

Business and finance

Large association has 400 unsold homes amid 'massive market slowdown'

<https://www.insidehousing.co.uk/news/news/large-association-has-400-unsold-homes-amid-massive-market-slowdown-60249>

London's housing market has been stagnant for some time but with this story, Luke was able to bring to light a new way in which it is affecting housing associations.

He had spent the previous months assiduously cultivating contacts in the office of Emma Dent Coad, MP for Kensington, in order to cover the ongoing fallout of the Grenfell Tower fire.

Ms Dent Coad, after receiving complaints about the huge London housing association Notting Hill Genesis, asked for a meeting with chief executive Kate Davies.

Immediately after the meeting, one of her staff briefed Luke on everything that Ms Davies had said, including that the association currently had 400 homes sitting unsold, an unusually high number.

Luke spoke to other housing association figures, who told him this was part of a "massive slowdown" in the London housing market.

By speaking to the sector about the wider implications of this figure, Luke was able to write a story that didn't just reveal information about a very serious issue at one organisation, but also connected it to a wider problem for social landlords in the capital.

Ten thousand workers face threat of pension changes as deficit rises again

<https://www.insidehousing.co.uk/news/news/ten-thousand-housing-workers-face-threat-of-pension-changes-as-deficit-rises-again-58678>

This story was the result of Luke having regular conversations with actuaries working for the social housing sector. They told him they would be informed about the change in the deficit of the Social Housing Pension Scheme before it was made publicly available and agreed to tell him when it happened.

As a result, he exclusively revealed that the deficit on the scheme, which most housing associations are signed up to, had increased to £1.5bn, meaning social landlords would have to pay 50% more towards paying it off.

Experts provided Luke with exclusive data showing that around 10,000 workers in the social housing sector had defined benefit pensions with the scheme. Actuaries, meanwhile, told him that most housing associations would seek to close such pensions in response to the increased deficit.

As a result, Luke was able to report that the pensions of 10,000 workers in the sector were at risk as a result of the increase in the deficit.

Although this story initially seemed like one that only finance directors would be interested in, it ended up having direct relevance to thousands of people in the sector, providing vital information to *Inside Housing's* readers about their future financial security.

First Priority: the inside story of a housing association that almost went bust

<https://www.insidehousing.co.uk/insight/insight/first-priority-the-inside-story-of-a-housing-association-that-almost-went-bust-58864>

The story of private investors buying up homes for people with learning disabilities has been one of the biggest ongoing issues in the social housing sector for some time now.

Luke had reported on it before the regulator declared First Priority, a housing association signing lease deals with these investors, compliant. But it was this event that really got the sector's attention.

Luke's feature on First Priority and the unsustainable deals it signed up to with private investment funds was a forensic, in-depth account of exactly what went wrong that almost caused the housing association to become insolvent.

He worked hard to gain access to the investors, conducting challenging interviews and forcing one of them to admit that they had actually created First Priority to provide itself with investment opportunities.

Luke used these and conversations with anonymous whistle-blowers to build up a narrative of who did what when, and what went wrong.

He also used the Freedom of Information Act to obtain emails that showed huge shortfalls in tenants' rents causing a financial black hole.

This investigation was a crucial intervention in a major story that is not being told outside of specialist media but has potentially huge implications.

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Large association has 400 unsold homes amid 'massive market slowdown'

NEWS 22/02/19 7:00 AM BY LUKE BARRATT

Housing associations have warned of a "massive slowdown" in the London sales market, as it emerged that one large organisation currently has more than 400 unsold units on its books.



Picture: Getty

Sharelines

▶ Notting Hill Genesis has 400 homes sitting empty amid a "massive slowdown" in market sale in London, Inside Housing can reveal #ukhousing @NHGHousing

▶ Housing associations have warned of a slowdown in the London sales market, as it emerged @NHGHousing has more than 400 unsold homes on its books #ukhousing

Notting Hill Genesis (NHG) has 87 private sale and 319 shared ownership homes that are currently empty. Some of these homes have been the subject of offers and the association is hoping to convert others to rental units.

The London market is currently being hit by cautious buyers delaying purchases in the build-up to Brexit, over fears that a no-deal exit from the EU would trigger an economic crash.

An NHG spokesperson said: "The lack of clarity around Brexit is having a profound effect on the sales market, with people unsure about whether to buy at this stage, questioning what will happen to house prices and whether interest rates will rise."

