



CABINET
8 DECEMBER 2016

CHANGES TO THE GOVERNANCE
ARRANGEMENTS FOR LEASOWE
COMMUNITY HOMES

Councillor George Davies, Cabinet Member - Housing and Community Safety (and Deputy Leader of the Council), said:

‘It is important housing providers in the borough operate within high standards of governance. This report provides the Cabinet and the Council with important information on changes to the Governance Arrangements for Leasowe Community Homes.’

REPORT SUMMARY

- 1.1 The purpose of this report is to advise that the Council, as a Company Member of Leasowe Community Homes (LCH) will be required to vote on proposals for LCH to move to a Board that is selected on the basis of skills rather than by constituency nominations and for the company to leave Your Housing Group (YHG) of which it is currently a subsidiary and to become a subsidiary of Pierhead Housing Association (PHA).
- 1.2 Leasowe Community Homes Board (LCH Board) has agreed to move to a Board recruited for the skills and experience necessary to enable the organisation to move into more diverse and commercial areas of business and demonstrate it meets the standard required by the Regulator, the Homes and Communities Agency (HCA) for the current business in the new operating environment.
- 1.3 YHG and the LCH Board are satisfied that the substitution of PHA for YHG is in the interests of LCH’s tenants and of all three organisations.

RECOMMENDATION/S

It is recommended that the Cabinet and full Council;

- 1) **Agree that Leasowe Community Homes becomes a subsidiary of**

Pierhead Housing Association and enters into an Intragroup Agreement with Pierhead Housing Association in the terms set out in the Appendix 4.

- 2) Agree that Leasowe Community Homes moves to a Board of Directors that is selected on the basis of skills rather than by constituency nominations.**
- 3) Agree to the removal of Your Housing Group from the constitution of Leasowe Community Homes.**
- 4) Agree that Leasowe Community Homes Memorandum and Articles of Association be revised to reflect the changes and the Minority Protection Agreement be replaced by the Intragroup Agreement.**
- 5) Authorise the Council's nominees as Company Members of Leasowe Community Homes to agree the necessary changes to Leasowe Community Homes Memorandum and Articles of Association as set out in Appendix 3.**
- 6) Authorise the Council's nominees as Company Members to vote on the changes (and associated matters) proposed and referred to in this report at the forthcoming Leasowe Community Homes Meeting.**
- 7) Refer these agreed decisions to the full Council meeting on 19 December 2016 for confirmatory approval to the extent that they relate to non Executive functions such as the Council's housing policies but subject to the condition that the Board of Leasowe Community Homes is satisfied after carrying out due diligence enquiries that the proposed arrangements are viable and in the interests of the company and its tenants.**
- 8) That the Council nominated Members on the Board of Leasowe Community Homes undertake and be provided with all requisite training necessary to be an effective Director on the Board of Leasowe Community Homes**
- 9) The Call-in procedure shall not apply to these (Executive) decisions, the Chief Executive having agreed it is in the public interest that they be taken as a matter of urgency on or before 19 December 2016 which is the deadline Your Housing Group has set for the Council's approval of the changes referred to above.**

SUPPORTING INFORMATION

3.0 REASON/S FOR RECOMMENDATION/S

- 3.1 To enable LCH to become a better and more viable provider of social housing for its current and future tenants by replacing its existing legal relationship by one with another suitable housing association.
- 3.2 To enable LCH to become involved in more diverse activities by equipping the company with a Board which is sufficiently skilled to have effective oversight of a more complex business and to manage the associated risks.

4.0 OTHER OPTIONS CONSIDERED

- 4.1 Initially it was hoped that a partnership of equals could be established with Pierhead Housing Association (PHA) with both it and Leasowe Community Homes nominating members to newly created Parent Board which would oversee both bodies. Unfortunately it has become apparent in discussions with the Homes and Community Agency that the latter would not approve such an arrangement and that the only viable alternative was for LCH to come a subsidiary of PHA.

