Does the *Building Safety Act 2022* remove the value of building warranties?

Pauline Lam and **Mark Fletcher** of **Russell-Cooke LLP** and **Aaron Walder** of **Landmark Chambers** ask whether the *Building Safety Act* is in need of reform following a First-tier Tribunal decision that could give insurers opportunities to avoid liability for remediation works under new build warranties.

KEY POINTS

- Does a recent First-tier Tribunal decision create opportunities for insurers to avoid their liability under new build warranties in respect of fire safety remediation works?
- The case of ***The Central, 163-65 Iverson Road***, has highlighted some unintended consequences of *Building Safety Act 2022*
- A Remediation Order was granted against the landlord despite the insurer previously agreeing to fund remediation works under new build warranties
- Landlords and developers may face risks where warranty claims were raised with insurers before the implementation of the *BSA*
- Potential reform of *BSA* is required to address the issue of insurer's liability under new build warranties.

The *Building Safety Act 2022* (*"BSA"*) was passed in 2022 to address a number of issues arising from the tragic Grenfell Tower Fire and the discovery of many years of questionable construction practices.

A body of case law is developing out of the *BSA* where parties try to take advantage of its provisions. This article focuses on what may be unintended consequences of the *BSA* that potentially have far-reaching implications for the construction, insurance and finance industries, as illustrated by the recent decision of ***The Central, 163-165 Iverson Road (LON/00AG/BSA/2024/008).***

The statutory framework

Section 123 of the *BSA* provides interested persons with the right to seek a Remediation Order ("RO") from the First-tier Tribunal ("FtT") requiring a relevant landlord to remedy specified relevant defects in a specified relevant building by a specified time. The key definitions are:

- An **interested person** means, amongst other things, a person with a legal or equitable interest in the relevant building or any part of it, which includes leaseholders.
- A **relevant building** is a building that contains at least two dwellings and is at least 11 metres high or has at least 5 storeys, which generally excludes buildings that are solely owned by leaseholders or on commonhold land.
- A **relevant defect** is a defect that arises as a result of anything done or not done, used or not used, in connection with a relevant building's construction, conversion into residential use or works completed within a period of 30 years ending on 28 June 2022, or works carried out after that period to remedy a relevant defect, which causes a building safety risk.
- A **building safety risk** is a risk to the safety of people in or about a relevant building arising from the spread of fire or the collapse of the building or any part of it.
- A **relevant landlord** is a landlord under the lease of a relevant building who is required to repair or maintain anything relating to the relevant defect.

A number of first instance decisions have

established that the FtT has a discretion as to whether a RO is to be made. To date, the FtT has granted ROs in all published cases save for one where the landlord in question was absolved or prohibited by statute from undertaking its repairing obligations under a lease, i.e. the landlord that was pursued was not a relevant landlord as defined by the *BSA* (***Flats 5, 15 & 29 Thanet Lodge, 10 Mapesbury Road (LON/00AE/BSA/2024/0007, 0500 & 0502)***)

Schedule 8 of the *BSA* further provides protections to leaseholders in respect of remediation costs of relevant defects and operates a "polluter pays" cascade of liability. Generally, developers are considered to be the "polluters", and so are required to be responsible for the costs of the remediation, and if unavailable, landlords with the financial means are to shoulder the burden of such costs. Only if neither are available would certain types of leaseholders be looked to for remediation costs. The *BSA* also seeks to pierce the corporate veil by including into this equation companies associated with the developer or landlord.

The facts

In The Central, it was not disputed that the building in question was a relevant building. The building's construction completed in around 2016 and the current landlord purchased the freehold in early 2017, before the tragic events at Grenfell Tower in June 2017. After this date a number of fire safety defects had been identified. However, the purchasers at The Central had the benefit of a Premier Guarantee New Build and Social Housing Warranties after the design and construction of the building had been signed off by Premier Guarantee Surveyors Limited.

When the fire safety defects were discovered, the leaseholder protections measures introduced by Schedule 8 of the *BSA* had not yet come into force. The landlord wished to avoid passing potentially crippling remediation costs to the leaseholders and therefore began protracted negotiations with interested parties about how to best undertake the works, rather than strictly enforcing the contractual obligations of the leaseholders under the term of the leases of the building.

Amtrust Europe Limited, as the underwriter of the Premier Guarantee New Build and Social Housing Warranties initially admitted liability for some of the remedial works and paid for the costs of the building's Waking Watch and installation of a fire alarm system, amongst other costs. However, in 2023, and shortly following the coming into force of the leaseholder protections provisions in the *BSA* (Paragraphs 34 and 41 of Decision), it changed its approach and stopped making payments.

This led to Amtrust entering into a Participation Agreement with the leaseholders providing it with the right to pursue claims against the landlord in their names, which includes an exclusive right to progress such claims as it sees fit and to determine settlement parameters in April 2024. On the same day, an application for a RO was issued in the leaseholders' name against the landlord.

