FIRST - TIER TRIBUNAL
PROPERTY CHAMBER
(RESIDENTIAL PROPERTY)

Case Reference	**:**	**MAN/00BY/LSC/2017/0099**
Property	**:**	**1-80 Hollin Bank Court Blackburn BB2 4GY**
Applicant	**:**	**Sophie Sacofsky**
Representative	**:**	**Mr Brian White**
Respondent	**:**	**RMB 102 Ltd**
Representative	**:**	**Mr Jonathan Upton, Counsel**
Type of Application	**:**	**Landlord and Tenant Act 1985 – s27A & S20C, & Para 5A Sched. 11 Commonhold Leasehold Reform Act 2002**
Tribunal Members	**:**	**Regional Surveyor N. Walsh (Chair)** **Regional Judge S. Duffy** **Tribunal Judge C. McNall**
Date and venue of Hearing	**:**	**15 April 2024 – remote CVP hearing**
Date of Decision	**:**	**17 May 2024**

DECISION

DECISION

The Applicant is liable to pay the Respondent the amounts of £175.00, £187.50 and £206.25 per flat in respect of the insurance rent for the 2021, 2022 and 2023 service charge years.

REASONS

Background

1. The Tribunal received an application, dated 21 April 2024, from Ms Sophie Sacofsky under section 27A of the Landlord and Tenant Act 1985 ("the 1985 Act"). The Applicant is the long leasehold tenant of Flats 1, 9, 27, 31, 41 & 68 , 1-80 Hollin Bank Court Blackburn BB2 4GY ("the Property"). The Respondent is the current freeholder of the building.

2. The Tribunal was requested to determine whether the service charges in respect of the Property are payable and/or reasonable. However, the Applicant is only challenging the "Insurance Rent" under clauses of the leases and whether the insurance premiums for the service charge years 2021- 2023 were reasonably incurred for the purposes of s.19(1) the 1985 Act. The Respondent is responsible for arranging the building's insurance, a proportion of the cost of which is recoverable from each lessee. While the Insurance Rent is a separate and distinct charge it is considered a service charge in accordance with section 18(1) of the 1985 Act.

3. On 29 August 2023 a Tribunal Legal Officer issued directions for the Applicant to set out her case, the Respondent to reply and for a determination to be made on the basis of the parties' written submissions. By way an Order dated 28 November 2023, Regional Surveyor Walsh considered the submissions from both parties and ordered that the mode of hearing would be by way of a video link. Additionally, Regional Surveyor Walsh issued additional case management directions to support a face to face hearing if required.

4. Following receipt of an application from the Applicant's representative, Mr White, to join the hearing from Israel, the UK Foreign Commonwealth & Development Office confirmed that the Government of Israel has not granted permission for oral evidence to be given remotely via video link to the UK courts and tribunals from its territory. Accordingly, on 16 January 2024 the Tribunal ordered that neither the Applicant nor her representative were permitted to give oral evidence remotely from Israel in these proceedings. Mr White confirmed prior to the hearing by video link that the Applicant was content to rely upon the written evidence previously submitted and did not wish to submit any additional oral evidence at the hearing. Mr. White explicitly acknowledged both before and during the video link hearing of the

need for him to limit his role to advocacy. He acknowledged that these restrictions may prejudice the Applicant's ability to make her case in the most effective manner.

5. On 13 February 2024 the Applicant applied to the Tribunal to both serve an amended statement of case and for a disclosure order. The Tribunal refused permission to file an amended statement of case. However, the Tribunal allowed, in part, the request for a disclosure and ordered the Respondent to:

   (i) Provide the Applicant with copies of all comparative insurance quotations obtained for the service charge years 2021-2023 pertaining to Hollins Bank Court.

   (ii) Provide the Applicant with copies of any Guarantee Letters issued to Zurich re Augustus being able to meet its insurance obligations.

   (iii) Provide the Applicant with copies of the Augustus accounts for the years of 2021 -2023.

6. The video link hearing was held on 15 April 2024 at 10:30am the Tribunal sitting at the Manchester Tribunal Hearing Centre, Piccadilly Exchange, 2 Piccadilly Plaza, Manchester M1 4AH. Albeit the hearing commenced some 20 mins late, at 10:50am, due to sound connection difficulties.

The Property

7. The Tribunal decided that it was not necessary to conduct an inspection of the Property. We understand that the Property comprises 80 residential flats contained within two four-storey blocks. We are also informed that the blocks were constructed between 2007 and 2008 of traditional brick and concrete materials under metal pitch roofs, and total some 6,810 square meters.

The Lease

8. The Tribunal was provided with copies of the Applicant's leases made between Taylor Wimpey Developments Limited (1), the various original tenant purchasers (2), CE Lock Mill Blackburn Limited (the Company) (3), and CE Lock Mill Blackburn (Estate Company) (4). The Leases are for a term of 125 years from 1 January 2007 subject to an annual ground rent of £125.00.

9. In para 1 of Sch 6 the Respondent covenanted to:

"keep insured with the Insurers and through such agency as the Landlord shall from time to time decide:

1.1.1 the Building in its Full Reinstatement Cost against the Insured Risks;
1.1.2 Loss of Rent if the Landlord so requires; and
1.1.3 liabilities in respect of property owner's and third party risks in relation to the Estate in such sum as the Landlord shall reasonably require."

