- The second respondent further contends that the appellants cannot make a connection between the Sale Agreement and the EMD: as Lewison J stated in the High Court proceedings: “Entry into the estate management agreement was not, I think, a necessary consequence of the development of the overall estate.”

Conclusion

HHJ Walden Smith asked herself what the parties, given the words used in clause J4, reasonably understood those words to mean.

Payment of the service charge demands

The fact that the first payments were made without argument did not alter the way in which the lease ought to be construed as they could not form part of the matrix of fact.

Background knowledge which would have reasonably been available to the parties

The background knowledge reasonably available to the lessee when entering into the lease would have been limited.

Information on the Register

The lessees would be taken to know what was registered at HM Land Registry. In June 2000, a title note was registered. It referred to:

- The headlease;
- The deed of apportionment and variation dated 29 December 1997, and
- The assignment of part and to other documents.

No reference was made to the 1996 agreement. HHJ Walden Smith therefore concluded that it did not form part of the matrix of fact as it would not have been a document that would have been “reasonably available to the parties”.

© Amanda Gourlay, 2013. Not to be reproduced without the author’s written permission.
Further, the EMD was not a necessary consequence of the development. The tenant would not have been aware, when entering into the underlease, that there would in the future be a document such as the EMD.

**Terms of the underleases**

WEQEM covenanted to provide the services set out in Part I of the Fifth Schedule, namely services to the Estate.

The Estate was defined as the West End Quay Land. Any doubt as to the meaning of Estate was dispelled by the reference to the land as being that which was registered under title number NGL758149.

By clause E3 the tenant covenanted to pay to the Block Management Company a block service charge and to the Estate Management Company an estate service charge.

The service charges were payable by the lessees “in accordance with … Clauses I and J”.

So, reasoned HHJ Walden Smith, clause J4 must be read in the context of it being for services provided to the Estate under the Fifth Schedule. That Schedule contained no requirement for services to be provided to the Retained Land.

Clause J4, which set out the matters to be included in the service charge, did not extend the services to be provided and the services for which the tenants are liable to pay. The reference to “the Basin” in clause J4 went no further, in her judgment, than ensuring that the matters in the headlease were covered.

In HHJ Walden Smith’s judgment, the reference in clause J4 to “the company authority or body which manages and maintains the whole area known as the Paddington Basin of which the Estate forms part” is not identifying the area for which a service charge is to be paid but the body to which payment is to be made.

The words “or otherwise” in clause J4 allowed for a wide interpretation and thereby included the possibility of payments that may be made pursuant to an unspecified document other than the headlease. However, it was not to be interpreted to widen the obligations to be undertaken to provide services to include services provided for the retained land.

The wording of clause J4, given its “natural and ordinary meaning”, was too generalised. A reasonable person having all the background knowledge which would have reasonably been available to the parties in the situation in which they were at the time of the contracts would not have recognised that the underlease obliged them to make a contribution to works and services provided on the retained land pursuant to an agreement not yet entered into.

It was not therefore to be construed that services were to be provided and paid for in respect of both the retained land as well as the West End Quay land.

The appeal was dismissed.
Observations

The facts in this case – and the sheer number of parties, many with very similar names – made this one of the most challenging cases I have tackled on this blog. In the end I was reduced to drawing a diagram in order to keep a handle on the various interests at play.

By contrast, the law applied by HHJ Walden Smith is clear.

*Cherry Tree Investments Ltd v Landmain Ltd* [2012] EWCA Civ 736 is a useful addition to my file of case law on contractual interpretation.

The *Universities Superannuation Scheme* case is often relied upon by parties who have not conducted themselves as the terms of the lease require.

It allows the wayward party to argue that whilst it may not be able to squeeze itself into the lease and fasten all of the buttons, its actions have been compliant with the overall spirit of the agreement, so that no sanction should follow from what is really little more than a technical breach.

It is not always a very appealing argument, as is illustrated by the Upper Tribunal’s decision in *LB Southwark v Woelke* [2013] UKUT 0349(LC) (coming soon).