

April 2018

Post Grenfell: Impact of cladding on the valuation of high-rise residential blocks – the current position

Introduction

Following events which unfolded at Grenfell Tower in June 2017, the safety and replacement of defective cladding to apartment buildings has been a subject of ongoing focus for residential valuers. The purpose of this paper is to summarise the various Government led Reviews targeted at construction related matters, along with emerging findings from the First Tier Tribunal (Property Chamber), which will have an impact on the approach surveyors take when valuing property located within high-rise residential blocks.

Progress to date of Government led Reviews

Immediately following the Grenfell Tower tragedy, the Government established a Building Safety Programme and initial screening tests were made available at no cost to building owners, to identify whether the cladding was of “limited combustibility” as this is one way that buildings over 18m can meet current Building Regulations.

The Ministry of Housing, Communities and Local Government (MHCLG) releases a monthly Building Safety Programme Bulletin which contains data on progress in identifying high-rise residential buildings with unsafe cladding combinations. The latest Bulletin notes that, as at 15th March 2018, 319 buildings over 18m had been confirmed as having Aluminium Composite Material (ACM) cladding, of which 301 were “unlikely to meet current Building Regulations

guidance”. One hundred and fifty-eight of the affected buildings are social housing blocks, while 130 are privately owned (this figure includes residential, hotels and student accommodation blocks).

A recent report published by the MHCLG revealed that only seven social housing buildings have finished installation of replacement cladding. Only a further six had begun to replace the cladding, made of aluminium composite material. Data is still being corrected on remediation of private sector buildings.

Running in tandem with the ongoing Building Safety Programme is a major independent review of Building Regulations and Fire Safety with a focus on their application to high-rise residential buildings. The Review is being led by Dame Judith Hackitt who is the former Chair of the Health and Safety Executive. The review is future focused and will not cover the specific circumstances at Grenfell – these matters are being dealt with through a police investigation and a separate Inquiry led by Sir Martin Moore Bick.



New Capital Quay, Greenwich (Photo: Galliard Homes)

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Interim findings of the Hackitt Review were published in December 2017 and suggested that “the current overall system is not working effectively and needs to be overhauled”. The interim report has highlighted several major shortcomings in regulation and other areas affecting fire safety that will shape more detailed recommendations set out in the final report, originally scheduled for release in spring 2018, but now delayed with the final date for publication yet to be determined.

The interim report sets out six broad areas for change:

- ensuring that regulation and guidance is risk-based, proportionate and unambiguous
- clarifying roles and responsibilities for ensuring that buildings are safe
- improving levels of competence within the industry
- improving the process, compliance and enforcement of regulations
- creating a clear, quick and effective route for residents’ voices to be heard and listened to
- improving testing, marketing and quality assurance of products used in construction

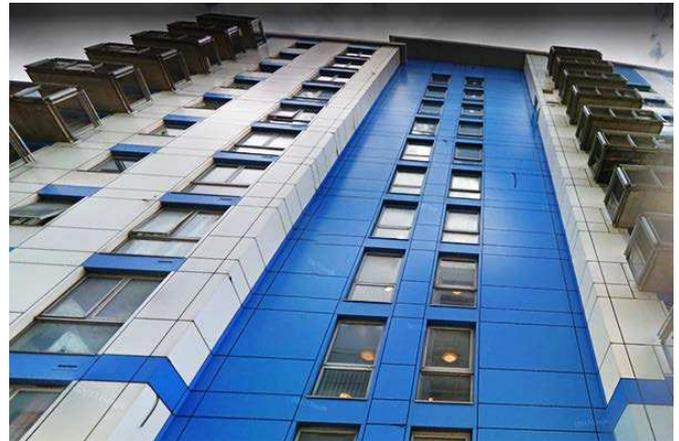
Of further significance was the guidance to landlords contained within the Interim Report. Dame Hackitt has advised landlords waiting for direction from the review on what cladding materials to use, “not to wait, but to consider what materials have already been identified and tested as safe” and to make sure that those who carry out remedial work are competent and that the work is quality assured.