Giant London association L&Q warned last month that a "downturn in the property market" would see it halve its anticipated surplus this year.

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Downturn: why is L&Q cutting its surplus in half and what does it mean for the sector?



Major builder reveals discount sale of 200 homes to associations amid 'uncertainty'

Geeta Nanda, chief executive of Metropolitan Thames Valley, told *Inside Housing*: "In London, if you look at resales, shared ownership, staircasing, new build shared ownership, we're seeing generally a slowdown.

"Market sale is that much worse. It's an incredibly quiet market at the moment and again, people are not committing. We're seeing a massive slowdown in terms of market sale."

One finance director, who preferred not to be named, added: "The tide's receding and people are being left visible."

An NHG spokesperson said that "the majority" of the 87 market sale homes are under offer and NHG is "interested in pursuing any avenue for converting [the 319] into rented homes".

The spokesperson added: "Our first-tranche [shared ownership] and private sales for this year are below target, but that is consistent with what the housing sector is experiencing as a result of challenging economic and political conditions. We are keen to explore all possibilities for how we could make these homes available for affordable housing."



The downturn is mainly being felt in the London market, although associations have also reported difficulty selling homes in parts of the South East.

However, Jon Lord, chair of Greater Manchester Housing Providers and chief executive of Bolton at Home, told *Inside Housing* this was not an issue in the North, adding: "Obviously, the big variable on all this is Brexit. But we're not seeing anything like what's in the South East and London."

Steve Douglas, chief executive of consultancy Altair, said: "Government needs to recognise that the new model for housing associations, which was significant amounts of cross-subsidy, doesn't work in a market downturn.

"If government wants to continue to sustain a building programme, it needs to now support housing associations in a counter-cyclical manner."

The NHG figures were revealed to *Inside Housing* after chief executive Kate Davies cited them in a meeting with Emma Dent Coad, Labour MP for Kensington.

Ms Dent Coad said the empty homes "demonstrate the risk involved for housing associations who decide to act as property developers".

Read more about Brexit



Brexit and the social housing sector: the key risks As the tortuous process of exiting the European Union approaches its denouement, the country remains in a state of uncertainty about what exactly is going to happen. *Peter Apps* recaps the key risks to the social housing sector

Downturn: why is L&Q cutting its surplus in half and what does it mean for the sector After L&Q revealed it is likely to cut its surplus by £158m this year, *Peter Apps* asks what this means for the financial model which has defined the housing association sector since 2010

What housing associations are doing to stress-test for Brexit With the UK's departure from the EU looming, *Luke Barratt* looks at what housing associations have been doing to prepare

Regulator writes to housing associations with no-deal Brexit warning The regulator has issued a warning to housing associations over the threat of a no-deal Brexit, outlining key risk areas including shortages of crucial materials, a housing market crash and difficulties accessing 'business-critical' data

Sector draws up contingency plans for no-deal Brexit The country's largest housing associations are putting in place contingency plans to protect the future of their organisations

How would the sector cope with a no-deal Brexit? As uncertainty around Brexit mounts and a no-deal looms, *Inside Housing* asks what it could mean for the housing sector

Current grant system won't work in a falling market The government needs to think again about grant to prevent housing association development from collapsing in a falling market, writes *Matthew Bailes*.

S&P would downgrade half its rated housing associations after no-deal Brexit The credit ratings agency Standard & Poor's (S&P) has said it will downgrade associations it rates if the UK leaves the European Union without a deal

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Ten thousand housing workers face threat of pension changes as deficit rises again

NEWS 19/10/18 7:00 AM BY LUKE BARRATT

Ten thousand housing workers could be transferred to less generous pension schemes following the announcement of further increases in the deficit in the sector's multi-employer pension scheme.



Sharelines

► Ten thousand housing workers could see their pensions changed to less generous schemes #ukhousing

Employers were this week told that the deficit on the Social Housing Pension Scheme (SHPS) will increase to £1.5bn, meaning employers will have to increase their contributions to pay it off by 50%.

The housing associations that will be hit hardest by the change are those with employees on 'defined benefits' schemes – pensions which pay a guaranteed amount on retirement. As well as increased contributions, they will see the cost of future benefits rise by 30%.

According to pensions experts, many housing associations will seek to avoid these costs by moving employees on defined benefits to defined contributions, which are calculated based on the amount paid in and are less generous as a result.

