Governance
A discussion paper

July 2009

TSA

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Our discussion paper Building a New Regulatory Framework, published in June, sets out our initial thoughts on the TSA's regulatory framework and standards. This paper is a supplementary paper on the governance standard.

Good governance is fundamental to successful organisations. It enables them to deliver their aims and objectives and, in particular, to deliver excellent quality services to tenants, ensure the proper use of public funding and safeguard the reputation of the sector.

The purpose of this discussion paper is to seek views on the TSA's existing framework and on our initial thoughts on the options for the future framework.

Application of the standards across the domain

We do not expect our standard on governance to apply to local authority landlords because they are public sector organisations that have other rules on governance and financial matters. We do, however, believe that the principles of good governance apply universally and we will share with the Audit Commission concerns that arise in the course of

our work that relate to the governance of housing services within local authorities.

In respect of profit-making registered providers, standards may be set in relation to the management of their affairs only so far as they relate to the provision of social housing. Therefore, in formulating governance standards we need to ensure that the standards can be applied across whole entities for not-for-profit registered providers and across the housing activities of for-profit providers. The TSA needs to consider what requirements if any, it can place on for-profits' boards.

Existing approach

The TSA has inherited the Housing Corporation's approach to regulating governance. The Regulatory Code (the Code) sets out the fundamental objectives of housing associations in meeting the Housing Corporation's regulatory requirements on viability, governance and management. The governance section of the Code requires housing associations to:

- operate according to the law and their constitutions

- be headed by an effective board with a sufficient range of expertise – supported by appropriate governance and executive arrangements – that will give capable leadership and control

- maintain the highest standards of probity in all their dealings

- protect public investment seek and be responsive to residents' views and priorities

- deal with the Housing Corporation in an open and co-operative manner notifying any anticipated or actual breach of the Code or anything that might significantly affect its ability to fulfil its obligations under the Code

- demonstrate, when carrying out all their functions, their commitment to equal opportunity, working towards the elimination of discrimination and demonstrating an equitable approach to the rights and responsibilities of individuals promoting good relations between people of different racial groups

- operate a framework that effectively identifies and manages risks

Our publication How We Regulate Governance sets out our general approach to regulating governance. When regulating governance we aim to assess how a board:

- leads the association in establishing its mission, strategic direction, values and operational policies and standards as per publication. Significant issues that determine these objectives need to be properly and fully apprised and then translated into corporate and operational plans accompanied by appropriate structures for risk management and development. Clear management targets and executive responsibilities are essential. A board also needs to set and evaluate policies and standards for service delivery, communicate with stakeholders,

at the same time controlling behaviour in the organisation as a whole

- monitors performance against agreed targets and milestones, critically appraising financial, development and operational achievements

- complies with all statutory and regulatory requirements through effective and regular internal and external audit of all financial, control and assurance systems

- holds management to account by rigorously challenging assumptions and policy proposals. This will require scrutiny of plans for performance improvement and changes in activities or direction

- guarantees the probity of all aspects of the association's work

- fosters an appropriate governance style for the association in a deliberate and reflective way, at the same time appraising its own performance as the governing body

The Code is supplemented with a range of circulars, good practice notes and publications that promulgate best practice in governance.

Our view of housing associations' governance is informed by:

- the **self assessment compliance statement** (confirmation of compliance, identifies any areas of weakness or non-compliance and plans for addressing them) completed by all groups or individual associations is a key and significant part of our regulatory engagement. It demonstrates how a board is taking primary responsibility for its compliance with the Code. The statement informs our overall regulatory plan for future engagement with each association, and forms an important piece of evidence in our assessment of governance

- other **standard returns,** in particular the Regulatory and Statistical Return, which provides key data on performance indicators, governance and compliance

- **board meetings** and board papers

- we may from time to time, either as a result of our own concerns regarding governance or in reaction to events, need to undertake a more **detailed review** of an association's governance

We publish our overall assessment of housing associations' compliance with the regulatory framework as Regulatory Judgements. The TSA's judgement on governance is summarised under four straplines.

In response to events over the past year, we have modified our regulatory engagement and where housing associations' performance is cause for concern, we have intensified our regulatory engagement with boards, chairs and senior staff of housing associations. We have also requested additional information on performance where necessary.

Question 1
What elements of the existing approach to the regulation of governance should the TSA carry forward?

New legislative basis

The Housing and Regeneration Act 2008 (the 2008 Act) allows the TSA to set standards for registered providers in matters relating to the management of their financial and other affairs.

The TSA must have regard to its fundamental objectives and better regulation principles when formulating its governance framework and in particular the following:

- to ensure that registered providers of social housing are financially viable and properly managed
- to encourage investment in social housing to contribute to the environmental, social and economic well-being of the areas in which the housing is situated
- to avoid the imposition of an unreasonable burden on public funds

The 2008 Act allows for standards to be national or local and tailored to the specific circumstances of an area. The TSA believes that a national standard on governance is necessary in order to facilitate meeting its fundamental objective of ensuring registered providers of social housing are financially viable and properly managed. A national governance standard will ensure that there are clear requirements for registered providers.

