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Publications — Autumn 2017

Quarterly Housing Update

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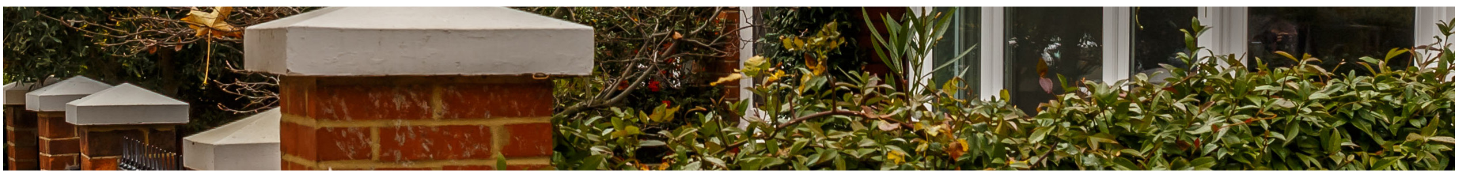

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Foreword

The last few weeks have been busy ones in terms of announcements and reports on a range of housing topics. As we approach the date of the Chancellor's Autumn statement one can't help wondering what more may be coming. Housing seems to be close to the top of the political agenda with the Government concerned about its appeal to young voters who are struggling to access housing in the way their parents did.

Speculation around SDLT cuts for first time buyers is out there as is the old chestnut of local authority borrowing caps on the Housing Revenue Account being lifted. We are also told that the supported housing settlement is to be announced this Autumn. In previous years we've seen similar stories appear only for there to be nothing in the Chancellor's statement. Is this Government soft market testing ideas before deciding what to move forward with? The coverage of the SDLT cut has, for example, not been wholly positive, with commentators highlighting the risk that it may push up house prices.

What we do know from recent statements, is that an additional £2bn is to be invested by Government with the promise of there being more social rented housing in areas of greatest need. Alongside the announcement of the new rent settlement, this is welcome news for the sector.

We shouldn't lose sight of the fact, however, that huge amounts of money are also being poured into the Help to Buy scheme so the drive to help first time buyers remains. Quite how the country weans itself off this particular funding stream is not clear, but it can't go on for ever.

Interest rates may be going up next month although probably only marginally. We've heard that before and it's not happened, so we'll have to wait and see what the Bank of England's monetary policy committee determine. Mark Carney has made his position pretty clear in the interviews I've listened to.

Rising interest rates will impact on borrowing costs. If the rise is small, one hopes it will not prove too difficult for people to manage, but the spectre of rising costs is obviously a worry for many. Equally, whilst rent certainty is good news for the sector's landlords, it is less so for tenants. The Institute for Fiscal Studies' report "The cost of housing for low-income renters" contains some telling statistics about the increasing impact of benefit cuts on the ability of tenants to pay. This will undermine the benefit to landlords of the CPI plus 1% rent settlement in some areas.

Disquiet around benefit changes amongst some Conservative MPs had been evident for some time. We have now had a significant announcement regarding LAH caps with more to come on supported housing. What the sum of these parts looks like we will have to see.

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The rise of the "for profit" registered provider

Since the implementation of the Housing and Regeneration Act 2008 (the 2008 Act), it has been possible for profit-making organisations to be registered with the social housing regulator, opening up a range of new possibilities and new entrants into the social housing sector. Yet for some time, uptake of the new flexibilities was slow; relatively few "for profit" providers have actually been registered and of those registered, even fewer have developed at scale.

Over the past year or so, however, we have seen an ever increasing number of clients registering "for profit" registered providers (RPs), and we are seeing a genuine flow of new capital into the sector, with developers, investors and entrepreneurs now registering "for profit" RPs.

So what is behind this trend? For many developers - either because they believe that they are not getting an appropriate value from traditional RPs for the affordable units on a development scheme - or because of the challenges of multi-phase developments involving a traditional RP - the establishment of an "in house" RP offers a real and viable alternative to traditional delivery of affordable housing obligations. One particular attraction is that the establishment of a for-profit provider allows whole sites – including the affordable elements – to be developed, owned and managed within the same corporate group so speeding up development (because the need to negotiate with third party social landlords is removed), reducing transaction costs and enabling a single standard of estate management on an ongoing basis and economies of scale in having a single housing manager for all tenures on site.

The advantages are even clearer for developers in the Build to Rent (BTR) sector, where (notwithstanding the concept of the "Affordable Private Rent" mooted in the Housing White Paper, and the fact, as a matter of planning law, that affordable housing provided under a planning obligation does not have to be provided by an RP) it is often the case that a s106 agreement will mandate that the affordable housing is required to be owned by an RP. And here, the fact that BTR operators are fundamentally set up to receive long term rental income, together with the management efficiencies of having single management across an entire BTR scheme, means the arguments in favour of setting up an 'in house' RP are particularly compelling.

For other applicants, the fact that registration enables an organisation to access grant funding from the HCA (or from the Greater London Authority (GLA) in London) to finance social housing provision is a key driver. Rented housing provided with HCA/GLA grant funding must be owned by an RP, and we have now seen the allocation of grant funding to for-profit providers.

