Devonshires

IT'S THE LAW: Stock Rationalisation

Taking Stock

What is it?

Stock rationalisation involves the transfer, from one landlord to another, of tenanted properties along with their associated assets and the business of managing those properties.

Why do it?

Registered Providers are charged by the HCA with optimising the return generated by their assets. By undertaking an asset management review an RP will be able to identify those properties it holds which are:

- underperforming financially (with running costs disproportionate to the income being generated);
- a type of stock that doesn't sit well with the RP's core strategy (an RP may wish, for example, to divest itself of care homes requiring specialist resources if its strategy is to maximise general needs supply);
- worth a lot of money and which, if sold, could provide cash to be used in other areas (the sale of a town house in a posh part of Westminster might fund the construction of 3 new houses in Brent); and/or
- located outside the RP's principal geographical area (an RP with 90% of its stock within Newcastle may not wish to be responsible for an estate in Plymouth acquired as a result of a merger).

A stock rationalisation programme can raise funds to be invested in new stock or reinvested in improvements to current stock. There may also be a positive effect on service delivery to the residents affected. The RPs involved can concentrate on resourcing and infrastructure to deliver outstanding customer service within a smaller more logical geographical area. They can also concentrate on, and so be better at, the management of a narrower range of housing types.

It's not all about the property

It's critical to remember that stock rationalisation doesn't just involve the transfer of property. Also being transferred are the landlord's obligations to the residents under their tenancy agreements, the business of managing the property and the assets of that business. In many cases employees will also be transferring.

Ready to rumble?

Stock rationalisation is complex and multifaceted. Preparation before going ahead and marketing the stock or deciding to submit a bid is essential. If you've decided you want to go down the rationalisation route and have identified a chunk of your stock to dispose of, your first step is to "get to know" it so that any potential issues can be identified, investigated and, if possible, resolved even before the stock is marketed. At this stage you'll need really good lawyers - so give us a call.

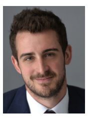
The Scouts are right. Be prepared

Preparation is key to the success of any rationalisation programme. As a minimum this should include:

- **Title review:** This may seem obvious, but you should ensure that title to all of the properties you are looking to dispose of is registered and, more importantly, that you are the registered owner. In addition, you should be reviewing any title covenants and restrictions to ensure that (a) you are free to sell your property, (b) there aren't any restrictions stating you can only sell your property to a specific person or entity and (c) the sale won't trigger a liability to pay part or all of the proceeds to a third party.
- **Local searches:** Often RPs don't hold much information on the planning history of their stock. Especially where you are looking to dispose of properties that are less than 25


Elad Yasdi
Partner
020 7880 4314
elad.yasdi@devonshires.co.uk


Aruna Sarwar
Partner
020 7065 1846
aruna.sarwar@devonshires.co.uk


Mark Foxcroft
Solicitor
020 7065 1861
mark.foxcroft@devonshires.co.uk


Kirsty Thompson
Partner
020 7880 4384
kirsty.thompson@devonshires.co.uk

years old, you should consider ordering local searches (or at least the more formal LLC1 part). These will identify planning agreements, planning and building regulation records, certain financial charges and enforcement notices against breach of planning. Advanced warning of these means that you can get ready for the inevitable questions that a buyer will raise and, if necessary, take action early to remedy problems or withdraw a property from the programme.

- Third party consents: If any of your stock is leasehold, the landlord's consent will often be required before transfer can take place. After going through the process of identifying and marketing your stock, the last thing you want is a delay caused by an uncooperative landlord. Any required consent should be sought at the earliest opportunity and the landlord's conditions for giving consent (if any) ascertained. The need to obtain third party consents doesn't only arise on leasehold transactions. Whilst less common, you do still need to look out for this on freehold property too.
- Removal of charges: If the stock is charged, you will need to arrange for the charge(s) to be discharged as soon as possible. You should consider whether this is to be done pre-exchange or post-exchange. If post exchange it would be usual for the agreement to be made conditional on the charge being released. Any charges should be identified early on, and lender requirements obtained in advance of exchange so that you can be sure that there won't be any issues when you need to action the release.
- Construction and planning: If you are transferring recently built properties, you will need to provide the Buyer with building warranty documentation (e.g. NHBC), planning permission sign offs, building regulation consents, evidence of discharge of section 106 obligations and, possibly, collateral warranties from the contractor and sub-contractors. No well advised buyer is going to proceed without seeing these. They can be surprisingly difficult to track down. So the earlier you start that process the better.
- Tenancy agreements: Whilst some buyers want to see all the relevant tenancies, most will proceed having just seen a sample. But remember this will be more than just the form of agreement you use today. On a long established estate you will often find that different tenants occupy under different forms of agreement dating back years. You will usually be expected to warrant that you have disclosed all relevant types – so it's important that you do your homework.
- Assets: You will need to compile an inventory of those assets that will form part of the sale and those which will be excluded. This can range from the cleaning equipment in the store cupboard of a single block to the desks, computers and the photocopier in an estate office. It goes without saying, so we'll say it – you need to check that you do actually own the equipment.
- Contracts: As we said, a stock rationalisation disposal is effectively the sale of a business. You will often have entered into various contracts in connection with that business, from cleaning the common parts through to security. It may be that these contracts can be novated or assigned to the buyer or they may have to be terminated on completion. That will depend on what the contract says, how cooperative the service supplier is and what the RPs want. As a start you will need to identify and review all the contracts to see what they say.

And another thing or two (or three)

Consultation: The HCA's Tenant Involvement and Empowerment Standard requires RPs to consult with residents if they are proposing to change their landlord. The consultation must clearly set out the costs and benefits of relevant options to the residents. This can be a stressful and confusing time for residents. Having your residents on board with a transfer will give you more confidence that the decision you have made in selecting the purchaser was the right one. Having residents in opposition is not where you want to be.

Employees: Transfer of Undertakings (Protection of Employment) obligations may arise in respect of employees employed in connection with the properties being transferred. If so, the procedure in the TUPE Regulations must be followed and the employment contracts for any transferring employees will transfer to the Buyer. As well as applying to your employees, there are also often arguments about the application of TUPE to employees of any contractor providing services to those properties.

Reputation: A stock transfer is, amongst other things, a transfer of people. Whilst the disposing RP may not be directly impacted if the incoming landlord fails to provide a great level of tenant satisfaction, you shouldn't underestimate the potential adverse impact on your reputation. If the disposing RP is seen as abandoning its tenants to something worse, there will inevitably be, at the very least, PR consequences. RPs should consider that whilst selecting a preferred bidder.

Do or do not- there is no try

To conduct a successful stock rationalisation programme, commitment is essential from the RPs project team. The project team should include representatives from housing management, IT, HR, finance, rent accounting and property services with a dedicated project leader of sufficient seniority in the organisation to be able to 'command' people to get things done. Large stock rationalisations can be all-consuming. RPs should not underestimate the resources they will need to dedicate if they want the programme to run smoothly and to time. The disposing RP should not expect its involvement to end on the day of completion. Post-completion issues including the transfer of records and rent arrears reconciliation will continue until around 3 months after the completion date. In many cases post-completion matters run beyond this.

The tiny print

Find out more

Neil Toner
Partner, Head of Real Estate
020 7065 1823
neil.toner@devonshires.co.uk