THE SCOTTISH HOUSING REGULATOR

Scottish Housing Quality Standard
Progress update 2008/09

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Introduction

1. This report provides an overview of progress towards the Scottish Housing Quality Standard (SHQS) by social landlords. It covers:

- the rate at which social landlords are bringing their houses[1] up to the Standard;
- the costs associated with this improvement; and
- the challenges and risks for the delivery of the 2015 target.

Background

2. The Scottish Government's Purpose and Strategic Objectives, and the 15 National Outcomes it aims to achieve, are set out in Scotland Performs. Social landlords' delivery of the SHQS is a significant contribution to the achievement of a number of these National Outcomes[2]. To meet the Standard, a property must pass all five of the SHQS criteria:

- compliant with the Tolerable Standard;
- free from serious disrepair;
- energy efficient;
- provided with modern facilities and services; and
- healthy, safe and secure.

   Each criterion consists of a number of elements which number approximately 50 in total. These elements range from, for example, having a minimum of six electrical sockets in a kitchen to having at least 100mm of loft insulation. More detailed information about the Standard is available on our website: http://www.scottishhousingregulator.gov.uk .

3. The Scottish Government expects all homes rented from social landlords to meet the Standard by 2015, and it asked each landlord to submit a Standard Delivery Plan (SDP) in 2005. The Scottish Housing Regulator has responsibility for monitoring landlords' progress towards this target. The information in this report is based on these SDPs and other information collected from landlords by SHR, Scottish Government and Audit Scotland.

4. The measures that we have collected annually have been different for registered social landlords (RSLs) and local authorities. Five local authorities had not yet finalised their SDPs as at 31 March 2009 (mostly those that had been participants in the Community Ownership Programme), so they have not been asked for the information reported here and are excluded from this analysis. From 2010 onwards, we will collect the same monitoring information from all social landlords, so that we can analyse the whole sector's progress towards SHQS on a consistent basis.

5. To date, our monitoring of the SHQS has focused solely on whole house compliance. This does limit our capacity to report fully on progress towards the SHQS, as we cannot include improvements to elements within those houses that still do not comply with all of

[1] For simplicity the word 'house' is used here to describe any type of dwelling
[2] Directly: "We live in well-designed and sustainable places …." and indirectly the Outcomes on health, children, inequalities, communities and the environment.

the 50 specific elements of the SHQS. From next year we will start to measure compliance rates with the five different criteria that comprise the SHQS. This should allow us to assess more precisely the level of progress.

6. This report complements our analysis of the broader performance of RSLs. You can see this at http://www.scottishhousingregulator.gov.uk/stellent/groups/public/documents/webpages/shr_statistics.hcsp#TopOfPage .

Progress to date

a. Compliance

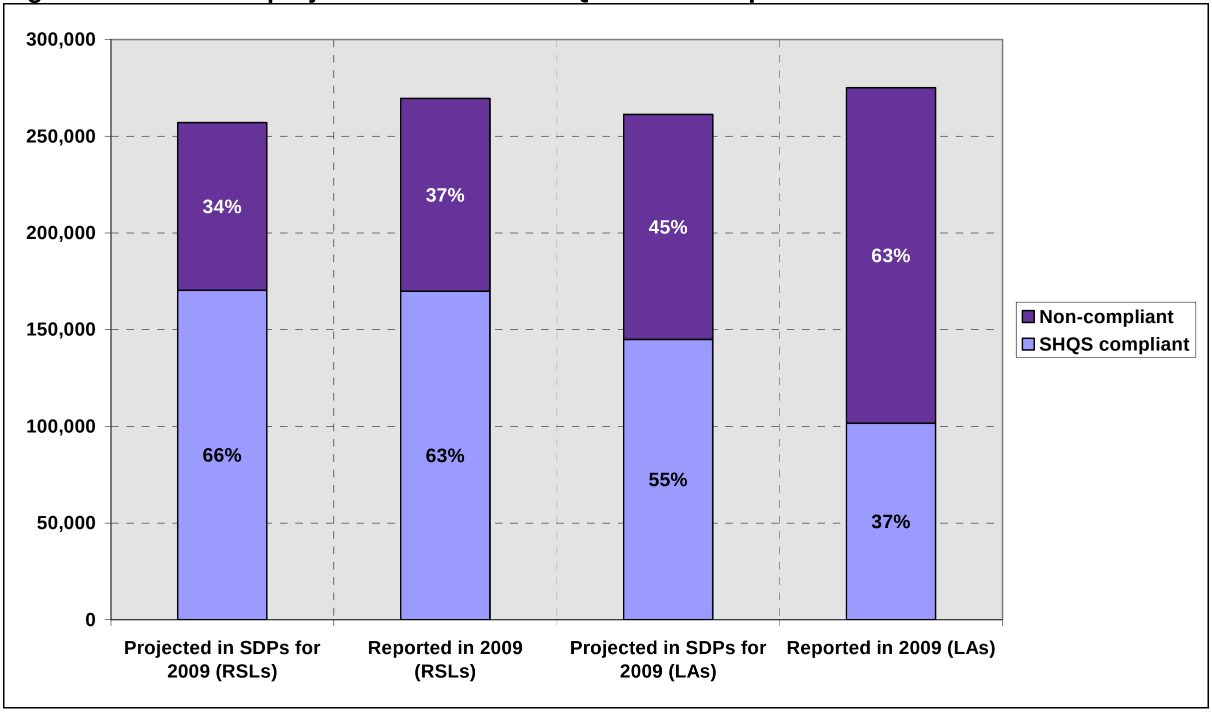
7. In 2008/09:

- RSLs reported that they brought 21,135 houses (8% of their stock) up to the Standard;
- this is almost exactly the number they had planned (in the previous year) to improve (21,263); and
- local authorities reported that they brought 26,595 houses (10% of their stock) up to the Standard.