11. In para 2 of Sch 6 the Tenants covenanted to:

"pay to the Landlord in advance yearly (and proportionately for any period less than a year):

2.1.1 the Insurance Rent Percentage of the gross cost to the Landlord of performing its obligations under paragraphs 1.1.1 and 1.1.3 of this schedule; and

2.1.2 the whole of the gross cost to the Landlord of performing its obligations under paragraph 1.1.2 of this schedule

including in each case the cost of any insurance valuations carried out by or on behalf of the Landlord all such payments to be made on each 1st January and 1st July (or such other day or days as shall be notified in writing to the Tenant)"

12. In clause 2:

"the Insurers" means such reputable insurance company or underwriters as the Landlord may from time to time nominate

"Full Reinstatement Cost" means the amount determined from time to time by the Landlord as representing the full cost (including demolition and similar expenses professional fees and expenses the cost of any works required by statute and Value Added Tax where applicable) which would be likely to be incurred in connection with reinstating the relevant parts of the Estate in accordance with this Lease at the time when such reinstatement is likely to take place having regard to all relevant factors (including the time at which loss or damage may be sustained any possible delay in the commencement and carrying out of reinstatement works and any possible increases in building costs)."

"Insured Risks" includes "such other insurable risks as may from time to time be required by the Landlord".

Law

13. Section 27A(1) of the Landlord and Tenant Act 1985 provides:

An application may be made to the appropriate tribunal for a determination whether a service charge is payable and, if it is, as to-

(a) the person by whom it is payable,
(b) the person to whom it is payable,
(c) the amount which is payable,
(d) the date at or by which it is payable, and
(e) the manner in which it is payable.

14. The Tribunal has jurisdiction to make a determination under section 27A of the 1985 Act whether or not any payment has been made.

15. The meaning of the expression "service charge" is set out in section 18(1) of the 1985 Act. It means:

> *… an amount payable by a tenant of a dwelling as part of or in addition to the rent–*
> *(a) which is payable, directly or indirectly, for services, repairs, maintenance, improvements, or insurance or the landlord's costs of management, and*
> *(b) the whole or part of which varies or may vary according to the relevant costs.*

16. In making any determination under section 27A, the Tribunal must have regard to section 19 of the 1985 Act, which provides:

> *(1) Relevant costs shall be taken into account in determining the amount of a service charge payable for a period-*
> *(a) only to the extent that they are reasonably incurred, and*
> *(b) where they are incurred on the provision of services or the carrying out of works, only if the services or works are of a reasonable standard;*
>
> *and the amount payable shall be limited accordingly.*
>
> *(2) Where a service charge is payable before the relevant costs are incurred, no greater amount than is reasonable is so payable, and after the relevant costs have been incurred any necessary adjustment shall be made by repayment, reduction or subsequent charges or otherwise.*

17. "Relevant costs" are defined for these purposes by section 18(2) of the 1985 Act as:

> *the costs or estimated costs incurred or to be incurred by or on behalf of the landlord, or a superior landlord, in connection with the matters for which the service charge is payable.*

The written submissions

18. The Tribunal was provided with a hearing bundle which contained the key documentation and written submissions. Including the Applicant's statement of case, three witness statements by Mr White, the Respondent's statement of case and the Respondent's witnesses' statements of Messrs Wilson and Dines. The Applicant's reply and copies of the extensive correspondence between the parties and with the Tribunal. Both parties provided the Tribunal with skeleton arguments and authorities in advance of the hearing.

19. The Applicant's case in simple terms is that the insurance premiums have been systematically inflated, by a variety of means, to maximise the monies being extracted from leaseholders. The Applicant contends that the connected nature of the companies and individuals associated with placing the building's insurance and the lack of any effective market testing has resulted in leaseholders being charged substantially in excess of the market rate for building insurance. The Applicant's detailed grounds of challenge were:

    (1) That VAT should not be included in the reinstatement value.

    (2) That 30% of the Building Declared Value to protect against inflation of reinstatement costs is excessive.

    (3) That the "commission" payable to Penult Capital Partners ("PCP") and Arthur J Gallagher (UK) Ltd ("Gallagher") for insurance services was not reasonably incurred.

    (4) That the captive reinsurance agreement between the insurer, Zurich, and Augustus Insurance Company Ltd ("Augustus") is relevant and indicative that the insurance premiums were not reasonably incurred.

    (5) That the rebuild costs per square foot applies were too high.

20. The Applicant also submitted insurance estimates from alternative providers, Royal Sun Alliance (RSA) and China Taiping, which she claimed were comparators as to what the reasonable insurance premiums should be for the years in question.

21. The Respondent in its written submissions contended that the insurance premiums in 2021, 2022 and 2023 were reasonably incurred. Referencing the insurance market practises outlined by the Respondent's witnesses and the case authorities cited, the Respondent contended:

(1) It was prudent and sensible to include and make an addition for VAT, which was the standard practice for insurers. Indeed, the far more likely risk would be that the building would be partially damaged in the event of an insurable event rather than destroyed, and so VAT would be payable.

(2) The inclusion of an inflation uplift protection prior to commencing works of repair or rebuild were simply a standard protection and practice which was included in all such policies. It did not increase the premium because the insurance premium was calculated on the Declared Value with this standard protection included as the industry norm in all policies for no extra charge.

(3) The case law cited (Williams v London Borough of Southwark (2001) 33 HLR 22.) demonstrated that commissions were allowable when linked to the payment for services as opposed to purely a discount or inducement for placing insurance. Further the level of the commission received is shown to be well within the bounds of reasonable by reference to the comparators produced and by reference to the findings of the Upper Tribunal in Octagon Overseas Limited v Cantlay [2024] UKUT 72 (LC).

(4) The Respondent citing the Supreme Court's decision in Aviva Ground Rent Investors GP Ltd v Williams [2023] UKSC 6 and Braganza v The Riverside Group Ltd [2023] UKUT 243 (LC); [2024] L. & T.R. 3, contends that the freeholder has discretion as to how it manages the insurance arrangements at the Property, subject only to a 'rationality' test. Citing Cos Services Ltd v Nicholson [2017] UKUT 382 (LC) and Waaler v Hounslow LBC [2017] EWCA Civ 45; [2017] 1 W.L.R. 2817 47, the Respondent averred that not only a reasonable process has been adopted but the outcome was also reasonable and competitive insurance premiums levied.