5.0 BACKGROUND INFORMATION

- 5.1 The operating environment has changed dramatically since the transfer of the Council's housing stock in Leasowe to LCH in September 1999.
- 5.2 At transfer there was a board of 15 comprising five local authority nominations, five tenants and four independent people and Liver (Arena/YHG). YHG holds 51% of the company's votes in a general meeting with the remaining 49% split equally between the tenants and the Council.
- 5.3 In 2014 the Board and Company Members agreed to a change of board directors' terms of office to three terms of three years in order to comply with the National Housing Federation (NHF) Code of Governance recommendations and that tenant and Council board directors would go through the same interview process for places on the Board. The latter was agreed in September 2015
- 5.4 A Minority Protection Agreement drawn up at the date of transfer was interpreted as meaning that decisions of the Board (e.g .approval of the business plan) require the agreement of a majority of the Directors in each of the categories nominated by YHG, the Council and the Tenants. This has not recently worked well because of disagreements between all three categories of Board Directors.

5.5 LCH is proposing to make changes to its constitution in the light of wider scale changes in the housing association sector and to forge a new relationship with PHA.

6.0 THE IMPETUS FOR CHANGE

6.1 Social housing is under considerable pressure: reductions to rents charged, cuts to current operating budgets, lack of demand and reduced lettings income following benefit reductions for LCH's traditional tenants, reduced and/or no grant or subsidy for new build developments mean that resources are no longer available to run the social housing business as they once were

6.2 There has been an increasing number of complaints about the services to tenants delivered by YHG on behalf of LCH pursuant to a service level agreement which culminated in a petition from tenants to LCH. This has been combined with disagreements between LCH and YHG over the cost and quality of the services delivered centrally by YHG to LCH as one of its subsidiaries.

6.3 As a Charity and Registered Provider, LCH's ability to use its funds for non-charitable/non-social housing purposes is strictly limited. It can only do so where there is a very strong business case and its charitable assets would not be at risk. LCH would therefore never be in a position where it was expected to fund risky activities or those that may not be in accordance with the investment criteria for charities prescribed by the Charity Commission and the HCA.

6.4 The LCH Board agreed that it needed to develop into more diverse areas of work to create other income streams that would replace or supplement previous public subsidies. Moving into building social housing, build for sale, build for shared ownership, together with the development of joint ventures are all new and challenging activities that should be explored. They offer potential rewards but with significantly different risks. It is essential that the Board of the company has the skills to manage those risks, ensuring that profits are made which are brought back to LCH to replace lost government subsidy. Those activities can be pursued through its proposed constitutional arrangements with PHA including the joint creation of a commercial subsidiary to carry out those activities which will bring income to replace the reduced public subsidies.

6.5 For risk management reasons as well as taking regulatory guidance, LCH needs to ensure that it has a sufficiently skilled and experienced Board to have oversight of such new ventures.

6.6 It is clear from the HCA that they require expect stronger commercial and business skills from LCH's Board for the future.

7.0 THE EXPECTATIONS OF THE REGULATOR

7.1 The HCA has flagged up concerns that the Housing Association Boards should be sufficiently skilled to be able to understand the more diverse activities that they would be involved in.

7.2 All registered housing associations must operate to a recognised code of governance. LCH has adopted the 'NHF Code of Governance: promoting excellence for housing associations'. The main expectations with reference to this review of L'H's governance are:

- Board Directors must act in the interests of the organisation and not on behalf of or representing any constituency or interest group
- The Board should be at least five and no more than twelve members
- Recruitment to board vacancies must be open and transparent and be based on the board's considered view of the skills and attributes required to discharge its functions
- Maximum tenure for all non-executives must in total be nine years
- When a board member is nominated or elected, the organisation "must ensure that those coming forward bring skills and experience that meet the needs of the board, and that they are fully aware in advance of the responsibilities that they will undertake. New board members must not be appointed without undergoing a due selection process to establish their suitability."