8. Taken together, this means that by the end of 2008/09 50% of social landlords' houses complied with the SHQS[3]. In 2005, according to their Standard Delivery Plans, social landlords' aggregated projections forecast that 61% of all houses in the sector would comply with the SHQS by 2009. Figure 1 shows that RSLs fell just short of their 2005 projections by 3 percentage points, but local authorities fell short by a more substantial 18 percentage points. In terms of individual landlords' figures, 87 RSLs and 4 local authorities met or exceeded their forecast pass rate for 2009. This represents 51% of all social landlords but only 35% of all houses in the sector.

[3] The Scottish House Condition Survey (SHCS) also measures SHQS compliance, although the figures cannot be analysed by individual landlord. For 2008 the SHCS reports 39% compliance; over half of the difference to the figures reported here can be accounted for by progress between 2008 and 2009.

Figure 1: Landlords' projected and actual SHQS stock compliance rates in 2009

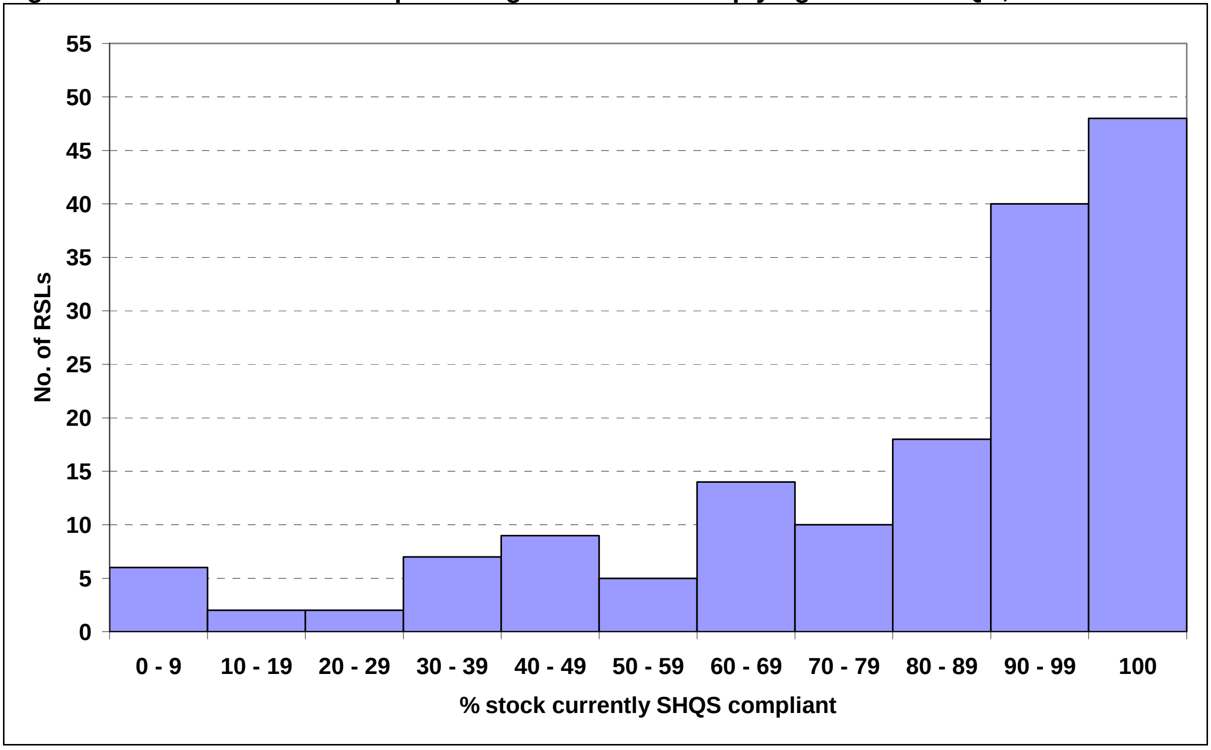


Source: SDPs, APSR 2008/09 and Audit Scotland performance information 2008/09, excluding local authorities that did not submit SDPs in 2005

9. The compliance levels vary greatly between individual landlords and different types of landlords. Not surprisingly, these variations largely reflect the differences in types and ages of houses owned by the different landlords, geography, limited availability and fuel types in certain remote areas, but also the previous investment strategies and decisions made on procurement and interpretation of SHQS.

10. In 2008/09, 48 social landlords reported that all of their houses met the SHQS; this equates to 25% of all social landlords, and is a similar figure to the previous year's analysis. Figure 2 shows the distribution of landlords' compliance rates. Of the 19 local authorities who provided comparable information, 10 showed compliance levels of under 30%, 5 between 30% and 70% and, in 4 local authorities, more than 70% of houses complied with the SHQS.