The hearing & oral submissions

22. At the commencement of the hearing Mr Upton, Counsel for the Respondent, raised an objection to the late submission of the China Taiping insurance quotation. Mr Upton stated that the time period for the submission of evidence had long past, the Applicant had failed to comply with Tribunal's directions and this quotation had been supplied very close to the hearing. Mr Upton considered that it would be prejudicial to his client if the Tribunal were to accept the insurance quotation into evidence. Mr White contended that quotation provided important evidence as to what a reasonable insurance premium should be set at.

23. The Tribunal adjourned for ten minutes to consider this preliminary issue. On returning the Tribunal outlined that it would not permit the quotation to be adduced into evidence and it would disregard it for the purposes of these proceedings. Allowing the China Taiping quote to be

adduced as evidence would have unduly prejudiced the Respondent's case and in any event that there was no reason why the quote could not have been submitted within the time frame allowed in the Tribunal's previous order.

24. Mr White then opened by helpfully confirming to the Tribunal the matters which the Applicant did not take issue with. He confirmed that the Applicant accepted she was contractually obligated under the terms of the lease to contribute towards the cost of building insurance. He also confirmed that the percentage division amongst each flat of 1/80th or .0125% is not disputed. Mr White also confirmed that he agreed with the analysis of statute and case law set out in Mr Upton's skeleton argument.

25. Mr White outlined that the key to the reasonableness test was set out in the Waaler case which confirmed that reasonableness was not just about the rationality of the process. It was the S19(1) test of reasonableness and reasonably incurred and having regard the RICS and ARM codes. What is reasonable was set down in Waaler and has regard to the Forcelux two stage test.

26. Mr White quoted para 67 of the Cos decision :

"It remains a mystery, having heard the evidence adduced by both parties, why there is such a discrepancy between the premiums charged to tenants under the landlord's block policy and the premiums obtainable from other insurers on the open market. It a mystery which the landlord has been wholly unable to explain."

27. Similarly, Mr White contended that the onus for justifying the premium charged here was on the freeholder not the leaseholders. The freeholder should have had a clear audit trail to demonstrate and yet there was no proof or audit trail produced by the freeholder to support its claims of testing the market.

28. Mr White then took the Tribunal through the document titled "Statement of Facts and Issues in Dispute – Not agreed by the Respondent" setting out what his understanding was as to which paragraphs were agreed and highlighting some key matters where disputes remained.

29. Mr White drew the Tribunal's attention to Notes 9 and 10 of the financial accounts of Augustus Insurance Company Limited in 2021 and 2022, which detailed payments between connected parties and companies.

30. Mr White also referred the Tribunal to the document produced by Artex "An Alternative Approach to Commission for Property Owners & Managing Agents - A Case Study". This detailed how companies could be less reliant on commission payments and generate enhanced profits by using a captive re-insurance model, by which they meant reinsuring

a proportion of the risk via a subsidiary company in return for a greater proportion of the insurance premium paid by leaseholders.

31. Next, Mr White addressed the question as to whether VAT should be added to and included within the re-instatement value. He contended it should not as to do so would inflate the insurance premium unnecessarily. If the Property was completely destroyed and rebuilt, it would be classed as a new build and would not attract VAT as a new build. He gave the notional example that if you insured a property for £100 without adding 20% for VAT, and 50% of the property was destroyed and the £50 plus to rebuild plus VAT at 20% would only equate to £60 and be less than the sum insured.

32. Mr White submitted that the Royal Sun Alliance insurance premium estimate supplied by the broker Reich was an important comparator as to the level of a reasonable insurance premium. He accepted that the indication of the likely insurance premium was predicated on positive information, but he asserted that this was indeed the case. The building possessed an EWS1 fire safety certificate, and the building's claims history was negligible, and that the latter point being acknowledged in Mr Wilson's witness statement.

33. Mr Wilson, the Respondent's first witness, was introduced by Mr Upton and proceeded to respond to the questioned posed of him by Mr White. Mr White drew his witness's attention to footnotes 9 (Related party transactions) and 10 (Immediate and ultimate controlling party) to the 2021 and 2022 Augustus Financial Accounts and to paragraph 28 of his witness statement:
"*Potential conflicts of interest are managed by ensuring Augustus's shareholders are separate to those of RMB 102 Ltd. Augustus is not a member of the group of which RMB 102 Ltd forms a part.*"

35. Mr Wilson accepted that the statements in the financial accounts as to the ownership of Augustus and the shareholders of the company that owned Augustus, TMWB, were correct. However, he explained that Augustus and the holding company were governed very separately. There being very different focuses and board meetings held for the respective companies. He stated that in reality the shareholders mentioned have very little knowledge or understanding of the day-to-day issues. He took the relevant decisions and so there was in effect separation between these connections.

36. In response to questions concerning paragraph 26 of his witness statement and the underwriting losses incurred by Augustus, Mr Wilson explained that he was referring to losses incurred in the 2015/16 financial year, but he accepted that this was not within the service charge years in question.

37. Mr Wilson explained that while PCP had just 4 employees: this reflected the fact that the company had access to the services of 32 employees at E & J as well as their professional subcontractors. He

advised that in 2022 the portfolio was offered to Ecclesiastical who took on approximately 1/3 of the portfolio producing a saving of 15%. According to Mr Wilson, Ecclesiastical were simply not interested in insuring the remainder of the portfolio. He added that the market had "shut" for building of this nature where there were fire safety risks and works of a fire safety remediation required.

