

## **Overview of Encumbrance for New Supply with Capital Grant Service Agreement**

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### *Rationale and background*

1. Where MSD provides up-front development funding to Providers to increase the supply of public housing and support the growth of Providers, it requires an adequate level of reassurance that the relevant Properties will remain available for public housing.
2. In the context of the Transfer transactions in 2016 and 2017, encumbrances were thought to best support the Government's bottom line that Tenants in Properties that are sold will continue to be housed for the duration of their need, and that people who need housing support can access it. In particular, an encumbrance requires the Provider to use the Property in accordance with the "purpose" as set out in the encumbrance (which includes public housing and any other purpose agreed by MSD).
3. In the context of the New Supply Development Funding and Capacity Services Agreement (the **New Supply Services Agreement**), it is important to MSD that the Properties in respect of which it is providing up-front funding are continued to be used for public housing for the term of the New Supply Services Agreement.
4. MSD considers that encumbrances provide the most practical and least disruptive mechanism to secure this obligation in respect of the Properties. An encumbrance is a very common instrument for a third party to register an interest on the title of a property, and MSD views it as the most appropriate instrument.

### *Why is an encumbrance required in addition to the New Supply Services Agreement?*

5. Although the Provider has a contractual obligation pursuant to the New Supply Services Agreement to provide the Property to MSD for public housing purposes, if the Provider were to sell the Property in breach of that contractual obligation and/or it was let to a private tenant in breach of the Services Agreement, in the absence of an encumbrance over the Property, MSD would have no way to subsequently require the relevant Property to be used for public housing.
6. By registering an encumbrance in respect of the Property, even if the Provider were to sell the Property and/or it was let it to a private tenant in breach of that contractual obligation, the encumbrance would run with the land and would provide MSD with specific enforcement rights against the new owner or relevant landlord that the property be used for public housing.

### *How does the encumbrance relate to a bank's mortgage?*

7. The encumbrance will rank in priority to a bank's mortgage. There will be a separate Financier Direct Deed which regulates the position between the bank and MSD, and which acknowledges that the bank has security over the relevant Property, but that the encumbrance ranks in priority to the bank's mortgage.
8. Due to the diversity of commercial arrangements, MSD has not developed a "standard" Financier Direct Deed as it considers there will be a spectrum of Financier Direct Deeds. These could range from a short-form letter agreement in the case of small scale New Supply Services Agreements (where (if relevant) MSD would acknowledge the bank has security over the New Supply Services Agreement if the bank has a

General Security Agreement in relation to the Provider), to more detailed and bespoke Financier Direct Deeds for larger scale New Supply Services Agreements.

9. MSD expects the Financier Direct Deeds for larger scale New Supply Services Agreements to acknowledge that in the event the Provider is in breach of the New Supply Services Agreement:
- the bank will have the ability to step-in and appoint an appointed representative (subject to certain criteria), who will assume the rights and obligations under the New Supply Services Agreement;
  - the appointed representative will have the ability to novate the New Supply Services Agreement to a suitable substitute entity, ensuring that the services relating to public housing continue to be provided;
  - if a novation is not possible, and following an unsuccessful formal sale process, MSD will have the ability to arrange an acceptable public housing outcome; and
  - if MSD is unable to arrange an acceptable public housing outcome, MSD can terminate the New Supply Services Agreement and MSD will remove the encumbrance.,