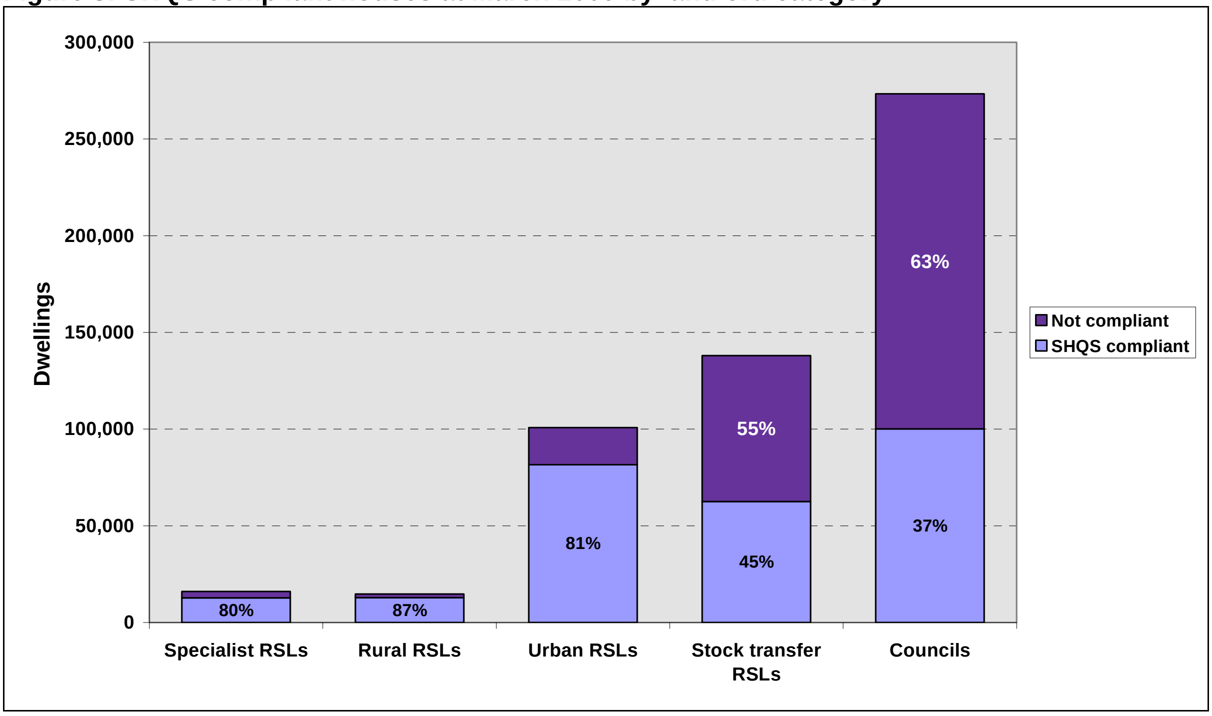
Figure 2: Number of RSLs and percentage of houses complying with the SHQS, 2009



Source: APSR 2008/09

Figure 3 shows the SHQS compliance rates grouped by category of landlord. It shows that most of the houses that do not comply with the SHQS are owned by local authorities and RSL stock transfer organisations.

Figure 3: SHQS compliant houses at March 2009 by landlord category



Source: APSRs 2008/09 and Audit Scotland performance information, excluding local authorities that did not submit SDPs in 2005

11. Local authorities' returns to Audit Scotland for 2008/09 show that the highest level of non-compliance by criterion of the SHQS are in the Energy Efficient and the Healthy, Safe & Secure categories. To date, we have not collected annual updates from RSLs about SHQS compliance by criterion. The most recent data from the Scottish House Condition Survey (SHCS)[4], which relates to houses surveyed in 2008, shows that RSL houses generally appear to be more energy efficient and in a better state of repair than local authority houses, as summarised in Table 1.

Table 1: Comparison of local authority and RSL stock quality

	Local authorities	RSLs
Median NHER[5] score – energy efficiency	7.1	7.6
Median SAP[6] score – energy efficiency	70.0	74.0
Properties with any disrepair	88%	77%
Properties with disrepair to critical elements	68%	53%
Properties with extensive disrepair	36%	23%

Source: Scottish House Condition Survey 2008

12. These differences can be at least partly explained by the fact that RSL houses are generally newer than local authority houses; not surprisingly, the SHCS also shows that energy efficiency is higher and rates of disrepair are lower in newer properties (for all properties in Scotland, regardless of tenure). So Table 1 and Figure 3 reflect the fact hat local authority and stock transfer RSL properties were built mainly between 1919 and 1982, whilst three fifths of other RSLs' houses are modern. Importantly, measuring disrepair in the stock is only one of five broad criteria of SHQS and it does not necessarily equate to SHQS compliance.

b. Investment made

13. Figure 4 shows the level of local authorities' total investment in their houses (adjusted for inflation to 2009 prices) since 1997. It shows consistently higher expenditure since the SHQS was announced in 2004. Aggregate expenditure was 55% higher in 2008/09 than it was in 2002/03.