38. Mr Wilson also explained that the insurance process involved taking an overview of the construction, the claims history, etc. He outlined that the rate allocated to Hollin Bank Court, which historically had been low, would now need to change to reflect fire safety remediation issues and that each building was individually rated as allocated by the insurer.

39. In response to Mr White's questioning Mr Wilson confirmed that there were written records of the insurance tender process. He explained that he did not re-tender every year but usually every 2 to 3 years as the position and the appetite of the market does not change significantly from year to year.

40. Mr Wilson emphasised that no one was willing to take on the remaining portfolio because of the known and unknown risks associated with insuring blocks of flats. Additionally, there were significant adverse fire safety issues at Hollin Bank Court, including Phenolic insulation between the bricks, High Pressure Laminate Cladding, UPVC on the stairwells, and timber balconies. Mr Wilson claimed that, given these issues, another insurer would not insure the property on the basis of a new business application.

41. During cross-examination, Mr White suggested to Mr Wilson that there were no detrimental safety issues present at the Property, highlighting that the building was less than 11 metres in height and possessed an EWS1 certificate. However, Mr Wilson disagreed explaining that an EWS1 certificate related to the safety of persons and their evacuation. It did not relate to the likely rate of burn or damage to a building and the associated risk from an insurance perspective.

42. Mr White questioned Mr Wilson as to why the captive company was so profitable, paying dividends of c. £2.5m in 2021 and c. £2m in 2021 and 2022 on turnover of c. £3.6m and c. £4.25M, for those respective years. Mr Wilson explained that it was necessary to have re-insurance in place and that Augustus dealt with around 550 – 700 claims per annum and that the preponderance were water and subsidence claims. He went on to explain that insurance is a volatile business exacerbated by climate change. Of the 4 or 5 insurers active in the market for risks such as this, all would require a captive to take out the frequent and volatile risks, leaving it to concentrate on the very infrequent but more catastrophic risks. Indeed, Zurich had told him that without a captive in place they would "drop him like a hot stone".

43. Turning to the rates of commission in the table and graphs setting out the broker Arthur J Gallagher (UK) Ltd's peer group benchmarking of freeholder retained commissions between PCP and other anonymised freeholder clients, Mr Wilson highlighted that the commission rates were substantially below the average in this case explaining that, as a company, they were seeking to wean themselves off reliance on commission payments.

44. When questioned as to why VAT should be added to the reinstatement value Mr Wilson explained that the working assumption for insurance purposes was the potential for some form of extensive but partial loss and the need to allow for VAT on professional fees. He stated that he was not a structural engineer (by which Tribunal took him to mean a construction professional) but the practical and the standard approach in the insurance industry is to include VAT, the motivation for this being both prudence and the need to adequately cover for potential risks.

45. Regarding the 30% increase permitted to account for any price inflation between the time of an insurable event and the start of rebuilding or repairs, Mr Wilson explained that this practice originated in the 1970s when inflation rates were exceptionally high. He stated that it had become a customary component of all insurance and incurred no additional expense as it was included in the given coverage. If, for instance, you desired to decrease the uplift to 10%, there would be no corresponding decrease in the premium since it was purely determined by the declared value. He recommended that it is crucial to bear in mind that if a major disaster occurs soon after the start of an insurance period, which includes activities like demolition, obtaining planning permission, and tendering, it could take a significant amount of time, possibly 2 to 3 years, to fully rebuild. In such a scenario, Mr Wilson concluded that it would be prudent to increase the coverage by 30% to account for this delay.

46. Mr White asked Mr Wilson if he was aware of a recent and similar First -Tier Tribunal case (CAM/12UD/LDC/2022/0049) in which the companies RMB102 and E&J were the Respondents. Mr Wilson said he couldn't recall the details of this case.

47. The Tribunal asked Mr Wilson if he undertook any 'spot testing' of insurers on an individual property basis to compare the rates of insurance premiums with the portfolio approach. Mr Wilson advised that there were approximately 600 properties in the insurance portfolio of which between 350 to 400 properties were residential building comprising of flats. He stated that usually 25 to 40 buildings were tested on an individual basis with the market to assess if more competitive rates could be obtained.

48. The Tribunal then heard from Mr Dines, the Respondent's second witness. In response to Mr White's questions Mr Dines outlined that Hollin Bank Court had always used Augustus to provide reinsurance.

He was unable to advise whose idea it was to use Augustus in the first instance, because that decision predated him joining the brokers Arthur J. Gallagher ('AJG'). He outlined that Zurich set the pricing for the premium, not Mr Wilson, and if Zurich could secure cheaper re-insure elsewhere in the market it would do so and not avail of the services of Augustus.

49. As per his witness statement, Mr Dines confirmed that the "Day One" provision is a common clause in an insurance policy, and in his experience allowed for uplifts of between 30 – 50%. Mr Dines also totally disagreed with the Applicant's position of not making provision for VAT in the reinstatement costs. Reiterating the same points that Mr Wilson made, but emphasising that if the building were 95% destroyed it would not be classed as a new build and would attract a full VAT charge on the rebuilding works. Mr Dines also explained to Mr White the breakdown between the buildings and terrorism cover and the respective providers of this cover.

50. Mr Dines denied that the benchmark data of retained commissions produce by AJG was 'cherry-picked'. He explained it was representative of the general level of commissions paid and comprised of other freehold companies not connected with the group of associated companies in this case. It was anonymised purely to protect the reputational risk to the clients who were asked to participate in this benchmarking exercise. Mr Dines outlined that he was not involved in the process of setting the commission level, which was undertaken at a group level, and it was not influenced at a broker level.

