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Housing and Planning Act 2016: a Creditor's Perspective

Following lengthy debate, the Housing and Planning Act 2016 finally received royal assent on 12 May. Although not yet fully in force, the Act introduces significant changes to both the private and the social rented sectors in the United Kingdom. This briefing focuses, in particular, on the key changes affecting social housing provision in England and how these changes are likely to be perceived by funders to the sector.

For a sector already struggling to adjust to the effects of the rent reductions introduced by the Summer 2015 Budget, the first half of 2016 has been dominated by further uncertainty. Creditor concerns relating to early drafts of the Housing and Planning Act 2016 (the "Act") have combined with anxieties over Britain's future in Europe to impose significant constraints on funding options available to registered providers.

With the publication of the final version of the Act in early May, at least some of those fears may now have been allayed.

Housing Administration

One of the more controversial aspects of the Act during its draft stages was the provision for a new type of insolvency procedure for private registered providers of social housing, known as "housing administration".

The objectives of housing administration comprise the objectives of "normal administration", i.e. primarily to rescue the registered provider as a going concern, but also include the additional objective of keeping social housing properties in the regulated sector and ensuring that the relevant properties continue to be owned by a registered provider.

An application for housing administration can only be made by the Secretary of State (for Communities and Local Government), or by the regulator (the Homes and Communities Agency) with the Secretary of State's consent.

Other insolvency procedures, including winding-up, ordinary administration and the enforcement of security, are not permitted in respect of registered providers unless notice has been provided to the regulator and a notice period of at least 28 days has elapsed. Upon the making of a housing administration order, any ordinary applications for administration are dismissed and therefore housing administration will effectively take priority over any other insolvency procedures; it is only in circumstances where the regulator considers this not to be the appropriate route that other insolvency procedures may be pursued.

Whilst the main principles of housing administration have, in substance, been retained from the draft versions of the Bill, the key concerns of creditors have been substantially

Key issues

- Housing Administration regime has been adapted to accommodate creditor concerns
- Requirement to provide Starter Homes may reduce the supply of other forms of affordable housing
- Extension of Right to Buy to housing associations may lead to some depletion in stock
- Deregulation may lead to differentiation and increased due diligence by funders
- "Pay to Stay" will be complex and expensive to administer
- Voluntary implementation of shorter fixed term tenancies by housing associations would lead to a greater turnover of tenants and higher administrative costs

reduced by the inclusion of provision for an automatic termination of housing administration after one year, in line with the procedures applicable to corporate administration under the relevant provisions of the Insolvency Act 1986.

Although practical experience of corporate failures within the sector have been thankfully rare, creditors (and in turn valuers) have always drawn considerable comfort from the right of secured creditors to realise void units in order to repay debt. The lack of certainty created in prior drafts as to whether (or indeed when) units could be sold, threatened to create a significant headache for creditors, as well as for borrowers seeking to comply with asset cover covenants in their existing financing documents.

By giving creditors more certainty as to the likely end point of housing administration, legislators have allayed fears that creditors might otherwise have been subject to an indefinite moratorium on enforcement, whilst the housing administrator sought to rescue the failed provider.

The Act has also mitigated concerns regarding the future of MV-ST (or "Market Value Subject to Tenancy") valuations which had been raised during the drafting stage, at a time when the preservation of properties within the regulated sector was proposed to be the primary objective of housing administration. By subordinating this objective to (amongst others), the objective of safeguarding creditors' interests, it is hoped that the final version of the Act will preserve the ability of registered providers to rely on MV-ST valuations and minimise the need to top-up security portfolios.

The Act does not however allow the holder of a qualifying floating charge to block the appointment of a housing administrator, as is possible (in limited circumstances) in respect of corporate administration proceedings. In this context, and given that the stated objectives of housing administration include keeping social housing within the regulated sector, housing administration is more closely aligned with other special administration regimes such as those in the utilities sector, rather than true corporate procedures.

Nevertheless these sectors have shown a continued ability to attract a mixture of bank and bond investors, and it is to be hoped that these may offer some encouraging parallels for the future funding of social landlords once the provisions of the Act relating to housing administration have been implemented.

Starter Homes

The Act contains provisions to encourage the provision of "starter homes" for first-time buyers between the ages of 23 and those under 40. Under the Act, local planning authorities (LPAs) in England must promote the supply of starter homes and this duty will be a material consideration in the grant of planning permission for residential development. A home will only qualify as a starter home if sold at a discount of at least 20% to market value, capped at £450,000 in Greater London and £250,000 elsewhere.