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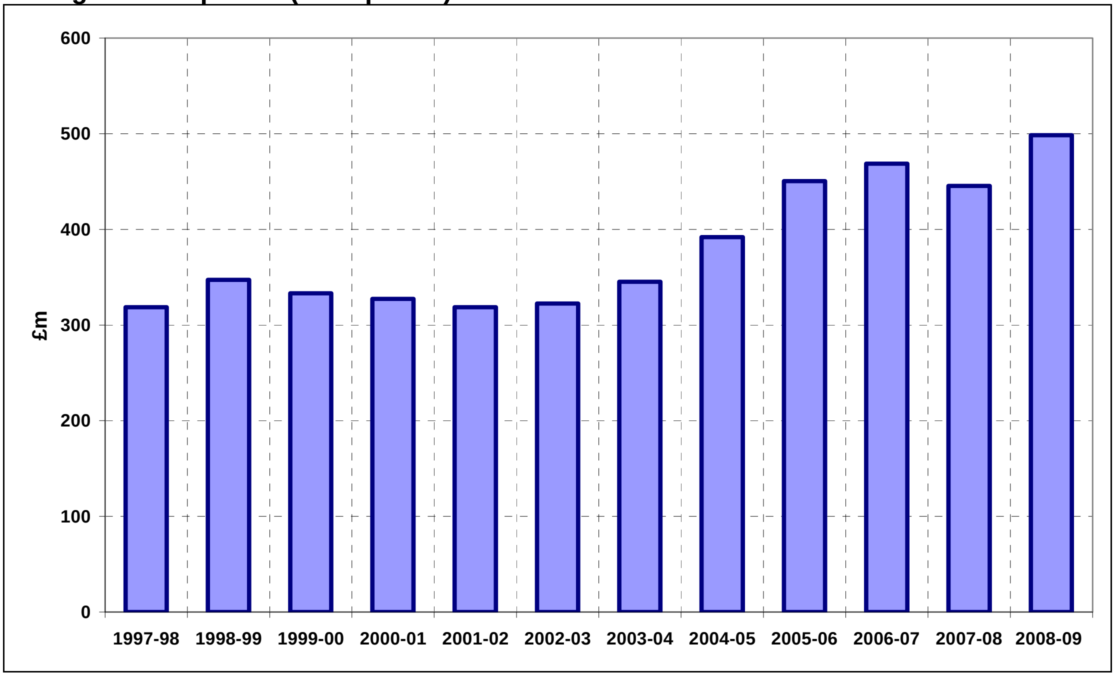
[4] http://www.scotland.gov.uk/Topics/Statistics/SHCS

[5] The National Home Energy Rating (NHER) measures energy efficiency on a scale of 0 (poor) to 10 (excellent)

[6] The Standard Assessment Procedure (SAP) for the Energy Rating of Dwellings takes into account different factors and is measured on a scale of 0 (poor) to 100 (excellent). The scores are on the SAP 2001 scale though other scales exist (2005 and 2009).

Figure 4: Housing Revenue Account gross capital expenditure by local authorities with stock throughout the period (2009 prices)

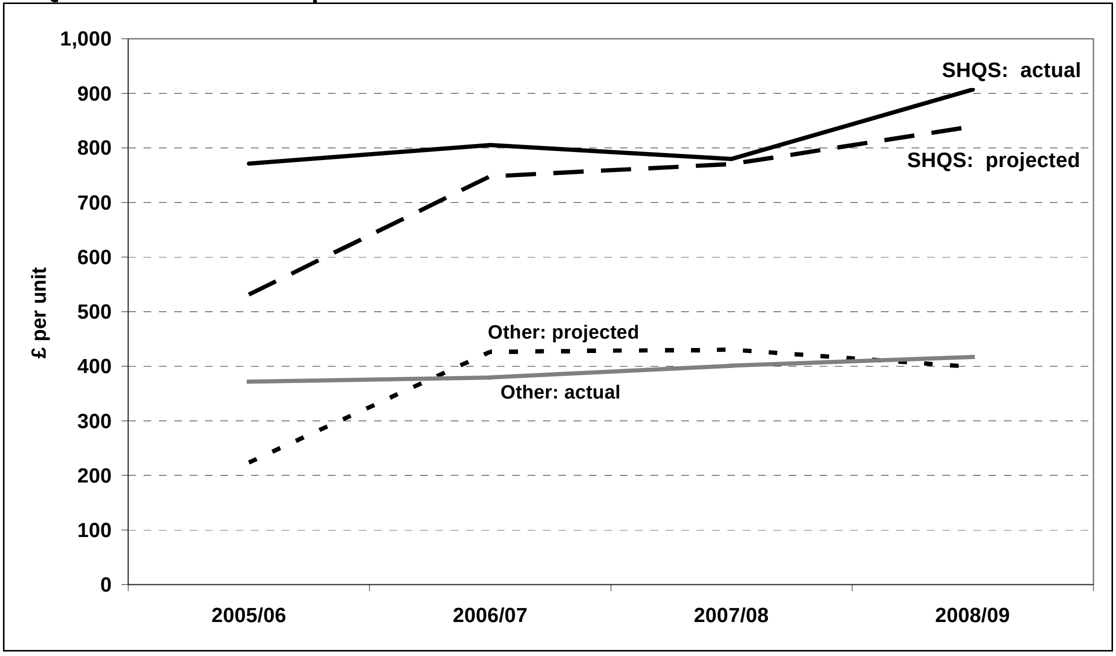


Source: Scottish Government local authority housing income & expenditure

14. Local authorities' average annual investment has increased by around a third since SHQS was launched, and their annual returns since 2005 show that 62% of their total annual investment is now related to SHQS. So, local authorities are spending more on the SHQS in both absolute and relative terms. This is a clear indication that local authorities are prioritising investment to achieve the SHQS though it is important to recognise that expenditure in 2008-9 in particular contains new build expenditure as well as investment in existing stock

15. The amounts that local authorities have spent on SHQS compliance and other housing investments are largely in line with their 2005 projections, as shown in figure 5. We report above that local authorities did not achieve their projected level of houses to be fully compliant with the SHQS. Taken together, this suggests the original SDPs may have underestimated the scale of the task and/or overestimated the quality of the houses. It may also reflect changes away from whole house programmes of work to programmes focussed on specific elements of the SHQS, reviewed phasing for investment or difficulties in controlling capital costs.

