House of Commons
Communities and Local Government Committee

The work of the Regulation Committee of the Homes and Communities Agency


Report, together with formal minutes, oral and written evidence

Ordered by the House of Commons
to be printed 2 September 2013
The Communities and Local Government Committee

The Communities and Local Government Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department for Communities and Local Government.

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The committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the internet via www.parliament.uk.

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The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the internet at www.parliament.uk/parliament.uk/clg. A list of Reports of the Committee in the present Parliament is at the back of this volume.

The Reports of the Committee, the formal minutes relating to that report, oral evidence taken and some or all written evidence are available in a printed volume.

Additional written evidence may be published on the internet only.

Committee staff

The current staff of the Committee are Glenn McKee (Clerk), Sarah Heath (Second Clerk), Stephen Habberley (Inquiry Manager), Kevin Maddison (Committee Specialist), Emma McIntosh (Senior Committee Assistant), Mandy Sullivan (Committee Assistant), and David Foster (Assistant Media Officer).

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Summary

The Regulation Committee of the Homes and Communities Agency is responsible for ensuring that the registered providers of 2.6 million homes in the social rented sector are financially viable and properly managed.

On 15 July we took oral evidence from the Chair of the Regulation Committee, Julian Ashby, on his work since April 2012. We have concerns about the reporting of financial viability of providers. During 2012 the Cosmopolitan Housing Association ran into serious financial trouble. But the Regulator’s published financial viability assessment failed to reflect the serious weakening in its position until after it had been rescued. The case had implications for the sector when in May this year the ratings agency, Moody’s, downgraded all but one of the English housing associations citing the Cosmopolitan episode as demonstrating the challenges the Regulator would face if he had to step in to protect entities and their creditors in extreme situations.

It has now emerged that the Regulator is unable to use his statutory powers or provide a frank assessment of concerns about a provider’s financial viability fearing that it might trigger a re-pricing of the provider’s debt and therefore undermine its viability. Instead, rather than use his financial viability ratings to convey his assessment of financial viability, the Regulator uses the governance ratings to signal concerns about financial viability. This approach lacks openness and is confusing. We conclude that the practice should cease. In addition, the Regulator should work with other regulators to examine and review how they have addressed his concerns that use of statutory powers may be counter-productive.

The Regulator has a limited responsibility for consumer regulation. We noted that of the 111 complaints that related to a breach of consumer standards referred to the Regulator, not a single case of serious detriment was found. To have the assurance that the Regulator is discharging his consumer protection obligations effectively, we call for an annual external check to be carried out.
1 Introduction

The social housing sector

1. There are some 1,500 social housing providers in England. Although collectively they undertake a diverse range of activities, such as provision of community services, regeneration, market rent tenures and housing sales, for most of them being a social housing provider has been, and is still, the predominant activity. Historically the main players have been non-for-profit housing associations. As local authorities stopped building houses in the 1980s, housing associations became the main providers of social housing for rent to people in need of housing. In addition, from the 1980s onwards many local authorities set up, and transferred their stock to, housing associations. Together the providers manage around 2.6 million homes with around 60% of that stock held by just 5% of providers, while approximately 1,100 providers hold fewer than 1,000 homes each.\(^1\)

2. The Homes and Communities Agency (HCA) is the national housing and regeneration agency in England. It provides investment for new affordable housing and to improve existing social housing, as well as for regenerating land.\(^2\) The 2010 Spending Review announced reform of affordable housing, including a “continuing, but more modest” capital investment.\(^3\) The Department for Communities and Local Government, through the HCA and the Greater London Authority, will invest £4.5 billion in affordable housing in 2011–15, which, according to the National Housing Federation, represents a 63% real terms reduction on the previous spending review period.\(^4\) To offset smaller capital grants, housing providers can charge increased rents for new lettings up to 80% of market rent. This is creating a move from capital subsidy to revenue support paid through benefits supporting increased debt.\(^5\) The HCA has stated that “the traditional social housing model that has existed for the past 25 years is in flux and the key issue for boards [of registered providers] is how they respond to that change and how they position their organisations”.\(^6\) Reduced levels of grant have meant that providers need to incur debt to a greater extent than previously if they wish to fund development. This brings increased risk, which some providers have sought to mitigate by diversifying into other housing tenures such as temporary accommodation, student accommodation, market rent and housing for sale. Providers are also looking to new business opportunities to cross-subsidise their social housing.\(^7\) In addition, the Government is implementing an ambitious programme of

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\(^1\) HCA 2012 Global Accounts of Housing Providers, p 4  
\(^2\) HCA website: www.homesandcommunities.co.uk/aboutus  
\(^3\) HM Treasury, Spending Review 2010, October 2010, p 49  
\(^4\) Ev 45 (National Housing Federation), para 3.5; figures from the HCA show the following:

<table>
<thead>
<tr>
<th>Spending Review Period</th>
<th>Total Investment</th>
<th>Average Annual Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008-2011</td>
<td>£8.4 billion</td>
<td>£2.8 billion</td>
</tr>
<tr>
<td>2011-2015</td>
<td>£4.5 billion</td>
<td>£1.125 billion</td>
</tr>
</tbody>
</table>

Reduction in average annual investment: £1.675 billion (60%)


\(^5\) Ev 16, Ev 17 (Moat), paras 3, 12–17  
\(^6\) HCA Sector Risk Profile, para 2.3  
\(^7\) Ev 47 (Places for People)
welfare reform: housing benefit is being subsumed into Universal Credit, which will be paid direct to tenants rather than as currently to landlords. (We examined the implementation of these changes in a recent Report.\(^8\)) The impact of these changes are not yet clear, but is likely at least to be felt in a perception of greater risk to income flows, in increased tenant arrears and in increased costs of debt collection for providers.

**Regulation**

3. The Regulation Committee of the HCA currently regulates social housing providers in England. The rationale for state intervention through regulation in the provision of social housing rests on three main factors:

a) limited competitive pressures towards the provision of good, efficient service;

b) the presence of substantial public subsidy; and

c) regulation helps to underpin the provision and terms of provision of private sector lending to the sector (providers are currently holding long term loans of around £48 billion).\(^9\)

4. Until 2008 the regulation of social housing had remained broadly unchanged for over thirty years. Different types of providers were regulated by different bodies: the Government, through the Department of Communities and Local Government (DCLG) and its predecessors, was responsible for regulating local authorities; arms length management organisations (ALMOs) were regulated by local authorities and the Housing Corporation (the predecessor of the HCA) regulated housing associations. On top of this, all local authorities, ALMOs and housing associations were subject to scrutiny by the Audit Commission. The Cave Review, published in 2007, criticised the system for being overly strict on some providers.\(^10\) In response to the Review’s key recommendation that there should be a single, independent regulator, the Tenant Services Authority (TSA) was set up to cover all social housing providers. The scope of TSA regulation covered consumer and economic regulation. It set standards covering consumer and economic issues and had a range of monitoring and enforcement powers to ensure that providers met those standards.\(^11\)

5. By 2010 the situation had changed: the Coalition Government had a commitment to much greater localism, and there was an imperative to make significant savings across government, including through a reduction in the number of quangos. The TSA was abolished in April 2012\(^12\) when regulation of the social housing sector in England passed to the HCA, which discharges its regulatory functions through its Regulation Committee. The Committee is chaired by Julian Ashby. (Mr Ashby entered the social housing sector in 1974

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\(^8\) Communities and Local Government Committee, Ninth Report of Session 2012–13, Implementation of welfare reform by local authorities, HC 833

\(^9\) HCA, 2012 Global Accounts of Housing Providers, p 12

\(^10\) DCLG, Every Tenant Matters: A review of social housing regulation ("the Cave Review Of Social Housing Regulation), June 2007, p 15, para 5.77, recommendation 58

\(^11\) DCLG, Review of Social Housing Regulation, October 2010, paras 2.4–2.8

\(^12\) DCLG, Review of Social Housing Regulation, October 2010, para 2.9
following a career in international merchant banking. He has been Chief Executive and Chair of many associations and as a consultant he specialised in trouble-shooting, governance, mergers, strategy reviews, organisation and structure, risk management and personnel issues. He conducted four Statutory Inquiries and previously was Deputy Chair of the TSA.¹³ Chair of the Regulation Committee is a three year appointment, with the possibility of renewal, and with a commitment to work up to 2.5 days per week.¹⁴ The Regulation Committee is supported by about 110 regulation staff (henceforth referred to as ‘the Regulator’). There are two regulatory objectives, similar to those of the TSA, set out in statute:

a) economic regulation—to ensure that registered providers of social housing are financially viable and properly managed; and

b) consumer regulation—to ensure that tenants of social housing have an appropriate degree of protection by setting consumer standards and performing a backstop role in this area.¹⁵

6. The system that has evolved is co-regulatory. The social housing providers are responsible for managing their own business, including their own risks. The role of the Regulator is to set standards and seek assurance that those standards are being met and risks are being managed. The Regulator has powers to:

a) set, revise or withdraw standards related to both consumer and economic matters;

b) undertake statutory inquiries; and

c) take action following a statutory inquiry including suspending or removing officers, ordering restrictions on dealings, making the decision to amalgamate non-profit registered providers and requiring private registered providers to transfer land.¹⁶

To ensure regulatory independence, the Secretary of State’s formal powers are limited, but he can, and has, made directions on specific standards to the Regulator.¹⁷

Our inquiry

7. Since 2011 we have embarked on a programme of reviews of the work of the ombudsmen and regulators covering the areas for which DCLG has responsibility. We carried out a pre-appointment hearing for Julian Ashby as the Regulator on 31 August 2011, and we recommend that the Secretary of State proceed with his appointment.¹⁸ We decided to give the new regulatory arrangements, which came into operation in April 2012

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¹³ Communities and Local Government Committee, Seventh Report of Session 2010–12, Pre-appointment hearing for the Government’s preferred nominee for Chair of the Homes and Communities Agency Regulation Committee, HC 1612, paras 12–15 and Annex A

¹⁴ HC (2010–12) 1612, para 6 and Appendix


¹⁶ HCA, Scheme of Delegated Authority for Use of Powers by the Regulation Committee, April 2012, www.homesandcommunities.co.uk/ourwork/functions-and-powers

¹⁷ DCLG, Review of Social Housing Regulation, October 2010, para 8.8

¹⁸ HC (2010–12) 1612, para 19
about a year to settle before we examined the performance of the Regulator. As preparation for our inquiry we invited written submissions and we had a background briefing on the sector from the National Housing Federation. We took oral evidence from the Regulator on 15 July 2013.

8. Many of those who responded to our call for written submissions were broadly positive about the Regulator’s performance since April 2012, though the HCA Regulation Committee’s proposals for change, which we cover in chapter 3, were not so well received. We were not carrying out an inquiry into the regulation of the social rented sector. The remit we set ourselves was narrower. We focussed on the work of the Regulator since 2012 and in particular on his two primary responsibilities: (i) his economic regulation objective, which is to ensure that registered providers of social housing are financially viable and properly managed, and (ii) his consumer regulation objective, which is to ensure that tenants of social housing have an appropriate degree of protection. Having heard the Regulator’s oral evidence we had concerns about what we were told on financial viability ratings (part of economic regulation) and we wrote to the Secretary of State on 18 July to draw his attention to the transcript. He replied on 25 July saying that he took our “points very seriously”, and was “grateful” to us for drawing the matter to his attention. He asked officials to write to the Regulator asking him to “clarify certain points from his evidence and provide assurance that these important regulatory powers are being used effectively”. Subsequently, the Regulator supplied us with a supplementary memorandum. We have used this report to expand upon our concerns. The Regulator’s performance against the economic objective is covered in chapter 2 and against the consumer objective at chapter 4. In chapter 3 we consider the Regulator’s discussion paper on proposals to revise the financial viability and governance standards, which is part of the economic objective.

19 For example: Ev 22 (Council of Mortgage Lenders), para 5, Ev 23 (Hyde Group), paras 1.2–1.3, Ev 33, Ev 34 (DCLG), paras 4 and 9, Ev 45, Ev 46 (National Housing Federation), paras 2.2 and 8.1, Ev 56 (Leeds Housing Forum)

20 For example: Ev 14 (Home Group), para 5 and following, Ev 18 (Moat), paras 22–26, Ev 32 (Circle), Ev 46 or 45 (National Housing Federation), para 3.8, Ev 48 (Places for People), Ev 50 (PlaceShapers), para 4.6 and following, Ev 55 (Luminus Group); Ev 56 (Leeds Housing Forum)

21 A copy of the letter is at the Annex to this report.

22 As above

23 Ev 11–12
2 Economic regulation

Introduction

9. In order to protect taxpayers’ investment in the sector, and to ensure that public investment is safeguarded and used for the purpose intended—the provision of social housing—and that unreasonable burdens are not imposed on public funds, registered providers must be financially viable and well governed. The taxpayer has invested £43.8 billion in the current social housing stock of just the 400 largest providers (which represents about 35% of the value of their housing properties). A failure of a provider would not only risk the loss to the taxpayer of the value of this historic subsidy, but also have a significant impact on the provider’s tenants. The Regulator explained that:

If there were a series of failures of providers, they would have dire consequences for the tenants of those providers. If lenders ever get to the point where they have to enforce their security, it ceases to be social housing. The protection that tenants have then relies on their tenancy agreements and not on the protection of their being within a regulated sector. We [the Regulation Committee] are very, very concerned about that.

Ujima is, to date, the only housing association to become insolvent (in 2008), although Cosmopolitan Housing Association came close to insolvency in 2012, with reported shortcomings in recognising and managing its financial risks. Cosmopolitan was eventually rescued by a takeover by Sanctuary Group, a process supported and facilitated by the Regulator.

Current pressures

10. The Regulator explained that providers’ financial viability was currently being challenged in three ways. First, with lower grant levels, new social housing for rent was developed with higher levels of debt than previously, which meant higher total interest payments. Second, some £40 billion of bank debt to the sector was “underwater”, i.e. the cost of providing the funding was more than the banks received in return. This meant that banks were more likely to seek re-pricing opportunities and so make existing debt more expensive. Finally, welfare reform might increase the proportion of rent overdue and therefore the amount providers would need to spend on debt collection and potentially evictions and court costs, as well as affecting their cash flow and costs of short term

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24 £41.6 billion of Social Housing Grant/Housing Associations Grant plus £2.2 billion Other Capital Grants: HCA, 2012 Global Accounts of Housing Providers, p 12
25 Q 53
26 “Ujima: why didn’t anyone step in?”, Inside Housing, 6 June 2008
27 HCA, HCA Regulatory Judgement on Cosmopolitan Housing Group Limited—L4375 Cosmopolitan Housing Association Limited LH1298: Chester and District Housing Trust LH429, December 2012
28 “Cosmo and Sanctuary strike historic deal”, Inside Housing, 27 March 2013
29 A re-pricing can occur when a loan covenant is broken. A loan covenant is a condition in a commercial loan or bond issue. Its purpose is to help the lender ensure that the risk attached to a loan does not rise unexpectedly. The breach of a covenant gives the lender the right to demand the repayment of the loan, collect penalty charges or increase the pricing (interest rate).
borrowing to provide working capital.\textsuperscript{30} In this report we have not set out to examine the basis for, or quantify, the risks identified by the Regulator as facing the sector. But it must be part of the Regulator’s job to be alert to the risks and the perception of risks which could affect the financial viability of social housing providers. From the evidence we received we are satisfied that he is.

11. A signal that providers of social housing are working in a more challenging climate was Moody’s downgrade of all but one of the rated English housing associations in May this year. Moody’s explained that this was driven by a downward “reassessment of likelihood of extraordinary support from the UK government […] in light of ongoing developments in the sector” and “reflects challenges for the Regulator […] to step in and protect entities and their creditors in extreme situations”, as demonstrated by the Cosmopolitan experience.\textsuperscript{35} When we asked the Regulator about this downgrade, he cited an earlier downgrade to housing associations’ credit ratings in February 2013, emphasising the general economic climate, rather than regulatory challenges, as the reason for Moody’s decision:

Moody’s has basically downgraded most of the providers in the sector on two occasions in the last six months. The first one-notch downgrade was at the same time as UK sovereign debt lost its AAA rating and was a direct consequence of that. At that point, they put the sector on negative watch, primarily driven by their perception of the level of Government support for the sector […] They eventually settled on a further one-notch downgrade for the majority of associations that they rated, but that was done with the removal of the negative watch […] They moved to a position that brings them broadly in line with the other main rating agency, Standard & Poor’s, and provides stability for the sector going forward.\textsuperscript{32}

12. When Moody’s announced the downgrade on 17 May 2013 its summary said that its:

revision in the support assessment reflects challenges for the regulator […] to step in and protect entities and their creditors in extreme situations. Many of the same issues were highlighted in facilitating the long-term viability of Cosmopolitan Housing Group, ensured in a merger with Sanctuary Group. This episode served to illustrate the difficulties in ensuring a satisfactory outcome when a housing association encounters financial distress. The recent discussion document issued by the regulator on proposals to adjust the regulatory framework leads Moody’s to be more cautious in its assessment of the likelihood of timely government action.\textsuperscript{33}

13. We share the assessment of Places for People that the "failure of Cosmopolitan sent shockwaves through the sector, resulting in Moody’s casting doubt on the effectiveness of the regulator and effecting a subsequent downgrade of Moody’s credit rating". It voiced concerns from the sector "that the regulator would struggle with multiple rescues, should such a scenario present itself".\textsuperscript{34} We note that the Regulator has commissioned a "lessons

\textsuperscript{30} Q 6 and HCA, Sector Risk Profile, 6 June 2012, www.homesandcommunities.co.uk/sites/default/files/our-work/sector-risk-profile-120611.pdf
\textsuperscript{31} Moody’s Investor Service, Key Drivers of Moody’s Downgrade of English Housing Associations, 17 May 2013, pp 1–2
\textsuperscript{32} Q 2
\textsuperscript{33} “Key Drivers of Moody’s Downgrade of English Housing Associations”, Moody’s Investors Service, 17 May 2013
\textsuperscript{34} Ev 47
learned exercise from the [...] case to ensure our approach to managing failures in individual providers is as robust as it can be. Recent press reports indicated, however, that DCLG had “blocked the commissioning of a review into the near collapse of Cosmopolitan Housing Group [...] on the grounds it is too expensive” at a cost believed to be more than £10,000.

14. We note that Moody’s, in downgrading its ratings for all but one of the English housing associations in May 2013, cited the Cosmopolitan episode as showing the difficulties in ensuring a satisfactory outcome when a housing association encountered financial distress and the challenges the Regulator would face if it had to step in and protect entities and their creditors in extreme situations. We welcome the Regulator’s intention to review lessons from the Cosmopolitan episode and ask for a copy of the review when it is completed. We are therefore concerned by press reports that DCLG has blocked the commissioning of a review. In responding to our report we ask the Government to explain whether it has blocked the review and, if it has, why and how it assessed the consequences of its decision for the independence of the Regulator and the regulation of the social housing sector.

The Regulator’s ratings

15. The new Regulatory Framework for social housing in England came into operation on 1 April 2012. It sets out the parameters under which the Regulator carries out his regulatory responsibilities. It requires the Regulator to “carry out annual engagement with larger providers to enable it to achieve a minimum level of assurance that economic standards are being met and to make public judgements on governance and financial viability”. The Framework defines the standard as follows:

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**Financial viability**

Registered providers shall manage their resources effectively to ensure their viability is maintained.

**Governance**

Registered providers shall ensure effective governance arrangements that deliver their aims, objectives and intended outcomes for tenants and potential tenants in an effective, transparent and accountable manner.

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16. The Regulatiry Framework also states that the Regulator should publish both financial viability and governance ratings of the larger providers:

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25 Ev 60, para 8
26 “CLG refuses to sign off on Cosmopolitan inquiry”, Inside Housing, 9 August 2013
28 HCA, The Regulatory Framework for Social Housing in England from April 2012, March 2012, p 1, which requires “Governance arrangements shall ensure [providers]:

- adhere to all relevant legislation
- comply with their governing documents and all regulatory requirements
- are accountable to tenants, the regulator and relevant stakeholders
- safeguard taxpayers’ interests and the reputation of the sector
- have an effective risk management and internal controls assurance framework.
The regulator will continue to publish graded assessments in relation to viability and governance as these are key areas where lenders, boards and others value assessments. The regulatory judgment will also comment on the assurance obtained with regard to the Value for Money standard.  

**Financial viability ratings**

17. Currently there are four financial viability ratings (or grades) which are set out at Table 1 along with numbers of social housing providers in each category in March 2013.

<table>
<thead>
<tr>
<th>Grade viability</th>
<th>Description</th>
<th>Number of providers</th>
<th>% of providers, as assessed by the Regulator, March 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>V1</td>
<td>The provider meets the requirements on viability set out in the Governance and Financial Viability standard and has the capacity to mitigate its exposures effectively.</td>
<td>108</td>
<td>80.6%</td>
</tr>
<tr>
<td>V2</td>
<td>The provider meets the requirements on viability set out in the Governance and Financial Viability standard but needs to manage material financial exposures to support continued compliance.</td>
<td>25</td>
<td>18.7%</td>
</tr>
<tr>
<td>V3</td>
<td>The provider’s financial viability is of concern and in agreement with the Regulator it is working to improve its position.</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>V4</td>
<td>The provider’s financial viability is of serious concern and it is subject to regulatory intervention or enforcement action. (Cosmopolitan Housing Association, Chester &amp; District Housing Trust, rating suspended)</td>
<td>1</td>
<td>0.7%</td>
</tr>
</tbody>
</table>

| Total           | 134                                                           | 100%                                                          |

18. The Regulator told us that he was in practice reluctant to give lower financial viability ratings because of a fear that doing so might breach a loan covenant and thus trigger loan re-pricing. While there are a “handful” of providers that are of concern to the regulator and a “small but steady flow of problem cases”, no provider has yet been graded V3 (where the provider’s financial viability is of concern and in agreement with the Regulator it is working to improve its position). The Regulator’s response led us to question what value the financial viability ratings had if the Regulator considered himself so constrained as not to be able to rate a provider in the lower grades. In his supplementary submission after the session the Regulator sought to clarify the position:

I want to make it absolutely clear that we will issue a V3 or V4 rating if we feel it is warranted. Failure to comply with a fundamental standard is a serious matter, including because it could impact on the price a provider pays for their existing debt, potentially making a bad situation worse. Our regulatory strategy is to work with any provider with weaknesses or serious exposures to deal with issues before it

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40 Tables on HCA website: www.homesandcommunities.co.uk/ourwork/regulatory-judgements, www.homesandcommunities.co.uk/sites/default/files/our-work/2013_08_28_regulatory_judgements_full_table.xlsx
41 Q 27; see also footnote 29 above for explanation of re-pricing and loan covenants.
42 Q 7
gets to the stage that a V3 or V4 is necessary; and that is why we have not issued any V3 ratings (and only one V4 rating) to date.\textsuperscript{43}

19. Our concerns about the shortcomings of the published financial viability ratings were underlined by the fact that the rating for the Cosmopolitan Housing Group published in 2008 was not updated by the Regulator until December 2012,\textsuperscript{44} even though the media reported that Cosmopolitan could face the possibility of insolvency two months earlier,\textsuperscript{45} and the Regulator had himself been monitoring the situation since early 2012.\textsuperscript{46} When we asked the Regulator why this was, he said that “the situation was moving so fast we were not quite sure where we would place them”,\textsuperscript{47} but in his supplementary submission he told us that the grading was “our rounded assessment [and] based on examination of providers’ financial planning and control framework and analysis of key financial information”.\textsuperscript{48} We conclude that the failure of the Regulator’s published financial assessment to reflect the serious weakening in the financial viability of the Cosmopolitan Housing Association raises questions about the operation and usefulness of the Regulator’s financial viability ratings. In this case the assessment of financial viability was neither timely nor useful. The eventual downgrading of Cosmopolitan to the lowest grade amounted to a futile exercise in locking the stable door long after the horse had bolted. We are not surprised that Moody’s paid such close attention to the episode.

\textbf{Governance ratings}

20. As is the case with the financial viability ratings, there are four governance ratings (or grades) which are set out at Table 2 along with numbers of social housing providers in each category in March 2013.\textsuperscript{49}

\begin{footnotesize}{
\begin{itemize}
\item \textsuperscript{43} Ev 11, para 2
\item \textsuperscript{44} HCA, HCA Regulatory Judgement on Cosmopolitan Housing Group Limited—L4375 Cosmopolitan Housing Association Limited LH1298: Chester and District Housing Trust LH429, December 2012, p 4
\item The HCA’s regulatory assessment that downgraded the Cosmopolitan Housing Group’s governance and viability to V4 and G4 indicated that the last regulatory judgment was published in February 2008. This was before Chester and District Housing Trust became a subsidiary of the Cosmopolitan Housing Group (in December 2011). The 2008 rating was published by the predecessor to the Tenant Services Authority (TSA), the Housing Corporation, under a traffic light system and gave green ratings for both viability and governance, meaning there were “no material concerns about performance” (Housing Corporation Assessment, “Cosmopolitan Housing Group L4375, Cosmopolitan Housing Association LH1298”, February 2008). Chester and District Housing Trust was similarly rated green for both viability and governance (Housing Corporation Assessment, “Chester & District Housing Trust Ltd, LH4291”, April 2007).
\item \textsuperscript{46} “Troubled Cosmopolitan’s future hangs in balance”, Inside Housing, 26 October 2012
\item \textsuperscript{47} “Troubled Cosmopolitan in rescue merger talks”, Inside Housing, 19 October 2012
\item \textsuperscript{48} Q 19
\item \textsuperscript{49} Tables on HCA website: www.homesandcommunities.co.uk/ourwork/regulatory-judgements, www.homesandcommunities.co.uk/sites/default/files/our-work/2013_08_28_regulatory_judgements_full_table.xlsx
\end{itemize}
}


Table 2: Regulatory Judgments—HCA Regulation Committee’s governance ratings (March 2013)

<table>
<thead>
<tr>
<th>Grade</th>
<th>Description</th>
<th>Number of providers</th>
<th>% of providers, as assessed by the Regulator March 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>G1</td>
<td>The provider meets the requirements on governance set out in the Governance and Financial Viability standard.</td>
<td>118</td>
<td>88.1%</td>
</tr>
<tr>
<td>G2</td>
<td>The provider meets the requirements on governance set out in the Governance and Financial Viability standard, but needs to improve some aspects of its governance arrangements to support continued compliance.</td>
<td>9</td>
<td>6.7%</td>
</tr>
<tr>
<td>G3</td>
<td>The provider does not meet all of the requirements on governance set out in the Governance and Financial Viability standard. There are issues of regulatory concern and in agreement with the regulator the provider is working to improve its position.</td>
<td>6</td>
<td>4.5%</td>
</tr>
<tr>
<td>G4</td>
<td>The provider does not meet the requirements on governance set out in the Governance and Financial Viability standard. There are issues of serious regulatory concern and the provider is subject to regulatory intervention or enforcement action.</td>
<td>1 (Cosmopolitan Housing Association, Chester &amp; District Housing Trust, rating suspended)</td>
<td>0.7%</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>134</td>
<td>100%</td>
</tr>
</tbody>
</table>

21. When we pressed the Regulator at the oral evidence session on the value of the financial viability ratings he said:

   We do find ways of signalling our concerns and we have particularly used the governance rating for that purpose because that does not have the same re-pricing trigger impact that a V3 or V4 would have.50

   He informed us that this “situation is well known to lenders”,51 but the Council of Mortgage Lenders’ submission implies that lenders take the regulatory judgements at face value:

   Although the challenges for the HCA’s regulation committee at the time it was established were considerable (and still are), we believe that it has had a strong positive impact to date. This is evidenced by predominantly strong regulatory judgements on financial viability and governance which most providers enjoy. Lenders and investors place great reliance on these.52

   The Regulator’s view was that “at the root of financial failures will almost inevitably be a failure in governance and by carrying out our proactive regulation of governance we seek to spot problems early and prevent them developing to the point where they have an impact on viability”.53

Conclusions on ratings

22. Ratings published by the Regulator should be reliable and capable of being understood at face value. The practice of using governance ratings to signal concerns about financial viability lacks openness and is confusing. It is misleading to the
taxpayer and tenants, and potentially also to lenders who, it appears, are expected to understand the coded message from the Regulator. We conclude that the practice should cease. We recommend that the Regulator publish accurate financial viability ratings.

23. Poor governance can undoubtedly undermine the financial viability of a provider but we are not persuaded by the argument that it is “almost inevitably” the cause of financial failures in general. Financial viability and governance ratings serve different purposes and assess the providers against different standards. The distinction between governance and financial viability must be maintained.

Use of statutory powers and transparency

24. The Regulator’s fears on financial viability focused on the risks of triggering a re-pricing. The Regulator felt unable to use many of his statutory powers. He told us:

in practice there are now severe limitations on how we can use these powers as a consequence of the financial environment where use of powers could lead to a breach of loan covenants and in turn re-pricing or repayment of existing debt.\(^{54}\)

There are cases, for example, where five years ago we might have moved fairly quickly to make statutory appointments to a board. We do not do that now. In a number of cases we have gone to the board and said, “We are not satisfied with the skills you have available to tackle this set of issues, and we require you to get some additional board members with the necessary skills.” They have invariably done that to our satisfaction. If they refused point-blank, we would make the appointments and take the consequences.\(^{55}\)

He explained that:

as far as possible, our approach has been modified to achieve the changes we expect to see in those who are underperforming without use of statutory powers. We are no less robust in our analysis and identification of issues.\(^{56}\)

The principal focus of our engagement is to identify issues and get them resolved. In the main, we undertake that work on a basis that is not greatly in the public view; it is direct engagement between regulatory staff and the providers.\(^{57}\)

25. The Regulator stated that he was “committed to robust, independent and transparent regulation”,\(^{58}\) but by favouring informal approaches over public and accountable actions, it appears to us that the transparency of the system is clouded. We asked the Regulator whether he had examined how other regulators overcame what he appeared to portray as the dilemma: the use of statutory powers or a frank assessment of concerns about a

\(^{54}\) Ev 60, para 12
\(^{55}\) Q 36
\(^{56}\) Q 42
\(^{57}\) Q 51
\(^{58}\) www.homesandcommunities.co.uk/ourwork/regulating-standards-0
provider’s financial viability would provoke a re-pricing and therefore undermine its viability. He told us that the Regulation Committee has “a different architecture” to that of most regulators, who typically operate a licensing system. He implied that the problem he faced was exclusive to, or acute for, the HCA regime. He appears to us to have overlooked the devolved administrations’ housing regulators. Nor are we convinced that the issues and the dilemma faced by the social housing Regulator in England are not encountered by other regulators in other sectors.

26. It is reasonable, and to be expected, that the Regulator is in regular communication with the sector and on occasion an informal approach will be sufficient. We are concerned when the informal approach becomes a Regulator’s exclusive method of operation. First, it is inconsistent with transparency. Lack of transparency makes it difficult for lenders, tenants and taxpayers to see how much and what action the Regulator is taking. Second, there is a risk that this approach may lead to too close a relationship with providers thus compromising the independence or judgment of the Regulator. Third, if the sector knows that the Regulator cannot, and will not, use his formal powers, that must undermine his position and effectiveness.

27. We conclude that the Regulator’s relationship with providers has to have a greater element of transparency. In addition, the Regulator should have available powers which he can use when a social housing provider fails to meet the required standards. We make two recommendations. First, that the Regulator work with other regulators to examine whether they have addressed his concerns that use of statutory powers may be counter-productive. Second, although the new regulatory regime is still at a relatively early stage, an experienced former regulator in another sector should review the operation of social housing regulation. The review’s report, conclusions and recommendations should be published.
3 The Regulator’s proposals to protect social housing assets

28. The new challenges faced by the social housing sector and, in particular, the growing diversification of the activities that the providers are undertaking, have meant the Regulator “does not feel that it obtains sufficient comfort [...] that social housing assets are not being put at risk from non-social housing activity”.60 Its discussion paper, Protecting Social Housing Assets in a More Diverse Sector, sets out the nature of these challenges and possible regulatory responses. The proposals for change focus on ring-fencing of social housing assets to ensure that social housing is not put at risk when providers diversify their activities, recovery planning and protecting public value on disposal.