51. Mr Dines confirmed having started his insurance career with Royal Sun Alliance (RSA) and agreed with Mr White that it was both a reputable and respected insurance company. He cautioned against reliance upon the Reich estimate as it is merely a provisional indication from RSA as to the premium, it was not a formal quotation and was dependent upon full information being declared. Mr Dines was satisfied that the approach adopted by his firm fully complied with the ethics required of it, as set out by AJG, and that there were appropriate checks and balances in place to ensure a reasonable and competitive premium.

54. During re-examination, Mr Dines stated that AJG had previously gone to the market to see if any insurers would be willing to quote for Hollin Bank Court on a stand-alone basis rather than as part of the overall portfolio. He advised however that no company was interested in quoting or providing insurance for Hollin Bank Court. He confirmed to the Tribunal that written records of this exercise exists. When asked by the Tribunal why he had not produced these records as part of his evidence previously, Mr Dines responded "no comment".

55. In reply, Mr Upton maintained that the Respondent's witnesses were impressive and highly experienced insurance industry professionals, whose evidence should carry great weight. He argued that Mr White, evidenced by the manner in which he has conducted his case, had

demonstrated a lack of understanding of the insurance industry, the relevance of a ESW1 for insurance purposes and value of a very rough insurance indication from RSA. He contended the Tribunal only had the expert evidence of Messrs Wilson and Dines to rely upon in making its determination.

56. Mr Upton stressed that it would be foolhardy not to insure for a VAT addition when a potential 95% destruction would not necessarily be deemed to be a 'new–build' and consequently a large and unfunded VAT charge would be incurred. Mr Upton claimed that Mr White had misunderstood the insurance inflation uplift factor and he emphasised the Respondent's witnesses' evidence which stated that whether an allowance of 10% or 30% is made, it made no difference to the level of the premium. This was a standard in-built risk factor inherently reflected within the pricing of all such policies.

57. Mr Upton emphasised that it was established law that the payment of commission was reasonable but in fact the term 'commission' is somewhat of a misnomer because what is permissible is for the payment of services. Mr Upton submitted that Mr White has not challenged any of the services provided or the nature of those services, as detailed in Mr Wilson's witness statement, nor has he put any questions to the witnesses regarding these services. Mr Upton argued that it would therefore be inappropriate for the Tribunal to entertain any challenge to the services provided.

58. Mr Upton took the Tribunal through the benchmarking evidence and documentation again. He made the point that while it may not be a perfect picture, the Tribunal should have regard to the fact that, in the similar case of Octagon Overseas Ltd and Cantlay [2024] UKUT LC 72 a 24% commission of the notional gross premium for services rendered was held to be reasonable. Mr Upton also submitted that the e mail from E & J Estates, which confirmed a commission rate of over 18%, related to 2018 and was not a relevant year for the purposes of these proceedings. Also, Mr White did not put this 2018 commission rate to either Mr Wilson or Mr Dines in cross examination and they therefore did not have the opportunity to explain the context surrounding this figure.

59. Mr Upton stressed that the witness evidence detailed that Zurich would not insure the building without reinsurance being in place so as to de-risk and insulate Zurich from the lower level claims for water damage and the like. He contended that there was no evidence that using a captive increased the insurance premium, and Zurich always possessed the option of by-passing the captive and simply re-insuring through the general insurance market. Mr Upton added that the Respondent had tested the market and there were no-takers.

60. Mr Upton submitted that the insurance estimate from RSA was merely a very provisional and rough indicative figure, it was not a proper quotation and certainly not on like for like terms. He contended that

Mr White has not produced true comparable quotations because there are none. He also submitted that insurance providers are not prepared insure a risk such as Hollin Bank Court.

61. In his closing submissions, Mr White contended that there were considerable contradictions in both the Respondent's case and its witness evidence. These included the statement by Mr Wilson about the separation of the companies and shareholders, and the statement that losses were incurred when this was in years outside the examination of these proceedings. The fact that Augustus's losses are capped at 125% of the premium.

62. Mr White emphasised that VAT would only become an issue if the re-build costs exceeded 90% of the sum insured. He outlined that it would be ridiculous to claim that the inflation protection uplift had no impact on the level of the premium. He had no idea as to how the commission benchmarking was derived or the companies included.

63. He questioned whether it was indeed true that a sample of 25 or 30 buildings had their insurance tested on an individual basis. There was simply no evidence presented to support this.

64. Mr White questioned why RSA would even provide an indicative estimate of insurance if they were simply not interested in insuring buildings of this nature. He said all that had been presented by the Respondent were bald assertions. The Applicant was not looking for the cheapest level of insurance and he considered a reasonable level for the insurance premium would be £15,000.00.

Determination

65. When determining an application under section 27A the Tribunal must apply a three-stage test:

(1) Are the service charges recoverable under the terms of the Lease? This depends on the common principles of construction and interpretation of the Lease.

(2) Are the service charges reasonably incurred and/or services of a reasonable standard under section 19 of the 1985 Act?

(3) Are there other statutory limitations on recoverability, for example consultation requirements of the 1985 Act as amended?

66. In this case there is no dispute between the parties in respect of (1) and (3), our examination is therefore restricted solely to stage (2). Indeed, helpfully the parties agree on the interpretation of the relevant case law and the issue in dispute relates to the application of the law to the particular facts and circumstances in this case.

67. We consider that, for reasons which we will expand upon below, that the key matter for determination here is adopting the stand back and look approach as to whether the 'outcome' test outlined in Waaler v Hounslow LBC [2017] EWCA Civ 45; [2017] 1 W.L.R. 2817 is met as set out paragraph 37:

> " In my judgment, therefore, whether costs have been reasonably incurred is not simply a question of process: it is also a question of outcome. That said it must always be borne in mind that where the landlord is faced with a choice between different methods of dealing with a problem in the physical fabric of a building (whether the problem arises out of a design defect or not) there may be many outcomes each of which is reasonable. I agree with Mr Beglan that the tribunal should not simply impose its own decision. If the landlord has chosen a course of action which leads to a reasonable outcome the costs of pursuing that course of action will have been reasonably incurred, even if there was another cheaper outcome which was also reasonable."