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Contributions to sector pension scheme deficit predicted to rise



Half of associations do not have plan for increased pension deficit, survey says



Sector pension scheme deficit rises to £1.5bn

SHPS data shared with *Inside Housing* by XPS Pensions Group shows there were 10,025 employees with defined benefit pensions in September, but this is thought to have fallen slightly below 10,000 since then.

A source familiar with the SHPS valuation told *Inside Housing*: "It's a watershed moment. Without any action or innovative thinking from employers, almost every employee will be in the DC [defined contribution] section in three or four years' time."

section in three or four years' time.

At the last revaluation three years ago, the deficit increased to £1.3bn and associations were asked to pay more to reduce it to £1bn.

Despite these increased contributions, however, a fall in the 'discount rate' used by actuaries to calculate the values of pension schemes has led to the increased deficit at this latest valuation by TPT Retirement Solutions – formerly known as The Pensions Trust – which manages SHPS.

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Housing associations have some flexibility within SHPS to keep employees on defined benefits but ask them to pay more, or change the benefits to which they are entitled.

Experts, however, told *Inside Housing* that most employers would shift employees from defined benefits to defined contributions.

Steve Simkins, pensions director at KPMG, told *Inside Housing*: "Employers have got to decide whether they're going to bear the cost or share the cost, or make benefit change. Benefit change could be to a less generous benefit structure or to defined contribution."

Chris Mapp, head of social housing at XPS Pension Group, added: "The majority still do [have defined benefit pensions] and quite a few still offer it to new employees, but I suspect that after this valuation, that will be pretty rare, and there will be a significant number of employers that decide as a result of these figures to terminate defined benefit accrual entirely."

Richard Soldan, partner at consultancy Lane Clark & Peacock, agreed, saying: "I think the trend is towards stopping defined benefits and providing defined contributions. That's certainly been the trend over the last few years and I think this will be the catalyst that will prompt a lot of associations to take that step as well."

Unions, however, reacted negatively to the news. Siobhan Endean, national officer for the sector at the union Unite, told *Inside Housing*: "Unite will resist any changes that individual social housing organisations attempt to make to their pension schemes if it will result in a detriment to our members."

"Pensions are deferred pay and members will not stand idly by if their employer is intent on cutting their retirement income."

John Gray, branch secretary of the housing association sector for Unison, added: "I'm making a general plea for people to stop and step back. Let's talk about this. I've got lots of members in my Unison branch who are members of the scheme. It's really important to them and their future."

"The whole yardstick for measuring the cost of liabilities in pension schemes is broken and loads of schemes have been closed down prematurely for no reason whatsoever."

How will this affect me?



If you're a social housing worker on a defined benefit pension within the Social Housing Pension Scheme, it's as likely as not that your employer is one of those which will seek to move to defined contributions.

According to Chris Mapp, head of social housing at XPS Pension Group, it is almost certain that this will result in the housing association paying less into your pension, whether this means there is an overall fall in the total contribution or just a rise in the percentage paid by you.

But the main difference, Mr Mapp says, is that where with a defined benefit pension, the risk falls on the employer, with defined contribution, the employee bears the risk.

With a defined benefit pension, an employer guarantees the amount that will be paid out at the end. If the investments made by the pension scheme fail to deliver that amount because of a downturn in the market or something else, the employer makes up that shortfall.

With a defined contribution pension, however, no specific pay-out is guaranteed. Instead, the only thing that is fixed is the amount the employer contributes to it. Therefore, the employee is the one subject to the vagaries of private investments.



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A Tattershall 07-Jan-2019

we were forced to accept our pension moving from defined final salary to defined contribution - if we did not accept then we were faced with dismissal and re-employment - no choice if you wanted to keep your security of employment.

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Regulation

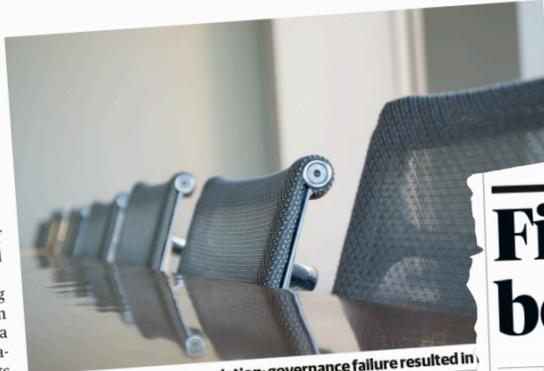
Fundamental failure of governance' at provider

Regulator appoints new board members at specialist association

Sophie Barnes

A housing association that provides homes mainly for adults with learning disabilities or mental health problems has a "fundamental failure of governance", the Regulator of Social Housing (RSH) has concluded. The RSH put First Priority Housing Association (FPHA) under review in January and has now published a report which states that the association does not meet the requirements for both the governance and viability standards.