Liability for costs associated with remedial works: emerging legal decisions

Determining who is liable for remedial works resulting from unsafe cladding has gained significant media coverage in recent months. For

blocks owned by social landlords, there is no additional cost to be met by secure and assured tenants. Long leaseholders in these blocks *could* however be liable to pay a contribution towards the cost of the works, depending on the wording of their lease agreements.

The Government has made repeated references to a commitment by social landlords not to recover the cost of remedial work associated with cladding safety from long leaseholders. Some social landlords *are* however seeking to recover a



The Cityscape block in Croydon (Photo: Google)

proportion of the cost of associated fire safety works from their long leaseholders. For example, the London Borough of Wandsworth is seeking to retro-fit sprinklers in all blocks of 10 storeys or higher and has obtained legal advice to the effect that the cost, estimated to be around £3,000 – £4,000 per unit, is recoverable. There is a legal argument ensuing that Local Authorities have a strict fiduciary responsibility to recharge private owners of properties in residential blocks.

As with long leaseholders in blocks owned by social landlords, flat owners in privately owned blocks could be liable to pay a contribution towards the cost of the remedial works depending on the wording of the lease agreements. The suggestion that freeholders should meet the costs has been described by some as “unrealistic”, for several reasons:

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- The current owners of some blocks may not have been responsible for commissioning the “flawed” work – on this basis they may be reluctant to fund the necessary works.
- Some private landlords may not be able to fund the works. For example, a lessee owned freehold block may struggle to raise the finance.
- Commercial companies should be mindful of the fiduciary duty of shareholders and the fact that this could create a conflict of interest for those considering who should meet the cost.

In recent weeks, the first of what is likely to be many applications to the First-Tier Tribunal (Property Chamber) have been heard and determined. While hundreds of blocks have been identified as at risk, work on the majority of these has not yet started, in some cases because of disputes over who should pay.

Of significance is the case of **Adriatic Land 1 (GR3) Ltd v Metis Management (Sheffield) Ltd [2018] EWLVT MAN FFT** (18 January 2018). This case involved a block of 118 flats where it had been discovered that the block had the same kind of cladding as at Grenfell. South Yorkshire Fire Service had served a notice on the tenant requiring the tenant to take various steps to comply with the Regulatory Reform (Fire Safety) Order 2005. These included remedying defects in the “compartmentation” of the property, that is the provisions to stop the fire spreading between the various floors and to address the risks caused by the cladding. The landlord claimed that the tenant was in breach with the terms of the lease as it had not replaced the cladding, nor had they taken steps to remedy the compartmentation issues. The First Tier Tribunal held that there had indeed been a breach of the covenants in the lease.

What is the First-Tier Tribunal?

The First-Tier Tribunal (Property Chamber) replaced the Leasehold Valuation Tribunal in England and is part of Her Majesty’s Courts and Tribunals Service. Each tribunal, which is entirely independent and impartial, consists of two to three members; comprising a chairman, now called a judge who is usually a solicitor or barrister, a qualified valuer or surveyor and in some cases a lay person with experience of leasehold issues. There are currently five regionally based tribunal offices (London, Northern, Midland, Eastern and Southern).

Another recent tribunal decision involved the leaseholders of a 120 unit block of flats in Salford known as “Fresh Building”. **E & J Ground Rents No 11 LLP v Various Tenants [2018] MAN 00BR** (24 January 2018). The building has similar cladding to that used at Grenfell. Leaseholders have been ordered to pay the £100,000 interim bill for the deployment of fire wardens until such time that a long-term solution is found for the defective cladding. In this case, the service charge for individual leaseholders has risen from £125 to £360 per month. Far higher sums will be involved when it comes to replacing the existing cladding.

A case which received widespread media coverage involved a block of 95 flats in Croydon known as “Citiscape” which was built in 2001 by Barratt Homes Ltd. As with recent similar cases, the dispute centred on the need to replace the existing cladding. The estimated cost in this instance was circa £2.4 million. The central issue in this case was the question of who should be responsible for paying for the removal and replacement of cladding found to be unsafe after Grenfell – the leaseholders who owned the individual flats or the owner of the building, Proxima GR Properties?