68. Before focusing on this important overarching question, we consider that it would be helpful to deal with some of the specific challenges raised by the Applicant.

Reinstatement re-build costs

69. The Applicant raised this ground of challenge within their application, but the Applicant's representative did not specifically advance this argument at the hearing. The Tribunal notes that while the Applicant asserts that the build cost price applied for reinstatement purposes is too high, no evidence has been produced to support this claim. Neither the Applicant nor her representative have a professional background in building construction and pricing. The Tribunal therefore places more weight upon the reinstatement cost assessment and exhibit TW7 to Mr Wilson's witness statement. This was produced by an RICS qualified surveyor from Cardinus Risk Management on 25 February 2022.

70. Having reviewed the methodology applied in the report, adopting a price per square metre for the gross internal area including the common parts and externals, the Tribunal concurs that this is the correct approach. The re-build price per square metre is also at the level the Tribunal considers to be reasonable based up its own expert knowledge. The reinstatement value derived prior to any addition for VAT is an appropriate and reasonable figure for insurance purposes as at the date of the report.

Whether or not VAT should be added to the estimated reinstatement costings?

71. The Tribunal considered Mr White's submissions and arguments that VAT should be excluded from the reinstatement value insured to be misconceived. There is no dispute between the parties that in the event

of only partial destruction of the residential blocks, then VAT would be chargeable on the rebuild costs and that it was only in the event of total or near total destruction would VAT not be payable. The reconstruction being deemed to be a 'new-build' given such a catastrophic loss.

72. The Tribunal considers that the purpose of insurance is to provide cover against risks and a range of possible outcomes. We consider that the most likely occurrence is for partial damage to the buildings, incurring VAT, but even if this was not the most likely outcome it is within the range of reasonable possibilities and so the leaseholders should be insured against such an occurrence. To do otherwise would neither be reasonable or prudent and could leave the landlord susceptible to a challenge of not providing reasonable cover or at worst a negligence claim in the event of VAT not being recoverable on reinstatement works.

73. The definition of Reinstatement Value within clause 2 of the lease specifically provides for "including ..... Value Added Tax where applicable". It is difficult to see how the freeholder could be expected to forego this contractual obligation nor why leaseholders would wish to expose themselves to such a risk for a relatively small saving in monetary terms of 20% of the annual premium.

74. The notional example used by Mr White gives rise to an obvious, empirical, difficulty. If the rebuild value were (say, for ease of explanation) £1m excluding VAT and the insurance cover was for a maximum of £1m. Then, whilst it is true that a significant but partial loss equating to say 50% of the notional rebuild value (£500,000) with VAT at 20% (£100,000), this would still only total £600,000. Arithmetically, £1m less £600,000 would still in theory provide substantial 'headroom'. The problem with this example is of course that this position does not hold true across the entire range of possible outcomes and costs. Once damage costing more than £833,333 (i.e, 5/6ths of £1m) occurs, then the addition of VAT at the standard rate would take the reinstatement costs above the sum insured, meaning there will be an uninsured shortfall. If uninsured, and if the Respondent was not to bear that cost itself, it would fall to be recovered through the service charge.

75. The Tribunal sees however an even more fundamental problem with the scenario advanced by Mr White. Namely, any insurer may simply refuse to pay any VAT no matter what the percentage rebuild required if the insurance cover was taken out on the basis purely of the reinstatement building costs net of VAT.

76. For these reasons, the Tribunal finds that there are no grounds to suggest that the insurance premiums have been artificially increased by the addition of VAT. Rather to the contrary the addition of VAT is an appropriate, prudent and reasonable approach by the Respondent in discharging its obligations under the Leases.

Whether a 30% addition to the Building Declared Value to allow for a time lag between an insured event occurring and remediation, with associated inflationary risks, reasonable?

77. The Applicant's challenge to this addition again comes from the premise that the Respondent is seeking to artificially inflate the level of the premium so as to maximise its commission and insurance income.

78. Neither party drew the Tribunal's attention to the definition of Reinstatement Value within Clause 2 of the Lease which specifically cites this as a relevant factor to have regard to and to insure for:

"having regard to all relevant factors (including the time at which loss or damage may be sustained any possible delay in the commencement and carrying out of reinstatement works and any possible increases in building costs)."

79. The Applicant's assertions have not been supported by any evidence however to suggest that this is not a standard and prudent clause to protect against delays and cost inflation prior to commencing reinstatement works in the event of an insured event occurring. This is evidenced by the definition of Reinstatement Value specifically stipulating this as being a relevant factor. The Applicant and her representative have been engaging with insurance professionals and seeking alternative quotations, one such being from the broker Reich. We are surprised, if this addition was not a standard practice within the insurance industry, that the Applicant has not been able to confirm this with the various insurance brokers and professionals approached and obtained at the very least a statement for evidence to that effect.

80. The Tribunal considers that this is a reasonable and prudent practice, and we can see the significant dangers in not having such cover in place. The Tribunal also accepts the evidence of Messrs Wilson and Dines, both practitioners within the insurance industry, that this has becomes such an entrenched and standard practice that it comes at no extra cost to the declared sum insured. We also accept that seeking to remove this cover, which we do not consider to be a prudent or reasonable action, would not necessarily result in a reduction for this insurance cover by insurance providers.