29. We have not taken detailed evidence on the proposals in the discussion paper and we are not in a position to reach conclusions or make recommendations. What we set out in this chapter are some observations which may assist deliberations and implementation of any changes. The sector is changing significantly. As Places for People pointed out: “income from operations outside social housing [is being used] to subsidise the development of [providers’] social housing businesses whilst also using the strength and predictability of the social housing activities to compensate for the risks inherent in the other activities”.61 We commend the Regulator for seeking to update the regulatory regime as the sector changes. We also welcome the fact that the Regulator is considering the need to protect social housing assets.

30. That said, many providers have been critical of the ring-fencing proposal, telling us that it is too prescriptive and too much of a ‘one-size-fits-all approach’.62 Leeds Housing Forum, for example, told us that:

> Of particular concern [...] is the ring-fencing proposal, which as written would restrict the activity of Housing Associations to the provision of general needs rented housing and pretty much nothing else (bar a minor tolerance of 5% activity). The scale of social investment, regeneration activity, and care related activities some [Registered Providers] currently undertake [...] would have to drastically reduce, and in many cases may stop altogether.63

The g15 Group, representing fifteen of London’s largest housing associations, said that:

> The HCA should stay true to the principles of co-regulation. It is the job of each [housing association] board to assess risks in the round and satisfy itself that appropriate strategies are in place to mitigate them. As part of this, the board may decide to place diverse activities into separate subsidiaries and should limit its investment in them to an amount which does not place existing social housing

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60 DCLG, Protecting Social Housing Assets in a More Diverse Sector, April 2013, para 19
61 Ev 48
62 Ev 15 (Home Group), para 10, Ev 20 (g15), para 2.2, Ev 32 (Circle); Ev 53 (Luminus Group), para 12, Ev 56 (Leeds Housing Forum), para 4
63 Ev 56, para 4
assets at risk; alternatively it may choose another approach. But it should not be for the regulator to prescribe what it should do.\(^{64}\)

Similarly, Home Group commented on the recovery planning proposals:

> We submit that the main focus for the regulator is to develop a system that is proportionate, balanced, represents value for money and which acknowledges the pre-eminent role of the boards of providers to co-ordinate recovery planning (rather than the regulator). The sector would not benefit from the introduction of an arbitrary and prescriptive system of recovery planning, which would run contrary to the principle of co-regulation underpinning the Regulatory Framework.\(^{65}\)

31. When he gave oral evidence to us the Regulator was sympathetic to the call for a more tailored approach:

> I cannot over-emphasise the extent to which associations differ very widely in their size, scale and range of activities [...] They are very different and have different needs. It does not make it easier to regulate but those are differences that we have to recognise in the arrangements we make to monitor and regulate them [...] We are not seeking a one-size-fits-all-solution.\(^{66}\)

Nevertheless, he explained that:

> The regulatory architecture we have to work with is one that sets standards, and then we have a set of powers that we can use to make sure those standards are met. That is the way the regulatory system has been set up. It is not a system we have devised. That is the statutory arrangement.\(^{67}\)

32. At the evidence session the Regulator said that his proposals were not set in stone and he had reservations about ring-fencing social housing assets in all circumstances:

> I am not convinced that ring-fencing is necessarily the most appropriate tool for the majority of associations. [...] The rationale for having it in the discussion document is to get providers thinking about the extent to which it is reasonable to use social housing assets, in which the taxpayer has put significant investment, to support commercial activities.\(^{68}\)

Subsequently, the Regulator indicated in a newspaper article that he had dropped his proposals for ring-fencing for not-for-profit providers and that he would undertake a further consultation exercise on detailed proposals in due course.\(^{69}\) It would have assisted our deliberations if he had communicated his change of mind directly to us.

\(^{64}\) Ev 21, para 4.2  
\(^{65}\) Ev 15, para 11  
\(^{66}\) Qq 40, 70  
\(^{67}\) Q 64  
\(^{68}\) Qq 67–69  
\(^{69}\) “The way ahead”, Inside Housing, 9 August 2013
33. Moody’s has commented that “the practical implementation of these proposals will be challenging and it is unclear whether they will effectively improve intervention and oversight”.\textsuperscript{70} We support the aim of protecting social housing assets and tenants from the risks associated with non-social housing activity by providers but the current proposals lack flexibility and appear to cut across the system of co-regulation which gives providers’ boards the responsibility to assess and mitigate risk. We welcome the decision of the Regulator to revise his proposals and to consult again.

**Resources and capacity**

34. The Regulator’s resources and capacity will affect his ability to regulate both existing and new standards. The evidence we received from providers suggested that the Regulator may not have sufficient resources to deliver a co-regulatory approach. For example, the Hyde Group stated that it is “concerned about the capacity of the Regulator to undertake co-regulation in regards to financial viability and governance”;\textsuperscript{71} PlaceShapers expressed “a continuing concern that the [Regulation Committee] may not be able to recruit and retain the calibre of staff needed to discharge its role effectively” and it had “numerous examples of regulatory staff appearing still to be more interested in ticking boxes to confirm, for example, that [...] Board meetings have been attended”;\textsuperscript{72} and Places for People warned us that “in order to prevent systemic failure and ensure robust and effective regulation, the HCA’s intellectual and financial capacity will need to be boosted”.\textsuperscript{73}

35. The Home Group pointed out that the Regulator’s proposals to amend the standards might require him to have a different resource profile than that which he had at present:

Inevitably, the increased level of information and data trail which providers will be required to maintain as part of the recovery planning process will not only require additional resourcing by providers but—critically—additional resourcing on the part of the HCA itself. Not only will the regulator need to recruit additional regulatory staff to support a significantly increased workload, but they will need to employ staff with a much more extensive skill set than is required at present. We are concerned that this capacity does not currently exist. Its development must be a fundamental pre-requisite to the successful implementation of any change.\textsuperscript{74}

36. The Regulator told us that:

We have the resources that I think are sufficient in financial terms at present, but [...] we need to significantly enhance our capacity to make high level business judgements about providers. We are doing that by reorganising within the obvious financial constraints that apply to us. I would hope by the end of the year that we will

\textsuperscript{70} “Key Drivers of Moody’s Downgrade of English Housing Associations”, Moody’s Investors Service, 17 May 2013
\textsuperscript{71} Ev 25, para 2.17
\textsuperscript{72} Ev 49, Ev 50, paras 3.1 and 3.3
\textsuperscript{73} Ev 48
\textsuperscript{74} Ev 15, para 15
have approximately three times as many senior managers in the regulation division as there were at the point when I took on responsibility.\textsuperscript{75}

37. The providers’ submissions about the resourcing, capacity and capability of the Regulator gives us grounds for concern. It appears that the current arrangements may not be adequate and need improvement. The fact that the Regulator himself has identified a need to increase significantly his capacity to make high level business judgments about providers appears to confirm the providers’ views. The reorganisation will have to be carried out without any additional resources and without a hiatus diminishing the Regulator’s scrutiny. We request that, once the reorganisation has been completed, the Regulator provides us with a report on the Regulation Committee’s capacity and capability to carry out its work.
4 Consumer regulation

The Regulator’s role

38. When in 2012 the HCA Regulation Committee replaced the Tenant Services Authority (TSA), the regulatory role changed.\textsuperscript{26} In its written evidence TPAS, a membership organisation representing over 1,800 tenant and resident organisations, told us that since “2012 there has been an opinion that TPAS hears very often, from its members and other people in the industry, that the regulator has withdrawn from its role in regulating the consumer standards”.\textsuperscript{77} The Regulator explained that:

The power to collect information about performance was revoked as part of the abolition of the TSA. There is no proactive monitoring against consumer standards because the Localism Act [2011] determined that that is not the role of the regulator [...] It has left us with two specific roles: one to set standards and the other, which is described as a backstop role, to take action where there may be systemic breaches leading to serious detriment.\textsuperscript{78}

The Regulatory Framework states that “the regulator’s assessment of serious detriment is based on the degree of harm or potential harm that may be caused to tenants by a breach of standards”.\textsuperscript{79} We note that there is no requirement for the breaches to be systemic for the Regulator to take action and we are unclear why this test has been introduced.

39. The Regulator told us that “there are at present four consumer standards” and he added that “although we set the consumer standards, in three of them they are the substantial result of Government directions”.\textsuperscript{80} This answer suggested to us that the Regulator regarded consumer regulation as an external imposition.

Tenants’ understanding of the system

40. The intention of the Government is that tenants and landlords resolve routine problems between themselves, within a more “localist” approach than previously;\textsuperscript{81} there is then a ‘democratic filter’ which aims to encourage local resolution via a designated individual or body, such as a tenant panel, Councillor or MP. If that fails, the next step would usually be to pass a complaint to the Housing Ombudsman, the role of which is to “resolve disputes involving members of the Scheme, including making awards of compensation or other remedies when appropriate, as well as to support effective landlord-tenant dispute resolution by others”.\textsuperscript{82}

\textsuperscript{26} Q 79  
\textsuperscript{27} Ev 35; see also Ev 31 (Residents’ Network, paras 19–23.  
\textsuperscript{28} Q 81, 83  
\textsuperscript{29} HCA, The Regulatory Framework for Social Housing in England from April 2012, March 2012, para 5.15  
\textsuperscript{30} Q 80  
\textsuperscript{31} DCLG, Review of social housing regulation, October 2010  
\textsuperscript{32} “Housing Ombudsman Service Scheme”, The Housing Ombudsman, February 2013
41. Despite this, many tenants still make complaints to the Regulator. In 2012–13, 421 complaints relating to consumer standards were submitted. No cases of serious detriment were identified and therefore the Regulator did not act on any of them. When we asked why this was the case, the Regulator explained that roughly three quarters of the complaints did not relate to breaches of the standards and therefore were not within his remit. However, 111 cases did relate to breaches of consumer standards and were referred to the Consumer Regulation Panel. Of these, 20 were investigated in further detail, but no cases of serious detriment were identified in 2012–13. Of the 111 complaints not a single case of serious detriment was found and we have to accept the Regulator’s judgement. A question about his operation of the procedure was, however, raised by a reported comment by a senior manager in the HCA. In April 2012, Ralph Smale, Strategic Regulation Manager at the HCA, was quoted by Inside Housing as saying that the consumer regulation system “puts us in an unfortunate position, we will be spending resources putting in place evidence to justify why we haven’t acted”.

42. It is not our job to review the individual cases which have been made to the Regulator. Parliament and the Government have given the Regulator certain responsibilities for consumer regulation. It is our job, however, to consider whether the Regulator has systems in place to carry out those responsibilities and that, prima facie, he is operating them effectively. Having reviewed the evidence we are not completely assured that the Regulator is discharging his responsibilities as we would expect. First, he has interpreted his remit as narrowly as possible. In responding to our report we request that he explain and justify his application of a test that breaches of standards should be systemic when he assesses serious detriment caused to tenants by a breach of consumer standards. Second, we formed the impression that the Regulator has treated consumer regulation as a distraction from his main job, economic regulation. In these circumstances we consider that a new arrangement needs to be developed to give the public and Parliament the assurance that the Regulator is meeting his consumer regulation remit and, if not, suggest improvements and changes. We recommend that the Regulator, working with a body such as the British and Irish Ombudsman Association, bring forward arrangements for an annual evaluation of the Regulator’s handling of consumer complaints by an external, independent reviewer to ensure that it meets the criteria of independence, fairness, effectiveness, openness and transparency and accountability. The reviewer should be appointed by the end of this year and complete the first evaluation in time to publish it no later than Easter 2014.

43. In the first year of operation, 310 complaints were wrongly directed to the Regulator, who then advised tenants of the correct channel. This is not only a waste of the Regulator’s time and resources, but frustrating for tenants. We recommend that the Government, working with the sector and the Regulator, should clearly publicise the correct complaints procedure regarding consumer standards to avoid misdirected complaints.

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83 Ev 61 (HCA Regulation Committee), para 19
84 “HCA panel rejects all calls for consumer regulation”, Inside Housing, 27 April 2012
5 Conclusion

44. The social housing sector is facing new challenges and risks, which mean that the Regulator has an important role to play in ensuring the continuing viability and success of providers. As we explained in the first chapter this is not an inquiry into the regulation of the social rented sector. But, having now carried out this limited inquiry, we intend to monitor developments and, subject to the demands of our programme, we intend at the least to examine the work of the Regulator again before the end of this Parliament.
Letter to the Secretary of State for Communities and Local Government from the Chair of the Committee

Julian Ashby, chair of the Regulation Committee of the Homes and Communities Agency appeared before the Committee on 15 July. His evidence gave me a number of concerns not least his answers on financial viability. I am therefore drawing the transcript of the evidence session to your attention. A copy is attached.

18 July 2013

Letter to the Chair of the Committee from the Secretary of State for Communities and Local Government

Thank you for your letter of 18 July about the evidence session the Committee held with Julian Ashby, Chairman of the Homes and Communities Agency’s Regulation Committee on 15 July. Thank you also for enclosing the transcript of the session.

I have read the transcript and particularly the line of questioning around the use of the financial viability ratings by the Regulator. I take your concerns very seriously and am grateful to you for drawing it to my attention.

As a next step, I have asked Peter Schofield, the Director General responsible for regulatory policy on social housing, to write to Julian Ashby asking him to clarify certain points from his evidence and provide assurance that these important regulatory powers are being used effectively. Once we have considered his response, I will write to you again.

A buoyant and financially stable housing association sector is essential if we are going to continue to deliver much needed affordable homes. An effective and robust system of regulation underpins this stability and I will ensure that this remains in place.

25 July 2013
Conclusions and recommendations

Assessment of financial viability

1. In this report we have not set out to examine the basis for, or quantify, the risks identified by the Regulator as facing the sector. But it must be part of the Regulator’s job to be alert to the risks and the perception of risks which could affect the financial viability of social housing providers. From the evidence we received we are satisfied that he is. (Paragraph 10)

2. We note that Moody’s, in downgrading its ratings for all but one of the English housing associations in May 2013, cited the Cosmopolitan episode as showing the difficulties in ensuring a satisfactory outcome when a housing association encountered financial distress and the challenges the Regulator would face if it had to step in and protect entities and their creditors in extreme situations. We welcome the Regulator’s intention to review lessons from the Cosmopolitan episode and ask for a copy of the review when it is completed. We are therefore concerned by press reports that DCLG has blocked the commissioning of a review. In responding to our report we ask the Government to explain whether it has blocked the review and, if it has, why and how it assessed the consequences of its decision for the independence of the Regulator and the regulation of the social housing sector. (Paragraph 14)

Financial viability ratings

3. We conclude that the failure of the Regulator’s published financial assessment to reflect the serious weakening in the financial viability of the Cosmopolitan Housing Association raises questions about the operation and usefulness of the Regulator’s financial viability ratings. In this case the assessment of financial viability was neither timely nor useful. The eventual downgrading of Cosmopolitan to the lowest grade amounted to a futile exercise in locking the stable door long after the horse had bolted. We are not surprised that Moody’s paid such close attention to the episode. (Paragraph 19)

4. Ratings published by the Regulator should be reliable and capable of being understood at face value. The practice of using governance ratings to signal concerns about financial viability lacks openness and is confusing. It is misleading to the taxpayer and tenants, and potentially also to lenders who, it appears, are expected to understand the coded message from the Regulator. We conclude that the practice should cease. We recommend that the Regulator publish accurate financial viability ratings. (Paragraph 22)

5. Poor governance can undoubtedly undermine the financial viability of a provider but we are not persuaded by the argument that it is “almost inevitably” the cause of financial failures in general. Financial viability and governance ratings serve different purposes and assess the providers against different standards. The distinction between governance and financial viability must be maintained. (Paragraph 23)
Communication with the sector and use of statutory powers

6. It is reasonable, and to be expected, that the Regulator is in regular communication with the sector and on occasion an informal approach will be sufficient. We are concerned when the informal approach becomes a Regulator’s exclusive method of operation. First, it is inconsistent with transparency. Lack of transparency makes it difficult for lenders, tenants and taxpayers to see how much and what action the Regulator is taking. Second, there is a risk that this approach may lead to too close a relationship with providers thus compromising the independence or judgment of the Regulator. Third, if the sector knows that that the Regulator cannot, and will not, use his formal powers, that must undermine his position and effectiveness. (Paragraph 26)

7. We conclude that the Regulator’s relationship with providers has to have a greater element of transparency. In addition, the Regulator should have available powers which he can use when a social housing provider fails to meet the required standards. We make two recommendations. First, that the Regulator work with other regulators to examine whether they have addressed his concerns that use of statutory powers may be counter-productive. Second, although the new regulatory regime is still at a relatively early stage, an experienced former regulator in another sector should review the operation of social housing regulation. The review’s report, conclusions and recommendations should be published. (Paragraph 27)

Review of the protection of social housing assets

8. We commend the Regulator for seeking to update the regulatory regime as the sector changes. We also welcome the fact that the Regulator is considering the need to protect social housing assets. (Paragraph 29)

9. We support the aim of protecting social housing assets and tenants from the risks associated with non-social housing activity by providers but the current proposals lack flexibility and appear to cut across the system of co-regulation which gives providers’ boards the responsibility to assess and mitigate risk. We welcome the decision of the Regulator to revise his proposals and to consult again. (Paragraph 33)

The Regulator’s resources

10. The providers’ submissions about the resourcing, capacity and capability of the Regulator gives us grounds for concern. It appears that the current arrangements may not be adequate and need improvement. The fact that the Regulator himself has identified a need to increase significantly his capacity to make high level business judgments about providers appears to confirm the providers’ views. The reorganisation will have to be carried out without any additional resources and without a hiatus diminishing the Regulator’s scrutiny. We request that, once the reorganisation has been completed, the Regulator provides us with a report on the Regulation Committee’s capacity and capability to carry out its work. (Paragraph 37)
Consumer regulation

11. Having reviewed the evidence we are not completely assured that the Regulator is discharging his responsibilities as we would expect. First, he has interpreted his remit as narrowly as possible. In responding to our report we request that he explain and justify his application of a test that breaches of standards should be systemic when he assesses serious detriment caused to tenants by a breach of consumer standards. Second, we formed the impression that the Regulator has treated consumer regulation as a distraction from his main job, economic regulation. (Paragraph 42)

12. We recommend that the Regulator, working with a body such as the British and Irish Ombudsman Association, bring forward arrangements for an annual evaluation of the Regulator’s handling of consumer complaints by an external, independent reviewer to ensure that it meets the criteria of independence, fairness, effectiveness, openness and transparency and accountability. The reviewer should be appointed by the end of this year and complete the first evaluation in time to publish it no later than Easter 2014. (Paragraph 42)

13. In the first year of operation, 310 complaints were wrongly directed to the Regulator, who then advised tenants of the correct channel. This is not only a waste of the Regulator’s time and resources, but frustrating for tenants. We recommend that the Government, working with the sector and the Regulator, should clearly publicise the correct complaints procedure regarding consumer standards to avoid misdirected complaints. (Paragraph 43)
Formal Minutes

Monday 2 September 2013

Members present:

Mr Clive Betts, in the Chair

Bob Blackman  John Pugh
Simon Danczuk  Andy Sawford
Mrs Mary Glindon  John Stevenson
James Morris  Heather Wheeler
Mark Pawsey

Draft Report (The work of the Regulation Committee of the Homes and Communities Agency), proposed by the Chair, brought up and read.

Ordered, That the Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 44 read and agreed to.

Annex and Summary agreed to.

Resolved, That the Report be the Second Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report, together with written evidence reported and ordered to be published on 8 July 2013.

[Adjourned till 4.00 pm, Monday 9 September 2013]
Witnesses

Monday 15 July 2013

Julian Ashby, Chair of the Regulation Committee of the Homes and Communities Agency

List of printed written evidence

Aster Group
Circle
Council of Mortgage Lenders
Department for Communities and Local Government
g15
HCA Regulation Committee
Home Group
The Hyde Group
Leeds Housing Forum
Luminus Group
Moat
National Housing Federation
Places for People
PlaceShapers
Residents’ Network
Secured by Design
TPAS
List of Reports from the Committee during the current Parliament

The reference number of the Government’s response to each Report is printed in brackets after the HC printing number.

**Session 2013–14**

First Report  The Private Rented Sector  HC 50
First Special Report  Committee’s response to the Government’s consultation on permitted development rights for homeowners: Government response to the Committee’s Seventh Report of Session 2012–13  HC 173

**Session 2012–13**

First Report  Park Homes  HC 177-I (CM 8424)
Second Report  European Regional Development Fund  HC 81 (CM 8389)
Third Report  The work of the Local Government Ombudsman  HC 431 (HC 615 & HC 650)
Fourth Report  Pre-appointment hearing for the Chair of the Audit Commission  HC 553
Fifth Report  Mutual and co-operative approaches to delivering local services  HC 112 (CM 8547 & HC 1091)
Sixth Report  Councillors on the frontline  HC 432 (CM 8582)
Seventh Report  The Committee’s response to the Government’s consultation on permitted development rights for homeowners  HC 830 (HC 173, 2013–14)
Eighth Report  The role of local authorities in health issues  HC 694 (CM 8638)
Ninth Report  Implementation of welfare reform by local authorities  HC 833 (CM 8635)

**Session 2010–12**

First Special Report  Beyond Decent Homes: Government response to the Committee’s Fourth Report of Session 2009–10  HC 746
First Report  Local Authority Publications  HC 666 (HC 834)
Second Special Report  Local Authority Publications: Government response to the Committee’s Sixth Report of Session 2010–11  HC 834
Second Report  Abolition of Regional Spatial Strategies: a planning vacuum?  HC 517 (CM 8103)
Third Special Report  FiReControl: Government response to the Committee’s Fifth Report of Session 2009–10  HC 835
Third Report  Localism  HC 547 (CM 8183)
Fourth Report  Audit and inspection of local authorities  HC 763 (CM 8209)
Fifth Report  Localisation issues in welfare reform  HC 1406 (CM 8272)
Sixth Report  Regeneration  HC 1014 (CM 8264)
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Oral evidence

Taken before the Communities and Local Government Committee
on Monday 15 July 2013

Members present:
Mr Clive Betts (Chair)
Simon Danczuk
Mrs Mary Glindon
James Morris
Mark Pawsey
John Pugh
Andy Sawford

Examination of Witness

Witness: Julian Ashby, Chair, Regulation Committee, Homes and Communities Agency, gave evidence.

Q1 Chair: Good afternoon, and welcome to this evidence session on the regulation of social housing in England. For our records, could you introduce yourself and indicate your position as well.

Julian Ashby: I am Julian Ashby, the Chair of the Regulation Committee of the HCA.

Q2 Chair: Thank you very much for coming to be with us this afternoon to talk about some quite important and challenging issues. Can I begin with one that I think slightly surprised many of us who think of housing associations as pretty firm-rooted organisations? Moody’s downgraded 26 of them, citing a weaker regulatory framework. Do you think that downgrading was a problem for you to deal with or a problem that you created?

Julian Ashby: I certainly do not think it was a problem we created. Moody’s has basically downgraded most of the providers in the sector on two occasions over the last six months. The first one-notch downgrade was at the same time as UK sovereign debt lost its AAA rating and was a direct consequence of that. At that point, they put the sector on negative watch, primarily driven by their perception of the level of Government support for the sector. They then reflected on that, and during that period the Cosmopolitan case, which you may or may not come to know of, was resolved satisfactorily. They eventually settled on a further one-notch downgrade for the majority of associations that they rated, but that was done with the removal of the negative watch, which had potentially threatened multiple-notch downgrades. From that perspective they moved to a position that brings them broadly in line with the other main rating agencies, Standard & Poor’s, and provides stability for the sector going forward. In that period, there was no loss of appetite by investors to invest in housing associations, nor have those two single-notch downgrades affected the margins at which such investment takes place. From our perspective, they are entitled to come to the conclusions they have come to. We are comfortable with the action they have taken and the response of the investment community to it.

Q3 Chair: Did they not cite your discussion document as one of the reasons for the downgrade? Is that true?

Julian Ashby: The view they have taken of that is one that would seem to be at odds with the view taken by the Council of Mortgage Lenders in their submission to you. It is not for us to arbitrate what the rating agencies and other lenders think about these issues.

Q4 Chair: It might be for you to be a bit more careful about how you phrase things in future, to make sure the rating agencies do not get so upset.

Julian Ashby: They were among those consulted about our proposals. We are in regular touch with the rating agencies, with CML and others on these kinds of development. As I say, that phrase was a part of the explanation they gave, but they also went on at some length in their explanation about their perception of the level of Government support for the sector.

Q5 Chair: Are there other issues around that you would have concerns about now in terms of the risk for the sector as a whole?

Julian Ashby: Specifically in relation to the downgrading issue or more generally?

Q6 Chair: More generally. Maybe the rating agencies have not caught up with reality yet and maybe there should be more downgrades on the way.

Julian Ashby: I think they have caught up with reality, but there was some catching up to do. Since the credit crunch, there have been perhaps three major issues that would have been of interest to them. The first is that inevitably, with less grant, new social housing is undertaken with higher levels of debt. That is inevitable, and to some degree riskier. It is also apparent that some £40 billion of bank debt to the sector is underwater; i.e. the cost of providing that funding is less than the banks get in return. They are unhappy with that situation and they seek re-pricing opportunities. That adds a degree of risk in the sector. The final area that affects most associations is welfare reform, which again can have an impact both on the level of arrears and on the costs of collection. There is a range of factors in play that make the sector riskier than it was in the high grant rate, pre-welfare reform environment that applied up to 2008. That is reflected now in the appraisal they have of the sector.
Q7 Chair: Very simply, then, given all this change of plan and slight worsening of climate, do you expect to see another Cosmopolitan in the next 24 months?

Julian Ashby: We continue to get a small but steady flow of problem cases coming to our attention. They are not on the scale of Cosmopolitan. Some can nevertheless be on a quite substantial scale, but they are usually more manageable. There were particular features of the Cosmopolitan case that made it very difficult to resolve. I can go into those now if you like, or wait until there is other questioning.

Q8 Simon Danczuk: All but one registered provider is in the top two viability ratings, V1 or V2. Could you explain why we should trust that assessment? How does it work? Why should we trust that assessment that they are all doing relatively well except for one?

Julian Ashby: There is more than one that is graded below 2.

Q9 Simon Danczuk: How many are there below 2?

Julian Ashby: I could not give an answer off the top of my head.

Q10 Simon Danczuk: How many providers are there altogether?

Julian Ashby: We only rate the 280 largest providers and we work through a programme of reassessing them. We have changed the grading system to one that has four levels, of which the top two are compliant, albeit that level 2 is compliant with issues that we wish to see addressed. The bottom two are non-compliant ratings.

Q11 Simon Danczuk: How many are in the non-compliant?

Julian Ashby: We have those ratings both for governance and for financial viability.

Q12 Simon Danczuk: On financial aspects, how many are non-compliant?

Julian Ashby: That will be a very small number and it will be very small for a specific reason, which is—

Q13 Simon Danczuk: I am just trying to get to the number. You say it is a small number. Is it 50 or 20?

Julian Ashby: It would be a handful.

Simon Danczuk: Five?

Julian Ashby: It would not be more than that. It is a very small number. It would be a small number primarily because non-compliance with the viability standard would almost certainly trigger a potential breach in covenant. We are very wary of making a situation worse by doing something that would trigger a covenant breach.

Q14 Simon Danczuk: So we should trust the assessment that is used.

Julian Ashby: Behind them is a lot of financial analysis and interrogation of business plans and strategies. We put a lot of effort into those and they can be relied on.

Q15 Simon Danczuk: Hyde Housing Association made a loss of more than £38 million, 24% of its turnover and 69% of its operating income. South Anglia Housing has more liabilities due to be paid in the coming year than the total value of its assets. There are a number of examples where there are failings in terms of financial viability. Are the two that I have just mentioned not in the top two?

Julian Ashby: I do not have information to give an answer on a specific case. I am concerned about the figures you have quoted because they do not strike me as being consistent with the view we have of those organisations. I would want to get to understand the information you have, and I would be very happy to give a written response to that.

Q16 Simon Danczuk: Thanks, Julian. Let me ask the question in a different way. In the executive summary of the 2012 global accounts you state that “performance of individual providers varies significantly”. I am trying to understand: if the financial performance of individual providers varies significantly, why are the vast majority of providers in the position of being at an acceptable level?

Julian Ashby: I understand the thrust of that question, but I have to take a step back. There is enormous diversity within the sector. Of the 1,700 associations on the register, an overwhelming majority own less than 1,000 homes and we scrutinise their accounts but do relatively little else. We focus our attention particularly on the 280 associations and groups that—

Q17 Simon Danczuk: Let me repeat the question, Julian. You said that “performance of individual providers varies significantly”. The financial performance varies significantly, yet the vast majority of providers are said to be in a good, healthy state of finances. Doesn’t that seem a contradiction?

Julian Ashby: If you look at performance as profitability it varies enormously. It does not mean, because an association makes modest surpluses, that it is poorly run. For example, in the case of a typical local authority stock transfer association, it will be expected to make a deficit probably in its first up-to-10 years of operation. As it invests very heavily in stock condition, it is doing that not out of surpluses but out of further borrowing. It eventually completes its work, rents continue to rise, it hits peak debt, and then eventually it moves into surplus and pays down that debt.

That is the profile of a typical group of associations that comprise quite a lot of the sector. The fact that they make no surpluses for a period is not, in our view, a reflection that they are poorly run or financially not being run adequately. They are not in that sense breaching our financial viability standard. They are operating their business plan as we expected it to operate, but it is different from a London & Quadrant or an Affinity, who may be making very substantial surpluses.

Q18 Simon Danczuk: Let me be honest, Julian. You are not providing me with a lot of comfort, but let me ask you the question in a different way. Hyde Housing Association made a loss of more than
£38 million, South Anglia Housing has more liabilities due to be paid in the coming year than the total value of its assets. You cannot tell me what their grading is. That sounds to me like they are at risk, but you do not know as chair of that committee whether these organisations are rated fairly, poorly or where they are rated. They are just not on your radar.

Julian Ashby: If I had notice of that question, I would be able to give you our analysis of the financial strength of both those organisations, and the reasons. If it is the organisation I am thinking of, Anglia is part of the Circle Group, which is a substantial group making large surpluses overall. I am not aware of a specific problem with one of its subsidiaries. You are giving me information that is news to me. I would want to be satisfied that I had a full picture of that association before making a response to you as to whether our grading of them is adequate.

Q19 Simon Danczuk: Finally, in terms of Cosmopolitan Housing Association, it took until December 2012 before your organisation did anything about them or registered them as a concern. There had been coverage in the media well before that, in October if not before. Why were you so behind the curve?

Julian Ashby: We were not behind the curve. We started picking up concerns about them in May of that year, and the action that we took—in fact, particularly the action in insisting that they got in additional support—was what uncovered further problems and then ultimately led to them being resolved. If you are looking simply at the change in the rating, that was because the situation was moving so fast we were not quite sure where we would place them. Most of our focus at that time was in getting the problems resolved, not on the issue of what the rating should be. We suspended the rating and then eventually—

Q20 Simon Danczuk: When did you suspend it? In May?

Julian Ashby: It would not have been as early as that. It would have been at a later stage, when the severity of the problems became much more apparent.