Perhaps the biggest group of new entrants to the sector, however, are equity investors - ranging from "blue chip" backed funds, through to family offices, private equity and entrepreneurs, where the fact that the RP should provide an attractive yield alongside potential for capital growth has made affordable housing an attractive investment. There is also no doubt that the deregulation measures have done much to reassure equity investors into the sector about the liquidity of their investment, but equally the increased trade of stock between RPs (both not for profit and for profits) has proved that social housing can now be treated as a liquid asset (i.e. social housing can be sold at any time to a traditional RP or to another institutional investor/REIT so allowing a clear "exit" strategy for equity investors from the sector). These clients are acquiring not only existing stock but are also increasingly buying new stock from developers.

And what of the future? Perhaps the biggest challenge in recent times in encouraging new entrants to the affordable housing sector has been the regulation of rents by government. The four year rent reduction regime was a significant deterrent to a number of potential applicants. However, the recent Government announcement heralding a return to the CPI+1% rent increase regime will – in our view – fuel further interest in the model from both developers and investors.

Traditional RPs who have come to rely on s106 schemes to form the backbone of their development pipeline could easily see such opportunities drying up as developers keep schemes in house or else arrange deals with new players. At the same time, opportunities for traditional RPs abound- many of the new players will not want a day to day housing management role and will want to outsource that role to established RPs, whilst the "for profit" RP model could herald a new model of joint ventures between traditional RPs and investors where genuine equity participation in affordable housing could be leveraged in - something that could be very welcome to RPs with balance sheet constraints.

The growth of the "for profit" part of the sector forms part of the ever increasingly diverse landscape in affordable housing provision and is a trend that shows no sign of slowing down.

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Are you protecting your most important asset?

By now, you will no doubt be aware of the forthcoming changes to data protection, effective from 25 May 2018, through the General Data Protection Regulation (GDPR). So important are the changes that the ICO has described them as "the biggest change to data protection law for a generation". Government has also announced its proposal to enshrine the changes into national law so that there is clarity on the position in a post-Brexit world.

Are you sitting comfortably?

The often repeated headline is the increase in the ICO's power to fine organisations for breaches of GDPR, from the current level of £500,000 to up to €20,000,000 or 4% annual global turnover, whichever is highest.

Whilst this is true, the changes should be viewed as more than just a financial risk for your organisation. Over the past few years, individuals have become increasingly aware of their personal data rights and have welcomed the increased control they will have under GDPR. We have also recently seen numerous high profile and potentially disastrous cyber-attacks putting individuals' – often sensitive – information at risk across a range of sectors, regardless of organisation size. As a result and in an increasingly digital world, around 80% of people think that they do not have adequate control over their data online.

Organisations are quickly realising that security of the personal information they hold and treating it fairly and transparently, could be one of their biggest assets – a thought echoed by the ICO:

"If your organisation can't demonstrate that good data protection is a cornerstone of your business policy and practices, you're leaving your organisation open to enforcement action that can damage both public reputation and bank balance. But there's a carrot here as well as a stick: get data protection right, and you can see a real business benefit."

Then we'll begin

Many of you have already been in touch with us to discuss how and when you should be preparing for the forthcoming changes and how exactly the changes might affect your organisations. Recent figures show, however, that a significant proportion of SMEs are still behind in getting ready for the changes.

It is not too late, but you do need to take action. This is an opportunity for you to take the following steps towards compliance:

1. Co-operation

- Talk to your senior decision makers and get their buy-in; GDPR puts data protection at the heart of your organisation. It should have the ear of your most senior decision makers, and should be considered in all aspects of your planning and business strategy.
- Policies and procedures will need to be considered and updated, and training should be rolled out to all staff members on the new legislation.

2. Consideration

- Now is an ideal time to audit what personal data you hold, why you have it and how long you are keeping it. The overarching principles of data protection law are clear that information should be "adequate, relevant and limited to what is necessary" and held only for the purposes it was originally obtained.
- Consider the processing conditions you rely on to ensure you are using personal data lawfully. If the personal data is sensitive in nature, more stringent conditions will need to be considered. If you rely on consent, you should review how you have obtained that consent to

ensure that it meets the new requirements of GDPR, refreshing your consents as necessary before May.

- Will you need to appoint a Data Protection Officer and, if so, who that will be? DPOs will be fundamental to ensuring ongoing compliance with GDPR. We are expecting further guidance from the ICO on this, but current European guidance states that those involved in the public housing sector should consider appointing a DPO as a matter of good practice.

3. Control

- Do you have adequate measures in place to ensure that data is kept secure and individuals' data rights can be observed? You should consider technical measures relating to your IT systems and software and organisational measures such as protocols, policies and procedures for the handling of data by staff.
- Ensure you have technical and organisational measures in place to detect and react to any data breaches and to mitigate the risks to that data and your reputation. Who within your organisation should receive reports of data breaches and decide what action to take?
- Who are you sharing data with? Are you entitled to do so and if so, do you have appropriate data sharing agreements in place to ensure that the data is kept secure and confidential? Ensure you appropriately vet those who will be processing data on your behalf.

4. Communication

- Communicate with your customers and key stakeholders. Let individuals know exactly what you are doing with their data, why and for how long. Your organisation needs to be transparent; your privacy notices will require more detail and will need to be reviewed.
- Individuals must also be told about their right to withdraw their consent at any time; their rights to access copies

of their own data for free; to rectify inaccurate information; object to things such as direct marketing and, in certain circumstances, to have their personal data deleted or transmitted directly to another organisation.