FPHA leases properties with 26 landlords and the regulator said the association is dependent on the goodwill of these landlords in relation to rent payments, which indicates a "fundamental failure of governance". The regulator has appointed new



First Priority Housing Association: governance failure resulted in board members for the association.

FPHA does not have "sufficient working capital" or the capacity to meet its debts when they fall due, the regulator found. The association has failed to get access to secure liquidity "because it continues to trade on the goodwill of its creditors and lender to its financial problem". The regulator also has concerns about FPFA's governance.

larity the adequacy of resources and the skills and capability of the board to maintain effective control of the organisation".

FPFA manages properties for Funding Affordable Homes, which recently became a real estate investment trust (REIT) and has borrowed money from Henley Investments,

First Priority opens books to landlords

Association fails to meet governance and viability requirements

Luke Barratt

A housing association found by the regulator to have a "fundamental failure of governance" has shared details with its creditors on how their housing portfolios are performing.

First Priority Housing Association, which has more than 700 tenants, was put under review in January, with a report from the Regulator of Social Housing (RSH) recently finding that it does not meet its requirements for governance or viability.

Following the regulator's notice, First Priority told *Inside Housing* it had provided all its creditors, or landlords, with performance details of their respective portfolios.

The RSH found that the association does not have "sufficient working capital" or the capacity to meet its debts and it "continues to trade on the goodwill of its creditors". It is understood that the regulator has appointed three new board



Details shared on housing portfolio

members at the association. According to data from the RSH, First Priority owns no properties itself. Rather, it leases homes from its creditors.

One landlord told *Inside Housing*: "We would hope that the business is robust enough for us to be able to move forward without doing anything. But that's going to come out in the wash in the next few weeks, with the questions that the [new] board members are going to be asking."

The association leases properties from 26 landlords, but *Inside Housing* understands that five of these own the majority of the stock that First

HCA urges caution over REIT deals

Social landlords should balance risk and reward carefully, says HCA

Luke Barratt

Housing associations should be aware of the risks involved in taking money from real estate investment trusts (REITs), the Homes and Communities Agency (HCA) has said.



Mr Walters: stress testing is crucial

comes into effect, associations could struggle to pay.

This policy is combined with the fact that the rent cut - which came into force for social housing in 2016 and supported housing in April this year following a year-long exemption - is currently driving rents down.

Jonathan Walters, deputy director for performance and strategy at the HCA, told *Inside Housing*: "Anything that's got any form of index-linked returns is going to be subject to the complexities of government welfare policy. We would always have concerns if people had too much index-linked finance in their portfolio

because as we have now seen, rents don't always go up with inflation.

"Rents are actually going down. Therefore if you've got index-linked finance, that finance is becoming more expensive every year because your rental stream is going down but your interest costs are going up. Investors and borrowers should think about how long the government will pay inflation-linked returns on the welfare bill."

The associations that have been involved with REITs so far have typically been smaller organisations. Mr Walters stressed the importance of business expertise for associations engaging in these transactions, many of which would have been subject to HCA approval before deregulation came into force earlier this year.

He added: "Boards need to understand what it is they're taking on and what happens in a stress situation. How will having this form of debt affect their organisation, and their ability to cope with distress? If they've got a grip of that and they can stress test it, that gives us a lot of confidence that they understand the risks and can manage them."

FIRST PRIORITY: A CAUTIONARY TALE

When a small supported housing provider entered into a series of leasing deals with investment funds, it nearly spelled disaster for its vulnerable tenants. Luke Barratt picks over the bones of the First Priority saga and asks what lessons the sector must learn

It's March 2018 - fund managers and private equity investors are heading to a crunch meeting with a housing association on the brink of collapse.

At stake are the homes of 759 of the UK's most vulnerable adults, including many with learning difficulties, brain injuries or physical and mental disabilities. If things go wrong, warns one investor, these people could be "out on their ear".