Q21 Simon Danczuk: But well before December.

Julian Ashby: As far as I am aware, before December.

Q22 Chair: I want to pick up on one point. You said in response to my earlier question about whether there would be another Cosmopolitan that there is a small number of problem cases that you are aware of. When I look at the ratings that Simon has just been referring to, there is a rating of V3. “The provider’s financial viability is of concern and in agreement with the regulator it is working to improve its position”. That sounds like a problem case to me, yet not a single association is rated in that category.

Julian Ashby: We tend to use the governance rating as the way of signalling our concerns about an association, because it is the Board that is responsible for both the financial viability and—

Q23 Chair: Why do you have a financial viability rating if you do not use it in those circumstances, then?

Julian Ashby: We do use it, but the circumstances—

Q24 Chair: It is not used for anybody here. Apart from Cosmopolitan, which is obviously in the bottom section, there is not a single organisation rated in V3. Everyone else is basically good or very good.

Julian Ashby: I see the point you are making.

Q25 Chair: It is quite an important point, isn’t it?

Julian Ashby: It is. A conclusion, though, that an association is not viable is a very serious conclusion to come to, because it is not simply saying that there are issues to address.

Q26 Chair: The wording is not “not viable”. It says, “Financial viability is of concern”. Not a single association in the country concerns you with regard to their financial viability.

Julian Ashby: The issue that highlights is the difficulty of giving a grading that could trigger a re-pricing.

Q27 Chair: So is it not worth the paper it is written on.

Julian Ashby: The issues that you are referring to are ones that we will need to think about further and, indeed, are thinking about further. It highlights the issue that plays out. It is the reason why I gave the debt of the sector being underwater as one of the major risks to the sector, with the re-pricing risk that can flow from that. If we use any of our statutory powers, we are potentially putting lenders in a position where they can re-price, so we tend to be very careful about how we approach those situations. We do not wish to make a difficult problem worse by triggering a re-pricing. That is one of the constraints under which we are operating at the moment, and we have to be extremely careful about it.

We tend to say to associations that are getting into that territory, “We wish you to do the following things to improve yourselves sorted out. If you do not do those things, we will take statutory action.” They generally see that if we are forced to take statutory action, it will put them in a worse position, so they tend to respond positively to the suggestions we make for improving their situation.

Q28 Andy Sawford: In how many cases have you done that, in the past 12 months?

Julian Ashby: I am just trying to think of the total number. There are probably at least 20 cases where we have been giving associations a pretty strong steer on the actions we expect them to take to resolve what we see as significant problems.

Q29 Andy Sawford: So there are 20 cases that really should be in V3.

Julian Ashby: They are not necessarily issues. It is because they cover both viability and governance concerns.
Q30 Andy Sawford: How many are on financial concerns? Half?
Julian Ashby: I would say significantly less than half.

Q31 Andy Sawford: Are we back to the handful?
Julian Ashby: We are back to the handful.

Q32 Andy Sawford: Why is the handful not in here?
Julian Ashby: I am not sure which document you are looking at.

Q33 Andy Sawford: Following the Chair’s question, we are looking at the number of providers where financial viability is of concern, and in agreement with the regulator it is working to improve its position. You have clearly described that is the case and yet they are not reflected in the figures. What confidence can the public, the Government and stakeholders have in all of your figures given that you are clearly sitting here telling us that you cannot publish the accurate figures?
Julian Ashby: We are talking about an area where our main concern will be governance, and if the board of the association does not get a grip quickly on its situation, then what is currently a V2 judgment would turn into a V3. We would approach that through the governance route, because it is the board’s responsibility to resolve potential financial failings first. That is the route that we are taking, but I understand the point you are making and we will reflect on it.

Q34 Simon Danczuk: The first question I asked you was whether we should trust the assessment that is used. Bearing in mind the last 15 minutes of dialogue, I am now asking you: should we trust the assessment that is used—yes or no?
Julian Ashby: You can still place reliance on the assessment that is used. You have put to me two cases that, on the face of it, sound in a very precarious—

Q35 Simon Danczuk: You have admitted that there are providers who should be in V3. You have said that to the Committee.
Julian Ashby: I said they are on the boundary of V2 and V3.
Chair: That is a slightly different form of words from what we have heard in the last 15 minutes.

Q36 Andy Sawford: There are only 25 in V2. You already classify a range where it is about governance, particularly in V2. The V3 is about financial viability. You acknowledge that there are serious issues out there for housing associations at the moment in terms of the market they are operating in and financial viability. You are telling us that we can trust a figure that indicates you have concern about no providers, yet you are also really telling us there are about 20 where you have had those conversations about financial concern.
Julian Ashby: I took your question to be about the number where we have discussions along the lines of, “We wish you to take action to address problems”, not as narrowly as addressing financial problems, but problems in the round. That includes a range of issues
in governance that could ultimately impact on financial viability at the point we begin to tackle them. There are cases, for example, where five years ago we might have moved fairly quickly to make statutory appointments to a board. We do not do that now because if we did so, it would trigger the potential of re-pricing for that association. In a number of cases, we have gone to that board and said, “We are not satisfied with the skills you have available to tackle this set of issues, and we require you to get some additional board members with the necessary skills.” They have invariably done that to our satisfaction. If they refused point-blank, we would make the appointments and take the consequences.

Q37 Mrs Glindon: Moving on to governance, six of the providers have had a G3 rating, and you touched on what you would do if there were concerns. What specific concerns are there with the governance of those six providers?
Julian Ashby: I could not answer that off the top of my head, because each of them will be a different set of issues. Generally speaking, it is if we have concerns about the competence with which they are managing their providers’ affairs. It may be issues of treasury management; it may be a range of different issues. It may be problems in their long-term financial forecasting. There can be quite a wide range of things that could trigger us having concerns about their governance. Usually, if it is graded G3, it is because they are being slow to correct the problem.

Usually we find if we identify an issue with an association it moves very quickly to address that. If it does not seem to understand the problem or seems to be very slow in doing so, we will move to a G3 judgment where we are basically saying: “You aren’t compliant with the governance standard and you are in danger of further intervention”. Indeed, there will be pretty close engagement on a regular basis with all the associations in that category.

Q38 Mrs Glindon: Would you say that the sector is complacent about its governance, or would you speak more highly of it?
Julian Ashby: The sector as a whole is aware that it is operating in a significantly riskier environment than it was five years ago. Our standards place very robust requirements on boards to govern their associations under those circumstances. They are aware of that for the most part; they find it quite challenging. I have talked to a lot of boards and they tell me they find it quite challenging. I do not think it would be fair to categorise them as complacent. Most of them are taking proper steps to work with their executives to address the particular issues that they have. Not all of them are successful at that, and we obviously take an interest in those in particular.

Q39 Mrs Glindon: Do you think that the registered provider boards have the skills and personnel to direct and manage their businesses through what the HCA has called “profound change” in the traditional social housing model?
Julian Ashby: It is a challenging time for boards. Some will struggle with that change, which is
something we remain concerned about and why we attach a great deal of importance to governance and to our continuing engagement with the larger providers of their governance. It is an area which will continue to be tested over the next few years as these various changes work through, but that is the nature of the beast. All associations have boards. Some are paid; some are not. They all have to comply with the governance standard. Indeed, as I am sure you are coming on to, we intend to strengthen the governance standard, particularly in relation to protecting social housing assets. That will be a further issue that they have to grapple with. It is right that the responsibility for managing competently independent organisations rests with their boards. It is not the duty of the regulator to be second-guessing boards. They have that responsibility; we are seeking assurance from them that they are discharging it competently. That is the route we follow.

Q40 Mrs Glindon: Do you think the main role of the regulator on governance would, in future, be to toughen the standards, as you said? If it is found that the sector itself does not have the skills and personnel to meet the standards, how can they be found? Where can they go to raise their standards and find the right personnel and people to do that?

Julian Ashby: At a sector level, the sector appreciates the degree of change it is going through and what that means for its boards. They put a lot of effort into strengthening their governance. One of the things that we most commonly request associations that are struggling in some respect to meet the standards to do is to commission an independent review of their governance. This is not something we carry out ourselves. We tell them to go to an independent firm and get external advice on how to strengthen their governance. If they are a problem case, we will have an interest in both the brief for that exercise and the output from it, but ultimately the sector has responsibility for its own governance and must step up to the mark in terms of doing that.

I cannot over-emphasise the extent to which associations differ very widely in their size, scale and range of activities—some are very specialist; some are very localist—and it is right that the skills the board has around its table reflect those differences. It is not that a London & Quadrant is looking for the same skills as a smaller, more local association, a specialist provider of housing for the elderly or one that does care and support on a large scale. They are very different and have different needs. It does not make it easier to regulate, but those are differences that we have to recognise in the arrangements we make to monitor and regulate them.

Q41 Andy Sawford: Your submission suggests your powers are not fit for purpose in the current economic climate, and you have repeatedly talked about the risk of re-pricing. The fear of causing providers to breach loan covenants is something you have raised. This clearly ties your hands, and it has come out in the questioning. Exactly which of your powers are not now available to you?

Julian Ashby: All the powers are there and are available to us. The issue is whether it would be prudent to use them.

Q42 Andy Sawford: Let me rephrase the question, then you can answer it. Which of your powers do you not use?

Julian Ashby: As far as possible, our approach has been modified to achieve the changes we expect to see in those who are underperforming without use of statutory powers. We are no less robust in our analysis and identification of issues. We will raise those issues with the executives and/or boards depending on the nature of the problem. We will be very demanding of them making changes and improvements, but we will seek to do that in effect by agreement, rather than by saying, “We’re going to issue an enforcement notice” or “We are not interested in your plans; we’re going to put three people on your board”. We are engaging with them without use of powers.

Q43 Andy Sawford: I think it is fair to say the Committee has an understanding of how you are approaching this. Two things arise from that. The first is: do you accept that whilst this may in your view be the intelligent way of using the powers currently, there is an impact on how relevant and easy to understand your role is to the outside world and the ratings that you use?

Julian Ashby: I can see that it is potentially an issue.

Q44 Andy Sawford: Do you think there is a way you could overcome that? For example, could you make viability ratings internal only?

Julian Ashby: They would be pretty pointless if they were internal only.

Q45 Andy Sawford: Are they not pretty pointless at the moment, in truth? They are not used, so they are pointless in that respect.

Julian Ashby: The 1s and 2s are used extensively. It is the 3s that give us the area of concern that you very rightly hit on as an issue. That is an area that we will think more about. It is a problem for us.

Q46 Andy Sawford: If you were separated from the HCA and were independent, would you be able to give a much fuller picture of financial viability?

Julian Ashby: I think it would make no difference on this issue. It is not about the location of the regulation function. It is about how we deal with cases in a way that does not make them worse by triggering a re-pricing, which could see an association with some financial difficulties become an association with very serious financial difficulties. It is a dilemma for us, which I think you appreciate.

Q47 Andy Sawford: Have you conducted any research into how this dilemma is overcome in other sectors? For example, listed companies forced to give profit warnings or the IMF publicly commenting on Governments’ fiscal policies that then has an impact on countries’ credit ratings. This is not a unique dilemma. Have you looked at how others are overcoming it?
Julian Ashby: We have an unusual regulatory structure in terms of operating not through a licensing arrangement like most regulators, but through a set of standards that we then have various powers to enforce. It is a different architecture. We do find ways of signalling our concerns and we have particularly used the governance rating for that purpose because that does not have the same re-pricing trigger impact that a V3 or V4 would have. That is understood, and the messages that we have put out through that, if you have read some of them, are pretty strong.

Q48 Andy Sawford: Do you think that is fair to lenders, banks or tenants?

Julian Ashby: That situation is well known to lenders, and I would say look at the CML submission to this inquiry in terms of whether they are broadly satisfied with the line we are taking on that.

Q49 Andy Sawford: Actually, most people seem satisfied, but that seems to be because they all have a vested interest in maintaining what seems to be a bit of a farce, to put it bluntly.

Julian Ashby: I do not think it would be fair to categorise CML in that way, but I do not deny the strength of the point you are making on the use of ratings that can trigger that kind of problem.

Q50 James Morris: Listening to this, I am slightly bemused. If I were a member of the public, would I not think “I have absolutely no confidence whatsoever in the regulatory environment that you are presiding over?”

Julian Ashby: Is that a question or statement?

James Morris: It is a question.

Julian Ashby: Could you repeat it?

Q51 James Morris: If I were a member of the public listening to this discussion, I would probably draw a conclusion that you are not an independent regulator, you are not having any effect in positively regulating the market that you are meant to regulate and you have failed to answer the question of how to resolve the dilemma that you have accepted as part of this discussion.

Julian Ashby: The first thing I would say is that the rating of associations is a part of what we do, but the principal focus of our engagement is to identify issues with providers and get them resolved. In the main, we undertake that work on a basis that is not greatly in the public view; it is direct engagement between regulatory staff and the providers. In an overwhelming majority of cases, it leads quite swiftly to a resolution of the problem that has been identified.

Q52 James Morris: The consequences of failure, though, could be quite devastating for tenants, communities—

Simon Danczuk: Taxpayers.

James Morris: It is not just a cosy little conversation.

Julian Ashby: If we did not do that job competently, then it would have the consequences you describe. I would argue that it is not leading to those situations because we are being successful in getting those problems resolved. At any one time, we have a significant case load that varies from those with whom we have minor concerns through to those about which we have serious concerns. We have regulatory staff engaging with those organisations on a very regular basis depending on the severity of the issues that we are dealing with. In all those cases, we track them through until, from our point of view, the issues are resolved and they drop back to being those that we will monitor on a regular basis, but not be engaged with on a much more intensive basis. That is a process that continues, and I would argue that we have become more effective in doing that over the last year, not less effective.

Q53 Andy Sawford: I am just thinking ahead to a few years’ time. Let’s hope that you are successful, but we have seen significant failures of regulation in this country in recent years, and there is a duty on us as Members of Parliament to look at this situation. If you are not successful and a number of housing associations fall in the next few years, what do you think the verdict would be on the approach you are taking right now to not be publicly transparent about the financial viability of housing associations? What would the verdict be on this Committee if we failed to properly address that?

Julian Ashby: The issue does depend very much on what triggered the collapses. We certainly take the potential for an association to get into serious trouble extremely seriously. That is one of the reasons why we published a discussion document about potential strengthening of the framework. We take extremely seriously our ability to tackle those problems. If there were a series of failures of providers, they would have dire consequences for the tenants of those providers. If lenders ever get to the point where they have to enforce their security, it ceases to be social housing. The protection that tenants have then relies on their tenancy agreements and not on the protection of their being within a regulated sector. We are very, very concerned about that, to the point that we have put forward ideas for strengthening the regulation which, as I am sure you are aware, have been of concern to a number of providers. We steer a course here—

Andy Sawford: I think you are restating your position, and there are other questions.

Q54 John Pugh: You have led us very nicely into the next round of questions. Having spent half an hour being attacked for not doing nearly enough, you are now going to be criticised for doing far too much. You talked about your proposals, which have been described as naïve in some provider circles. What is the effect of your proposals or the consultation document on co-regulation or the principle thereof?

Julian Ashby: I think it has no impact on that. As far as we are concerned, it remains that boards have the overriding responsibility to meet our standards. If we amend the standard to require boards, for example, to be satisfied, in undertaking any non-social housing activity, that if that activity goes wrong it will not bring down the social housing side, that responsibility would be for the boards of those associations to manage through. There is no change in the core
principle that it is for boards to manage risks and to meet our standards.

The question of how the standard is best amended and the role that ring-fencing could play is very much up for debate. This was a discussion document, not a set of proposals. We put forward a number of ideas and some of those, particularly around recovery plans and amendments to consent disposals, have been quite positively received. The proposals we put forward on ring-fencing have been fairly well received by lenders and not at all well received by providers.

Q55 John Pugh: One provider said you have failed to recognise “the sector’s capacity for business excellence”. From what you have said so far today, I think you are aware that you are dealing with a mixed sector.

Julian Ashby: We are dealing with a very mixed sector, and there are issues that have perhaps not been expressed sufficiently clearly in the discussion document. For example, we have never had a wish to inhibit the range of activities that associations carry out in support of their communities. Nor have we any intention of inhibiting associations from developing multi-tenure or mixed-tenure schemes, because that is the way of development in the future. However, we remain concerned about the use of social housing assets to undertake commercial activities.

Q56 John Pugh: On that, do you think greater regulation should apply to for-profit providers, who presumably have a better motive to do that than a not-for-profit provider?

Julian Ashby: In principle, ring-fencing is a more appropriate tool for for-profit providers because they are almost invariably subsidiaries of other for-profit organisations. Therefore, to preserve public value within a new for-profit provider, you would have a ring-fence, so it is appropriate under those circumstances. There is another group of associations where it is appropriate, which are those that choose to have a parent that is not registered with us. In those situations, if we do not regulate the parent company we have no means of knowing what is happening to surpluses across the group. There is a strong case for ring-fencing in those two circumstances, but we recognise that in relation to the rest of the sector, ring-fencing would be extremely difficult to operate because it would be difficult to know what should be inside it and outside it.

From our perspective, it is more important that associations manage all their risks than that they manage risks inside a ring-fence and we take no interest in what happens outside it. Our experience of associations using subsidiaries as a way of managing risk, which many of them do, is that they are not always successful in isolating the risk to a subsidiary.

If we relied exclusively on a ring-fence, we would have to be certain and satisfied that that ring-fence was effective. There is too much evidence that, in a range of circumstances, the risk bridges across from the subsidiary to the parent and it would not be wise to rely on that as the only mechanism for protecting social assets.

Q57 John Pugh: If your proposals, including ring-fencing and other things, are carried through, how do you expect the sector to change?

Julian Ashby: I expect that the sector will become more diverse over the next five years. We are not looking at a one or two year issue; we are looking at how the sector will develop over the next five to 10 years.

Q58 John Pugh: Would your changes facilitate that?

Julian Ashby: We expect the sector to become more diverse, not because we are desiring it or willing it. We think it is an inevitable response by the sector to the circumstances they now find themselves in that they will diversify their activities. We see our role, as the social housing regulator, being at heart to protect the social housing investment.

Q59 John Pugh: So yours is a response to the diversity.

Julian Ashby: It is in anticipation of further diversification. We feel that we want to put in place steps to enable that to take place without undue threat to the social housing assets.

Q60 John Pugh: Given that for some providers, this may not be wholly welcome, who actually decides at the end of the day what happens?

Julian Ashby: We decide at the end of the day. We will put forward proposals for formal consultation. We are some way away from that stage as yet.

Q61 John Pugh: When will you be at that stage?

Julian Ashby: We hope to be in a position to put forward proposals for consultation by the end of this year, but depending on other issues that may blow up that may not be the time scale. Our hope would be to do it this year. That would lead to strengthened standards. It is then the responsibility of associations to meet those standards.

Q62 John Pugh: In a sense, it is a unilateral decision on your behalf. No?

Julian Ashby: It is our role to set the standards, but we only do that after proper consultation. The reason we have done it in two stages, first with a discussion document, is that we wanted to flush out exactly the issues that have been flushed out. We will now approach the next stage of formulating our proposals significantly better informed as a result of that discussion process we have had, and indeed, as a result of a number of providers who have for the most part accepted the diagnosis of the need for change, some of them have also risen to the challenge, saying, “We do not particularly like this aspect of the proposals, but have you thought of approaching it in a different way?”

We have had some quite useful ideas coming out of this. We are reflecting on it all. The committee meets on Thursday, as it happens, to look at our next stage of drawing up proposals, but this will be an iterative process through the autumn as we discuss what we might do with the normal stakeholders that we engage with on a regular basis. That includes both providers and lenders.
Q63 Chair: You obviously have concerns and you have told us about a number of things coming together: lower rates of grant, more borrowing, more fluctuations in borrowing, more associations going for market-rented properties and various other commercial activities, and then the potential for arrears to grow as well due to some of the welfare reform measures. Is it the fact that all of these things coming together to give you concerns about housing associations as a whole is driving your demand for a new regulatory framework?

Julian Ashby: Yes.

Q64 Chair: Isn’t your proposal to bring in a new set of arrangements to cover all housing associations actually doing what we were trying to suggest earlier, which is trying to focus and identify associations where there are problems, and to flag those up, make them transparent and deal with them? Instead, every association in the country, however viable and however well run, is now going to be hit by a new set of regulatory measures.

Julian Ashby: The regulatory architecture we have to work with is one that sets standards, and then we have a set of powers that we can use to make sure those standards are met. That is the way the regulatory system has been set up. It is not a system we have devised. That is the statutory arrangement. We only have powers to enforce standards that have been set. In this situation, we need to set standards—

Q65 Chair: Would it not be helpful if you actually dealt with the powers you have and enforced them properly rather than going on to all the new powers?

Julian Ashby: There is considerable evidence that we are successful in getting providers to achieve the standards that we have set. We think that the standards do not address sufficiently the new trends and risks in the sector towards both diversification on the one hand and different types of risk on the other. We are not talking about wholesale changes to the standards, but refinements to the governance and viability standards in particular to reflect a riskier external environment. It is not our intention to have a series of prescriptions that everybody has to do this and that.

Q66 Chair: I do not know what a ring-fence is but a prescription that everyone has to do this and that.

Julian Ashby: If you have, as was part of that discussion document, a comply or explain basis, it is hard to say this is requiring everybody to do something if one of their options is to say it is not appropriate to their business model, and therefore explaining that they are going down a different route. I would take issue with that diagnosis. We are being much more flexible than it implies.

Q67 James Morris: Could you explain the rationale behind ring-fencing and tell us a little bit more about how it would work?

Julian Ashby: As I say, I am not convinced that ring-fencing is necessarily the most appropriate tool for the majority of associations.

Q68 James Morris: Why have you floated it at all?

Julian Ashby: We floated it as one of the suggestions in a discussion document while acknowledging that a number of difficulties are attached to it.

Q69 James Morris: What is the rationale for having it in the consultation document?

Julian Ashby: The rationale for having it in the consultation document is to get providers thinking about the extent to which it is reasonable to use social housing assets, in which the taxpayer has put significant investment, to support commercial operations. That remains a valid issue. You would expect us as the regulator to be safeguarding the public investment that has already been made in social housing. Looking to a period ahead when associations are likely to undertake significantly more commercial activity, you would expect us to have a view about how, in that context, we propose to safeguard the taxpayer interest.

Q70 James Morris: But it might not be a ring fence.

Julian Ashby: It might not be a ring fence. It is likely to be, perhaps, a ring fence for a small group of providers and other mechanisms that will have to some extent a similar impact for other groups of providers. We are not seeking a one-size-fits-all solution.

Q71 Chair: Are you saying it is a principle that no association should be able to raise investment resources for market-rented housing on the back of social housing?

Julian Ashby: We have not taken that view. We have expressed a view that the extent to which public and social housing is used for security for commercial activities should be limited to the extent that if those commercial activities fail, it should not cause the lenders to social housing to have to foreclose on their security. It is about managing the risk of commercial activities and setting plans for what they would do. For example, if these commercial plans did not come to fruition in the way they hoped, how would the association manage its way through that process? Those are the sorts of lines we are taking and they are very consistent with the recovery plan approach that has been broadly welcomed by providers in the same discussion document.

Q72 Chair: I am going on to what is called a living will, about how you get out of a problem if one occurs. Can you have a realistic living will that everyone can have some faith in as the plan that would be delivered if things got tough?

Julian Ashby: This is an idea that, in embryo and at its most basic level, would require providers to know about all their social housing in terms of how it is charged, what restrictions there are in title, to which lenders they have pledged it as security and how much free security they have. Those are very basic issues about the management of assets that become crucial in the context of a rescue. I would argue, and you would probably share the view, that it is information that any well run association ought to have at its fingertips anyway.
Q73 Chair: Would it be made public?
Julian Ashby: No, because it is commercial information. I would not expect it to be made public.

Then building from that, once they have that database about their assets and liabilities, for those who are undertaking riskier activities, the onus will be on them to demonstrate how they will manage it through, if they run into difficulties with those activities. In the event that they ran into problems with their social housing, what routes would there be to help manage through that process? Traditionally, the sector has coped with those problems by seeking another provider to take over full responsibility for all assets.

Q74 Chair: That information would be available to you and you would have to be confident it has been made available to the board of the association as well.
Julian Ashby: We would expect it to be driven by the board, hence my reiteration that this would not be cutting across the co-regulation principle. It would be the board’s responsibility to put these arrangements in place, and we would be seeking assurance from boards about the effectiveness with which they have done that.

Q75 Mrs Glindon: Do you think you have the capacity to deliver your existing system, let alone take on a more proactive regulatory role?
Julian Ashby: We have resources that I think are sufficient in financial terms at present, but the main force of that question is in terms of the level of expertise we need to regulate an environment that is getting riskier, in which the largest providers are diversifying and running more complex businesses.

We have taken the view as a committee that we need to significantly enhance our capacity to make high level judgments about providers. We are doing that by reorganising within the obvious financial constraints that apply to us. I would hope by the end of this year that we will have approximately three times as many senior managers in the regulation division as there were at the point when I took on responsibility. That is being done within existing resources.

Once we have those arrangements in place, I expect them to make it possible for us to do the kinds of things we are envisaging, but that is something we keep under very close review as a committee. Without those arrangements in place, and at the time when we were dealing with Cosmopolitan, we had to pull in resources from everywhere to focus on that. A number of other projects that we were trying to take forward had to take the back seat until we had Cosmopolitan resolved. It stretched our resources very thin. I am confident that it will greatly strengthen our capacity. Time will tell whether it is sufficient, but if we begin to get concerns that it is not sufficient, then we will take further steps.

As you know, we have already begun to discuss the possibility of charging fees as a way of strengthening our resources. That is something that we continue to have discussions about. No decisions have been taken, but we have the power, subject to various consultations and Secretary of State consent, to charge fees. That is an avenue that is potentially open to us to enhance the resources available. Both as a regulator and as a part of Government, we understand the constraints that there are on public expenditure.

Therefore, we do our very best to operate within those constraints.

Q76 Mrs Glindon: Do you consider that you have sufficient resources to carry out the recruitment that the Department says you are carrying out now?
Julian Ashby: Yes. That recruitment is the final stage of bringing in additional outside expertise to strengthen the senior management of the regulation division. We see that as a crucial step in strengthening the regulatory function.

Q77 Mrs Glindon: Can you say that the Department has met your requests for resources?
Julian Ashby: Our requests for resources in effect are routed in the first instance to the HCA, and then on to the Department. We live, as far as we can, clearly within very tight financial constraints that apply to the Department and to all of the HCA. We have taken the view that the first thing we should do is try to make the very best use of those resources, which is what we are doing through the strengthening of senior management capacity. We believe that will be sufficient, but it is a situation that we are watching very closely. If two or three cases came bubbling up that were of a very serious nature, we might revise that view, but, at the present time, we think the steps we are taking to strengthen our capacity are appropriate.

Q78 Mrs Glindon: So the statement that the Regulation Committee’s own public minutes recorded, that “Members remained concerned that the regulator did not have enough resources in the right place in order to deliver all the outputs expected of it”, will not hold.
Julian Ashby: That is a legitimate concern for other parties to have. Regulation is in a transition from a previous era in which problems were less complex and in which regulation was less outcome-driven and more prescriptive. We now need people who are capable of making quite complex business judgments.

That is what we are seeking to recruit. When we have those people in place, I am confident it will greatly strengthen our capacity. Time will tell whether it is sufficient, but if we begin to get concerns that it is not sufficient, then we will take further steps.

Q79 Mark Pawsey: Mr Ashby, I want to ask you a couple of quick questions about your committee’s role as a regulator of consumer standards. Tenants are looking to you and your committee to defend their interests. When you were put under pressure about whether or not there are housing authorities where there is any financial viability concern, you conceded that the picture perhaps was not quite as rosy as the figure of zero for V3 was showing. Yet there have been over 400 complaints about consumer standards and not one was judged to be a case of serious detriment. Are you just as complacent looking after the interests of tenants as you are in managing the financial viability of housing associations?
Julian Ashby: I would take a step back, if I may. We now have a very different role in relation to consumer
regulation from our predecessor body, the Tenant Services Authority.

Q80 Mark Pawsey: People will find it hard to understand that there have been 400 cases brought to the attention of your committee, but you have not found any where there has been a matter of serious detriment. Is that right? Is it just that everything is uniformly excellent or are your own standards too low?

Julian Ashby: There are four consumer standards, three of which are the direct result of directions from the Secretary of State. Although we “set” the consumer standards, in three of them they are the substantial result of Government directions. The policing of those standards is not something that is primarily done by us.

Q81 Mark Pawsey: But you would accept that somebody looking in from outside might take the view: “Hold on, here’s a body which is simply rubber-stamping and saying that everything is okay”. Julian Ashby: No. The power to collect information about performance was revoked as part of the abolition of the TSA. There is no proactive monitoring against the consumer standards because the Localism Act determined that that is not the role of the regulator.

Q82 Mark Pawsey: I must ask you then: to whom should tenants look for somebody to protect their interests in this sector?

Julian Ashby: The Act envisages that complaints by tenants should in the first instance go to their landlords, that they should be supported in that by tenant panels—

Q83 Mark Pawsey: We do not know whether or not the landlords are providing the right data to their tenants for the tenants to be able to do that scrutiny themselves.

Julian Ashby: I understand the point you are making, but our power to monitor the effectiveness with which landlords are undertaking the consumer standards was removed by the Localism Act. It has left us with two specific roles: one to set standards and the other, which is described as a backstop role, to take action where there may be systemic breaches leading to serious detriment.

Q84 Mark Pawsey: Has it led to a situation where tenants are in a substantially weaker position than they were previously?

Julian Ashby: That is primarily for others to answer. We operate a system whereby tenants continue to make complaints to us even though we are not the body to whom it is appropriate to make complaints. Roughly three quarters of those complaints do not relate to breaches of the standards and therefore are not within our remit. In those cases, we point them in the right direction to get them resolved. The way they should be resolved is by the landlords with the intercession of the tenant panel—

Q85 Mark Pawsey: You are saying it is nothing to do with your committee.

Julian Ashby: If it is not resolved they should then go on to the Housing Ombudsman. That is what the Housing Ombudsman Service exists for. We have a role, but it is not that role.

Chair: Mr Ashby, thank you very much for coming to give evidence this afternoon.
Written evidence

Letter to the Chair of the Committee from Julian Ashby, Chair of the HCA Regulation Committee

HCA Regulation Committee Oral Evidence Session

I am writing following the oral evidence session on 15 July to clarify important matters in relation to the HCA’s regulation of financial viability that I would like to be put on the record. I also wish to take this opportunity to provide reassurance about the financial viability of two providers mentioned in evidence: Hyde Housing and South Anglia.

The Committee questioned why we had not issued more non-compliant (V3/V4) viability judgements. I want to make it absolutely clear that we will issue a V3 or V4 rating if we feel it is warranted. Failure to comply with a fundamental standard is a serious matter, including because it could impact on the price a provider pays for their existing debt, potentially making a bad situation worse. Our regulatory strategy is to work with any provider with weaknesses or serious exposures to deal with issues before it gets to the stage that a V3 or V4 is necessary; and that is why we have not issued any V3 ratings (and only one V4 rating) to date. This approach, in conjunction with our proactive work on governance to spot problems early and the financial stability of the sector, means a failure against our viability standard should be a rare event.

Further information in relation to our regulatory approach is set out below.

The Basis of our Governance and Viability Regulation

Our regulation of financial viability is designed to give us assurance that providers meet the required outcome in the regulatory framework that “Registered Providers shall manage their resources effectively to ensure their viability is maintained”. Our rounded assessment is based on examination of providers’ financial planning and control framework and analysis of key financial information. Although judgements are based on the information available at any given time, this is inevitably a forward looking process. We look at viability over a 30 year business plan but focussing on the first five years.