- Ensure you have plans in place to communicate swiftly and effectively with the ICO whenever necessary.

Considering these issues will stand you in good stead in working towards compliance and protecting one of your most high profile and valuable assets.

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Top tips for procurement season

October is generally a busy time for social landlord procurement teams. Here's a checklist of key issues to consider when reprocuring contracts.

Do you need to advertise? – It is not every contract that needs a formal advertisement via the Public Contracts Regulations 2015. It's worth checking to see whether any of the exemptions in the Regulations apply. On the flipside, many development contracts linked to land deals do not get advertised, because of an assumption that these are exempted. Recent UK case law has clarified the position around advertising development contracts, so it is wise to seek advice before undertaking your procurement.

Low-value contracts – The 2015 Regulations introduced new requirements for UK contracting authorities when advertising contracts below the EU financial thresholds. The new rules apply to all central government contracts above £10,000 and all local authority, housing association and ALMO contracts above £25,000. Social landlords should also consider their internal standing orders and governance requirements for advertising low-value contracts.

Preliminary market consultation – Social landlords should consider the benefits of engaging with the marketplace prior to running a formal advertisement. Consultation is useful for identifying potential market interest and can help define the scope of the proposed contract and any social value requirements. Any consultation should be run transparently and so as not to give an unfair advantage or disadvantage to potential bidders.

Leaseholder consultation – Where externally provided works or services are intended to be recharged to leaseholders via a variable service charge, landlords may also have to consult with leaseholders on the proposed contract pursuant to the Landlord and Tenant Act 1985. Consultations should normally be undertaken before a contract is advertised. Landlords should ensure that their leaseholder and procurement teams are working under agreed joint timetables.

Third party frameworks – Third party framework agreements are a fast and efficient way for social landlords to procure contracts, especially when there is insufficient time to run a separate procurement exercise. Social landlords are still responsible for their own compliance with procurement law and should undertake due diligence on any frameworks to be used. Landlords should satisfy themselves that they can access the framework and that it covers the works, services or supplies being procured. The contract terms and prices set out in the framework should be able to be accepted with minimal negotiation. Many third party frameworks require users to pay joining and access fees, so this should be factored into procurement budgets.

Existing contracts – When looking to reprocure a contract, social landlords should check the terms of any existing contracts, especially around the contract term, rights of termination, and TUPE or pensions risk following termination. Advertising a programme before the existing contract has expired or been validly terminated, can create a risk of challenge for repudiatory breach of contract, so social landlords should check this before starting a reprocurement.

Tender documents – The 2015 Regulations require all procurement documents to be made available to bidders when the Contract Notice is published. This includes all tender documents, conditions of contracts, specifications and pricing documents. Crown Commercial Service guidance suggests that for complex procurements, some documents will not have to be made available until they are created later in the timetable. For most

Open and Restricted Procedures, however, documents should be ready at the start of the procurement.

Precedent documents – Every social landlord has them – that old tender document or services contract drafted years ago, that's recycled in a hurry for a new procurement exercise. Social landlords should ensure that all precedent documents are checked and updated regularly, to take account of legislative changes and best practice guidance. Similarly, old forms of contract should be checked to ensure they fit the scope and requirements of the new contract. Bespoke forms of contract negotiated for particular deals may not be appropriate for new exercises, so these should be used with caution.

Electronic procurement – 2018 sees the roll-out of some key deadlines about electronic procurement. Social landlords are expected to be running fully electronic procurements (ie via e-portals) by 18 October 2018. By this deadline, we should also have access to e-Certis, an online toolkit established by the EU Commission, which will specify the types of certificates and documentary evidence that can be asked for in procurement exercises. Social landlords who aren't already using e-procurement should make this a key priority in the forthcoming year.

Beware of extensions – Extending a contract by mutual consent is a basic principle of contract law, but can cause complications in terms of procurement compliance. The 2015 Regulations set out a list of permissible grounds for extending an existing contract. Contract extensions that don't fit into one of these grounds should be re-advertised in accordance with the Regulations and failure to do this may create a risk of legal challenge. Extensions may also trigger leaseholder consultation requirements and TUPE and pensions liability issues, so this should also be checked.

Data Protection Act update – As of 25 May 2018, the General Data Protection Regulation (GDPR) will be in force (see our article covering the changes on page 4). Contracting authorities will be under increased obligations around sharing personal data with contractors and sub-contractors, and ensuring that those organisations provide sufficient guarantees that they will meet the new standards in the GDPR. This will include checking that contractors and sub-contractors have appropriate technical measures in place, as well as appropriate policies and procedures, to ensure the security of personal data and compliance generally. The terms of any contract must also be clear about the purposes for which personal data is to be used. Contractors should only be acting on the explicit instructions of the employer, including in relation to sharing with further sub-contractors. Contracting authorities will need to update their tender and contract documents to reflect these new requirements.

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The accountability debate – can this help?

There has been much discussion around the sector over the last year or two about who actually governs the actions of housing associations (large and small), who they are accountable to and how best both to determine their mission and ensure that they remain loyal to and focussed on it.