7.3 Seminars and articles from leading figures such as Julian Ashby, Chair of the Regulation Committee at the HCA have been increasingly urging boards to ensure they are sufficiently skilled. In September 2013, Julian Ashby said that the HCA had dealt with a number of cases where poor governance had led to ineffective risk management. Those boards did not have sufficient skills to challenge or did not recognise the need for specialist or professional advice and he called on providers to regularly appraise their mix of expertise and ensure their boards are fit for purpose by refreshing and renewing skills regularly. This advice has consistently been reinforced and early this year Julian Ashby advised boards that if they did not have the necessary skills for diverse activities then they should not be involved in those activities.

7.4 In order for the HCA to be able to test the effectiveness of boards and their organisations a new system of In-Depth Assessments (IDAs) are now being carried out on registered housing associations. Through review of the company's documentation and intensive work on site, the HCA wish to ensure that governance and financial arrangements in each housing association do not put the social housing assets at risk. The HCA will be looking for evidence that the board has credible plans

and they will wish to obtain assurance that the board has the skills and drive to deliver those plans. The LCH Board understands that an IDA would consider a range of areas: strategy, structure, financial resilience, risk profile mitigation and governance.

- 7.5 Under governance the HCA will test the Board's understanding of business planning, management reporting and forecasting. They will wish to see the level of individual Board skills and effectiveness and the interface with the executive.
- 7.6 Through IDAs the HCA is 'raising the bar' in assessing registered providers' compliance with the regulatory standards and whether they are fit for purpose in a much more difficult operating environment. A key element will be the level of skills and experience on the Board to manage what will be more challenging businesses going forward.
- 7.7 The regulator has published four volumes of 'Learning from Problem cases' over the last twenty years. These reports chronicle, in some detail, the failures in the housing association sector. They are produced for boards and executives to learn from the mistakes and setbacks of others so as to avoid encountering similar fates.
- 7.8 The latest volume was published by the HCA in June 2015 and covers Cosmopolitan Housing Association (a Liverpool housing association that was brought to the brink of insolvency due to weak governance and management and a number of financial issues). Whilst there is a range of factors leading to problem cases the report sets out that the greatest root cause of failures has been through weak governance. The report states that 'in today's tough business environment, boards need skill, grip and effective teamwork if they are to exercise proper oversight of the executive and the operations of the organisation.'
- 7.9 The report goes on to highlight that 'we are seeing a higher bar for the standard and skills and competencies required for non-executives' and 'we are now seeing – if not universally – a more ruthless focus on skills, capabilities and the depth of knowledge in much board member selection.' The problem cases highlighted show that poor governance and risk management with, in many cases, weak board skills and oversight in more risky and complex non-social housing activities can lead to spectacular failures. One of the lessons is to ensure the board have the skills to oversee the new ventures that are part of the organisation's aspirations. This is a theme that Julian Ashby the Chair of the Regulation Committee at the HCA regularly comes back to as set out earlier.
- 7.10 In short the HCA expect housing associations to be involved in more diverse activities but that their boards are sufficiently skilled to have oversight of a more complex business and able to manage the associated risks.

8.0 LEASOWE COMMUNITY HOMES INDEPENDENT REVIEW OF GOVERNANCE

8.1 In 2015 LCH commissioned an independent governance review using Capsticks (a specialist national housing consultancy). They reviewed LCH's governance arrangements and completed a study on best practice in Large Scale Voluntary Transfer housing associations (LSVTs).

8.2 Capsticks referred to the changed operating environment and the need for appropriate skills and experience for a board to be able to control, support and direct the organisation in its business objectives and the fact that the NHF Code of Governance and HCA Regulatory Framework have both been strengthened in this regard.

8.3 Capsticks review of LCH's Board found that:

- All board directors agreed that with the future challenges a more skills base Board was required
- All board directors agreed that there were currently skills gaps, particularly around finance and business and commercial skills
- Many noted that the board relies on a small number of key board directors
- There was concern over the imbalance between focus on strategy and on day to day operations
- There were mixed views on the size and composition of the board whilst agreement that it needs to be skills based
- There was a view that the annual appraisal process needed reviewing
- It was felt existing tenant involvement was very effective
- Governance documents needed to be reviewed and updated, particularly the scheme of delegation

8.4 Capsticks made a series of recommendations:

- LCH move to a skills-based board and consider reducing the size of the board
- Nominated board directors should go through the same skills based appointment process as all other board directors
- If the board decides to move away from constituencies altogether, that arrangements be established to ensure adequate engagement with tenants

- Committee structures to be streamlined and task and finish groups to be considered for other business
- Revise the supporting governance documents
- Reduce the level of operational detail in reports and focus more on strategy

8.5 The report will be available to the HCA as part of any future IDA or regulatory review of LCH. The HCA would expect the LCH Board to have taken account of it and to have acted on the findings of an external independent review.