Our public judgements have two grades reflecting compliance with the required outcome—a V1 judgement indicates that a provider is meeting the requirements of the standard and has the capacity to mitigate its exposures and a V2 judgement indicates that a provider is viable but there are material exposures that need to be managed in order to maintain viability. There are two non-compliant judgements, the straplines for which are as follows:

V3—The provider’s financial viability is of concern and in agreement with the regulator it is working to improve its position

V4—The provider’s financial viability is of serious concern and it is subject to regulatory intervention or enforcement action.

Any grading of V3 or V4 is a very serious matter, indicating that the provider has or is about to fail financially.

Our viability requirements are part of a broader governance and financial viability standard. We issue separate judgements on the governance and financial viability elements of the standard but there is a close connection between them. At the root of financial failures will almost inevitably be a failure in governance and by carrying out our proactive regulation of governance we seek to spot problems early and prevent them developing to the point where they have an impact on viability. The grading system for governance broadly follows that of our viability regulation with two compliant grades (G1 and G2) and two non-compliant grades (G3 and G4).

Since April 2012 we have issued the following numbers of judgements at each grade.

V1 (108 providers) G1 (118 providers)
V2 (25 providers) G2 (19 providers)
V3 (0 providers) G3 (6 providers)
V4 (1 provider) G4 (1 provider)

The combined effect of forward looking financial regulation, proactive regulation of governance and the general financial strength of the sector (based on its very stable, asset based business model where there is constant demand for provision of social housing) means that failures of viability should be and are very rare events.

Hyde Housing Association

Hyde group’s financial statements were posted just prior to the select committee hearing. They have posted a loss of £2 million as a result of a fall of £27.7 million in the value of derivatives. The underlying surplus before tax was £25.7 million. We have not yet considered the latest accounts as part of our ongoing viability regulation. However, we are well aware of the reasons for this loss and are not concerned that it affects underlying financial viability. We will, of course, reflect on the latest accounts as part of our continuous review of viability.
This recorded loss is as a result of changes in accounting rules that are applicable to providers, such as Hyde, that have issued capital market bonds and have entered into derivative (swap) arrangements to protect against adverse movements in interest rates. Financial Reporting Standard 26 requires providers to state derivatives at fair value in the accounts. Doing so does not affect the cash flow of a provider and the “loss” is not crystallised unless the instrument is wound up. The sector is moving over to this method of accounting and the effect will be more volatility in surpluses and deficits. In most cases this volatility will not be indicative of underlying financial weakness at providers, unless there are other problems. To set this in context, Hyde Housing Association has (at 31 March 2013), cash balances of £41.6 million, agreed long term loan facilities of £1.5 billion and derivatives of £350 million.

A move to these new accounting rules is noted in our sector risk profile and exposure to derivative products such as those entered into by Hyde is something we monitor on a quarterly basis in our quarterly surveys of registered providers.

Our latest regulatory judgement, published in December 2012 confirmed Hyde as a V1, G1.

South Anglia

South Anglia is a subsidiary within Circle Housing Group. We regulate at a group level and Circle Group made a surplus of £21.4 million in 2011–12 and had total net assets and reserves of £374 million and has a V1 assessment for viability and a G1 assessment for governance. The current financial position of South Anglia is underpinned by the strength of the Circle Anglia Group as a whole, and reflects a planned period of investment in new homes and regeneration.

I trust this explanation is to the Committee’s satisfaction. I will, of course, be happy to provide any further clarification required.

Yours sincerely

18 July 2013

Letter to the Chair of the Committee from the Chief Executive of The Hyde Group

Re: Communities and Local Government Committee Hearing—15 July 2013

Earlier this week the Communities and Local Government Select Committee took evidence from Julian Ashby, the chair of the Homes and Communities Agency (HCA) Regulatory Committee. I am writing to provide some clarification in relation to figures which were cited during the committee’s questioning relating to Hyde Housing Association and to reassure you and the Committee that Hyde is in a strong financial position.

Committee member Mr Danczuk highlighted to Mr Ashby that Hyde Housing Association Ltd (the Association) had made a loss in 2011–12 of £38 million and went on to question whether Hyde’s V1 financial viability rating was an accurate assessment of our current viability. The figure of £38 million is indeed the accounting loss of the Association for that year. However, this figure includes £40.2 million of non-cash losses resulting from valuation movements on the Association’s financial instruments and the application of accounting standards, specifically FRS26 & 29. The Association made an underlying surplus of £2 million before these non-cash losses are taken into account.

The wider Hyde Group, of which the Association is a part, made an underlying surplus of £13.8 million in 2011–12 and has strengthened this position in 2012–13 with a surplus of £25.7 million (pre FRS26 adjustments).

The Hyde Group generated operating cash flow of £78.2 million in 2011–12 (2012–13 : £101.1 million), and this was more than sufficient to cover its interest costs and to contribute towards building more homes for those in need. The Hyde Group’s liquidity position is strong and therefore, given that we generate strong cash flow and have sufficient cash available to meet our ongoing commitments, the Association and the Group are in a strong financial position and are therefore not at risk.

This strong financial position is reflected in both our top (V1) financial viability rating issued by the Homes and Communities Agency (HCA) and the A1 credit rating issued to the Hyde Group by the ratings agency Moody’s. We believe these assessments to be a fair and true representation of the financial viability of both the Association and the wider Hyde Group.

I have included an extract from our accounts (below) that explains the valuation movements on financial instruments in more detail. Whilst there is a complexity to these accounting rules I hope you will take comfort from the fact that our key external financial stakeholders (being, for example, the HCA, Moody’s, our lending banks and our bond investors) all understand this position. As such, they recognise that these non-cash valuation adjustments do not impinge unduly on Hyde’s financial strength and where applicable have agreed to amend lending covenants to exclude these impacts.

I would be happy to clarify further should that be helpful.
Kind regards,

17 July 2013

Extract from Hyde Housing Association Financial Statement 2012–13, p13:

“In July 2010 the Group issued a listed bond. As a result of this listing the Group was obliged to adopt financial reporting standards—FRS 26 “Financial Instruments: Recognition and Measurement” and FRS 29 “Financial Instruments: Disclosures”.

The main impact of this accounting change was that the Group’s derivative transactions (primarily interest rate swaps) must be accounted for at market value. All derivative contracts are entered into in line with the group hedging policy which allows the Group to manage interest rate and other risks.

As noted in the Treasury section below, the Group has a Board approved Treasury Policy which requires us to ensure that we have between 70–95% of our borrowing at fixed rates at any one time. This provides increased certainty of cash flows (both current and future) for the Group’s financial assets and liabilities.

The Group achieves this mix of fixed/floating rate debt by either entering into fixed rate loans or by entering into variable rate loans and then entering into derivative instruments (interest rate swaps) to switch from variable to fixed rate lending. These derivatives are held for the long term in order to provide long term certainty to our cash flows. They are not actively traded by the Group and the Group did not enter into any new interest rate swaps during the course of the year.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

Due to limitations on the application of hedge accounting, volatility has been introduced into the Income and Expenditure Statement as market value movements are not fully offset by movements in the underlying hedged item within each period. There is no cash flow impact to the Group’s results as a result of adopting FRS 26.

Given that the reasons for entering into the derivatives remain commercially sound (ie they are intended to be held to maturity in order to reduce volatility in the Group’s cash flows), the Group has opted to report the underlying result of the Group before reflecting the impact of these accounting standards.

This approach reflects the manner in which the Group manages its risks. It is supported by funders of the Group who, where applicable, have agreed to amend lending covenants to exclude the impact of these accounting standards in recognition of the fact that the Group’s ongoing cash flows are not impacted and hence there is no change in the ability of the Group to continue to service its debt.

The inclusion of this accounting volatility decreases the reported 2013 surplus by £27.7 million (2012: £56.4 million). The large movement in value this year reflects the reduction in applicable long term interest rates during 2012–13. The impact on the prior year was more marked as interest rates were more volatile in that period. As and when long term interest rates increase, these accounting losses will reverse. They will also reverse as and when the applicable swaps reach their maturity. Commentary provided in the Report of the Board and Operating and Financial Review focuses on the Group’s underlying performance, unless otherwise stated.”

Letter to the Clerk of the Committee from the Executive Director of Finance, Circle

I am writing in response to the inquiry into the Regulation Committee of the Homes and Communities Agency by the Communities and Local Government Select Committee, and the session which took place last Monday.

During the session with Mr Julian Ashby, Chair of the Regulation Committee of the Homes and Communities Agency, Simon Danczuk MP raised some concerns about the liabilities of South Anglia Housing, one of the Registered Providers (RPs) which form Circle Housing Group. In order to address these concerns, I have written to Mr Danczuk and Mr Ashby to provide some context and explanation around our liabilities and assets. I would be grateful if you could make this information available to the other members of the Committee.

Circle Housing Group consists of nine housing association partners, including South Anglia Housing Limited. The Group consistently delivers a surplus in excess of £20 million, delivers operating margins of 27%, which are considerably above the sector benchmark, and has committed and available private funding of £550 million. This affords substantial financial strength to all members of the Group, including South Anglia Housing Limited.

South Anglia had net current liabilities of £5.8 million as at 31 March 2012. This position arises because South Anglia’s debt, which has wholly funded the business alongside public sector grant, is classified in the accounts as being repayable within one year. This is the contractual position with the Circle Housing Group’s
borrowing vehicle (Circle Anglia Treasury Limited). However, this is not the intended repayment profile. It is expected that loans will be repayable in line with the long term repayment profile of Circle Anglia Treasury Limited.

South Anglia has total net liabilities, which have been funded by debt, as it has made cumulative net deficits. This is a typical position for a Large Scale Voluntary Transfer organisation like South Anglia where there has been significant planned investment to bring Local Authority stock that has been transferred to it up to an acceptable standard. In addition, the Group and South Anglia Housing Limited made a strategic decision to deliver a significant part of the Group’s historic development in South Anglia Housing Limited. Development of circa 1,800 new affordable homes by South Anglia has also put pressure on its margins in the early years. However, the long term financial forecasts demonstrate that the debt will be repaid in an acceptable timeframe and loan covenant ratios are being achieved.

Investment has been made with regard to South Anglia’s stand alone financial strength, and we forecast that it will repay its debt within the life of its financial plan. Our overall financial strength as a Group is consciously used to enable the deficits to be made in the early years in addition to providing protection against any variations in economic conditions.

I hope this addresses the concerns raised in the session. If you have any queries or would like further information, please do not hesitate to contact me.

Yours sincerely,

24 July 2013

Written evidence from Home Group (HCA 01)

INTRODUCTION

1. The Communities and Local Government Committee has recently launched an inquiry into the economic and consumer regulation carried out by the Homes and Communities Agency (HCA) Regulation Committee.

2. This note provides Home Group’s (Home) contribution to the debate and puts forward a range of recommendations, which focus on the proposed changes recently set out in the HCA consultation document “Protecting Social Housing Assets in a More Diverse Sector: A Discussion Paper on the Principles for Amending the Regulatory Framework for Social Housing in England”.

3. Home, a social enterprise and a charity with a turnover of over £300 million is one of the UK’s largest providers of high quality housing and supported housing services and products. We house over 120,000 people a year in 55,000 homes in 115 local authority areas in England, Scotland and Wales. We are committed to building 7,000 new homes and bedspaces between 2013 and 2018.

EXECUTIVE SUMMARY

4. We believe that the HCA’s consultation on “Protecting Social Housing Assets in a More Diverse Sector: A Discussion Paper on the Principles for Amending the Regulatory Framework for Social Housing in England” is timely in the context of the changing and more challenging environment within which Registered Providers are now working.

5. However, we do feel that there are a number of proposals in the consultation document which, as they stand, could have a significant adverse impact on the ability of providers to develop social housing—particularly in terms of ring-fencing.

6. This note outlines our views on the proposals in relation to:
   — Ring-fencing of social housing assets.
   — Recovery planning.
   — Protecting public value on disposal.

RING-FENCING OF SOCIAL HOUSING ASSETS

7. In terms of principle, the rationale for ring-fencing is that in the event of a fundamental failure in non-core business activity the ring-fence will prevent social housing assets from being put at risk—effectively, the non-core entity is allowed to collapse without causing contagion to the social housing business. This may work conceptually, but overlooks the practical consequences of allowing a subsidiary to fail—for example, potential job loss, impact on customers, contractors, suppliers and the local economy—which would inevitably impact adversely on the registered provider reputationally. There might also be significant issues in relation to lender confidence and loan covenant compliance.

8. In a challenging environment, with major pressures on income from diminishing grant and changes in the welfare benefits system, it is critical for providers to be able to cross-subsidise social housing development by ancillary non-core activity—eg by offering homes for market sale. We are seriously concerned that the blanket
requirement for this non-core activity to be capped at a de minimis level in the region of 2.5—5% of turnover would have a significant detrimental impact on the ability of providers to deliver on development programmes across the sector.

9. Furthermore, it is unclear from the consultation document what activities fall within the scope of “social housing” and which do not. For example, does social housing encompass care, and if so to what extent? To what extent do other socially important activities such as community regeneration, property management and, in particular, mixed use development (eg social renting and market sale) fall within the social housing envelope? Without clarity on this, it will be impossible for providers to identify what activities would be within a social housing ring fence and what would be outside—a major issue in terms of strategy and business planning.

10. In view of these difficulties, and given the diverse range of business plans and capacity across the sector, we would submit that the focus of the regulator should be on ensuring that providers have put in place robust measures for the prevention of business failure, rather than the implementation of a restrictive one-size fits all approach through ring-fencing. We strongly recommend that the ring-fencing proposals be dropped from the review of the Regulatory Framework.

RECOVERY PLANNING

11. Clearly, it is an overarching imperative for the HCA to ensure the financial viability of registered providers, and as a matter of principle we would obviously support the regulator in considering measures which could enhance the financial viability of registered providers, such as through recovery planning. We submit that the main focus for the regulator is to develop a system that is proportionate, balanced, represents value for money and which acknowledges the pre-eminent role of the boards of providers to co-ordinate recovery planning (rather than the regulator). The sector would not benefit from the introduction of an arbitrary and prescriptive system of recovery planning, which would run contrary to the principle of co-regulation underpinning the Regulatory Framework.

12. We therefore agree that the Governance & Financial Viability Standard should require all providers to have knowledge, oversight and understanding of their assets, liabilities and business operations in a possible failure scenario. This is existing good practice, which most providers already operate.

13. Whilst we agree that the boards of “designated providers” should consider a regularly updated recovery plan aimed at specifying core information in the event of failure, we would be concerned if any code of practice would require the provision of the kind of extensive information and data normally seen in a due diligence exercise. We do not believe that this would be cost-effective, proportionate or meaningful.

14. We also believe that it is important to introduce clear criteria as to what constitutes a “designated provider”, required to provide more detailed information under the proposed code of practice. The suggested criteria of size, complexity and exposure to sector risks are nebulous terms, capable of inconsistent interpretation and application.

15. Inevitably, the increased level of information and data trail which providers will be required to maintain as part of the recovery planning process will not only require additional resourcing by providers but—critically—additional resourcing on the part of the HCA itself. Not only will the regulator need to recruit additional regulatory staff to support a significantly increased workload, but they will need to employ staff with a much more extensive skill set than is required at present. We are concerned that this capacity does not currently exist. Its development must be a fundamental pre-requisite to the successful implementation of any change.

PROTECTING PUBLIC VALUE ON DISPOSAL

16. Given that the regulator is under a statutory obligation to ensure that value for money is obtained from public investment in social housing, we understand the desire to regulate against the possibility of asset stripping by for profit providers who—unlike “not for profit” providers—are not subject to a constitutional restriction on the distribution of profits.

17. We are therefore supportive of the principle that the Regulatory Framework should be developed to ensure that the Public Benefit Value (PBV) attributable to a property is retained and used for social housing purposes on the property’s disposal outside the social housing sector. As non-profit providers are required to utilise gain for social housing activities, this places “for profit” providers on a similar footing and would prevent any risk of asset-stripping of publicly funded properties.

18. However, there needs to be greater clarity on what constitutes public expenditure and on how retained PBV funds should be utilised in the sector.

CONCLUSIONS/RECOMMENDATIONS

19. Home has serious concerns over the ring-fencing proposals outlined in the HCA’s consultation document and urges that they should be dropped. We believe that they are flawed and would have a major detrimental impact on social housing provision. The focus should be on ensuring that Boards of providers have in place considered and robust measures to prevent business failure.
20. In terms of enhancing the financial viability of providers, Home supports the principle of recovery planning, but is concerned that this should be proportionate and cost-effective and led by boards of providers, rather than the regulator. We are concerned that the regulator does not currently have the capacity to support the increased workload that implementing recovery planning would entail.

21. We agree that the Regulatory Framework should be developed so that if a “for profit” provider sells a property outside the sector, any PBV attributable to it should be retained and used for social housing purposes. Greater clarity is needed on what constitutes public expenditure, and on how retained PBV funds should be utilised in the sector.

June 2013

Written evidence from Moat (HCA 02)

ABOUT MOAT

1. Moat is a housing association providing affordable homes in thriving communities for people in the South East. For over forty years, Moat has delivered high quality general needs homes for affordable rent, retirement and independent living, and has a strong affordable home ownership offer.

2. Moat is one of the Homes and Communities Agency’s development partners and is also the government appointed Local Help to Buy Agent in Essex, Kent and Sussex. Employing over 300 people, Moat develops approximately 500 new homes per year, and excellent customer service to our residents.

EXECUTIVE SUMMARY

3. The introduction of the Affordable Homes Programme has brought about a substantial shift away from capital subsidy and toward revenue subsidy, collected through rent and Housing Benefit. The risks associated with this shift are largely in the hands of DWP—not DCLG or the HCA. This means that decisions on welfare policy have taken on escalating influence to the future financing and supply of housing.

4. Of the welfare reforms either already in place or to commence shortly, it is our view that the benefits cap presents the greatest risk to future build capacity, as it directly impacts on our ability to inflate rents. The absence of an inflation-linkage is likely to make the Affordable Rent model, or any subsequent model, significantly less attractive to investors.

5. Regarding HCA proposals outlined in the “Protecting social housing assets in a more diverse sector” discussion paper, we anticipate that a ring-fence approach—dependent on the model and definitions adopted—would lead to difficulties in securing finance for non-core activities.

6. In 2012–13, 70% of new funding in the sector consisted of capital market funding, equivalent to £3.8 billion which is more than double the figure of £1.5 billion for the previous year. As many housing associations become increasingly reliant on non-core activities to cross-subsidise social housing activities, we expect that a ring-fencing regime would have a negative impact on build capacity. This would undermine the supply of the very activity that the Regulator is seeking to protect.

7. Proposals on ring-fencing underpin a system of regulation based on the avoidance of mistakes; we believe that the balance needs to shift towards a system that supports housing supply through well-managed providers that assess and manage risks professionally and effectively.

RESPONSE TO SELECTED QUESTIONS

What has the Regulation Committee been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

8. In our view, the Regulation Committee has performed capably according to its current remit. However, we believe the remit is overly focused on the avoidance of mistakes. We believe that a more balanced approach would be to measure success in terms of the net increase in supply of affordable housing.

9. The Regulation Committee must form a key part of the drive to increase housing supply across the UK. We believe that this could be achieved by creating a more flexible approach which looks at whether providers are assessing and managing their risk effectively. This approach would more effectively allow for a certain amount of well-managed risk among providers.

10. We do not take the view that risk is uniformly undesirable; well-managed risk is essential to support new borrowing, which in turn, minimises the level of capital subsidy required to build new homes. Risk is therefore vital for securing new investment.

11. It is our view that some proposals, especially around the ring-fencing of social housing assets, may place new investment at risk. This assertion will be covered in more detail in sections to follow.

What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

12. As the Committee would be aware, the introduction of the Affordable Homes Programme brought a substantial shift in the government approach to subsidy, away from capital subsidy and toward revenue subsidy provided through rent and Housing Benefit. The risks associated with this shift are largely outside the control of the Regulation Committee.

13. The graph below crudely illustrates how the balance has changed in moving from the social rent model to the Affordable Rent model:

![Type of subsidy used](image)

- Rent/revenue subsidy - for which DWP is primarily responsible
- Capital Subsidy - for which DCLG is primarily responsible

14. This shift makes any decision on welfare critical to the future financing and supply of housing. In short, some of the most critical elements of risk for the sector are now not in the hands of DCLG or the HCA, but with DWP.

15. Under the Affordable Rent model, the level of future inflation-linked increases to the rent on the dwelling are crucial to the amount of borrowing that can be supported, and therefore, to the level of capital subsidy required in order to build the home. Rents for new homes are set at up to 80% of market levels and inflated each year by RPI + 0.5%. This approach provides a strong basis on which housing associations can borrow at attractive rates from the financial sector.

16. This model can only function if tenants who cannot afford to pay these rents from their own income continue to receive assistance from the state. We therefore remain concerned with changes—such as the benefits cap—which could disrupt the link between inflation and rent levels. We have undertaken substantial modelling which demonstrates the extent to which the benefits cap will prevent us and other housing associations from inflating rents in future. We therefore recommend that the Government makes an explicit commitment to indexing the benefits cap for inflation.

17. Typically, Housing Benefit accounts for 50% of the rental stream on new Affordable Rent properties, and more than 50% of the increased rent on existing properties converted from social rent. Nationally, the Housing Benefit bill is expected to rise by £1.4 billion over 30 years to pay for this model shift. However, this rise is only a fraction of the capital subsidy increase that would otherwise be required to sustain a similar increase in housing supply without Housing Benefit.

18. Similarly to other sectors of the economy, borrowing from banks for affordable housing has either subsided or become more expensive. In large part, this is due to wider economic problems which have forced banks to take a more risk-averse approach to lending. We have also received anecdotal evidence from our lenders that the environment of uncertainty over welfare reform has also contributed, as well as the funding of affordable housing post-2015. This uncertainty makes it appear a less attractive, higher risk investment than in previous times.

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Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

19. It is our view that extra resources would be helpful in order to ensure that the Committee can continue to perform its role soundly in the future—particularly given the diversification of the sector and the increase in “for-profit” providers.

20. However, we remain of the view that most of the sectors’ problems can be addressed within the existing framework of co-regulation. The emphasis of the Framework should be to ensure that risks are properly identified, profiled and managed; we would argue that this is the primary function of our Board.

21. A proposed change to the Framework that is of concern is the proposal to ring-fence social housing assets, as outlined in the HCA’s “Protecting social housing assets in a more diverse sector” discussion paper. In particular, our concerns relate to:

(a) The lack of clarity around the extra resources that would be made available (if any) in order for the Regulator to adequately police any new arrangements.

(b) The likely negative impact on our ability to borrow against our assets. We believe that ring-fencing proposals would be unduly restrictive and would reduce our flexibility to make sensible investment decisions. With capital grant reducing, housing associations need controlled flexibility to underpin the delivery of affordable housing.

In April the HCA published a consultation document, “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England”. Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

22. We are sympathetic to the idea of protecting social housing assets from ill-judged high risk activities. However, we strongly believe that a distinction should be made between not-for-profit providers who are taking measured and managed housing risk to support their social housing activities and for-profit providers, who will be driven by the desire for commercial return and the creation of shareholder value.

23. We are comfortable with the elements of the Framework being reviewed, but are concerned at the direction that the review is taking on certain areas. Our primary concern is with ensuring that proposals do not stop housing providers from undertaking legitimate non-core activities—especially those which might allow us to cross-subsidise social housing activities.

24. As previously mentioned, our main area of concern is with the proposal to introduce a ring-fencing mechanism to protect social housing assets. We are not convinced that a ring-fencing mechanism is the most effective way to achieve this aim. We believe that more weight should be given to advancing good practice, accountability and strong governance structures among providers. Each of these could be achieved through the existing framework of co-regulation.

25. The HCA discussion paper cites other regulated sectors which have put ring-fencing in place to safeguard public services and critical infrastructure—such as water supply, and air traffic control. Whilst we understand the thinking behind these comparisons, it is important to consider that:

(a) The reducing levels of capital subsidy mean that RPs are becoming more dependent on their existing asset base to secure capital for further development, and;

(b) Every sector operates beneath a unique set of circumstances under which it may be ineffective to apply the regulatory conditions of another sector. For instance:

(a) The affordable housing sector is made up of over 1,000 registered providers of varying size. This is vastly different to, for instance, water provision which is operated by around 20 companies, or the energy sector which is largely handled by 6 dominant suppliers.

(b) The sheer quantity of providers in affordable housing, in itself, minimises the risk that a failing provider would have an infecting effect on the rest of the sector in terms of the availability of finance, or that it would significantly reduce the number of units available to residents.

26. Finally, it is our view that ring-fencing arrangements would be problematic to both implement and police. A water-tight definition of what constitutes “core” and “non-core” activities would be required, which may lead to significant legal dispute and critically, distract from our core function of increasing housing support. We would also call for clarity over what extra resources would be made available to the Regulator to police ring-fencing arrangements, or indeed, what sanctions would be in place for breaches.

June 2013
INTRODUCTION

The g15 is the group of London’s largest housing associations and includes:

A2 Dominion
Affinity Sutton
Amicus Horizon
Catalyst
Circle
East Thames
Family Mosaic
Genesis

The g15 makes a significant contribution to London life. We are non profit distributing, independent but regulated charitable businesses for social purpose. Collectively, g15 associations house around one in ten Londoners and manage over 400,000 homes. We also invest over £25 million annually in economic and community development to create thriving, sustainable neighbourhoods across the capital—in areas such as employment, skills, education, health and well-being, volunteering, financial inclusion, family intervention, welfare benefits support, supporting older and vulnerable people and engaging younger people.

g15 members will deliver 40% of new affordable housing and 25% of all new supply in London between 2011 and 2015. To do so, we will raise £2 billion of our own private borrowings and resources to match £350 million of public funding—a ratio of six to one—to create 13,000 new affordable homes. Most of us provide a range of housing from social and private rent through to home ownership.

SUMMARY OF THE G15 SUBMISSION

We are pleased to make this submission in answer to the questions raised by the Select Committee about the effectiveness of housing regulation and would like to emphasise the following points:

— There is no “one size fits all” solution to regulation. The Regulation Committee must recognise that it is not possible or desirable to regulate new profit distributing entrants to the social housing market as if they were charitable housing associations. Equally, it must also be careful not to disrupt the arrangements for non profit distributing housing associations which in the main work well. The most significant risks facing the affordable housing sector are the result of changes to Government policy, especially in areas like welfare reform. If the Government and the regulator are genuinely concerned about sector risk, they must consider the combined impact of changes to funding regimes and welfare reforms, as well as the impact of social landlords diversifying their activities.

— It would be wrong to regulate housing associations as if we were utilities. We are very different in origin and nature and the regulator simply does not have the resources to regulate us in such a way.

— The fundamentals of the existing regulatory regime are right. The regulator should expect HAs to manage their own risk and make boards responsible for doing so properly. It should focus therefore on financial viability and adequacy of assurance arrangements. In recent years, housing associations have taken on more of the risk of funding the costs of new homes as a result of reduced government subsidies. We have only been able to do so because we have taken steps to successfully manage and mitigate risk. It is essential that the regulator does not limit our capacity to generate the surpluses needed to subsidise the provision of new social housing.

— Adherence to the EU procurement rules adds cost and wastes time. The value and benefits of compliance with these rules should be reviewed by the National Audit Office.

We have not provided evidence in answer to questions 5 and 6.

1. What has the Regulation Committee been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

1.1 It is still early days to judge the success or otherwise of the new regulatory arrangements. While we welcome the “co-regulatory” approach adopted by the regulator, in our view success can only really be measured over a longer period of time. However during this first year of the new regulatory arrangements there have been two events upon which it is worth commenting.

1.2 The first is the successful rescue of the Cosmopolitan Housing Group which was in serious financial difficulties. The regulator was faced with a very difficult set of circumstances yet managed successfully to effect a rescue into another, more secure association which meant no resident lost their home and no lender suffered any detriment. This is a very good outcome and a good test of the effectiveness of the new arrangements so early in their existence. Doubtless the regulator will want to reflect on how the problems arose
in this case and to put in place arrangements which prevent others from falling into such difficulties. It must do so in an open and transparent way so that lessons can be learnt.

1.3 The Committee will be aware that it is rare for housing associations (HAs) to get into serious financial difficulties. In the last 20 years there has been only one case of financial insolvency and that was dealt with by the regulator (then the Housing Corporation) under its moratorium powers. As in the case of Cosmopolitan, no tenants lost their homes and lenders suffered no financial loss. However this unblemished record does rely on there being sufficient other financially able HAs willing and able to rescue those that get into difficulty. The regulator therefore has an interest in ensuring that the conditions exist for HAs to remain financially viable. This is a critical element of its role and remains at the core of what the regulator should be concerned about.

1.4 The second issue we would comment on is the recently published discussion document, Protecting Social Housing Assets. To our mind, the debate this promotes reveals a real dilemma for the Regulation Committee where it seems to favour a “one size fits all” solution to a problem which only exists primarily for new entrants to the market who have constitutions allowing them to distribute profits to shareholders.

1.5 Before the Housing and Regeneration Act 2008, all landlords on the regulatory register were non profit distributing housing associations, and most were and remain charities. There is no doubt this Act has given the regulator a particularly difficult task. On the one hand it opens up the market to new entrants but the consequence is that the regulator finds itself dealing with a completely new breed of organisation with different motivations and expectations. It will not be possible or indeed desirable to regulate new entrants as if they were charitable housing associations. It is critical that the Regulation Committee recognises this crucial distinction and takes steps to develop arrangements which properly reflect the risks inherent in both types of organisation. We are disappointed to see that the first attempt to devise such a regime fails sufficiently to grasp the difference.

2. What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

2.1 The most significant risks facing the social housing sector arise from changing government policy. In particular the rolling out of welfare reform, including changes to housing benefit for those deemed to be under occupying their homes; an absolute cap on the amount payable to benefit recipients; and the payment of benefits direct to claimants, will all increase significantly the risk that social landlords may not be able to fully collect the rent due. In addition there is as yet no certainty from Government about the future rent regime for HAs, which is already eroding the confidence lenders have in the sector. Moreover, the prospects for future capital subsidy also remain uncertain. In this context HAs have continued to manage and mitigate risk; our record of no defaults is testament to our effective management of risk.

2.2 Whereas we believe the regulator is right to be concerned about the increase in risk in our operating environment, it is too simplistic to contend that this risk arises primarily from the “diverse activities” in which we engage. The delivery of new affordable homes is itself an increasingly risky part of our business. As noted earlier, for every £1 of government grant we receive we spend a further £6 from our own borrowings and resources. This significantly increased level of borrowing coincides with rents set closer to market levels and greater uncertainty over our future rent income. We contend therefore that if government and the regulator are genuinely concerned about sector risk, they must look as closely at the combined impact of rents, funding regimes and welfare reforms as at the perceived risks from diversifying business activities—applying unnecessary restrictions on the latter will not in any way mitigate risks arising from the former.

2.3 Our boards are responsible for the adequacy of risk assurance arrangements. The regulator’s role is to ensure that they carry out this role and to hold them to account should they fail to have adequate arrangements in place. It is not the regulator’s role to manage risk for boards or to become in some way a “shadow director” but the recent discussion paper strayed too far in this direction, suggesting that the adoption of particular structures would provide the answer. This is naive and in our view will not work.

2.4 There is an undercurrent in the Regulation Committee’s recent discussion document that all registered housing providers should be regulated in a similar way to the utilities. This could be appropriate for those providers motivated by profit distribution but it cannot be appropriate for charitable housing associations. We are very, very different to water, energy, telecoms or transport companies. We do not distribute profits and any diverse activity we undertake is intended to support and subsidise our regulated activity. With the utilities, it is the reverse—most want to shift as much profit as possible from the utility company to their parent company. Moreover, there are a lot more of us—300 developing HAs—whereas each utility service is delivered by only a handful of providers. The regulator simply does not have the capacity to regulate us in the way envisaged.