This is not a new debate, however, because it has been taking place from time to time over the last 30 years or more, as government policy has pushed the sector in different directions and made changing demands of it. A part of the debate over that period has been how to address the interests of the tenants who are housed and the executives who organise their homes. The debate has also extended to how best to ensure that staff at the sharp end of the business of the association can, alongside the tenants, have a real voice in both the plans for and delivery of the services which the association provides.

In the context of this debate, it is often said that the traditional housing association constitutional model has two glaring weaknesses:

- a lack of real accountability of the Board to any stakeholders, save for the HCA in a case of regulatory extremis or bankers in the event of financial extremis
- little "legally enforceable" input for tenants and non-executive level staff into the development of the wider strategic objectives of the association or real ability to hold the Board to account for the delivery of them.

The ownership and governance model of both Rochdale Boroughwide Housing (RBH) and Merthyr Valley Homes (MVH) turns the conventional and potentially polarised, relationships of Landlord/Tenant and Employer/Employee on its head into a truly co-operative approach of co-creation. It simultaneously recognises the divergent and sometimes conflicting interests of its various stakeholders, while bringing them together within a constitutional framework that makes this very diversity one of its strengths.

Traditionally constituted housing association boards are comprised of board members who have appropriate knowledge of and experience both within the sector and in the wider business world together (sometimes) with representatives from tenants, the council and other stakeholders. As board members, however, each of them must act in the best interests of the association rather than in the interest of the group that they represent (if any), on the board.

The tenant/staff mutual model adopted by RBH and MVH identifies the interests of each of the stakeholders and then reorganises them in a framework that might be a useful model for other housing associations to consider. Indeed, a few traditional housing associations have recently raised this possibility with us.

At the very foundation of the model are the shareholding members of the mutual association – tenants and employees, whose key role (beyond being owners of the organisation) is to elect the democratic representative body, which represents their interests within the governance of the association. Apart from direct interests of tenants and employees, this body may also comprise representatives from the council and other desired external stakeholders, thus ensuring that each participant has a voice and an ability to shape the strategic direction of the association and hold it to account.

This democratic body is charged with the responsibility of working with the board in establishing a policy framework, determining service outcomes, scrutinising progress towards achieving these outcomes and crucially, appointing and removing non-executive board members. All these functions establish it as a key player in influencing the overall strategic direction of the association and, one may also say, as the guardian of its social purpose.

The democratic representative body appoints board members (other than executive directors who are appointed by the non-executive directors). The board and the executive directors are charged with the responsibility of running the association within the established policy framework and delivering the outcomes identified by the representative body. The board itself is constructed around the knowledge and experience of its members but is ultimately directly accountable to the representative body.

By carving out the representative function of the board, vesting those functions within a representative body and making the board accountable to that body, RBH and MVH have managed to balance competing interests within the association in a manner which optimises the skills and knowledge that each of the stakeholders can bring and the contributions that each of them can make.

Another aspect of the model is its ability to give councils a stronger voice in the post ONS inspired de-regulated world, without breaching the anticipated regulations under Section 93 of the Housing and Planning Act 2016.

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When is a mortgagee exclusion clause (MEC) needed?

Where a party has the ability to retain control over the use of property and creates a restriction which may impact on that property's value or saleability, a mortgagee exclusion clause (MEC) may be needed. This will enable the property to be used as security or ensure the most value can be achieved from it. Legal documents containing such restrictions are usually local authority planning or nomination agreements.

Planning permissions, restrictions registered on the title and leases are inherently binding on land. They need to be reviewed to check whether they affect value or saleability.

You should be aware that sometimes an MEC may be nothing more than a 'red herring'. A document may purport to bind, or contain an MEC, but not, in fact, be binding. Such an agreement takes effect as a contractual arrangement and is only relevant to parties to it and would, therefore, have no impact on any funder or successor.

Any document may be made binding if it contains reference to its being made pursuant to one of the following statutes:

1. Section 106 of the Town & Country Planning Act 1990 which explicitly states that a planning obligation entered into pursuant to this statute will be enforceable against (a) the person entering into the obligation and (b) any person deriving title from that person.
2. Section 52 of the Town & Country Planning Act 1971 which was a pre-cursor to Section 106 and sometimes remains relevant. This section states in sub-paragraph (2): an agreement made under this section with any person interested in land may be enforced by the local planning authority against any person deriving title under that person in respect of that land as if the local planning authority were possessed of adjacent land and as if the agreement had been expressly made for the benefit of such land.
3. Section 33 of the Local Government (Miscellaneous Provisions) Act 1982 provides that where a document relating to a provision to carry out works on land contains a covenant expressed to be one to which this section applies, then this covenant shall be enforceable (without any limit of time) 'against any person deriving title from the original covenantor in respect of his interest in any of the land and any person deriving title under him as if that person had also been an original covenanting party'.

When charging security, we need to assess whether or not provisions in any document will affect the property for the purposes of a funder. As always, providing any such documentation as soon as possible helps to flush out any such issues and deal with them early in a transaction.

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Whistleblowing and the "public interest" test

The Court of Appeal has held in Chesterton Global Ltd (t/a Chestertons) and Anor v Nurmohamed that an estate agent's complaints about the manipulation of accounts, which potentially adversely affected the bonuses of 100 senior managers, amounted to a protected disclosure in the public interest. While he was principally concerned with his own position, Mr Nurmohamed did have other senior managers in mind and, as a section of the public would be affected, the public interest test was satisfied.