Figure 5: Local authorities' actual vs. projected investment per unit (in real terms) 2005 – 09 for SHQS-related and other planned investment

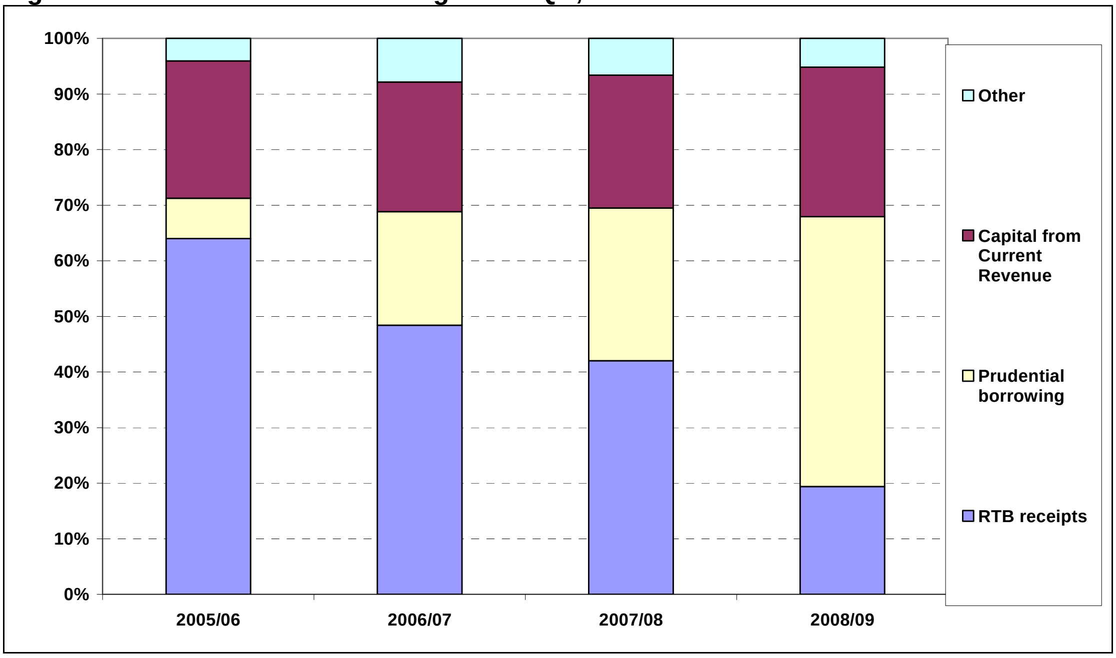


Source: Local authorities' Standard Delivery Plans and annual returns to SHR

c. Funding

16. Landlords' main sources of funding for SHQS work are retained rental income, income from Right-to-Buy (RTB) sales, and borrowing. Figure 6 shows the breakdown of funding sources for capital investment for local authorities since 2005. We can see from this that income from RTB sales has contributed a decreasing proportion and borrowing has increased in its place.

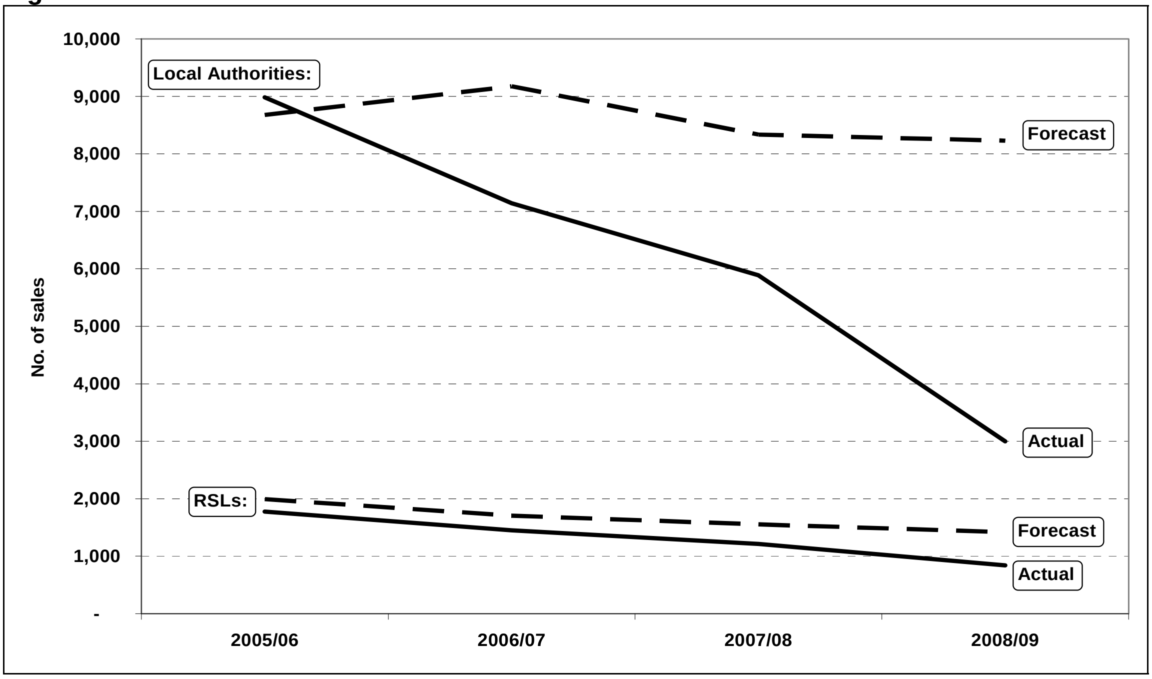
Figure 6: Local authorities' funding for SHQS, 2005 - 2009