Framework powers are included allowing the Secretary of State to make regulations to prevent the grant of planning permission for residential development unless a minimum number of starter homes are included or a financial contribution is paid. In March 2016, the Government published its approach to the regulations covering the starter homes requirement in a technical consultation paper which proposed:

- The starter homes requirement would apply to developments of 10 units or more (or on sites of 0.5 hectare and above).
- 20% of all homes delivered should be starter homes.
- Provisions would prevent sale of starter homes at full market value for at least 5 years following their initial sale, with tapered removal of this restriction for a period up to 8 years. No renting out of these properties would be permitted during the restricted period.
- There would be an exemption where the provision of starter homes would make the development unviable. Consideration would also be given to other exemptions for some forms of specialist housing – e.g. residential care homes, estate regeneration schemes and student housing.
- The Government will consider allowing commuted off-site contributions in lieu of starter home provision if the LPA agrees, and in cases where specialist older people's or private rented sector housing is provided.

This measure has been particularly controversial through the Parliamentary process, which saw the House of Lords' attempts to water the requirement down ultimately resisted by the Government. There are concerns that the starter homes requirement will place further pressure on house prices and reduce the supply of other forms of "affordable housing" provided through Section 106 agreements, since

developers are already in many cases required to provide affordable housing in their residential schemes up to the limit of viability of the development project. In addition, many lenders are concerned that allowing buyers to "cash-in" on the uplift in value of the property after a relatively short time could cause instability in house prices and a move to riskier lending. This issue is likely to remain controversial as the final details are ironed out.

Voluntary Right to Buy

In 2015, the Government announced plans to extend the statutory Right to Buy ("RTB") to tenants of housing associations, aiming to put home ownership within the reach of an additional 1.3 million families. However, due to significant concerns surrounding the legitimacy of legislating to force the sale of assets owned by charities and not-for-profit companies, RTB has been extended to housing associations on a *voluntary* basis ("VRTB"). This follows a compromise agreement reached between the Government and the National Housing Federation in October 2015.

Under the agreement, housing associations will be free to determine their own policy on VRTB, with the decision whether or not to sell an individual property ultimately resting with the association's board. Although there will be a presumption that tenants can buy the home in which they live, the voluntary deal envisages exceptions for certain types of properties, for example properties in certain rural areas; supported housing; almshouses and properties provided through charitable or public benefit resources.

Where associations exercise their discretion not to sell, they will be expected to offer their tenants an alternative property to buy through the concept of a "portable discount".

Whilst this is a voluntary scheme and the Act itself does not contain measures to implement a statutory RTB for housing associations, it does contain framework powers for the Secretary of State to publish home ownership criteria which will determine which tenants qualify for the VRTB. It also allows the Secretary of State to direct the regulator to monitor associations' compliance. Most importantly, however, the Act contains funding provisions to ensure that associations are fully compensated for any properties sold with the VRTB discount.

Nevertheless, the main concern for creditors surrounding VRTB has been the potential depletion of social housing stock, due to uncertainties over the viability of 'one for one' replacement. This is especially the case for social housing stock in London, where the Government has committed to a two-home replacement for every one sold.

However, creditors can take some comfort from the ongoing VRTB pilot scheme, which launched in January 2016. By April, out of more than 48,000 households to which the pilot scheme was marketed to, less than 1% of tenants had made a formal application to buy. Furthermore, out of the 19,000 households in the London pilot, only 96 applications had been processed, with affordability constraints being cited as the reason behind low take-up.

While this may only be a small sample, the pilot indicates that, at least for now, creditors' fears over rapidly depleting security may have been somewhat exaggerated.

Nevertheless, with full roll-out of the scheme due in the autumn, creditors may need to monitor their borrowers' stock more closely. Unlike statutory RTB, disposals of stock under VRTB will require mortgagees to formally release their charges using Form DS1. However, whilst this may necessitate higher spending on staff to monitor and manage consents for disposal, closer monitoring and more frequent valuations may help creditors to avoid "surprises" on this front.

Deregulation

Closely linked to VRTB is the clear step by the Government towards deregulation.

The Act introduces a number of deregulatory measures, aimed not only at giving associations more operational freedom, but also at returning them to the private sector. The most significant measures include:

- Removal of the constitutional consensus regime: associations will no longer need regulatory approval for mergers, restructuring, changes in status, winding up or dissolution. The old consents regime will instead be replaced by a notification system, the details of which are to be covered by directions to be issued by the regulator.

- Removal of the disposals regime: associations will no longer need permission from the regulator for sales, charging for security and changes of ownership but will instead only need to notify the regulator of the same.

- Abolition of the disposals proceeds fund: associations will no longer need to spend receipts

from RTB and Right to Acquire sales according to rules set by the regulator.

- Restrictions upon the power of the regulator to appoint board members to an association's board to circumstances where that would be required to ensure compliance with legal requirements.