The words "in the public interest" were inserted into whistleblowing legislation by the Enterprise and Regulatory Reform Act 2013 for disclosures made on or after 25 June 2013. The public interest test was introduced to reverse the effect of a case called Parkins v Sodhexo Ltd so that a worker cannot rely on a breach of their own employment contract, where there are no wider public interest implications.

Mr Nurmohamed was employed as a senior manager. Following changes to Chesterton's commission structure, he made disclosures to the area director and the HR director on three separate occasions in which he complained about manipulation of the company's accounts which he believed had an adverse effect on commission income. The effect was to make the company appear more profitable, to the benefit of its shareholders.

He was dismissed from his employment and brought various claims against Chestertons. The tribunal found that he had been automatically unfairly dismissed and that he had been subjected to detriment on the grounds that he had made protected disclosures. The tribunal noted that there was no authority on the meaning of "in the public interest" and held that a disclosure did not have to be of interest to the entirety of the public, as it was inevitable that only a section of the public would be directly affected by any given disclosure.

On appeal, the Employment Appeal Tribunal (EAT) held that the tribunal's reasoning had been correct and that there was no need for the tribunal to determine objectively whether a disclosure is of real interest to the public. The public interest test can be satisfied where the basis of the public interest disclosure is wrong and/or there was no public interest in the disclosure being made, provided that the worker's belief that the disclosure was in the public interest was objectively reasonable.

The Court of Appeal refused Chesterton's appeal, agreeing with the tribunal and EAT.

The decision in Chesterton shows that the public interest requirement is perhaps less onerous than it was intended to be. Provided that an employee can show that a breach of their contract affects a sufficiently large number of employees sharing the same interest, they can potentially pass the "public interest" test.

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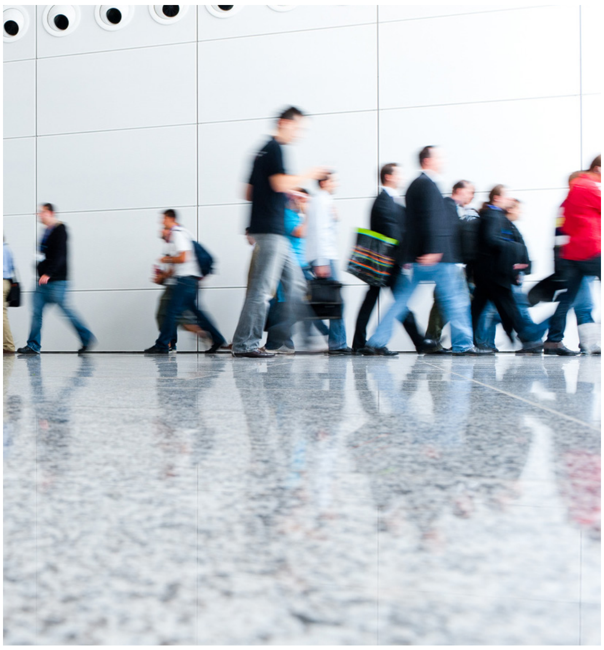
The findings of the Taylor review – modern working practices

The findings of the Taylor Review have been published. While the wholesale review of employment status which some envisaged has not come to pass, the emphasis on a simpler and clearer approach is certainly a welcome one for employers and employees. If the Review's recommendations are implemented, there will be changes that will affect social landlords.

The Review's purpose

The Government commissioned the Review in October 2016. Led by Matthew Taylor, the Chief Executive of the Royal Society of Arts, the Review considered how employment practices need to change. Amongst other things, the Review was asked to look into whether current definitions of employment status should be updated to reflect new and increased forms of working created by emerging business models, such as on-demand platforms and delivery services.



A shake-up of employment status?

The Review recommends that the Government takes a fresh look at existing law governing employment status and makes it simpler and clearer. There is an existing range of tests and factors which the courts have established to help them decide whether someone is an employee, a worker or self-employed. The Review recommended that they be considered and the legislation updated if necessary to incorporate them.

"Workers" replaced with "dependent contractors"

The Review recommends that the definition of "worker" is amended so that the obligation to provide personal service is no longer an automatic barrier to accessing basic employment rights. It also recommends a new classification so that people who are eligible for "worker" rights but are not employees, should be referred to as "dependent contractors".

The Review states that the dividing line should be between the new "dependent contractor" status and self-employment, so that being employed for tax purposes naturally means an individual is either an employee or a "dependent contractor".

Aligning employment and tax status

The Review also seeks to align employment status legislation and tax status legislation, so that the current difference between the two is reduced to an absolute minimum. The Review states that the dividing line should be between the new "dependent contractor" status and self-employment so that being employed for tax purposes naturally means an individual is either an employee or a "dependent contractor".

The Review suggests that an online tool could be developed to provide individuals with an indication of their employment status.

Casual workers

Zero hours contracts are here to stay! The Review notes that flexibility in the labour market is important and should be retained. However, there is an acknowledgment that employers "could be more forward thinking in their scheduling".

A potential significant change is that it recommends that the Government asks the Low Pay Commission to advise on the impact of bringing in a new higher National Minimum Wage (NMW) for hours which are not guaranteed in a contract.

The Review recommends that the Government re-examines the rules on what information needs to be provided to agency workers before accepting work. It recommends amending the legislation to improve the transparency of information which must be provided to agency workers both in terms of pay and those responsible for paying them.