Source: annual SHQS returns from local authorities

17. Landlords were already anticipating a decreasing number of RTB sales in their SDPs. But, as figure 7 shows, the scale of the downturn was greater than they forecast. Sales prices were initially higher than projected, with the effect that income from RTB sales was actually higher than projected for 2005/06, but fell to 52% of the forecast RTB income for 2008/09. This trend has been compounded by reductions in the prices (and therefore capital receipts) that local authorities have obtained for housing land, given the weakness of this market in 2008/09

Figure 7: Forecast and actual RTB sales from 2005 to 2009



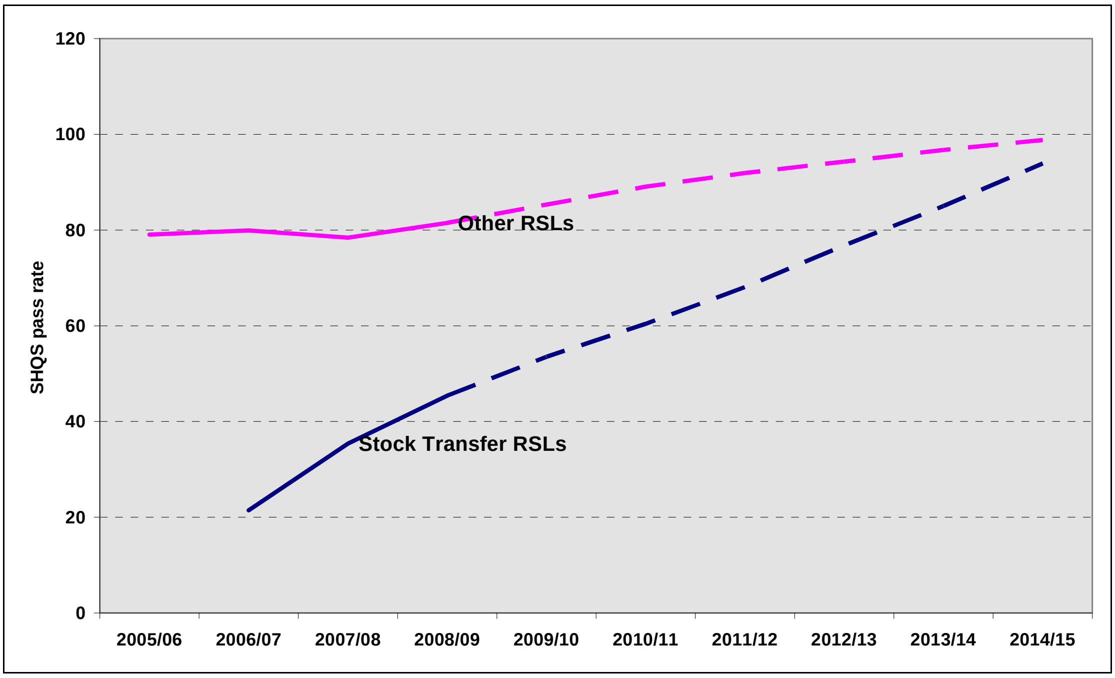
Source: SDPs, returns to Scottish Government and APSRs

Prospects to 2015

a. Compliance

18. We ask RSLs each year to report the number and proportion of houses currently complying with SHQS and their projections for these figures for each year until 2015. Figure 8 shows their reported actual compliance rates to 2009 and their most recent projections for stock transfer and other types of RSLs. We reported above that, apart from local authority landlords, stock transfer RSLs face the biggest challenge in achieving the SHQS, but figure 9 suggests that they are on course to meet the Standard at their current rate of delivering improvements. However, much depends on the underlying financial conditions facing the RSLs in the period up to 2015.

Figure 8: Stock transfer and other RSLs' reported and projected SHQS compliance rates to 2015



Source: SDPs and APSRs 2006/07, 2007/08 & 2008/09

19. As we report above, our monitoring of the SHQS has focused solely on whole house compliance, and does not reflect progress in elements of the SHQS. Landlords who have programmed investment work by element rather than through whole house programmes may see an acceleration of their reported compliance rate over the next five years. We will be in a better position to assess this when we start to collect information from landlords on their investment by element later this year.

b. Investment required

20. In early 2009, we surveyed RSLs to assess how the credit crunch was affecting their financial position[7]. As part of that exercise, we asked about funding to meet the SHQS. From this, we established that RSLs expect to invest around £500 per house[8] per year between 2009 and 2015.

21. From 2009/10 to 2013/14 local authorities project that their annual aggregate investment in houses will gradually decrease from £507m to £394m. This represents a decreasing level of investment per unit even taking in to account their forecast decreases in houses. Investment in SHQS-related work is also expected to decrease but less sharply, with the effect that its share of total investment will increase from two-thirds to three-quarters over the next five years. This equates to an average of just over £1,000 per house per year. This suggests that local authorities will have to invest twice as much into SHQS on a per unit basis between now and 2015 than RSLs.