Whether the "commission" payable to Penult Capital Partners ("PCP") and Arthur J Gallagher (UK) Ltd ("Gallagher") for insurance services was not reasonably incurred?

81. Mr White confirmed at the hearing that he did not disagree with Mr Upton's interpretation or analysis of the law or the case authorities cited. We assume that this also included the distinction drawn by Mr Upton between the permissibility of a 'commission' payment for services rendered under S19 of the Act, as opposed to a discount

reduction applicable to the overall premium and not directly linked to any services undertaken to justify such a payment. Mr Upton's skeleton arguments referring to the decision of Williams v London Borough of Southwark (2001) 33 HLR 22.

82. At the hearing Mr Upton and the Respondent's witnesses confirmed the levels of commission obtained for the various policies (buildings, terrorism, etc.) for the years in question. These explained that the commission rates had reduced year on year and significantly from the level of c. 18% in previous service charge years and as previously advised to Mr White by Landlord's agent.

83. The Tribunal also concurs with the parties' conclusions and analysis of the case authorities in respect of the permissibility of commission payments under the Act. We do not need to comment as to the veracity or independence of the commission benchmarking produced by AJG because we find that the commissions levied are within the acceptable range of reasonableness for the service charge years in question, having regard to the services rendered. As noted by Mr Upton, the Applicant has not sought to challenge the nature or extent of the services provided. While the reasonable level of commission payable will inevitably vary from case to case and the extent and nature of the services rendered for the commission payment, the Tribunal has noted that in the decision of Octagon Overseas Limited v Cantlay [2024] UKUT 72 (LC) it was held that a combined commission split between the broker and a group company of the landlord of 24% or 27.6% was reasonably incurred.

Has adopted portfolio approach and the use of a captive reinsurance agreement between the insurer, Zurich, and Augustus Insurance Company Ltd ("Augustus") resulted in reasonable insurance premiums within the meaning of S19 of the Act?

84. It therefore remains for the Tribunal to consider the overall insurance process adopted in the placing of this insurance and the outcome achieved, in absolute terms, and whether a reasonable premium has resulted.

85. The Octagon Overseas Limited case provides useful guidance in this respect and in particular the Deputy President's comments at para 61:

" I remind myself at this stage that it is for the Landlords to satisfy the Tribunal that the costs they have claimed have been reasonably incurred. The Landlords sought permission to appeal the FTT's determination that the burden of establishing that the commissions were reasonable fell on them, but they were refused. The leaseholders more than adequately discharged the burden of raising a prima facie case that needed to be answered by establishing that the premiums they were required to pay were not the result of an arm's length negotiation in an open market and included undisclosed sums to take account of services which the Landlords' agent had agreed to provide in return for

a commission calculated as a percentage of the premium. It was then for the Landlords to show what work had been done to justify that commission, and why the commission itself was reasonable."

86. In the present case, the issue extends beyond the commission payments but also includes the amounts paid to the insurance captive, Augustus, for reinsurance. The acknowledged connections between the various companies and individuals involved in the placing and providing the insurance for Hollin Bank Court means similarly that the Applicant has "raised a prima facia case that needed to be answered".

87. In deciding whether the portfolio insurance process and approach adopted provided a reasonable outcome for leaseholders the Tribunal was necessarily heavily reliant upon the witness evidence of the Respondent's insurance professionals. The Tribunal in making its determination must decide the weight to attach to this evidence and consequentially make findings as to its reliability and value.

88. Both Mr Wilson and Dines clearly have extensive experience within the insurance industry and provided helpful and clear evidence in respect of some of the issues in dispute in this case, such the insurance industry's approach to VAT. However, in respect of their responses and evidence as to processes applied to ensure fair and competitive insurance premiums, the Tribunal found their evidence to be lacking transparency, economical as to disclosures, contradictory and lacking credibility. In short, we do not find that the Tribunal was presented with the evidence required to show that the premiums charged were reasonable and not artificially inflated by the connected nature of the various parties or the adoption of a portfolio insurance approach.

89. The Tribunal finds it perplexing that despite Messrs Dines and Wilson admitting that they made numerous attempts to invite insurers to cover the entire portfolio and specific properties like Hollin Bank Court, none of the potential insurers accepted the invitation or that no documentary evidence of such was provided (whether to the Applicant, or the Tribunal) of these attempts. It was even more surprising that neither Mr Wilson nor Mr Dines mentioned in their witness statements that a sample of properties, in the region of 25 to 40, were market tested on an individual basis when the tendering exercise was being undertaken so as to test the competitiveness of individual building premiums in comparison with those derived from a portfolio approach. This was only mentioned by Mr Wilson when questioned by the Tribunal as to whether 'spot checks' were conducted on individual buildings. In his written and oral evidence Mr Wilson did not mention that such a check had been undertaken on the subject property. This only emerged upon Mr Upton's re-examination of Mr Dines.

91. Understandably, the Tribunal then explored whether this had produced an alternative estimate or quotation for the subject property. Mr Dines stated that no insurers expressed an interest in insuring the Property. Notwithstanding Mr Dines' and Mr Wilson's claims that this was

because of fire safety issues at the Property, which we will return to later, this appeared to be contradictory to the potential interest expressed to Mr White by RSA through the broker Reich. We considered these enquires to be important evidence and were surprised to receive the reply from Mr Dines of "no comment" when we asked him why documents corroborating these enquiries such as e mails, etc. had not been introduced into evidence.

92. The Tribunal deals with numerous S27A applications each year challenging the insurance premiums payable on residential blocks of flats. We agree with Messrs Wilson and Dines that obtaining insurance has become more challenging and insurance providers are scrutinising risks more closely. What the Tribunal is finding however, in contrast to Messrs Wilson's and Dines's conclusions, is not that buildings are being left uninsured because insurance companies are declining insurance cover per se, rather that premiums have been increasing significantly because of significant increases in building costs and greater awareness and caution amongst insurers as they become more cognisant of the inherent risks involved.