According to the Review's findings, some companies are relying on temporary workers to fill longer term positions, thereby avoiding taking on individuals as employees. The proposed solution is for the Government to introduce a right to request a direct contract of employment for agency workers who have been placed with the same hirer for 12 months and an obligation on the hirer to consider that request in a reasonable manner. For those on zero hour contracts who have been in post for 12 months, it recommends there be a right to request a contract that guarantees hours which better reflect the hours worked.

Greater transparency

The Review suggests that people could be provided with helpful information when they start work and recommends that the written statement of employment particulars which currently only has to be provided to employees, should also be provided to "dependent contractors".

The Review recommends that there should be a statutory requirement for both an employee and a "dependent contractor" to receive a written statement on day one of their job.

Good employment relations

The Review seeks to encourage the promotion of good employment relations via a push for greater transparency surrounding employers' practices in relation to their workforces. It recommends the introduction of new duties on employers to report certain information on workforce structure, such as the use of agency services, requests from agency workers for permanent positions and requests from zero hours workers for fixed hours after a certain period.

What are the implications for social housing providers?

It remains to be seen to what extent the Review's recommendations will be implemented, but in the meantime social housing providers should ensure that they understand which "status" category their staff currently fall into and how they may be impacted. For those using zero-hours contracts, be aware that there may be a new higher NMW rate for any non-guaranteed hours worked under such contracts. Social housing providers will also need to be aware that long-term use of agency workers and zero hours workers may no longer be a way of avoiding hiring a permanent employee or avoiding a guarantee for hours which reflect those actually worked.

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NEC4 contracts: evolution not revolution

The new NEC4 contract suite has been described as "an evolution not a revolution". Indeed, the substance and form of the NEC contracts remain largely unchanged. NEC is, however, an increasingly popular form of contract and those in the industry need to understand the refinements made in the new suite.

New contracts

It is worth noting that NEC have introduced two entirely new contracts into the suite:

1. NEC4 Design Build Operate Contract (DBO): This consolidates the Contractor's responsibility for design, construction and operation of a project into a single contract. It is intended to be flexible and enable a more integrated whole-life delivery solution allowing the services to be provided before, during and after construction works are completed.
2. Alliance Contract (ALC): This form joins all members of the project team into the one contract. This style of contracting will be familiar to those already using TPC / PPC. The ALC is intended for use on large, complex projects and contains an integrated risk and reward model. Note that it is only available in consultation form at present.

New features

In addition to the new contract mentioned above, NEC4 also introduces a number of new features to its existing range of contracts.

In our view, many of the new features are introduced in an effort to minimise the need for a lengthy schedule of amendments to each contract, via the 'Z' clauses. However, despite the changes, it is likely that clients will still require numerous project specific amendments to be made, particularly on more complex projects.

- Early contractor involvement: This is now included as an optional 'X' clause, allowing the parties to adopt two stage contracting in line with modern trends for this form of tendering.
- Value engineering: New provisions within NEC4 enable both the Project Manager and the Contractor to propose positive changes to improve the outcome of the project. This includes a right for the Contractor to propose a change to the scope to reduce costs, as well as a right for both the Contractor and Project Manager to propose an acceleration to achieve completion before the completion date.
- Contractor's design (in respect of design and build contracting): The design responsibility of the Contractor has been brought in line with the industry standard so that the requirement is now to use the skill and care normally used by professionals designing similar works. The Contractor is also now required to hold professional indemnity insurance and a retention of documents clause is included specifically for design information.
- Acceptance of programme: Is now deemed to take place if the Project Manager does not respond to the programme issued by the contractor. This is definitely one for Project Managers to look out for, as deemed acceptance of an unsuitable programme may have wide-ranging implications for the project, particularly if the contractor has obligations to interface with other contractors at particular points in the programme.
- Allowable costs (in respect of cost based contracts Options C, D, E and F): NEC has included clauses aimed at bringing

commercial finality to the costs due under the various variable cost Options of the NEC suite; it being accepted that what qualifies as allowable and disallowed costs was a constant bone of contention between parties using these Options. The 'Defined Cost' and 'Disallowed Costs' are now deemed accepted if the Project Manager does not respond within 13 weeks.

- Final accounting: On a similar theme, more certainty is given to the final accounting process. The Project Manager is now required to issue a final assessment of payment due to the Contractor within four weeks of the issue of the Defects Certificate. The Contractor may issue its own final assessment if the Project Manager fails to do so. The final assessment becomes conclusive if not challenged by either party.
- Dispute resolution: NEC4 introduces a four week escalation period, during which senior representatives of each party must seek to reach a negotiated solution. Only after this period can any proceedings be commenced. The mechanism is intended to enhance collaboration between parties. For construction contracts, this will not cut across the statutory right to adjudicate 'at any time'. However, for non-construction contracts, it will be a mandatory process.

In addition to the above new features, there have also been a number of changes in terminology. For example, the 'Works Information' becomes the 'Scope' and the 'Employer' becomes the 'Client'.

Further clauses relating to anti-corruption, confidentiality and an option to allow the Client to require undertakings to others (collateral warranties) have been introduced. There has also been an amendment to the assignment provisions allowing either party to transfer the benefit of any rights under the contract to another party. Employers will be looking to amend this provision.