How did we get here?

The story of First Priority Housing Association, censured in February by the regulator for "a fundamental failure of governance", is on one level the story of a small social landlord that got into deep financial trouble. But it is also a cautionary tale of the potential risks attached to a new kind of social housing investment.

At first glance, this model is disarmingly simple: private equity funds amass large portfolios of supported housing and lease them to housing associations, who then pay a monthly

return to the fund, which usually targets a yield of over 5%.

But simple doesn't necessarily mean safe. These funds invariably ask housing associations for lease payments linked to inflation, meaning they are unpredictable and could increase dramatically.

"You take on a lot of future risk," explains Bruce Moore, chief executive of large supported housing association Housing & Care 21, which has not struck any of these deals. "You lose the flexibility around future rent uncertainty or change of use or funding arrangements."

To date it has typically been small associations which have used this type of structure.

The homes are usually found by 'aggregators', who package them together and sell them to investment funds, usually taking around 1% of the purchase price as their payment.

Once sold in this way, supported housing becomes extremely valuable. One developer tells *Inside Housing* he

was offered £22m for a portfolio he said was worth £15m purely because the homes had long leases on them.

With investors demanding guaranteed returns, rents tend to be well above average, although they are usually lower than the cost of staying in a care home.

According to a recent data release from the Regulator of Social Housing (RSH), First Priority charges an average tenant £190.15 a week, more than double the English average for supported housing of £93.08.

Where it began

According to Guildford Council, one of the 88 authorities in which First Priority operated, First Priority received advice from a financial advisory firm to set its rents.

These rents, of course, are paid by local authorities through housing benefit. Solihull Council, another place First Priority operated in, tells *Inside Housing*: "When organisations charge high rents to those living in

supported housing and they subsequently need to claim housing benefit from the council, this can place significant financial pressure on the authority."

First Priority was set up in 2011 but the company fell dormant soon after.

To understand how it got involved in these deals, and how it eventually backfired, we have to rewind to 13 July 2012, when brothers Omar and Ryan Al-Hasso founded Henley Healthcare Investments (HHI).

The company does not call itself an aggregator, but does package supported housing units with leases and then sells them to investment funds. Many of the leases on the properties Henley sourced were with First Priority. A year after founding HHI, Omar Al-Hasso joined the board of First Priority, staying there for two years.

So did Mr Al-Hasso join the board specifically to create investment opportunities for HHI? And if so, does this represent a conflict of interest?

Andy Brandon, managing director

of HHI, says not.

"I'm pretty sure that even before he came to Henley, Omar had created First Priority with this idea in mind that the long-lease model might exist," he tells *Inside Housing*.

"Although with retrospect, you can look back and say 'conflict of interest', another way of looking at it - probably the right way of looking at it - is that this is how you need to make it work. Because you're not likely to get to any completely third-party housing association and say, 'Do this model'. We had to create something, and I think Omar was instrumental in creating the model in the first place."

Mr Brandon says that Mr Al-Hasso left First Priority's board "very quickly" after HHI started trading with the housing association, although another investor tells *Inside Housing* that he retained 'observer status' on the board, meaning he could not vote but still attended meetings and discussed decisions.

John Higgins, chief executive of

First Priority, insists: "Where the leases involved Henley, Mr Al-Hasso was not involved in the decision-making to avoid a conflict of interest."

Not everyone is as relaxed about Mr Al-Hasso's role.

Mr Moore comments: "Governance arrangements are crucial and it is important to ensure that these provide clear accountabilities without inherent conflicts of interest."

Problems started

First Priority began leasing homes from HHI in 2015 and, later, from other investors. One tells *Inside Housing* that no conflicts were declared when it bought its portfolio of homes.

The main funds buying these homes were Civitas, Equitix, Funding Affordable Homes (FAH), Henley Secure Income Property Unit Trust, and Supported Living Infrastructure Limited (SLIL).

Many of these investors do not make public the details of their deals, so it is difficult to track their involve-

"You can say 'conflict of interest', another way of looking at it is: this is how you need to make it work."

ment with First Priority over time.

One investor, however - Civitas - does share details. It launched in November 2016 and struck its first deal on 15 December that year, with First Priority. It then spent much of 2017 making further deals with the association, which would become one of its biggest counterparties.