In light of these measures, funders who previously took comfort from the regulator's consent regime may wish to carry out increased due diligence themselves on some borrowers, to ensure that interest rates are commensurate with the level of risk.

It is also possible that funders will, in future, differentiate more between individual associations. Whilst associations may no longer require certain consents from the regulator, many associations that are registered with the Charity Commission will, in certain circumstances, need to obtain consent from this body instead. In some respects the charities regime is more onerous than the current regulator regime.

However, what this procedure would involve is yet unclear and it remains to be seen whether funders will treat any such consent regime as a significant differentiating factor.

It should also be emphasised that the overall structure of regulation has been retained by the housing regulator and, in particular, regulation through the governance and financial viability standard linked to the duty of openness with the regulator.

Pay To Stay

The House of Lords has managed to soften the initial Government proposals of the "Pay to Stay" scheme in England under which social landlords may charge tenants market or near market rents depending on the gross income of their household. Initially the Coalition Government in 2012 gave social landlords discretionary powers to charge such rents to tenants with an annual income exceeding £60,000.

Now, under the Act, Councils no longer have discretion and must implement "Pay to Stay" in respect of secure tenants whilst for housing associations implementation remains voluntary. The main provisions of Pay to Stay are as follows:-

- Under the Act the minimum income thresholds will be £31,000 outside of London and £40,000 in London, (subject to a commitment in future regulations to allow for these thresholds to be reviewed and increased each year in line with the Consumer Price Index).
- Income will be defined as "taxable income" which will include employment earnings, pension income and investment income but not child benefit, disability living allowance or tax credits, and regulations are to provide for how Pay to Stay will interact with tax years i.e. whether it should be based on previous income or current income.
- The "household" has been defined as the tenant, any joint tenants and their spouses, partners or civil partners. Within a household, only the incomes of the two highest earners would count. The income for non-dependent children would not be included unless they are a party to the tenancy agreement and they are one of the two highest earners.
- No household in receipt of universal credit or housing benefit would be subject to the policy.

The House of Lords has been successful in securing a taper of 15% for each additional £1 per household that is received above the relevant income thresholds (i.e. £31,000 and £40,000). This has alleviated the position for those tenants on the cusp of the threshold, and combined with the 4 year rent reductions that the Government has already imposed, means that some tenants (for example in Camden) in this position are actually seeing their rents reduce. The Government will also consider how the taper system will work alongside universal credit and further details are to follow as this is rolled out.

From a creditor's point of view, the key issue will be whether the level of arrears increases as tenants may struggle to pay the higher rent. There will also be a considerable additional administrative burden on the relevant associations to check the incomes of their tenants, and associations that voluntarily adopt Pay to Stay may be challenged in finding efficiency savings to offset the additional administrative costs incurred. However, as Pay to Stay is a voluntary scheme, it remains to be seen what the level of take up will be.

Lifetime tenancies

Prior to the Act, local authority tenants were granted secure tenancies which were generally more advantageous than the terms of a tenancy in the private sector. In particular such tenancies allowed security of tenure for life and , in some circumstances,

for the tenants' successors (if a relation had shared the house with the tenant).

The Government's aim is to end lifetime tenancies for future social housing tenants. For Councils, it is mandatory to terminate the granting of secure tenancies, but for housing associations implementation of this policy is voluntary.

Lifetime tenancies will gradually be replaced with fixed term tenancies of 2-10 years as new Council tenants will not be eligible for lifetime tenancies. For a short transitionary period, lifetime tenancies will be portable for existing secure tenants who will be able to transfer their lifetime tenancy to other properties. Succession is also affected; family members will have the right to a tenancy but only at the fixed term level. The House of Lords gained a few concessions to the policy, namely:-

- Fixed term tenancies are to be permitted for a term of up to 10 years rather than the original proposed maximum term of 5 years;
- Fixed term tenancies will however survive whilst children up to 19 years of age live at the property (assuming that they were aged under 9 at the date of grant of the tenancy).
- Some tenancies are not affected which include introductory tenancies which last for one year (typically) as well as flexible tenancies.

For funders, occupancy of the housing stock may be more fluid if shorter tenancies are adopted by their borrowers. Again it remains to be seen whether arrears increase, and whether there will be any effect on the relevant housing association's covenant strength, due to the greater turnover of tenants and higher administrative costs that this change could impose.

There is some suggestion from housing associations that Local Authorities and housing associations should have closer partnerships to deal with displaced tenants, and this could initiate changes in the sector.

Associations may experience more voids in between tenancies giving rise to possible cash flow issues or, conversely, an opportunity to dispose of stock on an MV-ST basis (subject to title issues).

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