In conclusion, none of the changes are ground-breaking or drastically affect risk allocations or processes within the NEC suite. Many employers were already amending the NEC contracts to cover off the above issues anyway. Thus, in our view, the refinements by NEC make sense and reflect the day-to-day reality of using NEC.

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Tackling unfair practices in the leasehold market

The Government published its consultation paper on leasehold practices in July 2017.

This stems from the Government's concern at the leasehold sale of new homes and a lack of fairness and transparency to buyers.

We submitted a consultation response, following discussions with private developers, registered providers and other sector bodies. This article will examine the main proposals and share some insights from our research.

Grant of leases for new houses

The consultation sought views on limiting the leasehold sale of new houses (as distinct from flats, where leases are required to impose the key obligations relating to occupation), with exceptions, including shared ownership and retirement villages. It identified the likely lower capital value attached to a leasehold, rather than a freehold interest and the income stream created from the creation of the ground rent interest. It raised concerns that the implications of a leasehold, rather than a freehold ownership, are not fully understood by buyers.

Leases are not in themselves, intrinsically problematic. They are, on the contrary, an effective means of creating enforceable obligations for the management of estates. Our research indicated that a ground rent can help compensate a landlord for the acceptance of these obligations, encouraging the proper management of the estate.

Instead, developers have called for better and more detailed information to be provided to buyers, in the sales pack and in marketing material, to ensure that buyers are clear on the obligations they sign up to.

Ground rent

The consultation proposed that ground rents in respect of all new homes should be reasonable. There is evidence of excess (e.g. initial rents set at several £1000s), but care should be taken in determining what is reasonable. Responses on the level of rent varied, with initial levels set at 0.1% of the value of the property or fixed maximum figures. Rent reviews in turn could be limited to 0.1% of the value, or possibly to RPI.

Our research showed that the value of the ground rent will generally form part of the viability assessment of a development. Restricting the capital receipt from the ground rent could restrict the level of supply, especially of social housing.

Ground 8

Views were sought on whether long leases should be removed from the Ground 8 grounds for possession under the Housing Act 1988. Where ground rents exceed set limits, leases are assured tenancies, meaning landlords can seek possession where the rent is more than three months in arrears. If the landlord makes out the Ground 8, the court must order possession.

We found a generally positive response. If shared ownership leases are no longer assured tenancies, however, that will have the unintended consequence of making arrears of specific rent more difficult to recover.

Service charge

Finally the consultation sought views on whether to extend protection from unreasonable service charges to freeholders, who at present have no statutory protection from unfair charges. Responses to this were generally positive.

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The cost of unclear repairs and maintenance contracts

A frequent issue that we encounter in advising social landlords is a lack of clarity in the drafting of annexures to repairs and maintenance contracts, such as key performance indicators (KPIs) and pricing frameworks. A lack of careful drafting in these documents, or between them, can lead not only to difficulties in managing those contracts, but also time and money being incurred in resolving uncertainties and possibly disputes which divert the parties' focus away from the works being undertaken.

Obviously the best way to avoid such issues is to ensure that all the contract documents clearly record the terms agreed between the parties and there are no inconsistencies between them. If this hasn't been achieved and a dispute arises, then the contract will be interpreted objectively to ascertain the parties' intentions.

A recent case[1] demonstrated the court's approach to interpreting a KPI framework document and provides helpful guidance to those seeking to interpret their own contract documents. The repairs and maintenance contract provided for KPIs which, if met, would entitle the contractor to a bonus but, if not met, could also lead to a default notice and then termination. The employer became dissatisfied with the contractor's performance, issued a default notice and then terminated. After termination the contractor sought to argue that the contract did not specify the levels of Minimum Acceptable Performance (MAP) and therefore the employer had not validly terminated. This was because the KPI framework just gave examples of the MAPs in calculations and did not actually expressly specify the levels. The contractor successfully argued this at adjudication and in the Technology and Construction Court but the employer then appealed to the Court of Appeal.

The Court of Appeal found that it was common ground between the parties that the contract intended to provide for MAPs and the level of the MAPs could be ascertained from the examples. If there were no MAPs, then the employer would have lost its right to terminate and the contractor would have lost its entitlement to claim a bonus. As clauses had been included by the parties on these issues, those clauses would have been inoperable without the MAPs.

If you are faced with issues in the drafting of your contractual documents and the parties agree what was intended, or what should now be provided for, then the best way forward would be to amend the provisions by way of formal documentation signed by both parties. Parties should avoid informally adapting KPI frameworks or pricing frameworks as they run the risk of not taking care to understand the long-term implications of the changes, or one party being able to bring the informal agreement to an end by notice[2].

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[1]Sutton Housing Partnership Limited v Rydon Maintenance Limited [2017]

[2]The problems in such an approach were highlighted in the case of Mears Ltd v Shoreline Housing Partnership Ltd [2015]

New money laundering regulations – what you need to know

The Government enacted the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the MLR 2017) on 26 June 2017. These are based on the same principles as the pre-existing rules, but contain significant changes which affect how regulated organisations must structure their anti-money laundering functions and carry out checks.

The MLR 2017 apply to all organisations operating within the regulated sector which includes parts of the property industry. The rules will apply to RPs who carry out regulated activities which include undertaking "estate agency work" as an intermediary in property sales and providing lending, including recoverable grants.