It was near the start of 2017 that First Priority's problems began behind the scenes. It contacted HHI asking for a £2m loan, which it granted. The money was needed, it seems, chiefly because of problems with property management and rent collection.

"First Priority's board and [man-

agement company] BMA had managed these properties extremely poorly," recalls one investor.

"There were payments being made to us, which were the correct payments, but they weren't backed up by the collection of money from the underlying properties."

First Priority had also, the investor says, fallen behind on repairs, and although it had done fire risk assessments on its homes, it had not carried out the necessary work after those assessments.

Another investor claims that BMA "hadn't been collecting rents that were due, hadn't been pushing through rent increases, or claiming from housing benefit, [it] hadn't been - in some cases - actually claiming housing benefit, or not putting in the claims which meant they were time-barred".

Just as importantly, First Priority's void rate had risen to 26.5%, far above the English supported housing average of 4.7%. ▶

First Priority hires rescue advisory firm

First Priority, the housing association censured by the regulator for a "fundamental failure of governance", has hired special advisors to review its finances.

The association has appointed corporate rescue specialist Traynor, which advised Ujini: that association's difficult consultancy firm Grant Thornton internal advisors.

First Priority, which has 700 tenants - all with learning or mental health difficulties - these advisors will conduct of the association's financial due course".

"We want to present a robust plan to lenders, landlords that has been subject to scrutiny by external professional First Priority spokespeople."

A spokesperson for First Priority added: "We have initiated a robust plan to present a robust plan to lenders and landlords that has been subject to scrutiny by external professionals. This is a standard in these matters. These directors are confident and ongoing."

REIT warns of First Priority repeat

Fundamentum director says further governance failures are likely

Luke Barratt

A newly launched social housing real estate investment trust (REIT) has predicted at least one more organisation will run into difficulties like First Priority.

Speaking to *Inside Housing*, Christian Forbes, managing director of Fundamentum Property, said he believed another housing association would end up in the same situation as First Priority.

First Priority has had two board members replaced by appointees of the Regulator of Social Housing, which criticised it for a "fundamental failure of governance".



First Priority: "failure of governance"

I think there will be another First Priority? Another board seized? Yes, absolutely.

"We know the government is trying to regulate housing associations better. It wants to make sure they're financially viable. As an investment advisor, it would be foolish to think that because it's happened once in the past that it won't happen again."

First Priority strikes deal with creditors

Struggling housing association First Priority has declared "business as usual" as it struck a deal with its creditors, *Inside Housing* can reveal. The association's creditors have agreed to a company voluntary arrangement (CVA), a procedure that allows an insolvent company to pay its creditors over a period of time.

First Priority had been struggling with its finances, with the Regulator of Social Housing criticising it for a "fundamental failure of governance" in February.

The regulator said it did not have "sufficient working capital" or the capacity to meet its debts and it "continue[d] to trade on the goodwill of its creditors".

"We have worked hard to ensure that all our tenants keep their homes within our sector." John Higgins, chief executive, First Priority