The standards framework provides the criteria against which the TSA will assess registered providers. Failure to meet a standard will be grounds for the TSA to exercise its regulatory and enforcement powers. Therefore any governance standard must be enforceable. The full complement of the TSA's regulatory requirements must be set out within standards.

Question 2
Is a national standard rather than a local standard for governance the most appropriate approach?

The 2008 Act provides for the TSA to adopt or point to codes of practice to amplify standards. This provides a means of providing more detail on what is expected from registered providers in order for them to be compliant. For example, as the equivalent of paragraph 2 of Part I of Schedule 1 to the Housing Act 1996 relating to payments and benefits is not provided for in the Act, the TSA may wish to consider adopting a code on probity or remuneration. Another area that may lend itself to amplification through a code of practice is risk management and internal controls. Codes of practice must relate to one or more national standards.

Question 3
Are there particular areas within governance that lend themselves to further amplification by way of a code? If so what areas might such a code reflect?

In formulating a governance framework the TSA needs to consider what approach it wishes to adopt. There are a number of well established descriptions, standards and codes of practice that deal with governance in the for-profit sector, non-profit sector and the public sector. We would prefer to base our thinking on an existing recognised code of governance, albeit amended and tailored to suit the domain.

Options for governance standards

Option 1

This option builds on key principles from our existing Code and other widely recognised relevant codes of governance. Emphasis on the role of the board and the chair is drawn from the Combined Code. This approach prescribes some overarching principles that registered providers must work to, with sufficient flexibility to enable a range of diverse registered providers to operate to codes of governance that best suit their circumstances. For the sake of clarity, the codes being discussed here are general codes of practice, rather than statutory codes which are covered elsewhere in this paper.

This option is based on a broad requirement for registered providers to be well governed. Such a standard may be framed as:

Registered providers are properly governed.

A standard framed in this wide ranging manner requires some signposting. This may be done through guidance and interpretation:

Our interpretation is that for an organisation to be properly governed it needs to display the following attributes:

Board
Registered providers are headed by effective boards

- in control of the affairs of the organisation, demonstrate collective responsibility and accountability

- have a clear focus on the organisation's mission, purpose, values and set strategic direction

- of an appropriate size, balance of executives and non-executives (non-executives in the majority), diverse, and with relevant, current skills and expertise

- have mechanisms for recruitment, induction, training, continuous improvement

- conduct annual appraisals, refresh of board members as appropriate and have succession plans

- operate with appropriate levels of delegation with clarity around the role and scope of committees in particular audit and remuneration committees

- provide financial oversight to ensure ongoing financial viability

- monitor performance across all functions

Chair
Chairs of registered providers demonstrate leadership and are in control of their boards' affairs

- ensure that the appropriate frequency of board meetings and receipt of timely information

- clear division of responsibilities between the Chair and the Chief Executive

- facilitate clarity between board and management business

- ensure that the board has access to independent/specialist advice as required

Chief Executive and management
Chief Executives of registered providers manage their organisations in accordance their boards' overall direction

- ensure that the board receives the information required for them to fulfil their duties

- lead and manage the staff

- ensure their organisations have the necessary operational structures, systems and processes to deliver the business

Accountability
Registered providers must be accountable

- must be accountable to their tenants, the TSA and relevant stakeholders as appropriate

- adopt mechanisms to facilitate meaningful communication and accountability

Probity and conduct
Registered providers comply with their governing documents, all statutory and regulatory requirements and demonstrate the highest standards of probity in all of their activities

- must be accountable to their residents and have regard to all major stakeholders' views

- must consider the reputation of the sector and the proper use of public funding, when conducting their activities

- must be open and transparent and have appropriate codes of conduct, policies and

procedures for all functions and relationships (in particular procurement and remuneration)

- work to a 'widely recognised' code of governance, explain to the TSA their rationale for their choice of code and explain areas of non-compliance with their chosen code

Risk management

Registered providers maintain a sound system of risk management and internal controls that provides assurance to their boards on the security of the organisations' assets and the deliverability of objectives.

- the risk framework should identify all the major risks that might prevent providers achieving their objectives along with the necessary arrangements to manage risks and mitigate their impact

- the framework should be reviewed regularly by the governing body and updated where changes in the business or the external environment alter the providers risk profile

- the framework should be supported by a robust system of internal controls which is reviewed at least annually by the governing body to ensure its effectiveness

Question 4
Is this approach suitable for a diverse domain?

Question 5
Are there other key elements of governance that this option is missing?

Option 2

This option has the advantage of allowing more flexibility and includes less prescription, which can be seen as in keeping with the TSA's fundamental objectives of avoiding the imposition of unreasonable burdens, and regulating in a manner which minimises interference and is proportionate, consistent, transparent and accountable. However, this approach may be perceived as too wide ranging and difficult to enforce.

The governance standard could be framed in the following manner:

Registered providers have the appropriate structures, systems and processes to deliver their aims and objectives, in an effective, transparent and accountable manner.

