

## LEGAL STRUCTURE AND ANALYSIS

### PURCHASE AND REPAIR SCHEME

Step <sup>1</sup>	Explanation of Step	Analysis <sup>2</sup>
1	<p>If selected by the Authority, Mears enters into a contract with the Authority. This contract takes the form of a “Master Agreement”. Through this agreement Mears and the Authority commit to entering into a tax transparent Limited Liability Partnership once financial arrangements are in place for the purposes of acquiring and repairing properties which will be made available for rent.</p>	<p>No tax or accounting consequences anticipated at this stage.</p> <p>A limited liability partnership is most tax efficient for the Authority as it does not bear any Corporation Tax on net profits of the venture.</p> <p>The parties will take detailed tax advice prior to legal commitments being entered into.</p>
2	<p>The joint LLP is formed as a deadlocked vehicle so neither party has overall control. The parties enter into a limited liability partnership agreement which has been pre-agreed by lawyers for the parties based on sound principles of management and corporate governance and building in protections for the Authority that it has a veto on all decisions.</p>	<p>Care needs to be taken to keep the vehicle off the balance sheet of the respective members. Mears may utilise a charity to hold its 50% stake. The Authority may wish to use a separate</p>

<sup>1</sup> Steps correspond to annexed Structure Chart

<sup>2</sup> This explains any tax or accountancy points or the rationale behind the step.

The parties nominate equal board members to run the vehicle and will adopt business plans and protocols to manage risks and procurement strategies in keeping with best practice.

entity such as its pension fund to hold its stake but this is a matter for the Authority.

**3** The parties sign an Acquisition Agreement. This sets out pre- agreed acquisition criteria for housing units to be acquired including mix, location, condition, outline specification and number. Any specific concerns on type of housing are factored in.

The Authority will have input into the criteria based on its desired locations and strategy.

The Acquisition Agreement contains a process by which Mears forms a team to arrange the acquisition of units for the LLP and seeks input from the Authority before final sign off. An independent RICS surveyors report is obtained prior to each acquisition to verify condition, required works and anticipated costs. A RICS Red Book valuation will also be procured to provide the LLP with assurance that the portfolio meets investment requirement and good value is being achieved in the purchasing.

We are conspicuous of the issues created by acquisition outside of Brent and the relationships with the “host Borough”. We will look to mitigate impacts for that Borough and within the scheme source reciprocal access to property without affecting Brent’s risk management or objectives in securing the required number of units.

Against an agreed Schedule of Rates Mears Ltd will undertake the required improvement works to meet standard. Mears will undertake, through a KPI regime, to achieve the required works to the budget and complete works in the timescale required. Average Costs for improvement works is £15,000.

As part of Mears due diligence in approaching this requirement we have undertaken comprehensive market research. This includes current property price and volumes from local agents and marketing portals such as Zoopla and Rightmove. We have also used Hometrack data of the actual number of transactions and values achieved in the ley markets to assure

ourselves there is sufficient property on the market to the desired mix in the areas required. Within the model we have allowed for annual house price inflation on acquisition costs each year of the programme.

**4** Mears arranges finance for the LLP by way of a bond issued by the LLP to reputable financial institutions through a bank “Lead Arranger”. The bond finances the purchase of housing in waves through the Acquisition Agreement. Funding documents are entered into with the purchasers of the bond. These tend to be standardised in nature and prepared by the Lead Arranger.

The LLP will bear stamp duty land tax on each acquisition and claim Multiple Dwellings Relief to pay a rate of 1%.

The financing costs are all incorporated within the financial model.

The legal documentation signed by the Authority contains a financial model which shows how the bond is repaid through rental receipts which are paid up to the LLP and then on to the bond “note holders”.

**6** The Bond will be a fixed coupon at Gilts plus risk margin priced at time of issuance. The covenant will be viewed as Local Government type risk.

The Model attached has a number of contingent pricing and risk management factors; rent, inflation, coupon, lettings/acquisition plan. All of these factors are to be discussed with the Authority.

Annual inflation on the coupon will be required. We will seek a fixed rate rather than accept volatile RPI/CPI risk. A significant issue is the current freezing of LHA for the next four years as announced in the last budget. There are a number of ways in which we can manage this issue. The attached model shows no rent inflation during the first four years and a higher (2.5% assumption) rate thereafter rather than the 1.3% to 2% from year one. This mechanism is open to negotiation with the investors and will be agreed between the JV partners (Mears Ltd/LB Brent)

The model allows for a Debt Service Cover Ratio of 115% and a 6 month Debt Service Payment to be held in reserve within the JV. The model also shows surpluses being generated against adverse property issues during the term and to manage Exit.

5	<p>Upon purchase Mears will arrange refurbishment of the units to an agreed standard prior to tenants commencing occupation.</p>	<p>A specification is appended to the documentation so that the Authority can ensure that the units are to a required standard prior to letting.</p>
6	<p>The Authority has full nomination rights on the units (unless it is agreed to offer to a third party or in the market for private rents) through a nominations agreement. The Authority will be liable for payment of rent where it is unable to provide a successful nomination to a property after an agreed period (14 days from ready to let).</p>	<p>The Nominations Agreement mirrors standard LA documents. The JV will have an escalation process for seeking tenants to cover any void periods where a nomination is provided to mitigate this risk; market rent, host Borough nomination.</p>
7	<p>Mears arranges for it's not for profit Registered Provider, Plexus, to manage the units through the term of the finance. Plexus signs a 20 year lease to manage and maintain the units and, after the expiry of the lease, agrees to enter into a management agreement for the remaining term of funding with agreed key performance indicators which mirror those in the lease.</p> <p>Plexus will grant leases to those nominated by the Council and this process discharges the Authority's legal duty in respect of any persons nominated from the temporary accommodation list. No rights to buy will accrue to those tenants due to the statutory</p>	<p>Plexus will receive income for the provision of services through a management fee which is modelled as a percentage of rental receipts from tenants. The balance of rent receipts (after deduction of an agreed percentage of maintenance, voids and bad debts allowances, are payable to the LLP to allow the LLP to service its debt to the bond holders.</p>

exemptions.

Stamp duty will be suffered on the lease to Plexus but the lease arrangement avoids the LLP incurring large irrecoverable VAT charges which would otherwise create excessive tax costs for the project.

- 8 At the expiry of the finance, the LLP owns the housing stock. The parties can decide whether to sell the units, refinance them to release capital or merely continue to rent the units and keep the net income. Mears stake is intended to be held for charitable purposes so it cannot use any asset value to distribute to shareholders, creating a benefit to the community.

**Annexure: Structure Chart**