



THE SCOTTISH
HOUSING
REGULATOR

GUIDANCE NOTE

To: All Registered Social Landlords (RSLs)

Subject: Contract Compliance Following Transfer of Homes to Community Ownership

Issued by: The Scottish Housing Regulator

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Summary

This guidance note details the Scottish Housing Regulator's approach to monitoring contracts entered into as a result of homes moving to community ownership (formerly "*large scale voluntary transfer*") where there is a contractual Minute of Agreement. It supersedes **SHGN 97/28 "Post Stock Transfer Monitoring"**. This guidance will be of relevance to registered social landlords (RSLs) which have received stock transferred either from Scottish Homes or from a Development Corporation. Except for performance audits, the arrangement within this guidance will also apply to the two unregistered housing organisations that bought houses from Scottish Homes.

The guidance note sets out:

- The principles which underpin the Scottish Housing Regulator's approach to contract compliance;
- The role of the Scottish Housing Regulator in checking compliance by a registered social landlord with their contracted Minute of Agreement;
- The process which will be taken should non-compliance be identified;

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- The steps available to registered social landlords, should they identify that compliance will not be achievable or they wish to seek a variation in contract terms; and
- What happens to a contract when one registered social landlord is involved in a transfer of engagements to another registered social landlord.

Each transfer is individual and unique, and each contract is therefore different. It is not possible to cover every eventuality within this guidance note, and terms referred to such as “major repairs” may not be used in every contract. Each landlord should read this guidance in conjunction with their own Minute of Agreement and keep in mind the fact that their contract terms may differ from those used here. It remains the responsibility of each registered social landlord to ensure they understand their contract terms, have appropriate systems in place and are complying with their contract.

For any references to Communities Scotland (or Scottish Homes) please read the Scottish Housing Regulator.

If you have any questions about this guidance, you should direct them to:

The Scottish Housing Regulator
Highlander House
58 Waterloo Street
GLASGOW
G2 7DA
Tel: 0141 271 3810
Email: shr@scottishhousingregulator.gsi.gov.uk

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1 INTRODUCTION

- 1.1 Each sale of Scottish Homes' and Development Corporation stock and transfer to community ownership is governed by a legally binding contractual Minute of Agreement, which details the conditions to be met. The Agreement will usually include specific conditions which require monitoring at fixed intervals, or "*review periods*" (eg every 5 years). These conditions include:
- Expenditure on planned and reactive maintenance;
 - Expenditure on improvements;
 - The number and value of projected Right to Buy sales, and provision for clawback of excess receipts for Right to Buy sales;
 - The level of annual rent increases.
- 1.2 Each transfer of housing stock to community ownership has unique features and the contracted Minute of Agreement reflects individual aspects of a particular transfer. The precise conditions to be monitored and the review periods are likely, therefore, to vary from contract to contract.
- 1.3 Contracts governing the sale of homes from Livingston and Irvine Development Corporations have been assigned to Scottish Homes, and the agency has assumed the rights and obligations contained in the contracts.
- 1.4 The monitoring of contracts dealing with the transfer of local authority and health board housing properties to community ownership is not included in this Guidance.

2 PRINCIPLES WHICH UNDERPIN CONTRACT COMPLIANCE

- 2.1 The Minute of Agreement between Scottish Homes and a purchasing RSL is intended to reflect and articulate the commitments made to tenants and ensure public funds are protected. The aim of contract monitoring is to ensure that the contractual terms are being met. Where there is identified failure on the part of an RSL to comply with the contract, or an RSL seeks a variation in the terms of their contract, Scottish Homes will endeavour to ensure that:
- (a) the intended benefits of stock transfer for tenants continue to be met, such as:
- Increased tenant involvement;
 - Increased investment;
 - Enhanced local services and control;
 - Greater certainty about the future

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- (b) the RSL's financial security is protected;
 - (c) public funds are protected.
- 2.2 Scottish Homes' approach is to work supportively in partnership with RSLs and other stakeholders, and this extends to contract compliance. Where actual performance is materially different to contracted performance this will be discussed constructively with the RSL. The interests of tenants will be kept in mind when reviewing contract compliance and when agreeing to a variation in contract terms.