In demonstrating compliance with the governance standard registered providers must have regard to:

- all relevant legislation

- accountability to residents, the TSA and relevant stakeholders

- safeguarding taxpayers' assets and the reputation of the sector

A standard framed in this wide-ranging manner would need to be supported by some clear signposting of the areas that the TSA will assess. For example, the TSA will assess how the boards of registered providers:

- fulfil their role in leading their organisations and establishing an appropriate style of governance in keeping with expected standards in public life

- hold management to account, manage risks and monitor performance

- ensure that their organisations are accountable to all relevant stakeholders

- comply with all statutory and regulatory requirements

- ensure that tenants' needs are considered in the delivery of services an improvement plans

Question 6
Is a standard framed in this manner meaningful and enforceable?

Option 3

This option draws heavily on the Good Governance Standard for Public Services (which builds on Nolan principles) for the conduct of individuals in public life, by setting out six core principles (with more supporting principles for each core principle and guidance on how the principles can be applied in practice) for good governance for public service organisations.

This approach focuses on the ways different functions of governance can support each other. A governance standard based on this approach may be framed using the slightly amended (see underlined text) six core principles:

Registered providers must demonstrate good governance by:

- focusing on the organisation's purpose and outcomes for residents, <u>potential residents and interested parties</u>

- performing effectively in clearly defined functions and roles

- promoting values for the whole organisation and demonstrating the values of good governance through good behaviour

- taking informed, transparent decisions and managing risk

- developing the capacity and capability of the governing body to be effective

- engaging stakeholders and making accountability real

A standard based on these six overarching principles may be applied across a diverse range of providers. However, some of the terminology and focus of the supporting principles of the Good Governance Standard for Public Services are not applicable or relevant to registered providers or potential registered providers. So an approach based on the overarching principles with the flexibility to allow registered providers to

demonstrate compliance through a range of non-prescribed mechanisms, may be a more suitable approach.

Question 7
Is this approach suitable for a diverse sector including for-profit providers?

How will we regulate governance?

The TSA also has to decide how it will regulate governance. We will need to set out our expectations on how registered providers demonstrate they are compliant and how we will monitor compliance (including in what circumstances we might take special measures).

Critical to successful delivery will be not only the approach to standards that we establish, but the way in which we regulate. The new Senior Risk and Assurance Managers will take a lead role in establishing and managing effective relationships with the largest registered providers. They will be supported by risk and assurance teams and regional standards advisors who will manage the day-to-day relationship, supporting registered providers and their tenants in the delivery of excellent services. This approach reflects our initial high-level assessment of risk across social housing based primarily on the number of homes owned by a registered provider. This approach will be refined in due course.

We are considering applying a range of assessment methodologies including:

- self-assessment by registered providers' boards
- feedback/assessment from residents and stakeholders
- benchmarking and peer review
- independent validation/audit of a particular function/s
- accreditation
- the TSA's assessment of certain key indicators of good governance

We believe that using a combination of these assessment methodologies is in keeping with a co-regulatory approach. Over time we hope to move to a mature form of co-regulation, where we rely largely on self regulation by registered providers with the support of their tenants through effective tenant scrutiny, accountability, and external validation, backed up by our own intervention where a registered provider is not delivering a good service. However, initially the balance between self-regulation and formal regulation is likely to lean more towards formal regulation.

The 2008 Act gives the TSA a range of regulatory, investigatory, enforcement and general powers designed to allow a proportionate response when a landlord has failed to meet a standard or where its affairs have been mismanaged. Special Measures is the name we are giving to the level of regulatory engagement with registered providers whose performance falls below expectations. We are currently working on proposals.

Question 9
What do you consider would be an appropriate combination of assessment methodologies for compliance with the governance standard to begin with?

Question 10
Which areas within governance lend themselves to particular methodologies?

Publishing assessments and grading performance

It is our intention to be transparent about our views on registered providers' performance. Tenants and registered providers as well as other stakeholders will want to know how well they are performing, so we will publish our assessments. There are a number of options open to us in terms of designing an assessment and grading framework, including:

- producing an overall assessment of a registered provider's performance, ie an aggregate view of its performance across the full range of TSA standards

- producing a judgement against each of the national standards

Examples of the type of grading system may be used for a governance standard include:

- assessment of for example 'effective' or 'not effective' or

- excellent, good, satisfactory and poor assessments

Our experience is that certain groups of stakeholders are particularly interested in the regulator's views on the governance of individual associations. This suggests that a judgment against TSA's governance standard is likely to be a more meaningful approach.

How assessments are expressed in terms of grading systems is equally important. Our experience is that too many categories lead to lack of clarity around what the regulator's view is, whereas a simple pass or fail has proven to be too simplistic.

Question 11
What are your views on the potential options and grading system for assessing registered providers' compliance with the governance standard?

Responses

Please address responses to:

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London W1T 7BN

Alternatively, email your response to:
louise.hyde@tsa.gsx.gov.uk

Responses should arrive no later than
8 September 2009.

Responses will be placed on our website and, therefore, open to be viewed by all interested stakeholders. Respondents wishing to send a response in confidence should be aware that the TSA cannot guarantee to maintain confidentiality because of our responsibilities under the Freedom of Information Act.

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