2.5 We believe that the fundamentals of the existing regime are right. The regulator should expect HAs to manage their own risk and make boards responsible for getting this right. It should focus therefore on financial viability and the adequacy of assurance arrangements. Boards should have prime responsibility for meeting the regulatory standards. The regulator’s role is to deal with those situations where boards fail. This is entirely consistent with the co-regulatory principles that underpin the entire regulatory construct.
2.6 In terms of the EU procurement rules, these are followed by all housing associations yet our experience is that they have brought very little if any competition from outside the UK and add substantially to the time and cost of procuring goods and services. We do not contend that they undermine financial stability but they do cause delay and do nothing to improve value for money. Given that the rules have been in place for sometime now, we recommend the Select Committee to request the NAO to undertake a review of the impact that the regulations have had. We believe that adherence to these rules wastes time, adds bureaucracy and increases cost.

3. Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

3.1 The regulator has a dual role of regulating individual landlords and identifying systemic issues which might affect the sector as a whole. To do both roles it needs skilled staff and access to information which is current and accurate. We are concerned that the regulator currently does not have access to the skills and resources it needs to fulfil its obligations under statute. Whilst there are undoubtedly some very good and capable individuals, the heroic efforts of a small number of dedicated staff are insufficient for the task it faces. The regulator needs more resources and of sufficient quality: a properly resourced, risk-based approach to regulation requires the exercise of careful judgment and is preferable to unnecessary rules, applied inflexibly. But if additional resources are not possible given current spending constraints, the regulator should seek to obtain assurance from more expansive financial reporting and third party accreditation—such as auditors, advisers, rating agencies.

4. In April the HCA published a consultation document, “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England”. Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

4.1 In the g15’s response to the recent discussion paper on protecting social assets, we expressed our disappointment with the narrow view it adopts, focusing on only a limited range of proposals drawn almost exclusively from the utilities sector. Our prime concern is that while it is legitimate for the regulator to want assurance that social housing tenants’ homes should be protected from risk if things go wrong with non social housing activity, the proposals are focussed exclusively on protection rather than on ensuring that housing association boards and management are taking proper steps to see that risks are containable. We do not believe that it is the HCA’s intention to curtail all non social housing activity but the focus on “ring fencing” as a solution could have this unintended consequence.

4.2 Ring fencing and separation of non social housing activities is too simplistic as a solution. We agree that ring fencing can be useful and indeed it is already used by g15 members but it is not a panacea and is far from the only way of protecting social assets. If deployed in the way envisaged, it would be damaging to perfectly legitimate activity that creates the profits necessary to support our core social housing activity and which have been a feature of our businesses for many years. The HCA should stay true to the principles of co-regulation. It is the job of each HA board to assess risks in the round and satisfy itself that appropriate strategies are in place to mitigate them. As part of this, the board may decide to place diverse activities into separate subsidiaries and should limit its investment in them to an amount which does not place existing social housing assets at risk; alternatively it may choose another approach. But it should not be for the regulator to prescribe what it should do, not least because this would cut across the responsibilities of the boards of charitable HAs who have a legal duty to determine how best to invest their charitable resources for a return that is commensurate with the risk involved.

4.3 We believe the primary concern of the regulator must be to ensure that the arrangements we enter into are properly considered and managed to minimise risk. This is a key responsibility of the board of every association.

4.4 Finally, the g15 members exist to provide much needed affordable housing. In London the shortage of such accommodation is widely believed to be a factor holding back our economic recovery, both in the capital and in the country more widely. In recent years we have taken on more of the risk of providing new homes as government subsidy has been cut back significantly. We have only been able to do that because we have taken steps to manage and mitigate the risk. We are concerned that if the regulator proceeds with plans which rely upon the adoption of particular corporate structures that limit our capacity to generate the surpluses we need to subsidise our social housing activities then our ability to build new homes will be severely curtailed. It is those who most need good quality affordable homes who will suffer the consequences.

June 2013
Written evidence from the Council of Mortgage Lenders (HCA 04)

Introduction

1. The CML is the representative trade body for the UK residential mortgage lending industry. Our 110 members currently hold around 95% of the assets of the UK mortgage market. In addition to lending for home ownership, the CML’s members also lend to support the private rental market and social housing.

2. Over £60 billion has been lent by CML members to housing associations UK-wide for new-build, repair and improvements to social housing. This has enabled significant improvement in the condition of existing homes and communities as well as delivering new affordable homes without increasing the use of public money.

3. We welcome the opportunity to provide written evidence to the Communities and Local Government Committee on the regulation of social housing in England. The Committee’s oral evidence session with the chair of the HCA’s independent regulation committee is particularly timely, as the regulator and the sector address the challenges arising from the recent rescue of the Cosmopolitan Housing Group.

4. We have already responded to the HCA’s discussion paper on proposed changes to the core regulatory framework which are intended to ensure effective regulation of registered providers and the protection of social housing assets in a more complex and risky operating environment. Our responses to that paper are pertinent to the committee’s consideration of some of the areas highlighted in its call for evidence. In responding to the Committee, we have re-stated some of the key points we made earlier to the HCA.

Impact of the Regulation Committee

5. Although the challenges for the HCA’s regulation committee at the time it was established were considerable (and still are), we believe that it has had a strong positive impact to date. This is evidenced by predominately strong regulatory judgements on financial viability and governance which most providers enjoy. Lenders and investors place great reliance on these. The effectiveness and impact of the regulator has supported a continuing healthy appetite in private investment in the sector at favourable rates. There is currently no sign of that appetite diminishing.

6. Individual providers and the sector as a whole still enjoy strong credit ratings. We believe that recent downgrades by some ratings agencies should not be taken out of context as they reflect the wider sovereign downgrade. Although the Cosmopolitan case was cited by Moody’s, we believe that the regulation committee’s actions at the time secured a successful resolution which avoided loss and a moratorium. The regulator has since embarked on an exercise which should strengthen the sector for the future. The regulation committee has not been caught “off guard” to date, and we believe the regulator has a sound and comprehensive understanding of where the key risks lie in the providers it regulates.

Risks for Providers and the Sector

7. The risks which the sector faces, individually and collectively, are well documented and understood. The HCA’s 2012 Sector Risk Profile sets these out in more detail; these continue to represent the key risks for the sector. From the CML’s perspective, our members who commercially fund housing associations, continue to be concerned about the potential consequences for landlords’ income and financial viability of key aspects of the welfare reform changes which are now being implemented. In particular, we are concerned by the potential to disrupt landlords’ income through:

- Rent direct, and any delay in switching benefit payments back to the landlord instead of the tenant when there are ongoing rent arrears or persistent underpayment of rent.
- The under-occupancy deduction (“bedroom tax”) where tenants will face benefit deductions if they are deemed to be under-occupying their home
- The benefit cap under universal credit

8. We continue to be concerned that the Department of Work and Pensions is implementing these changes with an uncertain IT system, and an incomplete understanding of their impact not only on tenants but also on landlords, the credit strength of the sector and funders’ appetite to invest in it. Already we are seeing mounting arrears in some of the direct payment demonstration project areas, and some tenants/tenant groups struggling with the under-occupancy deduction. This all increases strain on landlords not only in terms of mounting arrears but also increasing resource costs for tenant support. We would like to see the regulator take greater account, through data collection and analysis, of the impact of these changes on registered providers as they are rolled-out.

9. Another key risk for the sector is the possibility that changes to banks’ capital cover requirements being considered by the Prudential Regulation Authority could substantially increase the cost of existing and new lending to the sector at a time when there is increasing pressure to attract favourably priced investment for new affordable housing development. We are engaging with the PRA on this issue, along with DCLG, HCA and HM Treasury.
Resources and Powers of the Committee

10. We are encouraged that the regulation committee has been able to recruit new members and now enjoys a good blend of skills and expertise which it can call upon. We believe that the proposals in the recent discussion paper, if translated into changes to the regulatory framework and approach to regulation, should provide the powers needed to tackle the challenges of for-profit providers, within the existing legislation.

Proposals to Protect Social Housing Assets in a More Diverse Sector

11. The discussion paper proposals are needed because of the increasing participation of for-profit providers in the sector and the need to sufficiently protect social housing assets and their associated “public value”. The increasingly complex group structures being adopted by some providers, which could see social housing assets exposed to risks and liabilities from non-regulated, non-core activity underline the need to strengthen the protection the regulator is able to provide. We believe the changes proposed, particularly around ringfencing, asset disposals and recovery planning should adequately provide the required additional regulatory protection. We recognise that there will always inevitably be tension between securing the required protection and allowing freedom to diversify into non-core activity. The issue is essentially about striking the right balance. The discussion paper has already stimulated debate in the sector as to what that balance should be. The CML is engaged in that debate, which will inform the next iteration of the HCA’s proposals in a formal consultation later this year.

Independence of the Committee

12. At the time it was established, we were concerned that it might be possible for conflict of interest situations to arise in the composition and work of the committee. We are comforted that the potential for conflict has been well managed and has not materialised, to date. Currently, we are satisfied that the arrangements in place to maintain independence are sufficiently robust and appear to be working. The independence of the committee, in the context of its relationship with the wider HCA as the government’s funding body for the sector, appears not to have been fully tested yet.

June 2013

Written evidence from the Hyde Group (HCA 05)

The Hyde Group is a leading provider of affordable housing and makes a significant contribution to meeting housing needs and improving people’s quality of life. The Hyde Group has close to 49,000 homes and houses over 95,000 residents. Hyde provides a range of social housing products ranging from general needs, intermediate housing products and supported housing.

Hyde is one of the largest housing association groups working in England, owning or managing homes in London, Kent, Surrey, Sussex, Hampshire, the East of England and East Midlands.

We welcome the opportunity to respond to this inquiry into “The Regulation of Social Housing in England.” We have responded to questions 1–4 and 6. We would be happy to discuss our response with the Committee in more detail.

In summary our response covers:

— The current threats to the social housing sector in England.
— Our views on the Regulatory Framework for social housing and how it could be enhanced.
— We believe that the Regulator’s oversight of the Regulatory Framework should be strengthened.
— The impact that the proposals in the HCA’s recent discussion paper about protecting social housing assets would have on the sector.

1.1 What has the Regulation Committee has been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

1.2 The new regulatory arrangements have not been operational for very long, and as such it is difficult to be certain how effective these will be. However, the Regulation Committee has successfully managed the transition from the TSA and has also successfully implemented the new Regulatory standards, including the model of co-regulation, which we welcome.

1.3 We believe that the Regulator ultimately managed the Cosmopolitan collapse well. However, the length of time it took for the Regulator to secure a settlement to the crisis caused some external stakeholders to conclude that the regulator was not as effective at dealing with these matters as had been the case previously. This in part led to weakened confidence in the sector by lenders and ratings agencies which may lead to increases in borrowing costs and restricted access to new debt.
1.4 A separate issue is the recently published discussion document, *Protecting Social Housing Assets*. The purpose of this document appears to be an attempt to finesse the current regulatory standards so as to protect social housing assets from being liquidated and distributed as profits to the owners of the new small cohort of “for profit providers”. We welcome the intent but are concerned that that the proposed one size all approach which, if implemented, will treat not-for-profit and for profit providers in the same way will serve to restrict the agility of those traditional RP’s who have established a track record of managing risks in a way to ensure both the protection of existing assets and the development of new supply. We believe that the Regulator should look to treat for-profit providers and not-for-profit providers as separate entities when looking at such risks.

2. What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

We believe that Housing Associations and the social housing sector face the following risks:

**Future support for social housing development**

2.1 To develop social and affordable housing on a large scale there is a need for support from government either in the form grant or discounted land. It is anticipated that post 2015 there will be no or very little grant available to develop social housing.

2.2 This expected reduction in grant means that the sector overall will not have the capacity to develop as many social housing properties. In addition more finance will need to be raised through loans and diversification of our business.

**Welfare reform**

2.3 Welfare reform poses one of the biggest challenges to the social housing sector. We have anticipated that the changes will have an administrative and financial impact on our business.

2.4 Welfare reform will lead to an increase in rent arrears, bad debts, management costs and staff costs. Ultimately, this will adversely affect the sectors ability to reinvest in services and new homes.

2.5 We are also concerned that welfare reform will have an impact on our residents’ ability to manage their household income. We are concerned about a consequential increase in evictions and homelessness.

**Borrowing capacity and financial climate**

2.6 The expected reduction in grant post 2015 means that we will need to increase borrowing to support the development of homes of all tenures. At present every £1 of grant must be matched with £6 of borrowing, with reduced grant we expect to see an increase in the level of borrowing required.

2.7 The sectors borrowing capacity is also impacted by the confidence that lenders have in the sector. The sector is seen as financially strong due to a secure revenue stream, asset base and government support. Uncertainty about rents from 2015—2025 and grant funding may impact on the sectors ability to borrow on favourable terms. We are awaiting the announcement on rents in the Spending Review on 26th June and hope for a favourable rent settlement of at least an annual increase of RPI on rents.

**Diversification**

2.8 One of the strengths of the social housing sector is its ability to diversify in reaction to changing circumstances. Diversification to more profit making activities, allows providers to reinvest in their social housing activities.

2.9 We believe that diversification can be well managed, but if it is poorly managed it poses a huge risk to the sector in terms of finance and reputation.

2.10 We are also concerned how the proposals in the HCA discussion paper may impact on the ability of the sector to diversify.

**Do the standards mitigate the risks?**

2.11 We believe that if the existing regulatory framework were applied and monitored with an adequate level of scrutiny, it would offer protection to social housing assets for not-for-profit providers.

2.12 We believe that the regulatory framework should distinguish between the risks profiled of for-profit providers and not-for-profit providers.

2.13 We believe one of the strengths of the current regime is co-regulation, we believe that it is important that boards are empowered to monitor and manage governance and financial risk.

2.14 We believe that the Regulator’s oversight of financial risk and governance should be strengthened.
Self regulation/co-regulation

2.15 We agree with and support the principles of co-regulation set out by the Regulator.

2.16 We are concerned that the Regulator’s oversight of provider governance arrangements and financial risk management is not robust enough and does not place enough emphasis on the responsibilities of the boards around governance and financial risk management.

2.17 We are concerned about the capacity of the Regulator to undertake co-regulation in regards to financial viability and governance.

EU Procurement

2.18 The introduction of public procurement legislation has been largely beneficial to the social housing sector. The regulations have encouraged use of procurement best practices and focus on value for money.

2.19 The current EU procurement process encourages the housing sector to move towards greater transparency, stakeholder participation, as well as a more robust and non-discriminatory decision making.

2.20 Negative impacts of EU procurement have been in regard to process, namely the cost incurred and the often lengthy timeframes. Furthermore, the understanding and application of the process can vary considerably between contracting bodies.

2.21 Finally we find in some circumstances only large contractors can compete on tenders which can make it more difficult to offer opportunities to SMEs. For SMEs a barrier taking part in some tenders relates to the costs of tendering, in both time and developing the skills to engage in the complicated process.

3 Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

3.1 We believe that as it stands, the Regulatory Framework offers protection to social housing assets for not-for-profit providers, and this is ensured through the co-regulatory approach. However, it lacks any form of direct oversight of financial arrangements and complex financial deals. Much of the oversight provided is on an exceptions basis as opposed to it being part of the regulatory process.

3.2 We are concerned that the Regulator cannot enforce this oversight due to capacity limitations. In light of this, we feel that the Regulator is not sufficiently equipped to foresee and prevent events where organisations may fail; meaning social assets may be put at risk.

3.3 We are concerned that the Regulator’s limited resources mean that it lacks the level of scrutiny to prevent such failures, hence the proposed blanket mechanisms.

3.4 We believe that the Regulator could strengthen the current framework by taking a more active interest in overseeing provider governance arrangement and financial risk management. This is provided for in the Regulatory Framework, but only on an exception basis. We believe this should be more routinely part of the regulatory process.

4 In April the HCA published a consultation document, "Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England". Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

4.1 We believe that the changes the Regulatory Standards suggested by the Regulator are not necessary for not-for-profit providers and could be damaging in several ways. We do believe that there should be stronger oversight of the governance and financial risk management arrangements of providers by the Regulator.

4.2 We feel that the comparison the Regulator has made with the utilities sector is not useful and would suggest a more similar sector is the charitable sector.

4.3 We believe that the Regulator’s proposals concerning recovery plans/living wills are good practice and support them.

4.4 We support the Regulator’s call to protect social housing assets from disposal by for-profit providers.

4.5 We believe that the Regulator’s focus should be on for-profit providers.

The proposed ring-fencing changes will have the following adverse consequences:

Financial

4.6 Loan Covenants: the proposals as they are currently envisaged may impact on loan covenants with lenders. We are unclear as to how providers would ring-fence social housing assets on loans that have been made available to organisations for general use.
4.7 We are concerned that the ring fencing proposals may act as a disincentive to institutional investors who see the balanced mix of returns offered by housing associations as attractive. In light of current and anticipated future levels of subsidy, institutional investment ought to be viewed by the sector and the government as an essential component of future funding.

Development

4.8 The proposals would impact on our ability to develop additional social housing and do not take into account current policy around innovation in increasing housing supply and developing mixed communities.

4.9 Planning and section 106 agreements: Like any other developer, we are subject to section 106 agreements on new schemes. These agreements may mean the provision of non social housing assets such as commercial units. Planning requirements may also mean that we are required to develop a mix of tenures on site which may mean non social housing assets—we have developed both student and extra care schemes via such arrangements. Current planning policy and government policy continue to encourage such mixes; the Regulator’s proposals do not recognise this tension.

4.10 Restrictions in borrowing and development of new social housing: We are concerned that the proposals put forward by the Regulator may adversely impact on our borrowing capacity and thus our ability to develop new homes. Reduction in grant has meant that we have had to rely on more debt to develop homes of all tenures. The proposed ring fence would severely limit providers borrowing capacity. Furthermore, with the possibility of nil grant post 2015, providers need to use their assets more effectively to raise finance to develop new homes.

4.11 Reinvestment in social housing: the ring-fencing restrictions proposed by the Regulator would severely limit the level of non-social activity providers are able to undertake, this activity often supports reinvestment in social housing. Most large housing associations already operate businesses where more than 5% of turnover links to activities other than social housing e.g. private sale developments. This activity is integral to our business and is managed so that it does not risk the social housing assets. Imposing a ring-fence would stifle innovation in the sector and the ability for the sector to deliver the new homes that are being encouraged by the Department for Communities and Local Government (DCLG) and the Greater London Authority (GLA).

Housing Management

4.12 Defining social housing—we agree with the Regulator that a definition of social housing would be useful and we urge that any definition should take into account the charitable objective of social housing. However developing this definition is not simple and we are concerned that classification could become a bureaucratic burden which does little to protect assets. As such, any future definition needs clarity whilst allowing some flexibility to allow for changes in the funding regime and product innovation. We are happy to work with the Regulator to unpick these issues and ensure that there is clarity around the definitions of different types of assets.

4.13 Mixed tenure communities—some assets which would not be viewed as social housing assets are integral to financing and delivering developments. For example our award-winning Packington Estate regeneration scheme in Islington required both commercial and private sale properties to be developed. Without the financial benefits of these commercial elements, we would not have been able to carry out this regeneration. We believe that creating mixed tenure developments served by suitable local commercial outlets is crucial to creating sustainable communities.

4.14 Community and social investment—The discussion paper does not make it clear how community and social investment services would be defined. We believe that our community investment services are core to the delivery of our social housing services and we invest significantly in them. The investment we make supports our wider vision of not just providing people with homes, but also supporting them in their homes and communities. Therefore we believe that such services should be regarded as part of our core business and would urge the Regulator to recognise this in the final proposals.

6. Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

6.1 The current consumer standards are high level and allow for provider innovation.

6.2 The consumer standards as they currently stand place little emphasis on continuous improvement and good practice, we would recommend that there is more of a focus on such areas through non statutory guidance.

6.3 The Hyde Group has a robust resident engagement and accountability structure which we are proud of. We however are unclear how other organisations implement similar arrangements in relation to the consumer standards. We would be keen to share our good practice in this area.

June 2013
Written evidence from the Aster Group (HCA 06)

Background to the Aster Group

The Aster Group offers housing, care, support and other services to over 70,000 people from Cornwall to Hampshire. Our Registered Providers, Aster Communities and Synergy Housing, own more than 27,000 homes. The combined Group has assets exceeding £1 billion, a turnover of £150 million and employs 1,500 people.

Our ambitions are to:

— grow our business;
— be brave and bold where we can make a positive difference;
— deliver value and choice; and
— be financially strong.

In considering our response, we have been very mindful of the views of our tenants and other customers. They recognise and support the need to diversify in order to continue to develop affordable housing in their communities.

Background to our Response

We welcome the opportunity to debate important matters as part of a sector-wide discussion and in addition to this response, have submitted our response to the Regulator on its latest discussion paper which affects the HCA’s economic and consumer regulation.

Following the adjustment to the Regulatory Code covering economic and consumer regulation in 2010, independent housing associations were able to achieve their social objectives and outcomes in whatever way they saw fit, subject to compliance with the general outcomes required by the new Regulatory Standards and their ability to operate in an environment of low (and diminishing) public subsidy.

We have already adjusted our business to fit this environment and have devoted significant resources to a pipeline of schemes which incorporate cross subsidy, either from development for sale or, market rent; all of which have risks we believe we are well capable of managing as the Sector’s competence and capability has increased over a period of time to reflect this. We would also maintain that these interventions, particularly in relation to market rented schemes, have been pursued with the active knowledge and encouragement of Government. With housing need/demand massively exceeding supply now is not the time to place unnecessary obstacles in the path of innovation in housing production.

The reality is of course, over and above the Regulatory Standard, there is an array of other controls to which housing associations are subject which work to effectively “ring-fence” or control what they do:

— Restrictions in loan agreements. Lenders are typically unwilling to accept greater risk without re-pricing their loan margins; any significant change to loan pricing is something they would only accept for a fundamental reason.
— The requirements of investors, who we believe will differentiate between individual housing associations as the bond market matures and reliance on it increases.
— Charity Law.
— Tax Law and its implementation

Responses

1. What has the RC has been doing since it was set up in 2012, how well has it done, are there other things it should have been doing, and what impact has it had on the social housing sector since its establishment?

The RC has not been in existence long enough to have had a direct impact on the Aster Group thus far, but, if it is to continue to safeguard the good name of the Social Housing sector (as its predecessor at the Housing Corporation—the Registration Committee—did), its role will be vital in ensuring the sector has a future as far as public investment is concerned.

2. What are the major risks facing housing associations and the social housing sector? Are the standards set by the RC on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

Aster sees the main risks facing housing associations and the social housing sector as welfare reform, and how the ending of direct payment of Housing Benefit to landlords in most circumstances will affect organisations. In addition, the restriction on benefits for social housing tenants under-occupying properties, and the turbulence in the global financial markets.

Aster considers its current highest risk activity is delivering new affordable housing, with lower or zero capital grant and higher income streams to support borrowing. This however would be affected should the proposals in the latest HCA paper on restrictions to diversify be implemented. We see cross-subsidy as an
essential element of our business strategy to deliver new affordable housing. This involves new and different risks; but ones we believe we are capable of managing and we see it as our business to manage risk in whatever way our Boards believe is appropriate; subject to demonstrating to the Regulator that it is being done appropriately. In our judgment the current Standards give the Regulator the necessary tools to do this.

Housing associations have branched out significantly since the new regulatory regime came into being and are about much more than social housing; we are an investor both in communities and housing. In addition, the business environment has changed and we are in agreement with the HCA’s rationale for reviewing how the regulatory framework protects social housing assets in a more diverse sector, but believe the majority of the tools it requires are already available to it either within its existing Standards or the external environment.

Other areas which are important to consider in managing risk are ensuring that the Boards have the right skill set. In addition, the HCA will need to ensure that it has the right skill set to manage risk in diversified areas without stifling innovation.

In terms of the effect of EU procurement rules on the financial stability of the sector, the border between services contracts and public work should be redefined with increased legal certainty for partnerships. There should be improved flexibility of public procurement and it should be applied only if added-value could be proved.

The EU procurement regulations complicate procurement activities due to the convoluted nature of the legalities involved and the resulting risk of challenge. Whilst all procurements vary, a realistic average cost for an organisation to undertake an OJEU-compliant tender would be a conservative estimate of about £25,000-£30,000. The introduction of the Remedies Directive in 2009 has made the potential of challenge greater primarily due to disgruntled bidders perceiving a misapplication of the regulations and the ease of initiating, and the impact of, a challenge. This, in turn, has led to the sector becoming increasing risk-averse and, in some instances, the introduction of increasingly burdensome evaluation criteria.

It is expensive for organisations to submit a bid and this prevents some from participating in the tender. SME’s were already reluctant to engage (as bidders) in procurements primarily due to the complexity and expense of completing procurement projects and the apparent knock-on effects of the Remedies Directive (see above) is that this has worsened the situation. The lack of SME engagement means that the chances of having a local organisation bid in a procurement subject to OJEU, is generally unlikely. Local firms not bidding make it infinitely more difficult for a contracting authority (a buyer) to award work to organisations based in the areas in which they operate. This means that organisations are not spending money in the local areas thereby affecting local employment and the economy which, coupled with Welfare Reform, can directly affect our revenue.

The lack of bidders means that competition is being restricted by the OJEU process thereby affecting value-for-money obtained. The procedures themselves are limiting—if the Restricted Procedure (2 stages) is used it excludes bidders at the PQQ stage on non-VFM grounds resulting in a smaller limited competition based on VFM criteria, if the Open Procedure (1 stage) is used it excludes the evaluation costs, and risk of challenge, can increase dramatically for the buyer. On top of this, in most cases negotiation is not allowed which can limit our ability to minimise cost whilst maximising benefits in the case of complex procurements.

3. Is the RC policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

There is a fair argument that the RC has not got the resources to implement their powers or to really understand the business the sector is now in. Decreasing HCA funding is pushing the sector to identify new income streams and activity—eg housing for sale, market rent, etc but HCA regulation is only recently looking at the consequences of that with its discussion paper. Experience with recent problem cases indicates opportunities are more complex now, which in turn highlights a greater need to understand the business of the sector.

4. In April, the HCA published a consultation document. Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

We can see that the business environment has changed which has brought about a need to review how the Regulatory Framework protects social housing assets in a more diverse sector. We believe that the consultation document selects the appropriate elements of the Framework to review.

We feel the HCA has put forward some constructive ideas in its latest discussion paper which are helpful; for example a comprehensively prepared “living will” should address the key concern, protecting social housing assets.

We worry though that a small number of admittedly high profile difficulties in the sector may be used as a proxy for an overly restrictive “one size fits all” approach to regulating a sector, whose range and diversity requires a much more tailored approach. Moreover, it may inadvertently (and unnecessarily) prejudice exactly the sort of innovation in supply that will be so vital to finding solutions to the already burgeoning housing
shortage throughout much of the Country. Any move that intentionally or unintentionally stifles that innovation will be of concern to our tenants and other customers.

We think there may be mileage in requiring associations with significant levels of non-regulatory activity (or plans to invest in such activity) to obtain independent credit ratings which are then annually updated. Many leading associations either have them or are planning to commission them as part of their future plans. The ratings process can provide an extremely detailed analysis of the overall exposures that individual associations face, and of the mitigations applied. In our view, reliance on ratings could provide a wholly more appropriate tailored approach to regulation than is currently offered through the discussion paper.

We start from the proposition that if we are to achieve our essential mission of creating and maintaining housing for those who are more vulnerable in our society in an environment with little or no capital subsidy, then we will need cross-subsidy. The alternative is that we stop developing affordable homes.

In addition, investing in the community is one of the best ways to invest in housing, after ensuring it is well maintained.

5. Are the arrangements in place sufficient to preserve the independence of the RC in relation to the HCA and the sector?

The independence of the RC in relation to the HCA and the sector as a whole is, if anything, stronger than the arrangements in place when the Housing Corporation was the Regulator of what were then Registered Social Landlords. That degree of independence is an important element in the robustness of the regulatory regime.

6. Are the standards set by the RC relating to consumer regulation adequate and are the monitoring arrangements sufficient?

The standards set relating to consumer regulation allow clarity over outcomes expected for tenants, landlords and stakeholders. There are no monitoring arrangements in reality with the exception of the serious detriment process. We feel this is a good thing as it suggests Government trusts the sector to provide good services, which is an interesting comparison with Care Quality Commission, which only regulates quality and has no financial or governance regulation because the quality of care is such a huge concern. The quality of housing management is generally good across the sector, which demonstrates that the monitoring arrangements are sufficient.

7. Concluding Comments and Additional Point

We believe that in setting out on the co-regulatory route, as detailed in the current Standards, we are well placed to deliver new affordable housing with minimal levels of Government capital grant support and in doing so to continue complying with the Standards.

We need to be allowed to continue on this path and be given the freedom to explore the ways in which we can achieve this individually. Clearly, because of the similarities of the businesses in our sector, there will be common themes. But, there are also significant dissimilarities.

Within this, we recognise that there are different risks we need to manage. We also recognise our fundamental duty as a not-for-dividend/community interest business in protecting our social housing assets.

Moving forward, we welcome the opportunity to engage about the use of our social housing assets, whilst maintaining our overall key mission as a not-for-dividend business; but with a greater ability to have a diverse housing portfolio.

June 2013

Written evidence from Residents’ Network (HCA 07)

1 The Residents’ Network helps residents to work with their landlords and hold them to account. Our activities include:
   — Holding workshops and conference calls to share good practice amongst residents.
   — Publishing regular newsletter to residents.
   — Issuing guidance on how to run an effective scrutiny panel.

2 We believe that residents can play a much bigger role in regulation. There are many good examples of residents working with their landlords to improve services and save money. You could build on this.

3 We also believe that the HCA needs some new powers:
   — It should make sure that all landlords support tenant scrutiny of services.
   — It should make sure that tenants can compare the quality of service at their landlord against others.
It should publish an annual report on the quality of service in the sector to go alongside the financial reports they already produce—this will reveal the value for money of the sector.

4 Our evidence concentrates on two of your questions:

Question 2 Are the established arrangements providing self regulation of the sector being adequately supervised and tested?

5 The Cave review from 2007 laid down the roots of the current regime. Julian Ashby wrote most of the report. He is now the chair of the Regulation Committee of the HCA.

6 The report describes:

"…a system in which tenants cannot switch and are put at risk of poor treatment by providers, which face limited pressures to offer good service and choice, or even to operate efficiently. Not that all providers will behave in this way. But when they do, the error will not be self-correcting, as it is in other market contexts. This is not a standard market failure but a consequence of the objective of delivering housing at affordable rather than market prices. It does, however, make a strong case for regulation to protect tenants."

7 The Cave Review led to a new body called the Tenants Services Authority being set up to protect tenants. Grant Shapps swept it away and replaced it with the HCA.

8 He asked the HCA to restrict itself to economic matters. Tenants were to use panels to hold landlords to account on service with the HCA acting as a backstop only where there was the risk of serious harm. Problems now have to be sorted out locally. Residents cannot call on the HCA to help them deal with issues of poor service.

9 We attach our Residents’ Network guide to scrutiny. It gives plenty of examples of panels that are doing well. They are making helpful suggestions on collecting more rent and cutting the time that homes lie empty. These panels are changing the way that landlords and tenants work together.