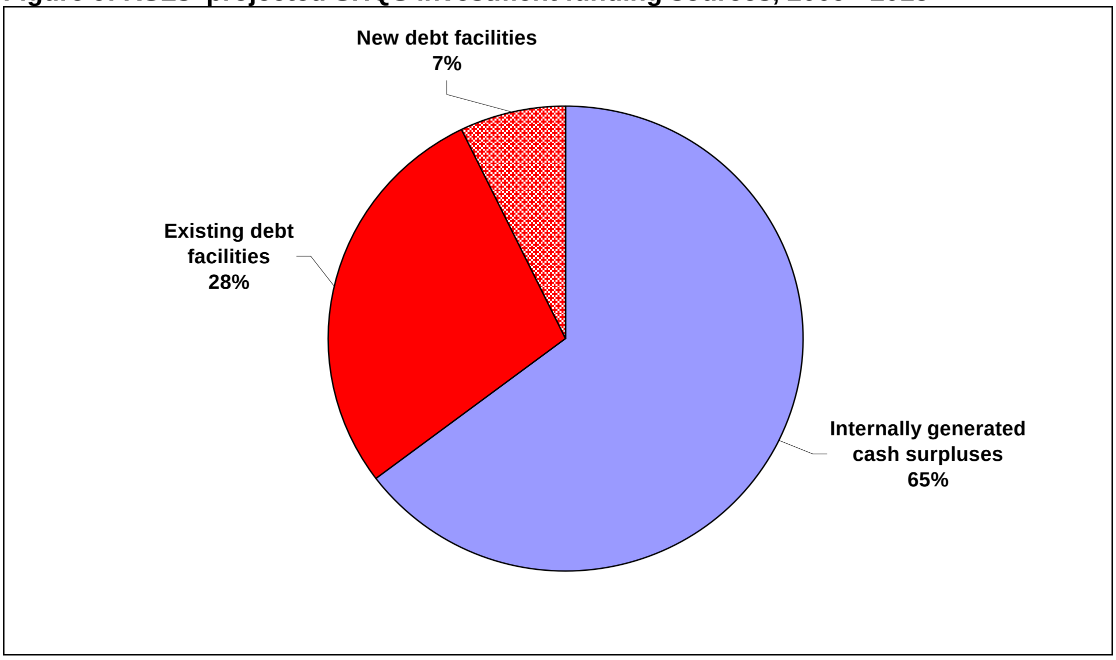
22. The above figures are sector totals and conceal wide variations between individual landlords. As might be expected, for example, stock transfer RSLs anticipate proportionately much higher investment in their stock than most other RSLs. And the overall higher figure for local authorities reflects their currently lower level of compliance.

[7] Survey on Private Lending and the impact of the credit crunch, SHR 2009. The figures exclude GHA and River Clyde Homes.
[8] 'per house' means divided by total stock, whether failing SHQS or not.

c. How do landlords plan to fund this?

23. According to our credit crunch survey returns, RSLs plan to fund two thirds of their SHQS investment through internally generated cash: mainly retained rental income and income from Right to Buy sales. When compared to their reported annual surpluses in their accounts over recent years, this might prove challenging for some RSLs. They plan to fund the remaining investment requirements from private borrowing, and as figure 9 shows a fifth of these loans have yet to be arranged.

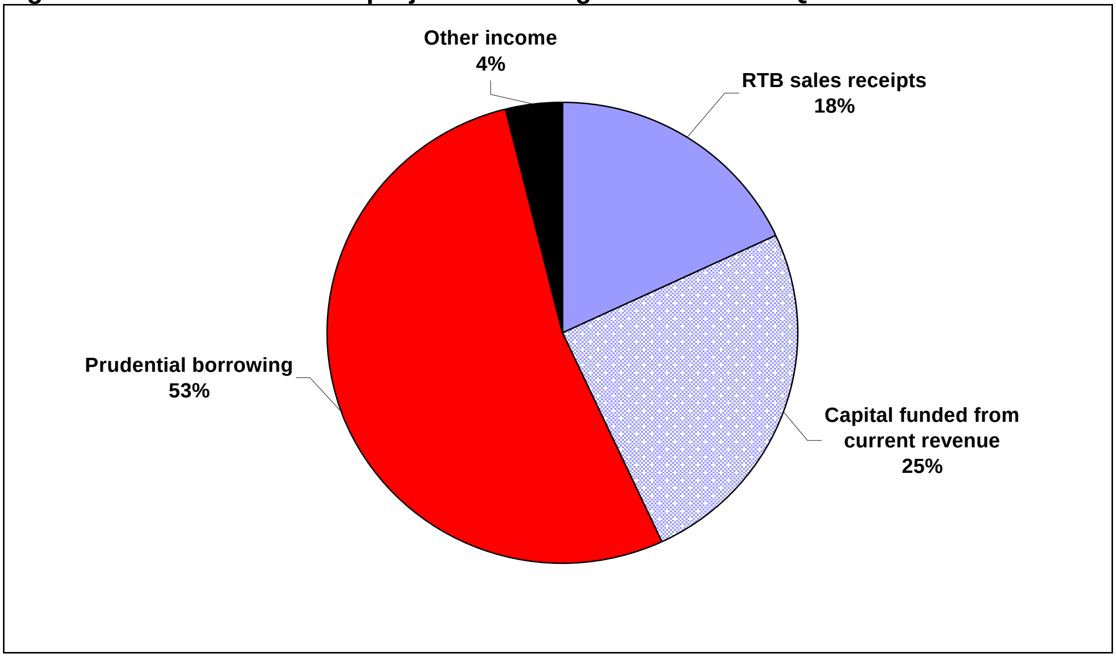
Figure 9: RSLs' projected SHQS investment funding sources, 2009 - 2015



Source: RSL Survey, 2009

24. As figure 10 shows, local authorities anticipate 43% of SHQS investment to be funded by internally generated surpluses (sales income plus capital from revenue, which is mostly from rental income), so they need to borrow more than half of the required funds to fully meet the SHQS investment requirements.