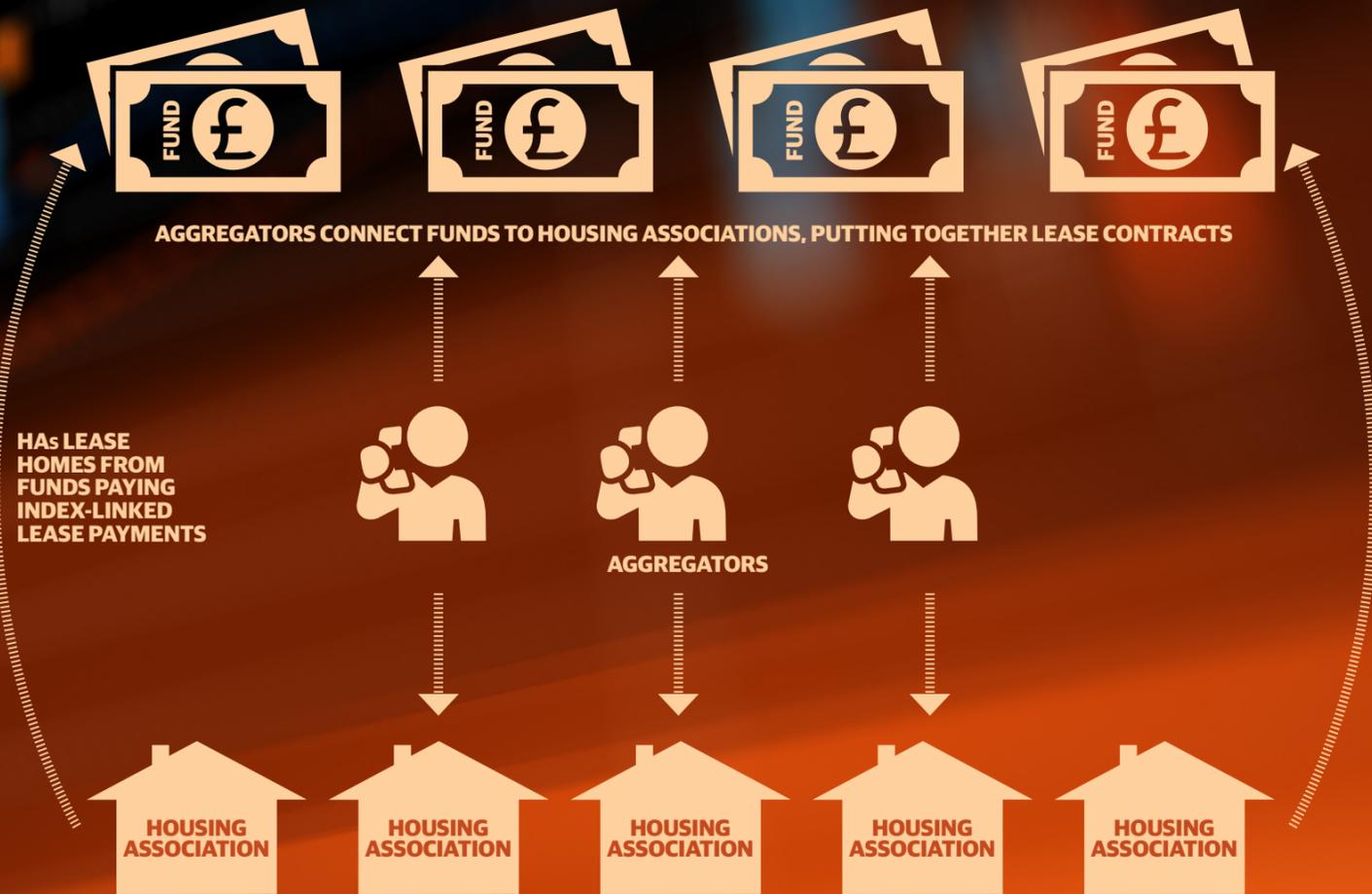
It does not own any homes itself but leases them from city investors, usually at inflation-linked rents.

At the time of the seizure it had 700 tenants but since then investors, including the real estate investment trust Civitas and the investor Funding Affordable Homes, have transferred their leases to other associations.

The remaining landlords and creditors have now voted to allow a CVA, enabling the organisation to remain in a more robust financial position.

John Higgins, chief executive of First Priority, said: "Our tenants are our number one priority and our ongoing focus is now on providing a high-quality service to them. We're working with a number of in-house maintenance technicians and housing managers across the UK to ensure a high standard of repairs."

A MODEL OF HOW THE DEAL WORKS



One investor describes this as the "number one" problem. He adds: "They simply failed to bring enough money in."

Paul Bridge, chief executive of Civitas, confirms the problems were "around the collection of rent and obviously the collection of void payments".

There was a voids insurance policy to cover some of these, while for those it didn't cover, BMA was supposed to invoice the care provider. According to one investor, BMA never did this.

Jonathan Walters, deputy director of strategy and performance at the RSH, highlights voids as the key to the problems at First Priority: "If a business' void rate is 30% to 35%, you simply cannot manage a cashflow-based lease business with 35% void rate. You simply can't do that. When we talked about 'a fundamental failure of governance', that's what we were talking about. You've entered into a lease for 30 years say, that's going up at CPI+1 [Consumer Price Index plus 1%], so

your lease payments are going up all the time. But if you're not collecting rents, you can't afford to meet that lease payment."

Uneconomic decisions

As for what drove such unusual levels of voids, Mr Walters' assessment is equally damning. "Some of the properties seemed to be in poor condition and First Priority had to work hard to ensure they met their commitments."

When contacted for comment, BMA tells *Inside Housing* it has signed a non-disclosure agreement and cannot discuss its work for First Priority.