"There’s greater co-operation between tenants and staff”—Housing association board member

"We now have a more ‘adult’ relationship with...residents...”—Staff member

10 A lot of talented and able people live in social housing. It is 18% of the population after all. Cave was impressed with many of the tenants that he met. Some of these led boards and took tough decisions. The Residents’ Network has members with great track records in the commercial and public sectors. They bring this expertise to their roles in scrutiny panels.

11 The HCA does require:

"…providers to support tenants both to shape and scrutinise service delivery and hold boards and councillors to account."

12 Many landlords are doing just that. Others ignore the requirement or pay lip service to it. But the HCA does not police this requirement. It may not even be able to do to the restrictions on its powers.

"The board gets the scrutiny panel it wants”—Resident

13 The Committee should be aware that there is no regulation of services at all at some landlords. The HCA only gets involved in extreme cases where life and limb is at risk. Of 500 complaints made to the Regulation Committee so far (including from MPs and councillors), not a single one has triggered HCA action. There are no sanctions for landlords that fail to take scrutiny seriously. It is great that so many landlords do work hard on scrutiny. The challenges from the Cave Review are still with us. Residents do not have the same rights as a normal consumer. They cannot take their custom elsewhere.

14 If a panel fails to get anywhere with its landlord there is nowhere to go. The HCA is rarely in a position to take the case up.

15 The scope of the panel can lead to frustrations. Many believe they have been set up to hold the board to account. They are restricted to looking at services. On a couple of occasions now we have seen panels working away very well on this as the HCA downgrades the landlord on governance and viability. These two strands of activity need to be tied together a lot better.

16 Service failure can be a good point of diagnosis for other problems. Where residents are saying that the repairs service is poor it is well worth looking into that in detail. You could find wider problems with the finances and governance of the landlord. Service quality and the landlord’s finances are two sides of the same coin. The Localism Act forces the HCA to look at the money but ignore the service. It makes no sense. They could be giving grant to poor landlords.

17 Housing inspectors used to pick up service problems. The regulator looked into these to see if there were deeper issues with governance. On a number of occasions the service flaws gave early warning of wider problems. Grant Shapps did away with this approach. It is possible that a properly resourced panel could act as an early warning system.
18 We would ask the Committee:
— To hear evidence from us and others that demonstrates the benefits of effective scrutiny panels.
— To encourage all landlords to help set up and support scrutiny panels.
— To give the HCA powers to ensure that all landlords set up panels where residents want them.
— To put in place an arrangement for dealing with disputes between panels and landlords.
— To ensure that the HCA takes the issue of service quality seriously—this could be by making sure that advice and support was made available to panels and taking account of the views of panels in HCA judgements.

Question 6 Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

“What standards? It’s not clear what they really are.”—Resident

19 The standards cover all the right services. They are open-ended to allow for tailoring at the local level. So you do not see lots of numbers and targets in there. This is a double-edged sword. It can be good that there is local discretion. One size does not fit all. But there are no hard and fast rules about what a resident can really expect.

20 There are two problems with the standards:
— There is a lack of reliable data. It can be hard to find out how your landlord is doing versus others. There is a lot of benchmarking going on. Not all landlords let tenants see the results. Poor performers claim the results are rigged against them. There is no-one to referee these disputes. All of this gets in the way of resident scrutiny
— The HCA does not monitor performance against the standards.

21 It is certainly true that some landlords do really well at agreeing local targets and reporting on these to tenants. But it can be very difficult to tell if the offer from your landlord is better or worse than for others. The problem with the system that Cave identified is still there. There is no switching so you only know about your landlord. The blinkers are on.

22 The HCA produces a useful annual report on the accounts of landlords. It does not do this for the consumer standards. This means that it is straightforward for the Committee to find out what landlords are spending. It is very hard to comment on the quality of services. So how can we tell if the sector is delivering value for the money it spends?

23 We would ask the Committee to:
— Make sure that tenants have access to easy to understand information comparing the performance of their landlord versus others—this will help tenants to hold landlords to account
— Require the HCA to produce an annual report of the performance of landlords against the consumer standards—this should bring together an analysis of cost and quality.

June 2013

Written evidence from Circle (HCA 08)

About Circle

Circle is one of the UK’s leading providers of affordable housing. With a dedicated team of more than 2,200 staff, Circle manages 65,000 homes, including supported and sheltered housing, for around 200,000 people across the UK. Our mission is to enhance the life chances of our residents by providing great homes and reliable services, and building sustainable communities.

The Circle Group includes 12 partners, Nine Registered Providers (RPs): South Anglia Housing, Wherry Housing Association, Old Ford Housing Association, Circle 33 Housing Trust, Merton Priory Homes, Mole Valley Housing Association, Mercian Housing Association, Roddons Housing Association and Russet Homes; two support & care partners: Circle Support and Invicta Telecare, and Circle Living for sales and management of shared ownership, market rent and private sale.

Summary
— Circle agrees that regulation to prevent the loss of affordable housing assets is necessary in an environment where Providers are taking greater risks.
— However, the proposals set out in the HCA’s discussion document earlier this year, are a disproportionate reaction to risk in the sector. In order to save the leakage of affordable housing it is probable that the measures will result in a significantly reduced capacity and appetite. The loss of benefit through consequent reduction in new homes will far outweigh the protection of existing assets.
— The proposals will inhibit Registered Providers in carrying out activities that act as a cross subsidy in new developments and regeneration. This comes at a time when providers’ capacity is already threatened by the consequences of welfare reform and low grants.

— In recent years, housing associations have come under pressure from government and housing regulators to “sweat their assets” (“Unlocking the Door” Housing Corporation 2006). With reduced levels of housing grant made available in the Affordable Rents Programme, cross-subsidy has therefore become an essential element of funding the construction of new affordable homes. Therefore while housing associations have engaged in a broader range of activities, this is largely a response to public policy developments which have encouraged diversification, such as the reduction of grant and the increased recognition of the role associations can play in providing market rented housing.

— It is important that the HCA does not adopt a “one size fits all” approach to regulation which places undue burdens upon providers that already have a thorough and robust self-assessment risk framework in place. A stronger self-assessment system whereby Registered Providers are identifying their diverse activities, the level of these activities and through the living will system how any losses would be managed by the organisation, would help the Regulator to focus on the relatively few high risk organisation or proposals.

— As such, we would call on the Government to ensure that the HCA has the resources it needs to carry out its regulatory duties effectively and focus this resource on particular Registered Providers which are more at risk. At the same time, the Regulator should be able to reach an individual position with organisations that are managing risk effectively.

RING FENCING

We believe that ring fencing “non-core” activity, however that is defined, is a “one-size-fits-all” approach which would make it more expensive for housing associations to build homes in the future and would reduce capacity and appetite within the sector. Although this may be appropriate in the utilities sector, business incentives are far more aligned in housing associations than they are in utilities companies. We would therefore encourage a differentiated approach, with the

Regulator strengthening the self assessment framework to enable it to focus on associations who are at risk of failure, and providing the necessary resources to reach an individual position between larger organisations and the HCA, rather than pursuing a blanket approach. We believe that the regulatory system should be structured in a way which maximises freedoms and flexibilities for housing associations whilst effectively managing risk.

LIVING WILLS

We support the principle of “living wills” but we have some concerns about how the document will be used and who will have access to it. A living will is likely to contain highly sensitive commercial material which could potentially be subject to a Freedom of Information (FoI) request. We therefore suggest that the living will should be kept as simple as possible and be signed off by the Auditor with the sign off submitted to the Regulator, but with documentation retained by the RP.

It should not be necessary for a copy to be lodged centrally with HCA and, like a conventional will, it should remain confidential until such time as it is needed. Due to the major work that would be required to write a living will, we would favour a differentiated approach where, an organisation which is at risk of failure would be required to review their position more frequently and provide more comprehensive information to the Regulator on their Recovery Plan.

DISPOSALS

We believe that rules for disposals for for-profit providers should reproduce as closely as possible the conditions that apply to disposals by non-profit providers. Where grant is attached to a property, disposals should be subject to direction by the HCA, but the remainder should not be subject to direction. There also needs to be greater clarity on what qualifies as “social housing” and whether this includes for example regeneration and commercial units. Housing associations will only be able to adapt to their changing operating environment if they are able to realise their assets where it is necessary to do so, with minimal interference from the Regulator.

CONCLUSION

We would encourage the Regulator to strengthen the self assessment framework to ensure a focus on good governance, and encourage all providers to adopt a thorough and robust approach to the assessment of risk and to plan for how that risk can be managed. In order for a differentiated approach to be successful, it is important for the HCA to be given the resources it needs to focus on particular associations which are more at risk and allow it to reach an individual position between large organisations and the HCA, rather than pursuing a blanket approach. In this way, the HCA can gain the assurance that it requires to adequately protect social housing
Written evidence from the Department for Communities and Local Government (HCA 09)

Context

1. The effective and proportionate regulation of social housing is of crucial importance in order to safeguard public investment, promote the supply of new homes and protect tenants. The Government’s vision for regulation was set out in the Review of Social Housing Regulation (published in October 2010). The overarching principle was that Regulation should be focused on areas where it is really needed. We concluded:
   - There needs to be proactive, robust and independent economic regulation of private registered providers of social housing that commands lender confidence, promotes new supply and safeguard taxpayers’ investment in the sector. The Regulator should have a strong focus on securing value for money for taxpayers.
   - The Regulator did not need to play a significant role on consumer protection. Whilst the Regulator set national consumer standards, we should rely on local mechanisms to scrutinise landlords and hold them to account. Routine inspection of landlord services should be abolished. The Regulator should only intervene in cases of actual or potential serious detriment to tenants.
   - Regulation should be based on the principle of co-regulation. The Regulator should act proportionately and in a way that minimises interference. Any intervention should be risk-based.
   - The institutional arrangements should be streamlined, whilst retaining the independence of the regulation function. The Tenant Services Authority (the standalone regulator established in 2008) should be abolished and its functions transferred to the Homes and Communities Agency. The regulatory functions should be exercised by an independent Regulation Committee within HCA. The strong case in principle for recovering some or all of the costs of regulation via fees levied on regulated providers should be explored further.

2. This vision for regulation was implemented via Schedules 16 and 17 to the Localism Act 2011, as well as a number of changes to the regulatory framework (including those set out in statutory directions to the Regulator issued in March 2012). The regulatory reforms came into effect on 1 April 2012.

3. The Government’s key expectations of the Regulator have not changed. It has a key role to play in supporting new affordable housing supply, upholding standards of governance and financial viability, maintaining investor confidence, and protecting historic public investment in the sector. We continue to look to the Regulator to focus on risk and exercise its powers proportionately.

Q1: What has the Regulation Committee been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

4. The Committee has performed well in its first 12 months and has helped maintain the continuity and effectiveness of regulation during the transition from the Tenants Service Authority to the Homes and Communities Agency. The Committee continues to develop its role in conjunction with the HCA Executive team and reviews ways it can add value and greater effectiveness to the regulatory regime. The Committee has importantly helped to maintain the continuity of regulation following the transfer of functions to the Homes and Communities Agency. An effective system of regulation that monitors and ensures the financial health of the sector has helped maintain its financial stability and retained the confidence of investors and lenders.

Q2: What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

5. The HCA published its sector risk profile in June 2012 and plans to update this shortly. Clearly housing associations are operating in a riskier environment than previously—as indeed are most private bodies—following the credit crunch. The changes being brought about through welfare reforms (e.g. the benefit cap and the removal of the spare-room subsidy) are also a particular issue for the sector, which is why we have designed and continue to design important safeguards to help protect providers’ income streams.

6. The Government believes that the regulatory standards on governance and viability are adequate to mitigate these and other risks that threaten the financial stability of providers. The recent case of Cosmopolitan Housing is a good example of effective regulatory responses where an individual provider encounters serious financial difficulties. The successful outcome for this case was in large part down to the important role that the
HCA and the Regulation Committee played. The HCA will shortly be undertaking an independently led “lessons learned” exercise to identify how the process can be strengthened. The Department welcomes this.

7. On a rolling basis the Homes and Communities Agency publishes governance and viability ratings of Private Registered Providers. This is an important part of the regulatory regime and allows the Regulator to work with individual providers to address any issues as and when they arise that may have an impact on their financial viability. This is in addition to the other reporting requirements on providers that are in place.

8. In previous discussions the Government has had with the National Housing Federation (the representative body for the majority of housing associations) about the sector’s inclusion under the EU Procurement Directive they have estimated the cost of compliance with the rules to be around £30 million or 0.3% of the sector’s turnover, so unlikely in itself to cause instability. The Government—lead by the Cabinet Office—is involved in negotiations with the Commission on its revision of the procurement rules and is pushing hard to make them simpler and more effective. The Government also pushed in earlier rounds of the negotiations to try and get the definition in the Directive regarding bodies governed by public law changed so that the 2004 decision to include the sector under the rules could be reversed. This ultimately proved unsuccessful as it received little or no support from other member states.

Q3: Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

9. The Regulation Committee is performing these functions effectively. No provider has failed in recent years, and no tenant has lost their home through provider failure. The environment is changing though, with increasing diversity of providers, and a move by some traditional registered Providers (mainly Housing Associations) into new, non social housing, activity. The past year has shown that the Regulator can respond to challenging cases eg Cosmopolitan Housing Association.

10. There has not been a need in recent years to use the most extreme Regulatory powers, such as the 28 day moratorium once insolvency proceedings have begun and this has only (technically) been used once in the past. Lender and Credit Ratings. Agency confidence in regulation has been maintained and any downgrades of individual Associations which have happened are attributable to the macro financial outlook, not any lack of confidence in Regulation.

11. Powers in the 2008 Housing and Regeneration Act furnish the Regulator with a range of instruments that enable effective regulation of the sector, but (as above) the sector and thus regulatory demands, are changing, hence the Regulator’s discussion document “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England, published in April.

12. On resourcing, the Regulator has recently taken steps to diversify its skills mix to meet the challenges of this new environment and is in the process of recruitment. The HCA keeps resources under continuous review and raises resource needs with us through sponsorship arrangements.

Q4: In April the HCA published a consultation document on diversification. Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?


14. Since the passage of the Housing & Regeneration Act 2008, both the economic background, and the nature of the regulated social housing sector have greatly changed. The economic downturn, followed by the 2010 Spending Review, and the priority of deficit reduction, have meant that capital grant for social housing is much reduced. The role of private investment in driving supply is more important, which exposes providers to the challenges of securing and maintaining borrowing. Prior to the 2008 Act, registration was restricted to “not for profit” providers, ie predominantly Housing Associations. The 2008 Act addressed the objective of enabling a wider range of providers to deliver social housing (via section 115). As at 19 June 2013 the Regulator has registered 24 profit making providers.

15. With this greater diversity, the risks to public value and social housing assets are growing. The Regulatory challenge must thus balance the need to diversify the sector, to bring in new sources of funding, with the need to protect public investment in social housing assets, and the security of tenants.

16. The consultation proposes a range of measures which would give greater assurance that social housing assets are not being put at risk by non social housing activity. These include changes to the Regulator’s consents regime, to ensure that for profit providers may not strip out public value from social housing assets, and proposals for ring fencing of social housing assets, from other, more risky, parts of the provider’s business (to protect these assets from exposure to non regulated parts of the business).

17. Some of the challenges of traditional not-for-profit providers diversifying into new, and more risky, areas are seen in the recent Cosmopolitan case. The provider’s role in student housing was a major factor impacting
their financial viability. The changes proposed by the Regulator are, in our view, necessary to get the balance right between encouraging new providers and investment into social housing provision, whilst protecting these valuable publicly funded assets from more risky commercial activities. We do not believe that adverse consequences will result—indeed it is necessary to make these changes to reflect the changing nature of the sector.

Q5: Are the arrangements in place sufficient to preserve the independence of the Regulation Committee in relation to the FICA and the sector?

18. There are strong statutory and administrative arrangements in place to ensure that the social housing regulation function is delivered on an independent basis. This is important in order to ensure that regulation continues to command investor confidence. The legislation continues to provide a discrete set of regulatory powers. An independent Regulation Committee was established by statute within the HCA to exercise this function and, under Section 92B of the Housing and Regeneration Act 2008 (as amended by the Localism Act 2011), the function cannot be exercised by HCA in any other way.

19. The amended statutory framework continues to provide no general power of Ministerial direction over the exercise of the regulatory functions. Instead the legislation provides certain limited direction powers relating to particular regulatory activities (such as setting standards for registered providers).

20. There are also robust administrative arrangements to underpin the independence of the regulation function. In particular there is a published protocol, agreed between the Regulation Committee and the HCA Board, outlining how the statutory functions and duties of the Regulation Committee will be exercised within the HCA.

21. The Government’s view is that together these statutory and administrative measures are sufficient to preserve the independence of the regulation function. These arrangements are working effectively in practice.

Q6: Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

22. The consumer standards, which are largely subject to Direction from the Secretary of State, are set by the Regulation Committee following public consultation, and provide a clear framework for delivering high quality social housing, value for money, as well as choice, opportunity and protection for tenants. Responsibility for delivering these standards lies with boards of private registered providers and councillors who govern local authority housing, and who are accountable to their tenants for the services they deliver.

23. The Government believes social housing tenants are best placed to monitor their landlord’s performance against these standards. They know their local patch and can see, at first hand, whether landlords are delivering, including whether services are efficient, economic and responsive to the needs of individuals and communities. Through the Tenant Involvement and Empowerment Standard, tenants have a range of opportunities to engage with, and challenge, landlords. For example tenants can monitor performance, get involved with consultations, scrutinise services, and form tenant panels. Such mechanisms are enabling tenants to hold landlords to account for delivery, challenge poor services, and press for improvements. To further help tenants monitor the consumer standards, Government is funding a programme of free training, support, and sector-led advice so that tenants understand their rights and are empowered to hold landlords to account.

24. Additionally, the Localism Act 2012 enables tenant panels, as well as councillors and MPs, to resolve routine complaints, so that the regulator can focus on addressing serious failure with a high risk of serious detriment to tenants. The Housing Ombudsman Service will collect information about tenant panels that have been designated by their landlord to handle complaints.

June 2013

Written evidence from TPAS (HCA 10)

INTRODUCTION

TPAS promotes excellence in resident involvement and empowerment through training, advice and accreditation. Formed in 1988, TPAS is a membership organisation representing over 1,800 tenant and resident organisations, and 240 social housing providers and contractors.

The Homes and Communities Agency (HCA) is the regulator of social housing in England but it may only exercise its functions through the Regulation Committee (RC).

Since the HCA took over the powers of regulating registered social housing landlords (RSL) in 2012 there has been an opinion that TPAS hears very often, from its members and other people in the industry, that the regulator has withdrawn from its role in regulating the consumer standards.

The CLG Committee enquiry regarding consumer regulation is therefore timely so that this anecdotal evidence can be elaborated upon.
However, it should be stressed that neither TPAS, TAROE nor any other tenant organisation has the capacity to fully undertake consultation on this issue.

The following report is based on what we have been able to do in a very short time period without resources, following an online survey publicised through Twitter, Facebook and the TPAS weekly online magazine.

**Summary of our Main Conclusions and Results from the Survey**

- 121 people responded to our survey.
- Just four in 10 people who completed the survey felt that the consumer standards are adequate.
- Three in every four people believe that the regulator should intervene more often than they currently do.
- Only around one in four surveyed took the opinion that the regulator should intervene more often than they currently do.
- Fewer than one in 10 stated that they thought there was sufficient information made available to them about the activities of the Regulatory Committee.
- TPAS recommends that a full scale independent consultation be carried out to determine the full extent of tenant, landlord and stakeholder opinion of the work of the regulator.

The findings of this survey and the conclusion we have drawn are also supported by TAROE, the Tenants’ and Residents’ Organisations of England.

TPAS and TAROE are willing to provide further information and to provide oral evidence in order to expand on any of the points made in this document.

1. **Context**

1.1 Recent figures released by the HCA show that out of 489 consumer enquiries received since 1st April 2012 none have been deemed to meet the “serious detriment” level set by the Regulation Committee.³

1.2 Under restrictions in the Localism Act 2011⁴ the Regulator is unable to use its powers in relation to a provider failing to meet a consumer standard unless the “serious detriment test” is met.

1.3 In addition to this restriction the HCA openly states that “Failure to meet one or more of the consumer standards does not in itself lead directly to a judgement of serious detriment by the Regulator.”⁵

1.4 TPAS believes that, in combination, the conditions laid out in points 1.2 and 1.3 have led to a disincentivisation for RSLs to successfully implement the consumer standards set out in the regulatory framework despite the fact that all RSLs “are subject to the regulatory framework and must all meet the applicable regulatory standards”.⁶

1.5 For these reasons, TPAS England welcomes this inquiry into the HCA Regulation Committee and welcomes the opportunity to contribute on the subject of consumer standard regulation.

1.6 TPAS is the leading national tenant participation organisation working to promote tenant empowerment in England. We are a membership organisation of around 240 registered social landlord members and 1800 tenant and resident association (TRA) members.

1.7 TPAS operates a free information and advice service for its members, training and consultancy services to members and non-members and we also accredit landlords and contractors that show they involve tenants in all aspects of their business.

1.8 The Department for Communities and Local Government recently appointed TPAS England and its partners to deliver a £1.2 million tenant training and support programme, the national “Tenant Empowerment Programme” under the name Tenant Central.

2. **The Survey**

2.1 Tenants and staff work and live each day in the sphere of consumer standards regulation. They are all directly affected by the regulatory standards.

2.2 TPAS wanted to give people an opportunity to answer some of the CLG Committee’s questions directly since these are the people that have the most direct experience of the consumer regulations in practice.

2.3 In considering these two points, TPAS decided that an online survey open to anyone with an interest in regulation of the consumer standards would be the most suitable method of consultation.

2.4 TPAS published the survey via our website, social media streams and through mail outs from our email database. The survey was open for one week only and in that short time 121 people completed it.

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³ [http://www.insidehousing.co.uk/regulation/hca-kicks-out-all-complaints/6527403.article](http://www.insidehousing.co.uk/regulation/hca-kicks-out-all-complaints/6527403.article)

⁴ [http://www.homesandcommunities.co.uk/ourwork/serious-detriment](http://www.homesandcommunities.co.uk/ourwork/serious-detriment)

⁵ [http://www.homesandcommunities.co.uk/ourwork/serious-detriment](http://www.homesandcommunities.co.uk/ourwork/serious-detriment)

⁶ Homes and Communities Agency (2012) *The Regulatory Framework for Social Housing in England From April 2012*
2.5 By a small margin, the majority of respondents were tenants, accounting for 45.5% of the total (figure 1).

![Diagram showing the distribution of respondents by tenant, landlord, and other categories.]

Figure 1: Total respondents classified by Tenant, Landlord (member of staff) and Other (please specify)

2.6 The survey asked respondents to consider questions relating to the consumer standards, the regulation of those standards and the regulation committee in general.

2.7 TPAS also provided an opportunity for participants to add any additional comments at the end of the survey. 33% of respondents chose to utilise the comment box. A selection of these comments are included in Section 7 entitled “Respondents’ Comments”.

2.8 Overall, the survey indicates a feeling of dissatisfaction with various aspects of the Regulation Committee and its remit more than it shows satisfaction or confidence. The following sections will draw attention to the results and their implications.

3. The Regulation Committee

3.1 This section looks at the questions from the survey that examined opinion surrounding the Regulation Committee’s overall competence.

3.2 Fewer than 1 in 15 (6.6%) of the people who completed the survey said they were “Happy” with the performance of the Regulation Committee.

3.3 Not a single respondent reported that they were “Very happy”.

3.4 The majority (60.3%) chose to select the “Neutral” option. This could be interpreted as a reflection of the perceived lack of transparency of the RC’s actions leading them to select the “neither/nor option” due to a lack of knowledge upon which to base their opinion.7

3.5 At the other end of the scale 33%, or one third, of respondents rated themselves as “Unhappy” or “Very unhappy”.

3.6 Disappointingly, almost half of the respondents (48.7%) expressed themselves as either “Not confident” or “Not very confident” in the RC to successfully do its job.

3.7 This is in contrast to just 12.4% of respondents reporting themselves as “Confident” or “Slightly confident” in the RC doing its job (Figure 2).

7 See points 3.7, 3.8 & 3.9
3.8 In response to the question “Do you feel that there is sufficient information made available to you about the activities of the Regulation Committee?” a clear majority of 82.6% answered with an emphatic “No”.

3.9 Less than one in ten (9.9%) of respondents said they felt that there was sufficient information made available to them about the activities of the RC.

3.10 Points 3.8 and 3.9 reveal a stark message. Namely that tenants, landlord staff and other interested parties who completed the survey hold a view that there is a definite lack of communication about the activities of the RC.

3.11 Overall the results in this section show very low levels of satisfaction, confidence and transparency in relation to the RC and its work.

4. Consumer Standards

4.1 When referring to the consumer standards set out by the regulator the results from the TPAS survey are more positive than those above. Slightly more respondents regard the consumer regulation standards as adequate than those regarding them as inadequate (Figure 3).
4.2 However, as the graph shows, the numbers of those that think the standards are adequate or not are equal. Communities and Local Government Committee members, along with the HCA, should not be satisfied to learn that such a low proportion of people (around 4 in 10) working with and affected by the standards think that they are adequate.

4.3 It should be acknowledged that since the standards were devised through a lay and collaborative process across all bodies involved in social housing, including tenants, the real dissatisfaction may not stem from the inadequacy of the standards themselves, but rather the lack of actions when organisations do not fully comply with the standards. This view is substantiated in the responses to the next question below.

5. Intervention

5.1 The survey then moves onto the topic of intervention. The respondents are conclusive in their opinions related to the topic of intervention.

5.2 In the question "To what extent do you agree that the regulator should 'only intervene in cases of serious detriment that have caused, or are likely to cause, harm'?" the majority (60.3%) of respondents disagreed or strongly disagreed.

5.3 Around 3 in 10 (30.5%) people who completed the survey agreed with the current HCA policy that the RC should only intervene in cases of “serious detriment”.

5.4 The level of dissatisfaction with the RC and how it intervenes in the industry is stark in Figure 4 as three out of every four respondents (76.1%) believe that the regulator should intervene “more often” or “much more often”.

5.5 Barely 2 in 10 people (21.5%) believed that the amount of times the regulator intervenes in cases should stay the same.
5.6 As covered earlier⁸ the regulator will only intervene in cases of “serious detriment”. However, in 127 cases since 2012⁹ the regulator chose to use its powers to conduct further investigations in order to establish whether there was “serious detriment”.

5.7 In conducting these investigations the regulator is allowed to use its powers of monitoring and enforcement.¹⁰

5.8 Relating to the part of the question for the inquiry set by the Communities and Local Government “are the monitoring arrangements sufficient?” the TPAS survey revealed that just 12.4% of the respondents believe that the monitoring arrangements set by the RC relating to consumer regulation are sufficient (Figure 5).

5.9 When asked to consider what actions the regulator had taken that they were aware of, the overwhelming majority of respondents said that they weren’t aware of any instances of the regulator using its powers of monitoring or enforcement.

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⁸ See points 1.1, 1.2, 1.3 & 1.4
⁹ http://www.insidehousing.co.uk/regulation/hca-kicks-out-all-complaints/6527403.article
¹⁰ http://www.homesandcommunities.co.uk/ourwork/serious-detriment
5.10 An incredible 80.2% of people that completed the survey were not aware of any instances of the regulator using its monitoring powers like commissioning inspectors or requesting performance information (Figure 6).

5.11 An equally definitive proportion (76.9%) was not aware of any instances of the regulator using its enforcement powers like issuing notices or enforcing a transfer of the management of properties to another provider.

5.12 The high proportion of people unaware of regulator activity in both instances could be contributed to by circumstances highlighted in an earlier question. In other words, a general lack of communication has lead to the tenants, landlord staff and others being unaware of the work that the RC is carrying out.

5.13 However, in both of these questions TPAS included a “Don’t know” option. This gave the respondents an option to choose if they felt that they were not sufficiently informed to answer the question. Indeed, between both the categories an average of 11.55% of people selected this option.

5.14 This leaves figures of around one in ten of respondents who were aware of actions taken by the RC relating to their monitoring and enforcement powers. These statistics paint a clear picture of perceived inactivity.

5.15 The findings highlighted in this section point to failures of the regulatory body in the eyes of the people that have to work and live by the consumer standards to intervene in cases on sufficient occasions. It indicates that a review of the “serious detriment” measure may be in order.

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11 See points 3.7, 3.8 & 3.9
6. FUNDAMENTAL OBJECTIVES

6.1 TPAS felt that it would be helpful for the Communities and Local Government Committee to see how the stakeholders rated the RC on each of its four consumer regulation objectives. These "fundamental" objectives are set out clearly on the HCA website and are enshrined in law through the Localism Act 2011.12

6.2 The survey asks the respondents to express an opinion on whether they think the RC has upheld their commitment to meeting each of the four objectives.

6.3 For example, with regard to the second consumer regulation objective the survey asks; “To what extent do you agree that the regulator ensures that actual or potential tenants of social housing have an appropriate degree of choice and protection?”

6.4 Only 1 in 5 (19.8%) of people who completed the survey responded positively saying that they “agreed” or “strongly agreed” with the question. TPAS regards this as a clear indication that social housing tenants and the members of staff at registered social landlords are unhappy with how RSLs are encouraged, or enforced, to involve tenants in decision-making procedures and how much security tenants have (Figure 7).

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12 http://www.homesandcommunities.co.uk/ourwork/objectives
6.5 This sentiment continues in the survey across the other three questions that relate to whether the RC is meeting its own “fundamental” objectives.

6.6 Only 25.6% of respondents thought that the regulator was meeting its first objective, which is related to the quality and management of properties.

6.7 Just 27.6% of the people who completed the survey believe that RSLs are encouraged to contribute to the wider well being of the areas in which their properties are situated.

6.8 While 27.2% agree that the regulator ensures that tenants of social housing have the opportunity to be involved in its management and to hold their landlords to account.

6.9 Only a minority of social tenants, staff employed by RSLs and other interested parties that completed the survey have stated that they believe the RC is meeting their fundamental objectives.13

6.10 TPAS believes that this is clear evidence that the social housing regulatory body is perceived to be under-performing with regard to the implementation of consumer standards.

6.11 TPAS further believes that this is a direct result of the decision to withdraw from pro-active regulation of the so-called “consumer regulation” in preference to the governance and financial regulations.

7. Respondents’ Comments

7.1 Below we have taken excerpts from the comments made in the dedicated section of the survey.

7.2 “There should be tighter requirements for tenant consultation on change of service, governance and company mergers.”

7.3 One respondent said that they were “unaware of the regulator and what they did”.

7.4 Another respondent simply asked “Without inspections how can standards be upheld?”

7.5 “The loss of the TSA is very notable and tenant involvement has noticeably reduced in significance.”

7.6 “The regulator needs to do more to ensure proper provision of social housing given the housing crisis”

7.7 “I feel the regulator should do random short notice inspections”

7.8 “The regulators should focus on tenants’ complaints and housing needs”

7.9 “Not all landlords work fully in the interests of tenants and there are lots of vulnerable tenants about.”

13 See points 6.4, 6.6, 6.7 & 6.8
7.10 “If there is no audit process then performance and standards can’t be driven forward”

7.11 “I feel strongly that the new regulation framework does not give enough say to collective tenant bodies, unless these are involved in complaints. Complaints are service failure. We involve our tenants in shaping services. If the regulator was more interested in that there would be less complaints.”

7.12 “Landlords need much greater monitoring and regulation, tenants need to be at the heart of these.”

7.13 “Feel that the consumer standards cover the key issues for customers however the fact that these are not regulated means that there is no impact and no real reason for landlords to meet these so poor landlords will continue to be poor”

7.14 “Difficult to comment on regulator involvement around “serious detriment” as there has been very little, if any that I am aware of. The bar for serious detriment is set very high and this could mean that some cases are not being dealt with”

7.15 Referring to the procedure whereby the Secretary of State appoints members of the Regulation Committee, one respondent remarked “How can this be independent when members are appointed by one person?”

