



TURNING THE KEY ON A NEW CARE HOME

IT IS COMMON FOR CARE HOME OPERATORS TO WANT TO EXPAND THEIR PORTFOLIOS WITH NEWLY CONSTRUCTED BUILDINGS. ONE ATTRACTIVE WAY OF DOING THAT IS FOR THE OPERATOR TO TAKE A TURNKEY LEASE OF THE NEW HOME FROM A PROPERTY DEVELOPER. JAMES ATKINS CONSIDERS THE FUNDAMENTAL CONCERNS FOR CARE HOME OPERATORS TO BE AWARE OF WHEN ENTERING INTO A TURNKEY CONTRACT.

A turnkey property is one constructed by the developer to an agreed timetable and handed over to the operator in a ready to use condition. A turnkey care home would be fully fitted out to the operator's desired specification and linen, furniture and crockery will often be provided as well. The operator simply turns the key and is able to run its business from the home.

NAVIGATING THE AGREEMENT

The principal advantage to the operator is that they get a ready to use home fully fitted out and operational to its desired specification. In return, the developer gets a tenant legally bound to complete a new lease for a lengthy term (usually 25 to 30 years) at a rent sufficient for them to secure funding for the development and turn a profit.

There are three basic but fundamental concerns for care home operators entering into agreements with developers for the construction of new homes. It is usually vital that the operator gets the building it wants; at the time that it wants it; and at the price that it has agreed to pay for it.

To maximise the chances of satisfying those three criteria the operator needs to take great care in agreeing the terms of the agreement for lease. It is that



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→ document that will set out the parties' obligations through the planning stage of the development and while the building is being constructed.

AGREE THE SPECIFICATION

The Specification and Planning Application is a very important part of the process. The developer should be placed under an obligation to build the home to an agreed specification and in accordance with an agreed form of planning application. The specification should be detailed enough to cover all elements of the build and fit-out.

It is advisable to limit the developer's ability to vary the specification as far as possible. They will want the right to vary materials and where such variations are immaterial then that is acceptable, but the operator should always be sure that the appearance, layout and quality of the home are unaffected. In general variations by the developer should only be allowed with the operator's consent.

The operator may also wish to vary the specification and should be allowed to do that as long as it does not make the development more expensive to build and fit-out. The overall contract period could be up to three years and so the operator's standard specification may change before

the building is completed. Those changes should be allowed. There should always be an over-arching obligation on the developer to build in a manner that will allow the operator to obtain its Care Quality Commission certificate (in fact, completion of the lease should be conditional on the certificate being obtained).

CONFIRM BUILDING OBLIGATIONS

The developer should be under an obligation to build the new home properly and using good quality materials. The building work should be carried out in accordance with current good practice, building regulations and the planning consent and the operator needs to reserve the right to inspect the build as it is going on and serve notice on the developer of any defects.

The operator should also, where possible, ensure that it has some say in the identity of the main contractor and the agreement for lease should set out the fundamental terms on which the contractor will be engaged. There should also be an obligation on the developer to appoint proper and reputable companies to the professional team and ensure that each of them has an adequate level of insurance cover.

The developer should be required to enforce the defects liability provisions in the



building contract to make sure that the building is handed over in good order and, where possible, snagging items should be properly remedied within two months of practical completion of the building.

The lease will almost always place an obligation on the operator to repair the property and that will come into effect when the lease is granted. It is therefore imperative that the operator has some sort of protection against responsibility for repairing build defects. It would be preferable to expressly exclude such liability from the terms of the lease and the operator should always take



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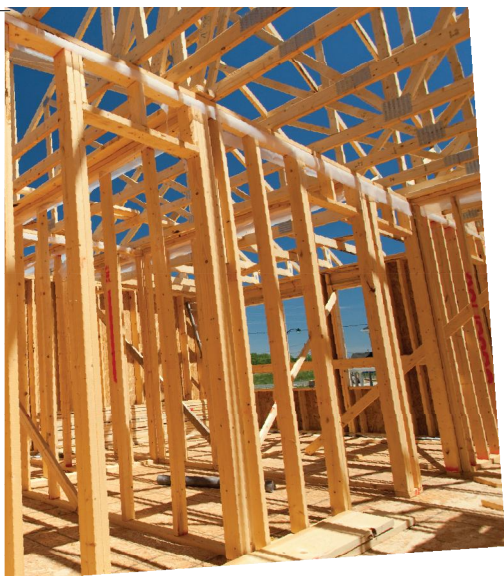
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collateral warranties from the lead contractor, architect and other members of the design and build team so that it can sue them directly in the event of any breach by them of their obligations arising from the construction.

The first step for the developer will usually be to obtain planning permission for the new building. They should be placed under a number of general obligations to deal with that application promptly and keep the operator informed of developments. The parties should agree a longstop date after which, if the developer has not obtained the planning permission, either party can

terminate the agreement. The operator will need to decide whether or not that long stop date should allow for an appeal against a refusal to grant planning permission or for judicial review of an approved application.

The parties should then agree a target completion date and the developer should be required to complete the building prior to that date. The circumstances in which the target completion date can be delayed should be limited as far as possible. The operator should also have the right to terminate the agreement if the target completion date is not met (unless one of the limited extension circumstances applies). That should operate as an effective incentive for the developer to complete the building on time but if it is possible there should also be some other penalty on the developer for missing the date, such as an extended rent free period for the operator on completion.

CRUNCH THE NUMBERS

The rent for the property will normally be agreed prior to exchange of the agreement for lease as the developer will need to show a definite income stream to its lender. If the rent is calculated by reference to the number of bedrooms then it is important that the number is fixed either by the planning application or the wording of the agreement.

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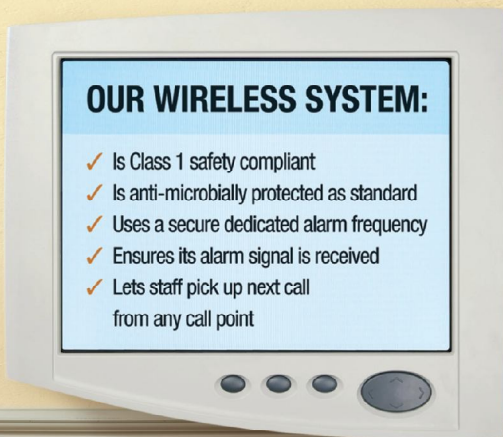
If, unusually, the rent has not been decided prior to exchange then any provisions in the agreement dealing with how the open market rent is to be calculated must be fair and produce a favourable rent for the operator. The rent review provisions in the new lease should also operate fairly and upwards only reviews should be avoided if at all possible. In the care home sector, it is often the case that there is a lack of local comparable properties for conducting an open market rent review, so a review system based in RPI might be preferable for both parties.

Turnkey leases are clearly an attractive method for care home operators to expand their residential care home portfolios. They allow operators to focus on the core area of their business, running care homes, and contract the construction of new homes to experienced developers. The agreement for lease is, however, a complex document and it is important to get it right otherwise operators can find that the developers are able to deliver a home that is different to that which the operator wanted and is handed over far later than anticipated.

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