What value do new build warranties have after the *BSA*?

At the final hearing there was a dispute about whether the lack of progress in undertaking the remediation works was caused by the insurer or the landlord. The leaseholders' representative explained (Para 41) that the change of the insurer's approach to stop paying out under the warranties broadly coincided with the introduction of the *BSA* and Schedule 8. This is because Amtrust's position is that its liability is limited under Section 7D of the warranty policy:-

> "The maximum the Underwriter will pay for any claim relating to Common Parts will be the amount that the Policyholder has a legal liability to contribute towards the cost of repairs, rectification or rebuilding works."

On this, the FtT commented in its decision at paragraph 42 of its decision as follows:-

"That does not seem an implausible explanation. Insofar as the leaseholders would no longer be liable for the cost of remedial works, as a result of the coming into force of Schedule 8 to the [*BSA*], the obligation to pay out under the policy would no longer arise. Since that time, and in particular, since the signing of the Participation Agreement, recourse has instead been sought against the [landlord]."

The FtT accepted that issues such as the existence of an insurance policy might be something that could be taken into account in the exercise of its discretion as to whether to make an RO, which is wide and unfettered by statute. However, the FtT said it would put it no higher than that (Para 53).

Following a three-day hearing, the FtT ultimately decided to grant a RO against the landlord on the basis of the following factors (Para 62):-

(1) The building remained un-remediated with significant relevant defects;

(2) The only party permitted to carry out repairs under the terms of the leases was the landlord;
(3) Given the delay to date, the FtT was not satisfied that the necessary remediation works would take place without a RO.

The wider implication of the decision to the construction and insurance industries

A key motivation for the *BSA* is to ensure that relevant defects are remedied as soon as possible. However, all works ultimately require funding. In those circumstances, the suggestion that the *BSA* has the effect of discharging insurers from liability, even where they have accepted this, is seriously alarming to not only landlords, but leaseholders and lenders who rely on the existence of new build warranties.

In The Central, the FtT declined to make a decision as to whether the insurer's liability under the New Build and Social Housing Warranties was indeed extinguished by the introduction of Schedule 8 of the *BSA*. It nevertheless held at paragraph 53 of its decision as follows:

> "On the issue of the insurers' liability, we consider that this is not something that needs to be resolved in determining whether to make a remediation order. There would appear to be much force in [the leaseholders' representative's] submission that the liability under the policy no longer arises by virtue of schedule 9 to the [*BSA*]. However, this arises an awkward question for [the insurer] in the present case given that the defects were known about and a claim was made under the policy, which was accepted (at least in part), two years prior to the [*BSA*] coming into force."

The implications are that insurers can and will now seek to avoid liability on their policies of insurance where they can say that the *BSA* has extinguished the leaseholders' liability for remediation costs. This would render countless similar policies worthless and undermine the entire basis on which the developer industry has operated for decades.

The landlord raised a number of arguments that the insurer retained legal liability irrespective of Schedule 8, and that it cannot have been the intention of Parliament to avoid third party contracts of insurance when Schedule 8 was implemented. Indeed, the reference to insurers liability in different sections of the *BSA*, such as section 133(4), which requires a landlord to first seek third party funding such as those from an insurance policy before passing remediation costs to leaseholders, makes that clear. However, these arguments had no effect on the FtT.

If this position is correct, the troubling consequence is that it gives insurers the opportunity to either seek to avoid, or at least stop paying out on policies to undertake remedial works. Rather than funding works and then relying on their subrogation rights to pursue the parties legally responsible, insurers can instead direct their substantial resources to forcing landlords to undertake unfunded works using the names of the leaseholders. This will then put pressure on leaseholders, who understandably simply want to have their properties fixed.

Given the relatively modest litigation costs and risks of FtT proceedings compared with the stifling costs associated with fire safety remediation, in one sense it is perfectly rational for insurers to seek ROs. This is particularly the case where the FtT's current approach is to pay little regard to the motivation for seeking redress of the remedies available under *BSA*. Why would an insurer continue to meet the risks it agreed to assume and underwrite if it could instead transfer its liability elsewhere? Why should insurers even fund works if they can leave landlords to do this and then try and defend any future claims that come their way?

Both the industry and the wider public will need to wait before they know whether or not this is approach will ultimately be successful. The issue of who ultimately pays for remedial works will be a recurring issue for many years, and may require further legal reform if the *BSA* has not struck the correct balance. For example, given the further revelations from the Grenfell Tower Inquiry, is it right to consider landlords as ranking as high on the "polluter pays" principle? In many cases, the only criticism that can be levelled of developers and landlords are that they made substantial investment decisions that relied on a combination of the government, the regulatory regime, their professional teams and the wider industry and its professionalism and integrity. When so many others parts of the industry failed in managing the risks that they assumed, it appears increasingly harsh if the *BSA* deprives landlords of the use and value of their assets in order to solve problems that were not ultimately of their making. **CL**

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