8. SUMMARY OF OUR MAIN CONCLUSIONS

8.1 Through the survey the respondents have shown low levels of happiness with the performance of the Regulation Committee, very low levels of confidence in its ability to carry out its work and even lower levels of satisfaction with the level of transparency in carrying out the work.

8.2 Just 4 in 10 people who completed the survey feel that the standards are adequate.

8.3 3 in every 4 people believe that the regulator should intervene more than they do.

8.4 Only around one in four surveyed took the opinion that the Regulation Committee is meeting its “fundamental objectives”.

8.5 Less than 1 in 10 stated that they thought there was sufficient information made available to them about the activities of the RC.

8.6 TPAS surveyed 121 people who are affected by the consumer standards daily. Members of the CLG Committee and the HCA Regulation Committee should find the results of the survey critical of the current performance of the regulator, but also helpful in identifying areas for further improvement.

8.7 In response to various results quoted from the survey TPAS also recommends that the regulator take immediate action in improving the communication of its activities to tenants, landlords and stakeholders.

8.8 Overall however, In light of all of these factors TPAS recommends that a full scale independent consultation be carried out to determine the full extent of the tenant, landlord and stakeholder opinion of the work of the regulator.

8.9 TPAS is willing to provide further information and to provide oral evidence in order to expand on any of the points made in this document.

June 2013

Written evidence from the National Housing Federation (HCA 11)

1.0 INTRODUCTION

1.1 The National Housing Federation is the voice of affordable housing in England. Our members, housing associations, provide two and a half million homes for more than five million people.

1.2 Regulation is very important to the success of the social housing sector. The fact that the sector is regulated provides assurance to tenants, to lenders and to key partners such as central and local government. The current regulatory settlement, based on the Housing and Regeneration Act 2008 as substantially amended by the Localism Act 2011, has markedly shifted the balance of regulation so that it is higher-level and more strategic than previously.

1.3 The Federation’s approach has always been to argue for a strategic approach to regulation that avoids the focus on operational details that was the hallmark of previous regimes. This does not amount to “deregelation” as such, nor to “self-regulation”; but it does mean recognising that housing associations are autonomous, self-governing bodies and that the primary responsibility for them rests with their boards. The role of the regulator is not to supervise the board, still less to oversee or second-guess its decisions, but to satisfy itself that the board is competent to direct the association’s business. This approach has come to be known as “coregulation.”
2.0 Effectiveness of the HCA Regulatory Committee

2.1 It is very soon to assess the effectiveness of the HCA Regulatory Committee, which undertook its formal duties only in April 2012 when the Tenant Services Authority was formally abolished. The Federation regretted the loss of a separate agency because the role of regulation needs to be kept separate from that of investment.

2.2 We are, however, pleased to acknowledge that the record of the Regulatory Committee to date has been encouraging. It has maintained a clear focus on governance and finance and has avoided getting drawn into operational issues. Moreover, it has successfully managed the serious financial difficulty of Cosmopolitan Housing Group. This was resolved when Cosmopolitan was taken over by a larger association, ensuring that the position of tenants was protected and that lenders incurred no financial loss. The episode was an example of the way the sector works together with the regulator to safeguard tenants’ interests and head off any possibility of a default.

3.0 HCA Consultation Document

3.1 The Regulation Committee of the HCA has recognised that the operating environment is becoming more difficult and that, partly in response to this, associations are becoming involved in a broader range of activities. In addition, because of the lack of affordable, long-term bank finance as a result of lenders’ response to the financial crisis, housing associations have had to pursue more complex and innovative ways of accessing cheap, long-term funds.

3.2 We agree that this raises issues about effective risk management and that the regulator should expect providers to satisfy themselves, in a demonstrable way, that any risks are well understood and can be mitigated if necessary in order to protect social housing assets. Ring-fencing social housing, so that it is insulated from any failure elsewhere in the business, is an important way of achieving this. However, it is not necessarily suitable in all cases.

3.3 The regulator stresses that registered providers should be able to diversify their activities and undertake a wider range of socially beneficial activities (and indeed they are often encouraged to do so by central and local government), and we argue that the need for this freedom and flexibility means that the regulator should acknowledge the value of other approaches to risk management besides ring-fencing. This will include, for example, the holding of sufficient reserves or unencumbered assets to ensure that the organisation is in a position to mitigate risk.

3.4 This more flexible approach recognises one of the sector’s greatest strengths: its ability to augment public grant with funds raised privately. Since the introduction of the modern funding regime following the Housing Act 1988 and up until to 31 March 2012, housing associations have received some £37 billion of capital grants. At the same point in time they had total debt facilities (ie private finance) of just under £63 billion. This mix is likely to change going forward as private finance becomes even more prominent. In addition, since 2008, more and more private finance has been raised by housing associations selling bonds on the capital markets—in 2012 alone, about £4 billion out of a total of £5.4 billion was raised in bond finance.

3.5 The Comprehensive Spending Review in 2010 saw capital investment in housing cut by 63% in real terms—the biggest single cut to any capital budget across government. Despite this, housing associations have committed to deliver 170,000 new affordable homes over the period 2011 to 2015, and remain on track to do so.

3.6 This results, in part, from the affordable rent regime, which means that developing associations derive increased revenues by charging higher rents on new homes and a proportion of re-let properties. More significantly, associations have accessed greater levels of private finance and taken on much higher levels of debt. For every £1 the Government has invested in affordable housing during the current spending period, housing associations invested £6 of their own money.

3.7 These figures dramatically illustrate the ability of associations to raise private funds substantially exceeding their level of state support. This is possible because the Office for National Statistics recognises associations as non-state bodies, meaning that their borrowings do not count as public debt (ie that they are “off-book” from the Treasury point of view).

3.8 A problem with the regulator’s discussion paper is it treats “diversification” as if it were a single issue, and fails to distinguish the separate questions raised by the registration of for-profit providers. A few of these bodies have begun to register (having become eligible to do so under the Housing and Regeneration Act 2008) but as yet they account for a tiny proportion of the sector (24 registered providers out of 1784 in all). Clearly they present a challenge requiring a regulatory response. However, the issues they raise are about regulating the shifting of funds derived from social housing into a profit-distributing arm of the business. This has nothing to do with whether social housing assets are at risk, and it needs a distinct regulatory response.

14 TSA, 2011 Global Accounts of housing providers, March 2012
15 We use the term “for-profit providers” as shorthand; strictly speaking, these bodies are subsidiaries of unregistered for-profit group parents.
4.0 HCA REGULATORY POWERS AND RESOURCES

4.1 On the whole, the regulator’s existing powers should be adequate for its purposes, but there is one relatively technical change that would be helpful. The 2008 Act required all new registered providers to hold stock, a departure from the previous arrangement in which non-stockholding group parents of social landlords could register. Existing non-stockholding parents were allowed a period of grace during which they could remain on the register, and this has now been extended indefinitely. The effect is to create an anomalous position that needs to be resolved; particularly since the HCA has identified regulatory benefits where a group parent is registered. We therefore suggest an amendment to the 2008 Act to give the HCA power to register a non-stockholding body that is a group parent of one or more registered providers.

4.2 The regulator’s resources are another matter. It is currently funded by government, although powers have existed since 2008 for fees to be levied on regulated bodies. Concern has been expressed in the sector about the regulator’s capacity to deal with the more complex issues arising in the current environment, and there have been some suggestions that it would be better resourced if registered providers were required to pay fees. The Federation has reservations about this: there is a risk that the Treasury would simply reduce its contribution by a corresponding account; and the difficulties should not be underestimated of devising a fee-collecting formula that strikes an equitable balance between different sizes and types of provider. It may be more productive to look at ways in which registered bodies may provide themselves, at their own expense, with more robust assurance, available to the regulator, that risks are well managed.

5.0 CONSUMER REGULATION

5.1 We think the current approach to consumer regulation strikes the right balance. The fact that the regulator’s powers are available only in cases of “serious detriment” means that it is able to act in the event of really serious or systemic shortcomings on the part of a registered provider. But the “serious detriment” test means that the regulator no longer gets involved in trying to define in detail the relationship between social landlords and their tenants. This leaves space for landlords to engage with their tenants to identify the right approach for each organisation, a process that could not have taken place when a standard set of requirements was imposed centrally. Tenants meanwhile retain access to landlords’ complaints procedures and if necessary to the Ombudsman, in addition to legal remedies.

6.0 RISKS TO THE SECTOR

6.1 Welfare reform poses a number of challenges for the sector. The Federation strongly opposes the social sector size criteria (the so-called “Bedroom Tax”). We have long argued that penalising social tenants because they are deemed to have a “spare” bedroom will force thousands into hardship. With so few smaller homes for people to downsize into many will be forced to absorb the cut. Arrears will rise as tenants struggle to pay their rent. This will be compounded by other changes such as the removal, under Universal Credit, of tenants’ option to have their rent paid direct to their landlord.

6.2 The cumulative impact of these changes will reduce the already stretched incomes of households across the country. They will also have a significant impact on housing associations’ operating costs and will pose a strategic risk that will play out over time. Universal Credit, for instance, will not be fully implemented until 2017. Associations are investing significant sums to manage the long-term financial impact of welfare reform. The effect of this will be to reduce the resources that would otherwise have been available to meet housing need.

7.0 EU PROCUREMENT RULES

7.1 The CLG Select Committee has raised a specific question about the requirement for housing associations to follow EU procurement rules and whether this has any effect on their viability. The answer is that the EU rules, which were (wrongly, we believe) extended to associations in 2002, have made procurement slower, costlier and more bureaucratic and therefore divert resources that could otherwise be applied to meeting housing need. But these additional costs, although unnecessary and unwelcome, can be allowed for in business planning and are therefore unlikely to have a direct impact on viability.

8.0 CONCLUSION

8.1 We are encouraged by the performance of the HCA Regulation Committee since it assumed its responsibilities in April 2012. However, we stress that it is not possible to arrive at a definitive judgment after such a short time. We agree that the sector is becoming more diverse in several respects and that regulation needs to evolve to take account of this. An important part of this is the management of risk to ensure that social housing assets are protected, but we do not agree with the regulator’s suggested reliance on ring-fencing to the exclusion of other ways of managing risk. A more flexible regulatory approach will still protect existing social housing, but will also allow the sector to continue to bring together public and private resources to meet housing need.

June 2013
Written evidence from Places for People (HCA 12)

INTRODUCTION AND GENERAL COMMENTS

We welcome the opportunity to respond to the Select Committee’s inquiry on the regulation of social housing in England.

Places for People (PfP) is one of the UK’s leading property management, development and regeneration companies. PfP owns or manages 141,297 properties in the UK, has assets in excess of £3.3 billion and has a turnover in 2013–14 of approximately £480 million. We are one of the leading registered provider groups in the country and work in 205 local authority areas.

Our vision is to create aspirational homes and inspirational places. Our approach goes much further than simply building homes. We look at what an area needs to be able to thrive—whether it is new schools, shops, leisure facilities, job opportunities and access to learning and training or specialist support services.

We are not a charity although we are a not-for-dividend organisation.

Like many other Registered Providers of social housing (RPs), we submitted a response to the HCA’s recent discussion paper on the ring-fencing of social housing assets. In our response, we raised a general issue: whether the Regulator’s proposals run counter to what we understand is current government policy for RPs to widen housing choice and increase housing production. In light of this question, and the Select Committee’s current inquiry, we feel it is useful to consider the fundamental purpose of social housing and its regulation.

Our responses to the detailed questions raised by the inquiry are set out overleaf.

What has the Regulation Committee has been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

Since the Committee was set up in 2012, there has been a shift to “back-stop” consumer regulation with a heavier focus on financial viability and governance and we agree with this.

The recent failure of Cosmopolitan sent shockwaves through the sector, resulting in Moody’s casting doubt on the effectiveness of the regulator and effecting a subsequent downgrade of Moody’s credit rating.

What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

We agree with the range of risks identified in the HCA’s June 2012 Sector Risk Profile—reductions in grant, sales exposure, treasury risks and risks to income as a result of the changes brought by Welfare Reform. RPs have prepared and planned for these risks and it is the planning for these risks that has encouraged diversification to avoid RPs simply reducing their activities and levels of service.

As mentioned above, we are satisfied that the regulatory standards on governance and financial viability are adequate; however there have been concerns about the HCA’s ability to effectively enforce these standards in an increasingly diversified environment. The entrance of “for-profit” providers in the sector also creates an issue for the HCA in terms of oversight at a group level and this needs to be managed appropriately.

We agree with the co- regulatory approach favoured by the HCA—we agree that it is for RPs themselves to understand the risks they face and to manage them effectively via the governance controls they have in place. The HCA’s role is to set the framework and obtain assurances that the standards in such framework are being met. We feel that the HCA has done this overall. However from the HCA’s recent discussion paper we sense the danger that it intimates that RP Boards are not sufficiently able to direct and manage RPs with diverse business interests. If the RP sector is to continue to benefit from income generated by mixed business models, RP boards need to be in a position where they are able to take measured risks and expand their businesses, particularly so that they can provide community services and be effective contributors to regeneration schemes and to mixed-tenure development. Across the sector, the increased emphasis under the 2010 Regulatory Framework on improved governance arrangements and the quality of Board Members recruited since those regulatory changes in April 2010 in particular should give the HCA some comfort in this regard for the rest of the sector.

Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

As said above, the recent failure of Cosmopolitan had a profound impact on the sector and resulted in the downgrade of 26 housing associations’ credit ratings by Moody’s in February this year. There have been concerns in the sector that the regulator would struggle with multiple rescues, should such a scenario present itself.
The sector has become increasingly diverse, mainly in response to the key risks set out above. This diversification has presented the regulator with challenges, at the same time that its resources have been reduced. The HCA is now drawing up proposals for a fee structure to address these concerns and reduce its dependence on support from CLG but the concern is that the sector will make up for a shortfall caused by funding cuts. We recognise, however, that in order to prevent systemic failure and ensure robust and effective regulation, the HCA’s intellectual and financial capacity will need to be boosted.

In April the HCA published a consultation document, “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England”. Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

PIF understands and agrees with the HCA’s rationale for reviewing how the Regulatory Framework protects social housing assets in a more diverse sector.

RPAs are increasingly looking at new business opportunities to cross-subsidise the development of new social housing due to reduced levels of Government grant and long term debt on low margins.

The reduced funding climate along with Welfare Reform means that the sector is facing risks to its balance sheet that it has not faced for many years. RPAs have a choice of either (1) reducing their activities and their positive input into local, normally disadvantaged, communities or (2) diversify and grow their non-regulated income generating activities. PIF appreciates and understands that this latter approach carries with it increased risk as there is an increasing number of RPAs who are diversifying.

As said previously, one issue that needs to be made explicit is whether the Regulator’s proposals run counter to what we understand is current government policy for RPAs to widen housing choice and increase housing production.

The approach of Government to the sector has been to:

1. Use RPAs for the efficient delivery of low cost accommodation to those in need of housing using grant to achieve this; and
2. Involve those RPAs in a range of other socially beneficial activities associated with the development and provision of housing—regeneration, the development of mixed communities, key worker and student accommodation and temporary accommodation to name a few.

The combination of the above factors has meant that RPAs have used the income from operations outside social housing to subsidise the development of their social housing businesses whilst also using the strength and predictability of the social housing activities to compensate for the risks inherent in the other activities.

We understand the result of this is that the HCA is not satisfied the current regulatory regime gives sufficient assurance that social housing assets are always protected from the risks of non-regulated activities. This is combined with the fact that third party stakeholders, such as the rating agencies and lenders, expect there is an “extraordinary level of support” to the sector and therefore if this was found not to be the case there could be a material impact on the cost and availability of funding, particularly where, under the regulatory reform of banks and Basel III, greater levels of capital will be required of lenders where credit ratings fall into single “A” territory or below.

We do not disagree with the HCA’s desire to protect social housing assets. However, we do question whether the “no risk” approach to social housing assets is the correct approach or whether what the HCA should be seeking to achieve is the “no default” objective of the sector with lenders, rating agencies and other third party stakeholders. There should be recognition by the HCA within its approach of the increased asset management freedoms now exercised by the RP sector. The result is that RPAs regularly dispose of social housing assets through appropriate investment decisions and how they further their objectives. RPAs need to be in a position that allows them to manage their assets and so the HCA’s approach needs to reflect asset management freedoms and the disposal strategies of RPAs.

We agree with the changes proposed by the HCA to the existing Governance and Financial Viability Standard and to the code of practice on recovery planning applying to designated providers on the basis of specified criteria. We believe that these changes will result in better understanding and documentation of the key financial and business information across RPAs and therefore provide the Regulator with a much stronger starting position when it has concerns with any particular providers.

In our response to the HCA discussion paper, we recommended that the HCA’s overall proposals need to be more cognisant of different approaches with RPAs that result in a detailed and thought-through process that allows individually negotiated transition plans to be agreed with the HCA which do not have risks of reduced credit ratings or covenant breaches.

We feel that the other key element to these proposals will be ensuring that the definition of Social Housing is widened to reflect eg mixed-tenure developments, care services and economic regeneration projects.
Are the arrangements in place sufficient to preserve the independence of the Regulation Committee in relation to the HCA and the sector?

The case for an independent regulation committee within the HCA is understood and accepted and the Committee appears to us to be operating independently. However, there could be a disjunction in approach and strategy between the Regulation Committee and the HCA’s investment arm and this may be an area for examination.

Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

We supported the shift to a more “light-touch” approach to consumer regulation and feel that by and large, the consumer standards set out in the HCA’s current Regulatory Framework are adequate. We strongly support the principle of co-regulation and feel that overall, RPs have the ability to effectively understand and manage the risks they face, subject to tenant scrutiny and challenge.

June 2013

Written evidence from PlaceShapers (HCA 14)

1. BACKGROUND

1.1 PlaceShapers is a network of almost 100 community-based housing associations formed in 2008. Between us we own more than 700,000 homes and provide housing and support services to more than two million people. These include health services, social care and a range of other community services.

1.2 Together we completed over 40,000 new affordable homes between 2008 and 2012 and we collectively plan to invest around £5 billion to deliver a further 32,000 new homes by 2015. As an alliance, our views therefore represent those responsible for over a quarter of the sector’s housing stock. Details of our members and more about what we do can be found on our website: www.placeshapers.org

1.3 We are pleased to provide this submission to assist the CLG Committee’s review of the HCA’s regulation. In doing so, we have relied heavily on the response we submitted to the HCA’s discussion document on proposed changes to the regulatory framework in advance of which we held two very useful round-table discussions with Julian Ashby, Chair of the HCA’s Regulatory Committee. The full version of that response is available on our website.

2. OUR SUBMISSION

2.1 For the purposes of your Inquiry, we have limited our submission to discussion of three key issues of particular importance to us, each of which we return to below. These are:

— The adequacy of the Regulation Committee (RC)’s resources for the job it is tasked with and the practical consequences that this creates for individual registered providers (RPs) (see section 3 below);
— The proposed changes to the regulatory framework (see section 4 below); and
— A continuing perception that there are those within the HCA and DCLG who, erroneously in our view, believe that the social housing sector should consolidate around a smaller number of “big” providers (see section 5 below).

2.2 This is not to say that we have no view on other matters of interest to you but rather to focus on specific matters of material importance to our members at the current time. However, to put these in context it is important to say that we believe in the need for the social housing sector to be regulated and are supportive of the co-regulatory approach to regulation adopted in recent years.

2.3 We also agree that regulation provides important comfort to our lenders and hope to see a continuing resulting benefit of this in respect of borrowing costs.

2.4 And we believe it important that the regulator has and will continue to have enforcement powers and the resources needed to ensure that the highest risk providers cannot be allowed to fail. This is where we believe the regulatory focus should lie going forward.

3. The adequacy of the RC’s resources for the job it is tasked with and the practical consequences that this creates for individual RPs

3.1 The first matter we wish to raise is a continuing concern that the RC may not be able to recruit and retain the calibre of staff needed to discharge its role effectively. We believe that as an independent regulator the RC should be able to flex its resources without delay in order to adapt to a rapidly changing environment and that being on top of current and emerging risks requires this.

3.2 Clearly the RC’s resourcing decisions must be made within the context of the budgets available to it and we note that consideration is once again being given to RPs being charged a fee for regulation in order to
increase the funds available for the task. This is an issue on which our members have a wide range of views, but common themes are the need for any future fees to be proportionate to the risk of the RP and to be linked clearly to the value of the regulatory service received. We also consider it crucial that any fees are in addition to and not a replacement for Government funding of regulation.

3.3 Sadly we have numerous examples of regulatory staff appearing still to be more interested in ticking boxes to confirm, for example, that RP Board meetings have been attended and that key documents have been reviewed on time. This is rather than working with RPs to really understand how their businesses are developing and how actual and emerging risks are being managed in the round. An additional perceived fixation with forensic examination of one-off historical problems does not improve the regulatory experience either. Indeed, this may well be diverting scarce resources from the real need to get to grips with what is happening in the sector now.

3.4 It is to the HCA’s credit that the imminent collapse of Cosmopolitan HG was averted and clearly the RC needs to have confidence that its resources are fit for purpose to deal with any such situations going forward. We have concerns that this may not always be the case.

3.5 We are therefore pleased to note that the HCA is currently recruiting a new set of senior staff to strengthen its regulatory team and we very much hope that this will lead to a more sophisticated approach to engagement with RPs than has often been experienced.

4. THE PROPOSED CHANGES TO THE REGULATORY FRAMEWORK

4.1 We now move on to our views on the HCA’s proposed changes to the regulatory framework.

4.2 As already mentioned, we have submitted a detailed full response to the HCA’s recent consultation document. Whilst we understand and agree with the rationale for reviewing how the Regulatory Framework protects social housing assets in a more diverse sector, we have requested a more permissive and proportionate approach than that outlined in the paper. This is because of concerns that the proposals as currently framed would constitute a significant setback to the contribution we make to our local communities.

4.3 Each year PlaceShapers members contribute significantly to the expansion of social housing stock and other housing tenures, to the provision of care and support in the widest possible sense and to much needed community investment activities. We do not see this work as the sector’s equivalent of casino banking—even if much of it might be considered to fall outside the narrowest definition of “social housing”.

4.4 Our governance structures and Boards have evolved to respond to the dual challenges of co-regulation and developing new community enterprises. We believe we do and can develop the right approaches to risk management in order to continue to manage social and non-social housing activities in the same organisation. Our Boards are geared up to do this now and we believe that a regulatory focus on genuine risk rather than turnover is what is required going forward.

4.5 RPs are increasingly looking at new business opportunities to cross-subsidise their social housing businesses due to reduced levels of Government grant and long term debt on low margins. PlaceShapers appreciates and understands that this creates different risks and knows that RPs have been preparing and planning for these. Indeed, in many instances, it is the mitigation of these risks that has encouraged diversification in the first place.

4.6 Despite our understanding of the context, we consider that the HCA’s initial proposals are in conflict with the approach of Government on both a national and local basis. An approach that seeks to protect social housing assets from any risk associated with non-regulated activities is unrealistic and is not proportionate. We believe this to be in conflict with one of the HCA’s fundamental objectives: to support the provision of social housing sufficient to meet “reasonable demands”.

4.7 We remain supportive of the co-regulatory approach favoured by the HCA. As a result, we believe that it is for RPs themselves to understand the risks they face and to manage them effectively via the governance controls they have in place. The HCA’s role is to set the framework and obtain assurances that the standards are being met.

4.8 The discussion paper appears to suggest an HCA view that RP Boards may not be sufficiently able to direct and manage diverse business interests. We do not think there is the evidence to support this and believe that the Regulator has sufficient powers to intervene in individual cases should such weaknesses be identified. This is far preferable to a general shift back towards a more prescriptive, less collaborative “rules” based approach.

4.9 If the RP sector is to continue to benefit from income generated by mixed business models, RP boards need to be in a position where they are able to take measured risks and expand their businesses as they see fit. PlaceShapers members demonstrate a clear success story in this strategy and the increased emphasis on improved governance arrangements and the quality of Board Members post April 2010 should give the HCA comfort in this regard.

4.10 Our major problem with the proposals as set out in the HCA’s discussion paper concerns the suggested ring-fencing arrangements. We do not believe that this question should be prioritised above others or that it is
necessary to artificially segregate varying activities (ie “social housing” from “non-social housing activities”) into separate organisations.

4.11 Arguably the biggest risks to social housing assets are ones that now come with social housing activities themselves, eg the impact of Welfare Reform, the development of new social housing stock at much reduced grant levels, the viability of assumed shared ownership development and sales etc.

4.12 Leaving aside the issue of how to define what would be regarded as a “social housing activity”, the key issue with the proposed ring fencing is that all RPs would be treated in the same way, without recognising the major differences in size, complexity and types of business now evident. The HCA refers to a “sector” without recognising that existing levels of diversification within the sector mean a sector-wide, “one size fits all” approach will not be fit for purpose in any regulatory framework and cannot be a proportionate response to risk.

4.13 Furthermore, the non-recourse to social housing assets proposals do not reflect the excellent track record that most non-social housing activities have had for years and the generated surpluses that have been reinvested in social housing activities and new assets. In the case of PlaceShapers members it does not recognise our excellent record in relation to wider investment in local communities. Stopping such cross-subsidisation would have a major and negative effect on the sector and a material impact on the plans of most PlaceShapers members. This is why we have urged a more proportionate approach that takes account of the materiality and scale of such activities and does not put everyone “in the same box”.

4.14 Additionally, as the HCA will be aware, the care sector already has its own regulatory regime so there is already a position of material overlap between regulators for RPs with care businesses. Any new approach needs to recognise this overlap as a live issue with increased costs for both RPs and the regulators. As such, there needs to be an accommodation between the regulators in order to deliver the statutory duty on the HCA to minimise regulatory interference for RPs.

4.15 In summary, if the HCA is not to undermine its commitment to co-regulation, any revised regulatory approach needs to recognise that the key responsibility for managing risks and approving sound business models lies with RP Boards and that it may well be that the risks within an RP’s business are best mitigated by developing other streams of business.

4.16 We believe that the HCA should accept that the time and costs required to establish new and potentially cumbersome governance models may not be justified where risks are low and that it will be reasonable for some RP Boards to decide against a move away from a business model that continues to work effectively.

4.17 As a consequence, we favour an approach that abandons the ring-fencing proposals in their entirety. Our preferred approach is to toughen the Living Will proposals to ensure that Boards maintain an appropriate focus on risk and that effective recovery plans are drawn up where necessary.

4.18 As an alternative, we have also recommended that the HCA’s RC considers a model of protection similar to that used by the CAA/ATOL. This would involve a sector wide levy under the HCA’s current powers of, say, £1 per social housing property per annum for the foreseeable future that would act as an “RP Support Fund” for RPs in financial difficulty. The aim of the Support Fund would not be to rescue RPs (due to the obvious moral hazard arguments) but to enable an orderly break up of an RPs business where it was in (terminal) financial distress. In testing this idea amongst our members we are aware of varying degrees of support but we nevertheless consider the idea as worthy of further exploration.

5. A continuing perception that there are those within the HCA and CLG who, erroneously in our view, believe that the social housing sector should consolidate around a smaller number of “big” providers.

5.1 The final matter we wish to bring to the Select Committee’s attention is our concern that there exists on the part of a minority of senior people within the DCLG and HCA a view that RPs of the size of many community based PlaceShapers would be better off merging with larger providers and that “big is best” in terms of driving down costs and generating surpluses that can be reinvested in more homes. This is not helped by the peddling of this view by the leaders of some of the sector’s more acquisition hungry large-scale providers.

5.2 The evidence does not support this view. There is no clear relationship between size and efficiency as numerous studies have shown. The HCA’s own data on RP global accounts shows that management costs and operating surpluses vary widely across the sector as a whole and within subsets of large or smaller providers.

5.3 Areas of chosen operation (both geographic and service) and/or the make-up of the stock itself are the acknowledged drivers for variations in unit management costs, not differences in organisational size. Cost differences are more likely to be linked to issues such as varying regional wage rates, levels of neighbourhood deprivation, levels of additional care and support provision, the varying age and property maintenance costs of stock, etc. These are unlikely to be seen in simplistic comparisons, an issue the RC needs to understand when considering value for money.
5.4 Furthermore, our own research confirms that many MPs and Local Authorities mourn the loss of locally based independent housing associations due to merger. Some mergers are undertaken for the best strategic reasons and do have customers' interests at heart but that does not always appear to be the case.

5.5 What the sector needs is a diverse range of excellent providers tuned into the needs of their local communities and able to work effectively with local partners to deliver new homes and improving services. Our own publication “Build local” which was launched by the Housing Minister, Mark Prisk at our Annual Conference on 30th May (and is available on our website) shows how our members achieve this.

5.6 In this light, we believe that DCLG, the HCA and its independently constituted regulator should acknowledge and be actively supportive of the benefits that come from our diverse sector. Yes, sometimes mergers will be needed and will be in the best interests of the organisations involved and their residents. But widespread consolidation is not what is needed. In respect of risk alone, there are surely much greater risks associated with consolidating social housing provision around fewer, larger providers, with any one failure having the potential to damage the sector to a far greater extent than currently imaginable.

We hope that this has been helpful.

June 2013

Written evidence from Luminus Group (HCA 14)

Executive Summary

1. There is a clear business case for streamlining, not increasing, the burden and scope of social housing regulation, with benefits to the taxpayer, the activities of social landlords and the communities they serve.

2. The existing regulatory burden will be exacerbated by the new proposals. The proposals for ring-fencing social housing assets and “living wills”, will constrain innovation and harm local people (most especially vulnerable ones), as socially responsible businesses are restricted in their aspirations to meet community needs.

3. There already is ample regulation of the social housing sector through numerous bodies, including the Health and Safety Executive, Housing Ombudsman, Companies House, Charity Commission, the stringent demands of funders, the detailed requirements of external auditors, review by local authorities, buttressed by accountability to local councillors and Members of Parliament.

4. Social landlords and tenants feel that the nature of social housing regulation, both current and proposed, seriously threatens their effectiveness in their mission as community anchors and their foundational role in supporting a lively economic recovery. Many believe, but for obvious reasons are apprehensive about stating publicly, that the existing framework generates unnecessary interference and excessive bureaucracy.

5. Some, like Luminus, have achieved privately funded house building programmes, with minimal public grant being accessed. Luminus has sustained the highest levels of customer approval and employee engagement in this and other business sectors, and has established a track record of excellence with a strong national brand.

6. These successes have been delivered in a context of burdensome regulation, that often has felt disproportionate. It routinely interferes with the effective running of the business and seriously diverts management time and effort. In that regard, the process of regulation has, in itself, generated business risks, with Board and senior management being frequently drawn into lengthy and time consuming “regulatory engagement”.

7. The argument for increased regulation appears not to have been made with proper consideration for the impact on social landlord businesses and the communities they seek to serve, but appears to have sprung from a distant, desk-top assessment of forms, ratios and knee-jerk assumptions, fuelled by a single problem in the sector (Cosmopolitan). Tenants have expressed surprise that a government department is being increased in size and cost during a time of public austerity. They cannot understand how such public expenditure will enhance the quality of their lives when their own social landlord experience is already positive and meeting their requirements.

8. The new proposals fail to grasp that, for many Registered Providers, the wider role of social and economic wellbeing of communities is their core business. While there is an important moral dimension to this, effective social landlords also clearly understand the commercial imperative underlying this aspiration: where communities thrive, neighbourhoods are desirable, homes are in good order and thus property assets continue to appreciate in value.

9. For successful social landlords who do not rely on government grant, and where tenants are in favour, there is a strong case for deregulation of the sector. Former arguments that regulation provided better financial terms for social landlords no longer apply.