Some investors are keen to blame BMA for all of First Priority's problems, but Mr Walters says that doesn't give the full picture: "Fundamentally, what undid the business was that some of the leases were probably ultimately uneconomic."

He adds: "One of the issues with First Priority was that it went from something like 50 to 60 units four

years ago to, by the time they ran into problems, over the 1,000-unit limit.

"Managing a business growing that fast is very difficult. If you haven't got the right policies and procedures, you might end up signing poor leases that aren't economic for you."

Funds such as these need to deploy capital quickly to provide the dividends their shareholders expect. But the small housing associations that act as counterparties can be ill-prepared for such growth. This can lead to the problems that First Priority encountered.

Last summer BMA was replaced as property manager by a subsidiary of First Priority called First Priority Property Management Services, since renamed Myshon.

In November, Mr Brandon remembers: "I got a call from John Higgins saying, 'We need some more cash'."

HHI put in another £2m to help fund Myshon's efforts with the management problems, but they seemed to persist. An email to Ashfield Dis-

trict Council, seen by *Inside Housing*, reveals that housing benefit payments to one tenant were leaving a shortfall of nearly £200 a week.

In January this year, the investors were told how bad things truly were. Mr Higgins tells *Inside Housing* that it was only in January that he and the board realised that there were some leases "where the lease rent was unsustainable at full occupation".

In other words, even with all the properties filled, First Priority still wouldn't have been able to afford its payments to the fund.

Why, one might wonder, would either party sign up to a lease so obviously destined to fail?

The middleman, whoever that was, would still benefit, whether by taking a 1% commission or selling the homes on at a profit.

Mr Brandon explains the January situation: "At that point, it became a bottomless pit. It wasn't a question of putting cash in to fix a short-term cashflow hole. It was a structural

problem it had with making losses that there was no point us trying to plug with short-term cash, because it would have just re-appeared."

Another investor adds: "It came as a complete bolt out of the blue, partly because we'd just received a payment." That January payment turned out to be the last to the investor.

Civitas also tells *Inside Housing* that it had received all rents in full from First Priority as of 31 January.

In February, Mr Walters recalls: "John Higgins phoned us up and said, 'We've got a problem'." The regulator sent its enforcement team in immediately, with those close to the situation soon fearing the worst.

Accepting the pain

First Priority appointed insolvency specialists Begbies Traynor, which quickly realised that its best hope was to reach a company voluntary arrangement (CVA), which would mean creditors accepting that payments would not be on time, and

First Priority paying only what it was able to.

Mr Brandon comments: "From where we were in March and how things were looking there, it was very uncertain. We had no idea that they could land or we could land a CVA."

It was at this point that investors, the regulator, HHI and First Priority locked themselves into a meeting to hash out a solution.

"Luckily all the landlords, ourselves included, accepted the pain that meant and it meant pain for everybody," Mr Brandon relates.

"But the result of that was in many respects a soft landing versus what could have happened if [investors] and we had not played ball and had gone into an insolvent situation."

For tenants, that pain could have seen them lose their homes.

Meanwhile with lease payments not coming in, some investors wanted out.

In May and June, Civitas, SLIL and FAH all transferred their properties

"What undid the business was that some of the leases were probably uneconomic."

to other small housing associations. The remaining creditors agreed to a CVA in July after negotiations, with all of them accepting reduced payments. Mr Brandon explains the current situation: "First Priority is in a limbo state. They are effectively collecting housing benefit and passing it through to the [investors] that stayed with them."

For First Priority, the storm may have abated but the story of lease-based supported housing is far from done.

The regulator has written to 30 housing associations with similar business models warning about "conflicts of interest" and the impor-

ance of "stress-testing".

It is also currently investigating four of them for possible breaches of its standards on governance and financial viability: Trinity, Inclusion, Westmoreland and Encircle.

Figures from the regulator indicate that the first three of these charge rents significantly above the average, just like First Priority.

Westmoreland has a void rate of 35% and Inclusion has 25.7%, according to the regulator - both are worryingly high. Trinity and Encircle did not provide a figure. One investor calls voids the "number one" problem at First Priority, and so it is difficult to ignore these numbers, though Neil Brown, chief executive of Inclusion, says they reflect "healthy growth" and Westmoreland said it was working on reducing this.

The regulator will issue judgments on those four housing associations soon. After that, the sector can judge for itself whether deals like this are worth the risk. ■