The changes reflect the greater emphasis in the EU's 4th Money Laundering Directive, which the MLR 2017 implement, of a risk-based approach. As a result, the MLR 2017 are considerably more onerous than their predecessor, the 2007 regulations.

In order to comply with the implementation deadline HM Treasury issued the MLR 2017 without detailed guidance. As a result, we are assisting a number of our clients in deciding how best to implement the rules, whilst monitoring the guidance being issued by industry bodies.

This is especially important given the heightened scrutiny that money laundering risks have attracted in recent years, especially in the real estate and finance sectors. As a result, the Royal Institute of Chartered Surveyors currently identifies money laundering as one of the most significant areas of risk facing the property industry.

Key changes

- **New roles and functions.** Organisations must, depending on their size and risk profile, appoint a board member or member of the senior management team with responsibility for compliance with the regulations. Although the MLR 2017 do not state this must be a different person from the existing Money Laundering Reporting Officer (MLRO), we consider it is sensible, if practicable, for them to be different people in order that the compliance officer can review the practices of the MLRO and provide them with recommendations. Organisations must also consider establishing an independent audit function to monitor compliance.
- **Training and screening.** Organisations must screen employees involved in anti-money laundering (AML) compliance and provide them with regular training. Training is key as any individual who undertakes tasks related to AML may be subject to civil penalties or criminal sanctions should they fail to comply.
- **Risk assessments.** It will be necessary to undertake organisation-wide AML risk assessments and individual risk assessments for each new customer and transaction.
- **More onerous customer due diligence.** The documentation required will be more onerous. It is necessary to identify the source of funds and the ultimate beneficial owners of companies or trusts. Simplified due diligence no longer applies automatically to particular categories of customers. There are now more stringent rules regarding reliance on the due diligence of another party such as a solicitor.
- **PEPs.** Politically exposed persons (PEPs) will now include UK government officials as well as overseas officials. As a result

PEPs are likely to be found on the boards of UK PLCs and public sector bodies. This elevates the risk profile of customers who would otherwise be low risk. There must also be approval from senior management for establishing a business relationship with a PEP and adequate measures must be taken to establish their source of wealth.

- **Trusts.** Trustees will need to be ready to provide details for a new register of beneficial owners of trusts. Beneficial owners are likely to include a trust's settlor, trustees, protector and beneficiaries.

All regulated bodies should update their AML personnel, policies and procedures to ensure compliance with the new regulations. This will involve filling the new roles identified above, re-drafting procedures, organising training for staff and setting up new audit functions.

Specific risk factors

It is important for organisations to consider risk factors specific to their own industry and business. The MLR 2017 list out particular factors to be considered, including the nature of an organisation's customers, geographic areas in which it operates, products or services, transactions and delivery channels. Activities involving high value property transactions or other large one-off movements of money will inevitably be higher risk.

Day-to-day operations will also be affected. Private and social housing landlords should consider the risk factors around accepting cash payments, especially if tenants produce large sums at short notice to avoid eviction.

Best practice

Given the risks, we are seeing some clients mitigating potential regulatory and reputational risks by implementing best practices which go beyond the legal minimum.

For example, some businesses are carrying out customer due diligence on their contract counter-parties. This is not strictly required, because these are not their "customers", but they are choosing to do so to manage risk. Others are changing business models to phase out cash payments and changing deal models to ensure that AML documentation is obtained at the very outset of discussions.

Obviously there are pros and cons to such an approach. No-one wants to add to their regulatory burden and this can impact on management time and overheads. It also necessary to ensure such an approach is consistent with other regulations, especially the upcoming General Data Protection Regulation which will tighten up the rules around the retention of personal data (see our article covering the changes on page 4). Having said that, the regulatory climate means that money laundering is a key risk for regulated businesses and regulators in the UK are increasingly sharpening their teeth. Implementing the MLR 2017 promptly and effectively is therefore an important task for regulated organisations.

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Housing Delivery Partnerships – Removing barriers through collaboration

Partnerships of all kinds are not easy things to get right. They take work and commitment, good will, flexibility and compromise. That is no less true of housing delivery partnerships. Partnerships between the private sector, housing associations and public sector organisations with the aim of increasing the supply of new homes of all types are a vital part of the effort to tackle the housing crisis.

But establishing such partnerships can seem daunting and organisations that are considering embarking on the journey may decide instead on a different route. That is partly due to a lack of knowledge and a perception that housing delivery partnerships are time consuming and overly complex to establish.

In the interest of furthering the understanding of how housing delivery partnerships are put together – and how the partners can make a success of them – our report gathers together the experience of six different partnerships in Cornwall, Brighton, Sheffield and London.

These partnerships are at various stages of their lifecycle and range from the delivery of a few hundred units to over a thousand, but common themes emerge in how the partners built strong partnerships that can overcome the unforeseen challenges that inevitably emerge. The report explores how partners have gone about building these strong relationships, gives a guide to the pitfalls partners might experience and how they can be avoided and describes the different kinds of structures that partners could adopt.

But most of all it gives those who are thinking of setting up a partnership to deliver homes a sense of the questions they need to be asking right from the outset. Only by asking the right questions will you come to the right answers and form an approach that is best suited to your circumstance and thereby delivering much needed homes in your local area.

To view our Housing Delivery Partnerships report go to www.trowers.com/hdp

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