10. The Committee is asked to consider whether there continues to be a need for a specific regulator for the sector, when there already exists an extensive framework for regulation of social landlords.
11. If regulation is thought to be necessary by a specific social housing regulator then it should be co-regulatory, proportionate and “light-touch” in approach, with an emphasis on minimising interference. It should be based on an annual self-certification by the Board that it has assessed and managed risk.

12. Any additional regulation over and above self-certification should be focused only on for-profit providers and those not-for-profit registered providers that are very high risk.

13. There should be no ring-fencing that will fetter not-for-profit providers.

**Introduction**

14. Luminus aims to be an example of the social housing sector’s Premium Brand, serving some 45,000 customers across Cambridgeshire. With an undergirding sense of social responsibility, Luminus has succeeded in inspiring employees and customers to coalesce around our “2020 Vision: the Road to Renewal”, a programme to rejuvenate communities and transform society so that towns and neighbourhoods are places of achievement and self-determination, with low crime rates and high indicators of quality of life.

15. Since March 2000, we have successfully developed a business model that is built upon cooperation, understanding and a celebratory approach to life and work. Although our access to social housing grant has been extremely limited during that time, we have still managed to develop several hundred much needed new homes in the East of England that are recognised for their contemporary design and high quality. We add to this a hands-on, down to earth local management approach, drawing on our staff skills and commitment and energising local support from tenants and street representatives across tenures.

16. Many of our business outcomes that have changed the lives of people and their communities are not measureable by metrics of social housing regulation. Yet, from the perspective of government and taxpayer, our daily interaction in communities—for example, preventing abuse of vulnerable people, undertaking mediation, tackling homelessness and worklessness’, encouraging a joined-up approach among public agencies, stimulating co-operation from private businesses, encouraging social enterprises—are the heart of a strategy enabling UK plc to remain buoyant during the current economic malaise.

17. The Company and its tenants feel that the nature of social housing regulation, both current and proposed, seriously threatens the effectiveness of social landlords in their mission as community anchors and their foundational role in supporting a lively economic recovery.

**The Business Case for Streamlining Regulation**

18. There is a clear business case for streamlining, not increasing, the burden and scope of social housing regulation, with benefits to the taxpayer, the activities of social landlords and the communities they serve.

19. Most social landlords’ experience of social housing regulation is that it is burdensome and disconnected from the real world in which they operate, where our focus is on helping and supporting communities, tackling anti-social behaviour, encouraging self-determination and being financially prudent in maintaining homes, while also seeking to build much needed new ones.

20. The Luminus business commenced in 2000, by acquiring 7,000 council homes in a poor state of repair. Since that time we have invested over £150,000,000 in improving tenants’ homes and neighbourhoods. The Company has also maintained a privately funded house building programme, with minimal public grant being accessed. Luminus has sustained the highest levels of customer approval and employee engagement in this and other business sectors, and has established a track record of excellence with a strong national brand.

21. However, these successes have been delivered in a context of burdensome regulation that has repeatedly interfered with the effective running of the business and seriously diverted management time and effort.

22. In that regard, the process of regulation has, in itself, generated business risks, with Board and senior management being frequently drawn into lengthy and time consuming “regulatory engagement”. These extensive discussions with, and explanations to, the regulator have grown in frequency and volume as the regulator has morphed from The Housing Corporation to the TSA (2008) and then the HCA (2011). They have had to be repeated as regulatory staff were made redundant or left. The regulator’s demands are resource-hungry, with extensive information previously provided having to be sent again. The substantial amount of repeat information the Social Housing Regulator deems necessary to perform its function appears disproportionate to the value of collecting that data.

23. Many social landlords believe, but for obvious reasons are apprehensive about stating publicly, that the existing framework generates unnecessary interference and excessive bureaucracy. A government enquiry in 2007 recommended that this burden of regulation be removed, becoming risk based and “light touch”. The opposite has occurred and many professionals and tenants find it difficult to assess how social housing regulation delivers value for money to the tax payer. Social housing regulation appears to have become an end in itself, not a contributor to improving the effectiveness of social housing. Moreover, the current predicted growth of the regulator’s manpower and activities adds to these concerns.

24. The argument for increased regulation has not been made with proper consideration for the impact on social landlord businesses and the communities they seek to serve, but appears to have sprung from a distant,
25. The existing regulatory burden (which includes frequent contact from regulation staff by email, telephone and in person; financial questionnaires; statistical data returns; annual accounts; fraud returns etc) will be exacerbated by the new proposals. We are concerned that the proposals for ring-fencing social housing assets and “living wills”, will constrain innovation and harm local people (most especially vulnerable ones), as socially responsible businesses are fettered in their aspirations to meet community needs.

26. There already is ample regulation of the social housing sector through numerous bodies, including the following:

- Health and Safety Executive.
- OFCOM.
- Charity Commission.
- Companies House.
- Financial Services Authority.
- HMRC.
- Equality Commission.
- Information Commission.
- Housing Ombudsman.
- Fire Service.
- Trading Standards.
- Environmental Health.
- Pensions Regulator.
- External Audit.
- Banks and other private funding institutions.
- Local authorities.
- Local authority councillors.
- Members of Parliament.

27. These bodies, groups and individuals cover a wide range of activities, interests and statutory requirements. Their detailed systems and processes focus on the performance, viability, legal compliance, good governance and responsible operation of social landlords. Funders, for example, engage very robustly with social landlords, requiring Boards and senior management to maintain effective, viable business plans and strategies. This is mirrored in the regulatory, monitoring and scrutiny by the many others referred to above. In this way, social landlords are continuously held to account and challenged.

28. In addition to these statutory processes, social landlords voluntarily submit to a wide range of independent sources of scrutiny, including Investors in People, ISO 9000 Standards, RoSPA and numerous external assessors that measure the business effectiveness against a range of metrics applicable within the best-run commercial organisations. Ultimately, social landlords are regulated by the strength of public opinion—their tenants and the wider community—that is monitored by independent press and media who take considerable interest in failure. Finally, courts have substantial powers to enforce the rights of all stakeholders. All of these are strong incentives for Boards and senior management to strive for success.

29. Many social housing businesses have developed robust business models, are acknowledged for excellent customer service and have a strong community presence. They draw on the capacity of their Board and senior management team to anticipate and respond to the numerous challenges encountered in a rapidly changing social and economic environment.

30. By contrast, the system of social housing regulation is based upon an approach developed in the 1980s that itself has not matured sufficiently to understand the sector’s capacity for business excellence. Regulatory principles appear to be grounded in prior judgements, sometimes evidencing political standpoints. While the sector has continuously challenged itself to be self-critical and to improve, there no obvious evidence that the regulatory system has mirrored this.

31. We share the National Housing Federation’s (NHF) concerns, expressed in its document “Protecting social housing assets in a more diverse sector, June 2013” that there is a considerable risk of “mission creep”. An experienced and diverse Board and senior management, and not additional regulation, is the key to meeting the challenges of the external operating environment. Our engagement with the regulator demonstrates no added value to the business, and in fact has diverted the Board and senior management from the essential task.
of running the business and developing creative solutions to the challenges presented by the economic downturn and the social problems that are being generated in its wake.

**COMMENTS ON THE NEW PROPOSALS**

32. The emerging proposals as published by the HCA give cause for concern. We concur with the NHF’s comment that “there is no need to regulate the flow of funds within the group by means of controls such as ring-fences”.

33. The new proposals fail to grasp that, for many Registered Providers, the wider role of social and economic wellbeing of communities is their core business. While there is an important moral dimension to this, effective social landlords also clearly understand the commercial imperative underlying this aspiration: where communities thrive, neighbourhoods are desirable, homes are in good order and thus property assets continue to appreciate in value.

34. As an example of adding value to communities that then benefit both the taxpayer as well as the citizen, Luminus has successfully developed a business model that engages communities in volunteering, training, education and employment. Recent research from the Housing Associations Charitable Trust (HACT) states that every volunteer is worth upwards of £11,000 to the local economy; placing people in employment is valued at £8,500. For Luminus that is an investment of £660,000 in the local economy in 2012–13. The proposals of the HCA will have a detrimental impact on the social value of our activities, and our ability to innovate.

35. In addition, there is little recognition in the proposals that, within an increasingly restricted grant regime, the need to cross-subsidise the funding of new social homes through other activities is not merely desirable, but vital.

36. The proposals to ring-fence such activities also fail to recognise that the sector’s increasing focus on mixed tenure developments is not purely driven by financial considerations. It is well understood throughout the sector and by our local authority partners in particular that mixed tenure developments are vital in creating balanced and vibrant communities.

37. The regulator should focus its attentions on for-profit providers and those engaged in high-risk activities, such as those whose business plans are predicated on the need to sell affordable homes.

38. The new proposals, partly a response to the problems experienced at Cosmopolitan, are an over-reaction, and wrongly imply a failing sector in need of intervention. This isolated incident should not be used to straitjacket the sector. Indeed, for successful social landlords who do not rely on government grant, and where tenants are in favour, there is a strong case for deregulation of the sector.

39. Former arguments that regulation provided better financial terms for social landlords no longer apply. There is now ample evidence that funders devise their own credit rating of each organisation and do not rely on a sector wide rating. In cases of repricing by lenders, the margin proposed is similar to that offered to private development companies. Indeed, funders are now taking every opportunity to reprice loans in the sector simply to bolster their own balance sheets with no reference to risk. Also see attached article by Derek Joseph, in Social Housing March 2013.

40. We support many of the comments put forward by the NHF, including “…in the spirit of co regulation, it should be for the board to decide what form of risk management strategy provides the necessary assurance.” There is also the risk that the regulator will seek to acquire commercially sensitive information through its insistence on being provided with “living wills”, whereas all it should need is an externally audited statement that such a document exists and is fit for purpose.

**CONCLUSION AND RECOMMENDATIONS**

41. In discussions with others in the sector, it is clear that the diversion of resources created by the current regulatory framework will be exacerbated the new proposals. Moreover, they fail to address the concerns of social landlords about the burdensome and intrusive nature of regulatory practices. Furthermore, the new proposals distance the HCA even further from earlier promises and expectations of a lighter touch, co-regulatory approach that arose from government research and public consultation.

42. In light of this, and having consulted others, our recommendations are as follows:

(a) The Committee is asked to consider whether there continues to a need for a specific regulator for the sector, when there already exists an extensive framework for regulation of social landlords.

(b) If regulation is thought to be necessary by a specific social housing regulator then it should be co-regulatory, proportionate and “light-touch” in approach, with an emphasis on minimising interference. It should be based on an annual self certification by the Board that it has assessed and managed risk.

(c) Any additional regulation over and above self certification should be focused only on for-profit providers and those not-for-profit registered providers that are very high risk.

(d) There should be no ring-fencing that will fetter not-for-profit providers.
Written evidence from Leeds Housing Forum (HCA 15)

1. What has the Regulation Committee been doing since it was set up in 2012? How well has it done? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

Content with the approach the Regulation Committee has taken to its responsibilities towards HAs.

2. What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

The major risk for the housing sector is the financial risk associated with welfare reform changes and changes to the grant regime. Well run housing associations should be able to adapt their businesses in order to respond to any reasonable implication arising from the changes. However, the impact of those changes, and the need to maintain a viable business, will lead to some of the other activities Associations do being either reduced or stopped altogether. The areas affected will likely be reduced development activity, and reduced regeneration and social investment activity. These things generally need subsidy to work, and either reducing grants for development or causing increased running costs for example through the increases to resources necessary to collect rent through the introduction of direct payments, reduces the surpluses and cash available to provide that very subsidy internally.

3. Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

The Regulation Committee appears to be working well, within the powers and resources available to it. There is sometimes a question about the ability of some of the HCA’s regulatory staff to deal with the challenges arising within the sector, where complicated group structures, financial arrangements and diversification activities lead to difficulties. Having exceptional staff within the HCA is vital in order to deal with the exceptional challenges which arise in Housing Associations from time to time.

4. In April the HCA published a consultation document, “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England”. Why changes are needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

There is a need to change to how the sector is regulated, in order that the public investment made into housing is not lost in some way. In particular this relates to the ability of private sector organisations to access grant now and the need to ensure that grant is used for “public” benefit in perpetuity. The challenge in this area is to ensure that grant does not leak into other parts of the private sector companies’ activities, or is distributed to shareholders in some way. But it also in relates to the increased tendency across the sector to diversify, often in order to create subsidy for other social housing activity. A way needs to be found which allows such activity to continue (to create the subsidy) without at the same time creating undue risk to the assets which have been publically funded.

There are a number of adverse consequences arising from the current “conversation” document, and responses have been provided by a number of interested parties. Of particular concern though is the ring-fencing proposal, which as written would restrict the activity of Housing Associations to the provision of general needs rented housing and pretty much nothing else (bar a minor tolerance of 5% activity). The scale of social investment, regeneration activity, and care related activities some RPs currently undertake, and plan to continue to undertake over forthcoming years, would have to drastically reduce, and in many cases may stop altogether. Registered Providers do so much more than simply provide general needs housing. RPs contribute to the sustainability of neighbourhoods and wellbeing of the people who live there. To effectively stop that activity would have serious consequences for the neighbourhoods in which RPs work, as it is highly unlikely that work would be undertaken by anyone else.

5. Are the arrangements in place sufficient to preserve the independence of the Regulation Committee in relation to the HCA and the sector?

No comments
6. Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

As tenants, a primary interest is that of consumer regulation and the bringing forward of complaints from tenants to be investigated and determined where they are “of serious detriment to tenants”. The understanding is that the HCA/Regulation Committee has already received a significant number of such complaints. However and so far, the majority have either been deemed not to have met the above primary requirement or, on investigation, have not been upheld.

Our concern is that, as yet, there has been no explanation of or statement on the grounds which have resulted in these conclusions by the regulator. As a body, tenants and their HAs are thus still in the dark as to what constitutes “of serious detriment to tenants”.

Fuller clarification would be of assistance to tenants not only in avoiding inappropriate complaints being brought forward to the regulator but in indicating where, for example, further negotiations and discussions with their HA may be a better mechanism for successful dispute resolution. It is understood that, towards this end, the regulator intends to provide a number of case studies. That such provision be treated as a matter of some urgency would be welcomed.

June 2013

Written evidence from Secured by Design (HCA 16)

I am writing from the police crime prevention initiative, Secured by Design, to provide our thoughts on the role of the Homes and Communities Agency’s (HCA) Regulation Committee ahead of your session with its Chair. I would put on record our firm view that the HCA has been pivotal in helping cut burglary and anti-social behaviour in social housing in England, with longstanding support for security standards. However, we would like to see the Regulation Committee take oversight of security standards to ensure they continue to benefit social housing residents for the future.

About Secured by Design

Secured by Design is a flagship initiative with the objective of designing out crime during the planning process and can be retrofitted to existing housing stock. We believe that residents have the right to feel safe in their homes, and security standards are about ensuring this is a consideration in both the planning process and retrospectively. In fact, independent research has shown that homes with low level security suffer 75% more burglaries than those with realistic Secured by Design level security, while criminal damage is also reduced by 25%.

Secured by Design is open to all sections of the construction industry provided they meet the security standards in our project. The scheme is self funded by our accreditation of a range of security products which can be shown to meet standards and reduce crime. Any surplus is reinvested in research and crime prevention projects across the country. There is no obligation on builders or architects to use these particular products, many of which are not related to construction. Notably, Secured by Design standards can be added through refurbishments meaning that the standard can be applied retrospectively at limited cost.

The implementation of Secured by Design principles in the design and build process has led to significant and sustainable reductions in crime in areas across the UK, including Nottingham, Glasgow, Kent and West Yorkshire. Notably, recent statistics from the Office of National Statistics have shown that high quality security products have contributed to the recent drop in burglaries.

Moreover, for the HCA specifically, by reducing burglary and anti-social behaviour, there are significant benefits reaped in terms of reduced maintenance costs and fewer void properties to protect. Undoubtedly this has also resulted in increased satisfaction of residents residing within properties falling under the HCA remit.

Role of the HCA Regulation Committee

1.1 We support the key consumer objectives of the Regulation Committee to ensure the provision of social housing is “well-managed”, of “appropriate quality”, and encourages registered providers to contribute to the social, economic and environmental well-being of their areas.

1.2 At Secured by Design, we consider the safety of homes to be a crucial element of improving well-being for communities, whilst also being imperative to the sustainability of the housing stock in England. The importance of security to the public is evidenced by The Future Homes Commission report published in October 2012 that noted that 43% of people interviewed stated that security was the most important aspect of homes. As such, we consider that the principles of security should be better embedded in the consumer objectives of the committee in order to boost residents’ satisfaction.

1.3 You may be aware that the security element of the Code for Sustainable Homes aims to "encourage the design of developments where people feel safe and secure; where crime and disorder, or the fear of crime, does not undermine quality of life or community cohesion", and credits are awarded for complying with this. The HCA's insistence on social housing meeting a certain level in the Code for Sustainable Homes is the correct approach and we would like to see a greater focus from the Regulation Committee in monitoring and protecting these standards. Adhering to these principles has been beneficial for ensuring more social housing tenants can live in a safe and secure environment and this must remain the case for the future.

1.4 The reliance on security standards as specified by Secured by Design ensures high quality and value for money. This has resulted in the significant growth of suppliers offering high grade products which meet the standard, at more competitive prices, and a keenness to ensure certification for products to meet security standards at tender stage.

1.5 The Regulation Committee cites the previous Government’s Decent Homes Guidance which states that the delivery of decent homes should not be an obstacle to landlords carrying out work falling outside its scope but achieving other local priorities, such as physical improvements to help design out crime. We consider a decent home to be one that is safe and secure, and there have been valuable examples of combining the Decent Homes Standard with our initiative, such as in Nottingham where crime was seen to fall significantly. Please find enclosed a case study for further information. We welcome the Regulation Committee highlighting the importance of work falling outside the scope of the Decent Homes scheme, but would call for more explicit oversight of the security of the England’s social housing stock.

1.6 We remain concerned that the trend towards de-regulation in standards will jeopardise the predominantly good quality of social housing and falling levels of crime. The Code for Sustainable Housing is at risk as well as other guidance; the loss of the Code for Sustainable homes, which references Secured by Design, could have serious implications for social housing and the safety of tenants. I hope that the Regulation Committee will respond strongly to these concerns on behalf of social housing residents in the England.

I hope you have found the content of this submission informative, and we look forward to seeing the Select Committee’s conclusions on HCA regulation.

June 2013

Written evidence from the HCA Regulation Committee (HCA 17)

What has the regulation committee been doing since it was set up in 2012? Are there other things it should have been doing? What impact has it had on the social housing sector since its establishment?

1. Since its establishment in April 2012 the Regulation Committee has taken decisive steps to shape the future strategic direction of social housing regulation. We have articulated our main strategic aim as the protection of social housing assets so that tenants and tax payers who have invested in the sector are protected and the sector remains attractive to private investment. We have three core elements to our approach to meeting our strategic goal: strengthening our framework; strengthening our operational approach; and strengthening our capacity.

2. More specifically we have:

(a) In June 2012, for the first time, set out the regulator’s comprehensive view on risks in the sector and communicated this to registered providers in our “Sector Risk Profile” document—which has informed our main activities.17

(b) Published a “Regulating the Standards” document setting out our methodologies for assessing performance so all providers are clear about our expectations.18

(c) Continued to regulate with a light touch regime for the smallest providers (for example alms houses and small scale co-operatives), whilst ensuring we have a proportionate and risk based approach to the largest associations, some of which now own up to 90,000 properties.

(d) Revised the approach to regulatory judgements on social housing providers, key documents where we make public our regulatory view on providers which are important to creditors and enable boards to hold executives to account. We subsequently published judgements on governance and financial viability for 113 of the c.250 providers for whom such judgments are produced.

(e) Overseen from the regulatory perspective the successful resolution by the sector of issues at Cosmopolitan Housing Group, a landlord owning c. 10,000 homes in North West England. This was one of the most complex cases in the history of social housing regulation where there was a possibility of provider insolvency.

(f) Overseen other significant case work.

18 http://www.homesandcommunities.co.uk/sites/default/files/our-work/regulating_the_standards_-_may_2012.pdf
(g) Started developing policy in relation to the diversification of the sector and started carrying out substantial stakeholder engagement on proposed future regulatory approaches.

(h) Overseen a restructure within the regulation directorate to improve capacity to regulate in a more challenging environment.

(i) Provided ongoing advice to government on issues relating to the social housing sector and its regulation.

3. These are the activities that we set out to do in the HCA corporate plan and are in our view a realistic and reasonable interpretation of the remit we have been given by legislation. Despite the challenging operating environment, the Committee has maintained the position that no tenant has lost their home and no investor in the sector (be they the taxpayer or private investors) have lost their money as a result of provider failure.

What are the major risks facing Housing Associations and the social housing sector? Are the standards set by the Regulation Committee on governance and financial viability adequate to mitigate those risks? Are the established arrangements providing self-regulation of the sector being adequately supervised and tested? What effect are EU procurement rules having on the financial stability of the sector?

4. We have a responsibility to keep abreast of risks facing the sector and communicate these in a clear way to stakeholders and hold them to account for how they are addressing those risks. We do this through our sector risk profile publication, the publication of other monitoring data and our on-going regulation of providers. The sector is facing risks from a number of sources. How these risks affect different providers and interact with other risks depends on the precise nature and business models of individual social housing providers.

5. The main risks we identify in the sector risk profile document are:

   — Asset related risks—In order to finance the development of new social homes in a world of constrained grant, providers are taking on more debt and having to rely on riskier activities such as market sales to cross subsidise social housing development. Taking on such activities places a high premium on effective risk management.

   — Liability risks—These risks predominantly relate to the liabilities of providers arising out of their funding arrangements. Private finance providers are under well publicised pressure to conform to Basel 3 regulatory standards on capital and liquidity management. As a result they are looking at ways to increase the interest rates they charge on debt, which given that rents are fixed, could result in less money available for new homes or other services. Additionally, as a result of the current, more constrained, lending environment some providers are turning to more complex forms of financing. Depending on the precise types of financial instruments that providers use they are likely to have to manage a greater range of liability risks than traditionally.

   — Income risks—Providers need to manage a greater risk of rent arrears as a result of a range of changes to the benefit system. Elements of the welfare reforms affect different types of provider differently so there is an ever greater premium on providers understanding their stock and tenant base and the specific features of the local areas in which they operate.

   — Cost related risks—as with many businesses providers are exposed to cost related risks eg costs of pension funds, build/maintenance costs etc.

Diversification of activities within the sector, which we discuss below, is in part driven by a response to many of these risks and in particular to enable cross subsidy for development in a lower grant environment. Diversification also brings with it its own specific risks to providers if not managed effectively.

6. The standards set on governance and financial viability are largely outcome focussed and seek to ensure that registered providers meet the criteria of being sufficiently well governed and financially viable. In turn we gain assurance that these standards are being met. In the main we think these standards are the right ones but we have identified that more could be done in the standards framework to clarify our position on the management of diverse activities in order to more clearly articulate that boards must understand their exposures and not put social housing assets at risk.

7. The regulator’s approach to seeking assurance on compliance with the governance and financial viability standard is set out in Regulating the Standards. We obtain our assurance and reach our judgements based on financial and statistical information and importantly the assurance that boards themselves get and the quality of controls and risk management. We carry out a routine suite of activities annually for all providers owning more than 1000 units, in a risk based manner seeking greater assurances from larger, more complex or riskier providers. In a rolling programme publish our judgments on the governance and viability of these providers. Within the context of the current regulatory framework, based on the principles of co-regulation, we believe that this approach allows us to gain adequate assurance on providers’ compliance with the regulatory standards.
Is the Regulation Committee policing the financial regulatory regime adequately to address both the risks of the failure of individual registered providers and systemic failure? Has it the power and resources needed to regulate effectively?

8. The Regulation Committee’s aim is to mitigate risks of failure and manage failure situations to protect social housing assets so far as possible, not to necessarily ensure the survival of every single provider. The regulation of the financial viability element of the governance and financial viability standard is designed to give early warning signals of potential failure. Where providers do get into difficulties our aim is to be prepared to take necessary action to support the resolution of problem cases and in extremis use our powers to do so.

We are commissioning a lessons learned exercise from the recent Cosmopolitan case to ensure our approach to managing failures in individual providers is as robust as it can be.

9. Because of the way the sector is funded there is a strong connection in this sector between failure of an individual provider and the success of the sector as a whole for delivering new supply of social housing. This is not a systemic risk in the classic sense but is very important at the sector wide level. Currently providers are able to borrow at preferential rates in part due to the expectation of government support (through regulation) in preventing failure. If a provider were to fail it is likely that this would lead to an increase in the price of debt limiting the capacity of the sector to develop new homes. We manage this risk through our regulation of individual providers and through close on-going liaison with financial institutions.

10. Although not strictly systemic risks, there are a large number of common risks faced by providers to which they are exposed to a greater or lesser degree. These are largely those explained in our sector risk profile, as examples, risks to income from direct payment of benefits to tenants, exposure to higher interest rates, headroom for changes in rental policy etc. As part of our regulatory approach we assess the degree of exposure of providers to those risks as part of our ongoing engagement seek to test providers' understanding of the risks to which they are exposed and their strategies for mitigating such risks.

11. More classic systemic risks arising from the interdependence of providers do exist in the sector, eg interdependence on pension scheme liabilities built up through a history of mergers and stock transfers, dependency on eg maintenance or building contractors or joint service provision. These systemic risks are important but the interconnectedness between providers is at a much lower order than, for example, in the financial services sector. It is therefore unlikely that a financial failure in one provider will create a domino effect through the sector or the economy as a whole but in line with our comments above may cause loss of confidence in the sector and increase the costs of borrowing. Currently exposure to such risks is examined through our financial regulation of individual providers. Our proposals on recovery planning as set out in our recent discussion document should enhance the sector’s preparedness to deal with systemic risks that exist in their particular networks of dependencies.

12. The regulator’s powers were developed in a benign pre credit crunch environment when there was a strong focus on consumer protection. In theory this gave us a graduated range of powers to regulate the sector. In practice there are now severe limitations on how we can use these powers as a consequence of the financial environment where use of powers could lead to a breach of loan covenants and in turn repricing or repayment of existing debt. Within the detail of our powers there are also some challenging issues. Our experience in planning for a moratorium illustrated that it would be challenging successfully to complete the process within 28 working days. Much would depend on the willingness and ability of secured creditors to work with the regulator and a lead bidder to reach a simple and fair solution. It is also essential that the regulator has sufficient robust data to enable prospective bidders to assess the value of the assets, which really means starting work well before an insolvency event triggers the moratorium process. One of the issues we face is that Industrial & Provident societies (which constitute a significant proportion of the sector) cannot be put into administration, making resolution of problem cases more difficult than would otherwise be the case. The standards based approach can sometimes make it difficult to deal with novel and more complex types of provider, where regulation by contract or other more bespoke means may be more appropriate.

13. Once the proposed strengthening of regulatory capacity and of the regulatory standards has been achieved then the regulator will be in a materially stronger position to cope with individual risks and systemic failure. Recent work restructuring the regulation directorate has been designed to release capacity to deal with more complex providers within our current regulatory model. Changes to the regulatory framework of the nature set out in our recent discussion document will inevitably mean the regulatory operational model will need to evolve and resources will need to be aligned accordingly. We are considering this alongside the development of policy. The regulator has the powers in the Housing and Regeneration Act to generate its own income for its functions through fees charging. This is an issue that the Regulation Committee keeps under close review.

In April the HCA published a consultation document, “Protecting Social Housing Assets in a More Diverse Sector: a discussion paper on the principles for amending the Regulatory Framework for social housing in England”<http://www.homesandcommunities.co.uk/sites/default/files/our-work/130404_regulatory_framework_discussion.pdf> . Why are changes needed, and are those proposed adequate? Would the proposed changes have any adverse consequences?

14. We set out why we think that changes to the regulatory framework may be necessary at the start of the discussion document. The need for changes flow directly from our analysis of risk in the sector as set out in
the Sector Risk Profile that we refer to above. In summary the main reasons for looking at the framework are twofold:

(a) There is a long term trend of diversification in the sector and we believe that in the current operating environment the drivers and incentives for providers to diversify activities are greater, particularly in order cross subsidise new supply in an environment of decreasing subsidy;

(b) The Housing and Regeneration Act gave providers freedoms on how they organise themselves and allowed new types of provider who operate on a for profit basis to enter the sector.

In line with our statutory objectives, our concern has been to ensure that diversification does not lead to undue risk being put on social housing assets and thereby putting historic investment at risk or make the sector less attractive to future investment. In feedback from our recent consultation exercise many in the sector were concerned that methods for dealing with these risks that we set out would act as a constraint on beneficial activities. We are continuing our dialogue with stakeholders to find an appropriate balance between protection of social housing and freedom for providers to carry out a range of beneficial activities. We remain determined to address the risk of recourse to social housing assets from commercial activities.

15. We made proposals in three main areas in the discussion document, these are: (i) “ring fencing” of social housing assets from risks caused by non-social housing activities; (ii) recovery planning (measures that providers can take to be better prepared for and thereby avoid failure situations); and (iii) proposals on capturing public value on disposals out of the sector by for profit providers. We deliberately framed the document as an open discussion with the sector and have sought feedback on alternative proposals and potential consequences.

Before the regulatory framework is changed we will conduct a formal consultation as required by statute on the detailed changes.

16. The changes that we have proposed in the recent discussion document describe how similar issues have been addressed in other regulated sectors, including in the financial services sector and make proposals about the applicability to this sector. The biggest balancing act in the discussion document is between ensuring the risks to existing assets are well managed by those providers engaging in diverse activities whilst not stifling a potential source of revenue for new supply. Throughout our engagement on the discussion document and in the responses that we are now analysing a range of alternative suggestions on how we can meet the twin objectives of protecting social housing assets and promoting new supply have been made. We are currently reflecting on the results of this initial phase of engagement and working through alternatives to determine what proposals we ultimately want to put to the sector in our formal consultation to change the regulatory framework.

Are the arrangements in place sufficient to preserve the independence of the Regulation Committee in relation to the HCA and the sector?

17. Within the HCA the statutory separation of functions between the HCA acting as regulator and the rest of the agency is elaborated upon in the protocol between the HCA board and the Regulation Committee, which works in practice. We carry out extensive on-going engagement with key sector stakeholders. The experience of the Regulation Committee has been that its independence is respected within the HCA and by the sector.

Are the standards set by the Regulation Committee relating to consumer regulation adequate and are the monitoring arrangements sufficient?

18. The Localism Act set out a new approach to dealing with consumer issues in social housing. Under this new approach the expectation is that issues are resolved at a local level wherever possible, with the housing ombudsman dealing with complaints that cannot be resolved. The role of the regulator in relation to consumer regulation is limited to: (i) setting standards which to a large part are policed by others; (ii) reaching a judgment and then dealing with the most serious breaches of the standards that have or are likely to lead to serious detriment to tenants on the basis of information received from third parties. We do not proactively monitor compliance with the standards.

19. The vast majority of the content of consumer standards is set out by formal directions from the Secretary of State. Our arrangements for dealing with potential breaches of the consumer standards as notified to us by third parties are as set out in the Regulatory Framework and elaborated up in the Regulating the Standards document. Essentially we operate a triage system where enquiries in relation to consumer standards are assessed and filtered in three stages. In the first year of operation of the new consumer regulation regime we received 421 complaints relating to consumer standards (stage 1). Of these 111 were referred to our Consumer Regulation Panel (stage 2) and 20 investigated in further detail (stage 3). No cases of serious detriment were identified in 2012–13. We are satisfied that the approach to dealing with potential breaches of the consumer standards is consistent with our remit in this area.

June 2013