



Homes &
Communities
Agency

The Social Housing Regulator

HCA Regulatory Judgement on Housing 21 – L0055

August 2013

Archived

The provider

Housing 21 (H21) is the registered provider and parent of a group which manages just under 19,000 properties. It operates throughout England and includes three main unregistered subsidiaries. The Claimar group with its own subsidiaries offers specialist and high dependency homecare services. Oldham Retirement Housing Partnership (ORHP) and Kent Community Partnership are both special purpose vehicles established to build, refurbish and manage retirement and extra care housing for local authorities.

H21's unaudited group turnover for the year ending March 2013 is £222m, including £106m of non-social housing activities. During that financial year it employed about 6,650 staff.

H21's core business is the provision of housing and care and support services for older people in non-institutionalised settings. It is an investment partner with both the Homes and Communities Agency and the Greater London Authority (GLA) and expects to deliver 1,672 units, as part of the 2011-15 Affordable Homes Programme.

Regulatory Ratings*

- **Properly Governed: G2**

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.

- **Viable: V2**

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.

*The regulator's assessment on compliance with the Governance & Financial Viability Standard is expressed in gradings from G1 to G4 for governance and V1 to V4 for viability. For both viability and governance the first two grades indicate compliance with the standard. A G3 or V3 assessment indicates a level of concern with the organisation's performance that is likely to be reflected in intensive regulatory engagement. A G4 or V4 judgement indicates a failure of governance or viability to the extent that the regulator is using its statutory powers.

Regulatory Judgement

This assessment updates the previous published assessment of H21's governance.

Our assessment is based on evidence gained from contact with the board and executive, a review of board papers and an independent external review into a private finance initiative (PFI) project. From this, the regulator has concluded that whilst H21's governance arrangements are adequate, it needs to improve aspects of its approach to risk management and its internal control framework to support continued compliance with the regulatory requirements.

In 2006, H21 established a non-registered subsidiary, ORHP, to manage a PFI project for the refurbishment, new build and subsequent management of 19 sheltered schemes and 819 bungalows. The establishment of this subsidiary was intended to ensure that involvement in the project did not place H21's social housing assets at risk. However, it subsequently became apparent that the parent remained exposed as a consequence of defective works under a related but separate operating contract managed directly by H21. The need to rectify these defects under the contract has resulted in significant additional costs being incurred by the registered provider, with an additional net loss of income of £12.3m. The income loss will be reflected in the group's March 2013 audited accounts.

H21 commissioned an independent external review, the brief agreed with the regulator, to examine the governance of the contract and learn lessons from the experience. The review revealed that the terms of the contract were onerous for H21, arrangements put in place to protect social housing assets were not wholly effective and that there was insufficiently detailed survey information for the properties within the contract. Management of the project and its risks was fragmented and there was a lack of adequate executive leadership.

H21 has taken steps to improve leadership and management of the project and its associated risks. In August 2013, ORHP concluded negotiations with Oldham Council and signed a revised Deed of Variation (DoV) as a basis for completing the project. A fully costed survey of the necessary rectification works has been completed and mechanisms introduced to improve the monitoring of the quality of work and to control costs.

Following the DoV, improvements are now required in H21's risk management arrangements to reflect remaining inherent long term risks in the project and to ensure that H21's social housing assets are not put at risk by the Oldham PFI. OHRP has a 23 year operating contract and tolerances within the contract remain tight. Close monitoring will be vital to avoid further problems with the management of costs and cash flows.

To provide the regulator with additional assurance H21 has therefore agreed to produce a comprehensive plan setting out the key controls and mitigations to manage the on-going risks linked to the revised project.

The second contributory factor in our assessment is that throughout 2012/13, H21 lacked a sufficiently robust internal control framework during a period of significant change in the organisation. Eight internal audit reports provided only limited assurance and one, no assurance, resulting in a significant number of recommendations. A new Group Finance director was appointed in August 2012. More recently, H21 has taken a number of steps to improve the internal control framework. It has implemented the majority of the recommendations, strengthened its governance and assurance arrangements through creating and recruiting to new

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posts and is taking a number of further steps to provide the board with assurance that an effective internal control framework is in place. Despite these improvements, in light of the recent events, H21 recognises that it needs to do further work to strengthen its internal controls and governance arrangements at executive, main board and risk and audit committee level.

Identified weaknesses in risk management, evident in the Oldham PFI and in internal controls were material factors in the regulator's governance assessment.

The regulator's assessment of H21's compliance with the financial viability element of the governance and financial viability standard is unchanged.

Based on evidence gained from contact with the executive and a review of the latest financial forecasts, annual accounts and the quarterly survey, the regulator has assurance that the financial plans are consistent with, and support, the financial strategy of the provider. The provider is forecast to continue to meet its financial covenants under a range of scenarios but needs to manage a number of exposures.

The business plan is funded to 2016 and includes a sizeable development programme (nearly 1,700 units to 2015).

Delivery of the development programme in the current housing market presents a risk to H21. The programme includes a number of mixed tenure schemes comprising units for rent, shared ownership and outright sale. Whilst sales values and programmes remain in line with budget, external pressures in the housing market and certainty of cash flow in a difficult market place remain a significant risk.

A significant proportion of H21's turnover is generated from non-social housing activities. H21 needs to manage exposures relating to risks posed by the changing operating environment to its care and health service business. A number of contracts are currently loss making, reducing the profitability of H21 as a whole. We are assured that management is addressing these through reprofiling contracts and exiting where appropriate.

There remains capacity across H21's business to manage these exposures, with sufficient headroom on funders' covenants throughout remainder of the plan. However, H21 will need to ensure sufficient on-going capacity to manage the exposures whilst ensuring social housing assets are not put at risk. The comprehensive plan that H21 has agreed to provide to manage the on-going risks of the ORHP project and revised DoV are key in providing this additional assurance.