93. The introduction of numerous significant alleged fire safety defects, mentioned for the first time in Mr Upton's skeleton arguments and introduced by the Respondent's witness only in oral evidence was surprising given the reliance placed upon this evidence by the Respondent's witnesses. Mr White did not raise any objections but we could understand that he may have felt somewhat ambushed by such evidence being introduced so late in the day.

94. Yet there appeared to the Tribunal a number of contradictions in the evidence presented in relation to fire safety, especially by Mr Wilson. Mr Wilson openly acknowledged in his oral evidence that he was not an expert in building construction, yet he stated that the fire safety building defects required remediation. He did not outline why that was nor if remediation was going to be undertaken by the freeholder either itself or by seeking funding from other parties or from leaseholders. He dismissed the relevance of the ESW1 certificate that the Property possessed as being not relevant because it related solely to safety of the occupants and not the potential insurable damage to the Property.

95. No building will be constructed with completely ideal or non-combustible materials. It is always a risk requiring assessment, and now generally assessed using the PAS 9980 fire risk appraisal methodology. Materials such as Phenolic insulation contained with two layers of brick or the presence of timber balconies in a block of flats below 5 storeys may well form an acceptable risk as it stands or as augmented with minor additional safety measures. We do not accept Mr Wilson's view that the fire risk appraisal of the external wall relates solely to safety of occupants and is not indicative also of the potential risks to the building. The rate of combustibility of materials, their propensity to emanate flame droplets or smoke damage are all relevant factors in not only considering how long occupants can remain in a

building and the time they have safely evacuate but also indicate the likely extent of fire damage and spread prior to the fire service being able to contain the fire and limit the spread of fire, heat and smoke damage. From our knowledge as an expert Tribunal, we consider that the height of the block, the nature of its construction and the fact it currently possesses a safety ESW1 certificate, it is unlikely that potential insurers would refuse to insure the premises solely for these reasons as suggested by Mr Wilson.

96. Mr Wilson in his oral evidence explained that any potential conflicts of interest were in fact managed because he took the day-to-day decisions and shareholders were not involved in low level day to day matters, and the board meetings that they attended were focused on other matters. The Tribunal is not convinced. The contradictions evident and the manner in which the oral evidence was given leads the Tribunal to question the objectivity and impartiality of Messrs Wilson and Dines' evidence. As it stands, the Tribunal has not been presented with one item of documentary evidence to suggest that the insurance premiums for the building are competitive. Rather, the evidence is that no other companies would insure these premises either individually or as part of a portfolio of properties irrespective of the premium rate: they simply were not interested. Following on from that, no documentary evidence has been submitted to show how premiums were calculated nor indeed how, in the event of no alternative quotations or insurers, how Augustus alighted on the amount it should charge for reinsurance and how this impacted upon the overall premium negotiated and ultimately agreed with Zurich.

97. Absent such evidence, the Tribunal does not consider that the Applicant's prima facie case has been answered and we must rely on what evidence there is. This is indeed limited in nature but what we are left with is the RSA indicative estimate adduced by Mr White.

98. The rough indicative figure produced by Reich indicates a premium of £11,789 based upon the Cardinus Report's Declared Value of £16.4m as at February 2023, less 20% to deduct VAT and a day 1 uplift of 10% to protect against inflationary uplifts for insured events. Clearly the Tribunal has found that any deduction for VAT is inappropriate so an adjustment must be made for this. Also, the evidence clearly suggests that the claims record at Hollin Bank Court has been relatively benign and would not adversely increase the premiums significantly.

99. The Tribunal has also not attached significant weight to Respondent's witnesses claims of existence of significant fire safety issues as a loading factor to the premiums. In any event, Mr Wilson indicated that this was not something he declared previously, the building possessed a low-risk insurance assessment for the years in question, and that this would be a factor for 2024 onwards and outside of the scope of the service charge years in question. The Tribunal considers also that the reinstatement value in 2023 would have reflected considerable building cost price inflation from the 2021 and 2022 years.

100. Reflecting all of these factors and making appropriate adjustments for these additions and deductions, we find the reasonable sum allowable for the gross premium to be as follows:

- 2021 - £14,000
- 2022 - £15,000
- 2023 - £16,500.

101. The Tribunal's figures being derived by adding 30% to the RSA indicative quotation to reflect the addition of VAT and the possibility and risk of additional price increases in the premium when the exact details are worked through, which equates to a figure of £15,325.70. We then deducted 10% to reflect that reinstatement costs had increased significantly since 2021 by the date of the Cardinus Reinstatement Value estimate in February 2023, which equated £13,793.13. This figure was then rounded to £14,000 on account of, by necessity, the approximate nature of this estimate given the limited evidence available to the Tribunal. The 2022 and 2023 years' premiums were uplifted by 7.15% and 10% to reflect building cost inflation and general insurance premium increases over this period.

102. This represents a sum of £175.00 for 2021, £187.50 for 2022 & £206.25 payable in insurance rent for each Applicant's flats based upon a 1/80th division.

Costs

102. The Tribunal accepted the Respondent's submission that the relative success of the parties is an important factor when considering whether to make an order in respect of the Applicant's s.20C and para 5A applications. The Tribunal informed the parties at the hearing that the Tribunal will determine these applications on the basis of written submissions from the parties and following the determination of the substantive application.

103. The parties are directed to make such written submissions within 42 days from the date of the Decision. This direction will however be stayed should either party appeal the Decision and for the duration until the determination of any such applications for permission to appeal to either this Tribunal or the Upper Tribunal (Lands Chamber).