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The Tribunal determined that cladding replacement constituted maintenance and was not an inherent defect, finding that the costs fell on the leaseholders who now have to find the money to pay the estimated £2.4 million bill. The Tribunal did not consider allocation of costs for the ongoing fire watch because these are unable to be recovered until the end of the current service charge year. These costs currently run at around £236,000 per year.

The Tribunal in the Citiscape case also addressed the potential for complex litigation to arise from future claims against developers and landlords. The Tribunal considered the difficulty if the lease “is of no assistance in determining how hard the property manager must knock on the other doors ...the manager had indeed knocked on the doors of both Barratt Homes Ltd and Proxima GR Properties Ltd but it had been firmly rebuffed. The tenant’s MP has knocked on the Government’s but so far to no effect.”



Fresh multi-storey tower in Manchester (Photo: Julie Twist Properties)

The tribunal also noted, “The difficulty with all these potential claims is that they are entirely speculative with uncertain outcomes. No claim could realistically commence until Sir Martin

Moore-Bick has reported following completion of the Grenfell Tower Inquiry. The tenants would find themselves mired in litigation for many years during which time their flats would be effectively unsaleable. The most vulnerable tenants would be those most at risk; those who need to sell their flats because of old age, infirmity, family breakdown and the like.” Consequently, the Tribunal found that a service charge is payable in respect of the estimated recladding cost.

Another issue which has come to light is the possibility of works, other than cladding replacement being required to ensure fire safety. A previous apartment block fire at Lakanal House which resulted in fatalities has come under renewed scrutiny. Internal modifications to the building which occurred when it was refurbished meant that the essential safety feature of compartmentation was breached. Remedial works in connection with compartmentation could also result in costs being borne by leaseholders. This again has potential implications for leaseholders, even where the external cladding has been found to be fire safe.

The situation currently faced by leaseholders is similar to that faced by Right to Buy purchasers who bought defective premises in the 1980’s. In these instances, concerned to protect Government Policy, legislative assistance was provided to homeowners. Given the magnitude of the current cladding issue, this is unlikely to be forthcoming to private leaseholders. A key difference between those properties and the current situation is that those properties were deemed to have a defect as a result of their design and construction while the decision of tribunal rejects the contention that the removal and replacement of cladding is a design and construction issue.

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Approach taken by surveyors when undertaking valuation for lending purposes

Where the surveyor suspects the cladding is of an ACM type, a recommendation to procure a test which meets the requirements of BS8414 (Fire Performance of External Cladding Systems) will be made. Where appropriate, the valuer will not be in a position to provide an assessment of market value until such time that confirmation has been received that the cladding material is fire safe. Surveyors will continue to identify and report fire safety other than those related to cladding; the events at Grenfell have not changed the responsibility of the inspecting valuer in that respect.

Valuers will however not routinely comment on Fire Risk Assessments where these have not been requested within the original valuation report. By doing so, this could inadvertently provide unrealistic assurances about the building beyond the scope of a valuation for mortgage purposes.

The emerging issue of liability for costs associated with the repair and replacement of defective cladding will only become clear on completion of the Grenfell Tower Inquiry. More cases will be placed before the First Tribunal and eventually before the higher courts. Until then valuers will continue to exercise judgement in identifying properties which could potentially be affected and request sight of the appropriate test results and specialist reports. For understandable reasons of fire and public safety, no publicly available register of buildings with defective cladding is available. e.surv continues to track and monitor buildings with known defects and will continue to notify lenders accordingly.

Feedback

This paper was produced by the Risk & Governance department of e.surv Chartered Surveyors. We aim to address the issues that matter to our corporate clients and therefore invite your feedback on this paper.

In addition, we are keen to hear about any other subject areas that are of interest to you so that we may consider covering these in future.

Please send your feedback to David Ward at david.ward@esurv.co.uk or ring 01536 535527.