3 ROLES AND RESPONSIBILITIES

Registered Social Landlords

- 3.1 RSLs who become owners of transferred stock, either from Scottish Homes or a Development Corporation, do so voluntarily and take on the risks and rewards of ownership. As independent organisations the governing bodies are expected to take appropriate steps to ensure they are informed about contract requirements and that adequate and appropriate controls are in place to ensure compliance. In some instances this may entail seeking clarification from their legal advisers or other consultants.
- 3.2 RSLs should not rely on either a performance audit or a verification visit at the end of a review period to inform them about their compliance with contracts. RSLs should monitor their own contract compliance.
- 3.3 If an RSL requires further information about any aspect of its contract, or believes it requires a variation in contract terms, it should contact the Financial Performance Team in R&S as the first point of contact with Scottish Homes, but may want to take legal advice first.

Registration & Supervision

- 3.4 As part of its supervisory role, R&S has overall responsibility for monitoring contract compliance which is carried out by the Financial Performance Team. This section works alongside the Performance Audit Team and complements the performance audit process.

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- 3.5 Any queries about contracts, arrangements for seeking a variation in contract terms or R&S's approach to monitoring should be directed to the Financial Performance Team in R&S in the first instance. In the event that a variation is sought (see Section 5) or there is a dispute about a particular contract clause, R&S will act in a co-ordinating role involving other Scottish Homes departments as appropriate. R&S will not be involved in direct negotiations with the landlord in order to avoid any conflict of interest.
- 3.6 The various stages of contract monitoring by R&S will be conducted as follows:
- (a) An Annual Contract Compliance Return ("ACCR") is issued for each contract on the anniversary of the stock transfer (or other mutually agreed date). **The purpose of the ACCR is to allow both the RSL and Scottish Homes to track compliance against the specific contractual conditions.**
 - (b) An RSLs' management of contract compliance will be assessed during the course of the performance audit. **This will involve assessment of the quality of internal controls and reporting arrangements to ensure they are appropriate for the RSL and the contract, and may include checking information provided in the ACCR, proportionate to the scale of contract involved.**
 - (c) At the end of each review period the RSL's actual performance against contract terms will be assessed. **This will use information provided by an RSL in its ACCRs and findings during the performance audit. It may involve a verification visit by R&S to confirm overall contract compliance.**
- 3.7 In the event that an RSL fails to return their ACCR on time, or it is not adequately completed, or the verification visit at the end of the review period is unacceptably delayed or unsatisfactory, R&S may choose to conduct a verification visit, an investigation, or may review an RSL's grading.
- 3.8 Very occasionally, specific contract terms may differ from an RSL's policies for other stock (eg rents for transferred stock may be higher than rents for an RSL's other houses). This will be recognised by R&S when carrying out the performance audit.

Other Scottish Homes; departments and divisions

- 3.9 Other departments and divisions within Scottish Homes have an interest in contract compliance and a role to play in the compliance process. Where enforcement of a contract is sought or an RSL requests a variation to the contract terms, the involvement of any of these departments or divisions may be asked for. Activity will be co-ordinated by R&S. The departments concerned, and their interest in contract compliance, is as

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follows:

- (a) Community Ownership Initiatives manage the original stock transfer process and have detailed knowledge of the individual transfers.
- (b) Central Finance will invoice RSLs for any sums owing at the end of a review period as a result of excess Right to Buy sales or underspend on maintenance and major repairs.
- (c) Legal Services provide advice within Scottish Homes on individual contract terms.
- (d) Regions have a strategic overview role and are well placed to identify changing housing need and demand in an area through their knowledge of local housing providers.