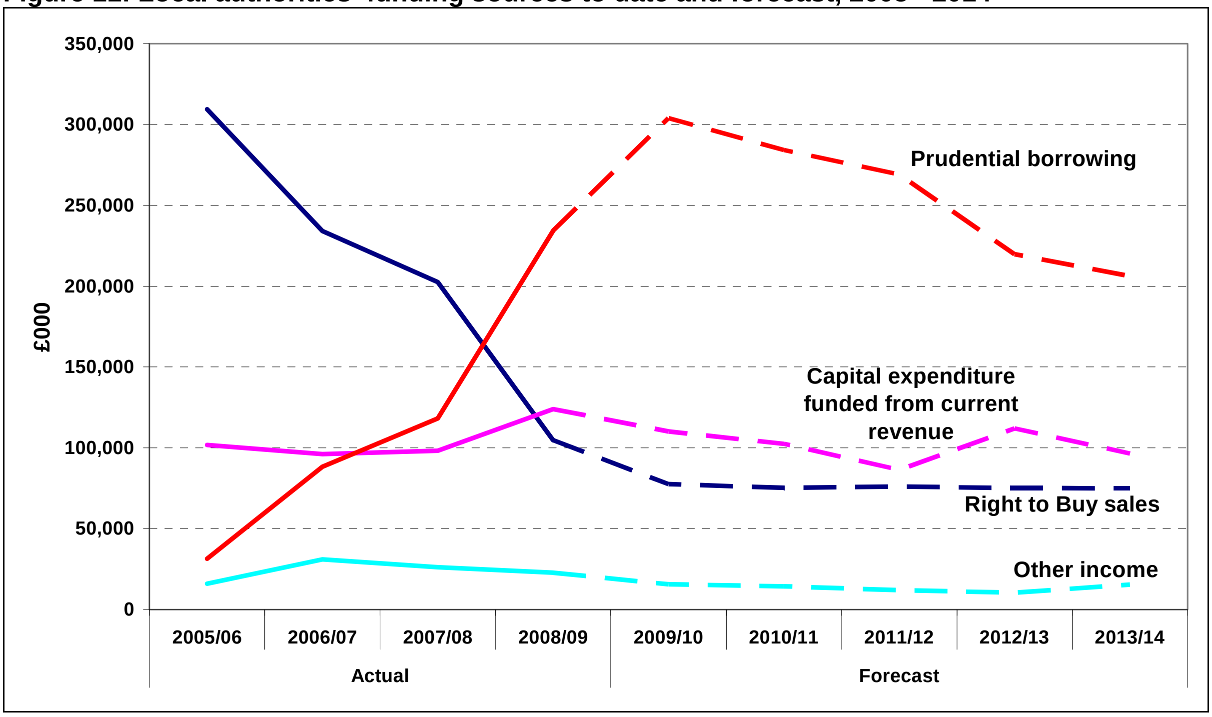
Figure 10: Local authorities' projected funding sources for SHQS to 2013/14



Source: COSLA/SG survey

25. These forecast funding streams are based on assumptions about income and expenditure, such as Right to Buy sales, future rent levels and cost increases. Figure 11 shows local authorities' reported funding for SHQS and other stock investment to date and their projections to 2014. It shows that the forecast decrease in investment levels described earlier is reflected mostly in decreasing borrowing requirements, whilst income from RTB sales is expected to level out.

Figure 11: Local authorities' funding sources to date and forecast, 2005 - 2014



Source: Annual Returns to SHR and COSLA/SG survey 2009

d. Challenges and risks

26. The scale and nature of the challenge that landlords face varies greatly. For some, meeting SHQS involves mostly maintaining their houses in their current state whilst others must make considerable investments over the coming years. From this, we see the key risks to the achievement of the SHQS by 2015 as:

    a) **The rate of improvement**. As many landlords are upgrading and replacing specific elements of the SHQS rather than doing whole house improvements, it is possible that there will be an acceleration in the number of reported whole house compliance in coming years. But, the sector's failure to deliver on its 2005 projections does present a risk to full delivery of the SHQS by 2015.

    b) **Constraints on the availability of funds, including:**
       i) reduced income from Right to Buy sales, which has decreased faster than most landlords anticipated;
       ii) a more uncertain private lending market in which the availability of funds and the terms and costs of borrowing are likely to become more challenging;
       iii) a more uncertain borrowing outlook for public bodies, including local authorities;
       iv) constraints on rent rises, including low inflation and affordability for tenants;
       v) potential increases in bad debts as a result of difficult economic conditions;
       vi) continued costs growth, both in the delivery of work to achieve the SHQS, but also more generally in social landlords operating costs; and
       vii) increased competition for scarce resources, including public funding.

    c) **Stock condition information.** If landlords get better and more comprehensive stock information, they may discover additional work that is required to achieve the SHQS. Of course, it is also possible that this could identify that landlords had initially overestimated the level of work required.

27. This means that landlords may need to make hard choices about the timing and type of investment they make in their houses, and to maximise available resources through the effective management of their costs. In Shaping Up for Improvement we commented that the ability of a social landlord to maintain a sustainable ratio between cost and turnover will be an important factor in determining how we engage with them in future.

The Scottish Housing Regulator
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The Scottish Housing Regulator, Highlander House, 58 Waterloo Street, Glasgow G2 7DA
Telephone: 0141 271 3810
Fax: 0141 221 5030
Email: shr@scottishhousingregulator.gsi.gov.uk
Website: www.scottishhousingregulator.gov.uk

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