4 PROCESS IN THE EVENT OF NON-COMPLIANCE

- 4.1 In the event of an RSL failing to comply with its contract terms, there are legal remedies available to Scottish Homes. However, Scottish Homes' preferred approach is to work constructively with an RSL through dialogue and negotiation. The aim is to ensure that tenants' expectations of the stock transfer are realised within the limits of an RSL's continued financial stability, whilst also protecting public funds.
- 4.2 RSLs should be aware that, should dialogue and negotiation not resolve matters, Scottish Homes will be prepared to pursue legal enforcement of contract terms.
- 4.3 The majority of non-compliance instances are expected to be identified through the monitoring process (the ACCR, performance audits and verification visits). Non compliance against contract terms may be due to a simple mistake or misunderstanding. Alternatively non-compliance could be more serious. The approach taken in an individual case will vary according to the degree of non-compliance.
- 4.4 Interpretation of contract terms is the most common reason for non-compliance and this can generally be viewed as relatively minor since the impact on the contract is minor. Examples of this are misinterpretation of the rate of RPI to be used, or the point in the year when RPI should be applied. In such an instance R&S will quickly agree actions with the RSL to return the position of tenants to what it would have been had the mistake not taken place.
- 4.5 Where necessary an RSL will be allowed a reasonable time period (eg 3 years or to the end of the next Review Period) over which to spread any adjustments required so the impact is minimised. No variation in contract terms will be necessary and, provided the RSL agrees, the matter can be resolved by letter with no further action required.

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- 4.6 However, major failures in complying with contract terms may occur. These are not expected to be common but may materially effect the expectations of tenants. They may be symptomatic of more serious difficulties facing an RSL (for example: financial instability; governance issues; poor internal controls).
- 4.7 Examples of non-compliance on a major scale may include:
- Consistent failure to spend sufficiently on maintenance and major repairs;
 - Ignoring contract terms and deliberate setting rent increases in excess of contracted limits;
 - Deliberately using incorrect data to complete the ACCR.
- 4.8 Scottish Homes views major non-compliance with contract terms very seriously. R&S will seek clarification of the situation with the RSL in the first instance before taking further action.
- 4.9 An RSL may itself identify that it is not going to be able to meet its contractual terms at the end of a formal review period (eg where there have been significant excess RTB sales and the RSL does not expect to be able to repay the clawback to Scottish Homes on the due date). In such an instance the RSL should contact the Financial Performance team in R&S at the earliest opportunity with full details and a proposal for remedying the situation.

5 SEEKING A VARIATION IN CONTRACT TERMS

- 5.1 A “variation” is where the terms of a contract are amended by mutual agreement between both parties.
- 5.2 Variations which are concerned with the efficiency and effectiveness of monitoring the contract, and which do not impact on the expectations of tenants will be considered minor variations. An example would be adjusting the date of the ACCR to match the RSL’s year end. It is expected that R&S and the RSL can agree such minor contract variations by letter without recourse to Legal Services or other solicitors.
- 5.3 Major contract variations arise when a need to change a key clause in a contract is identified, which could impact on the promises made to tenants at transfer and affect their expectations. These are changes which are so fundamental that a formal legal amendment is required to the contract.
- 5.4 A need for a major variation in a stock transfer contract can arise from a number of circumstances, examples of which might include:

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- changing tenant aspirations;
- changing housing need or obsolescence of the stock which results in falling demand;
- identification of repairs which are uneconomic;
- significant financial difficulties which mean that repayment of excess RTB sales, or the anticipated level of maintenance, may threaten the organisation's financial viability;
- a need to increase rents above the limits set out in the contract in order to guarantee continued financial stability; or
- a combination of the above.

5.5 Whether the RSL has identified a need for a major variation in contract terms themselves, or is already working with their Scottish Homes' regional office, the RSL must approach the Financial Performance Team in R&S with a business case for the variation which details the following:

- the consequences for the RSL of meeting the contract as it currently stands (the "do nothing" option);
- details of options considered and their consequences for the RSL;
- the preferred course of action and its impact on the contract terms; and
- views of tenants and consultation with other stakeholders.

R&S will co-ordinate the involvement of other departments and divisions within Scottish Homes in considering and assessing the business case.

6 TRANSFER OF ENGAGEMENTS

6.1 When an RSL transfers its business to another RSL, existing stock transfer contracts remain in force and will be assigned to the receiving RSL.

6.2 R&S expects every transferring RSL to make all contractual obligations known to the receiving RSL, and this includes stock transfer contracts. Similarly, receiving RSLs are expected to obtain full information about stock transfer contracts, and any existing or potential liabilities arising from the contract, as part of the due diligence process.