9.0 SKILLS AND APPRAISALS

9.1 Following the Capsticks review, the LCH Board agreed a set of skills that will be required moving forward to more diverse activities. The list of agreed skills is attached at Appendix 1.

9.2 From the surveys undertaken by Capsticks, board directors collectively identified a range of skills gaps, a number of which will be required for the future operation of the business going forward:

- Business growth and diversification
- PR and Communications
- HR
- Housing Management and service delivery
- Property development
- Legal services
- Commercial and financial skills

9.3 From previous discussions LCH has already noted that it will wish to retain skills that it has acquired in its early years work. These have included community development, resident perspective, tenant involvement, local authority and public sector working and voluntary and community work.

9.4 However from the above analysis there is a number of skills not presently in place which will be required for the future operation of the business going forward undertaking more diverse activities.

9.5 The Board undertook a skills gap analysis / appraisal process at the end of March 2016 which, together with an agreement on the skills required against its future work programme, will inform the Board's future structure.

10.0 WHAT ARE OTHER LSVTS DOING?

10.1 It is clear that the vast majority of LSVT housing associations have made significant changes to their governance structures. Many have moved away from constituencies which have equal numbers of board directors in each.

10.2 The NHF has also conducted a survey to 154 LSVT housing associations receiving responses from 76. Amongst their findings are:

- 29 now do not have a local authority board director, 12 have one and 11 have two on the board, the remaining 19 who responded have three or four
- For tenants there is a wider spread. 11 do not have tenants on the board, 6 have one, 30 with two or three on board, 15 have four and 11 have between five and nine.

10.3 Several organisations have moved away from the constituency model to a purely skills based approach without any nominations via constituencies.

Altair conducted a good practice study of LSVT associations as part of their review of governance of Magenta Living.

They concluded that most (70 out of 76) LSVTs have adjusted their governance structures due to the changed operating environment and need for business diversification. Most have moved to a more skills based board and most had moved away from the standard constituency model to a board that includes more independents with the required relevant skills. This has been done by reducing the number of tenant and council places but in the main still reserving a minimum number of constituency places.

11.0 PIERHEAD HOUSING ASSOCIATION

11.1 PHA was selected by LCH's Board as the preferred partner in a process which is described in the Detailed Business Case attached as Appendix 2.

11.2 The expected benefits to tenants are set out in the Detailed Business Case as are the projected financial consequences which are positive but subject to the outcome of the due diligence enquiries commissioned by LCH's Board. These have now been completed to the satisfaction of the Board.

12.0 WIRRAL COUNCIL APPROVAL

- 12.1 Officers and Board Directors from LCH have met with Officers of the Council and the Cabinet Member for Housing, outlining the issues detailed in this report.
- 12.2 From the discussions it was agreed in principle and subject to Council approval that:
- LCH and PHA create a new parent entity with its own skills based board that would govern LCH (in place of YHG) and PHA in accordance with the provisions of an Intra Group Agreement which would define the extent of the autonomy given to LCH's and PHA's Boards. Unfortunately as described above these proposals did not find favour with the HCA and have been replaced by a model which would broadly replicate the existing constitutional arrangements with LCH being a subsidiary of PHA in substitution for YHG.
 - Under the new Articles (in Appendix 3), the Board will consist of between 5 and 12 members of whom 2 will each be nominated by the Council and LETA (the Tenants Association) until 31 March 2020.
 - The existing Directors would be eligible to apply for a place on a skills-based Board and would undergo an interview process by an interview panel of the LCH Board. If they failed to match the required skills they will not be appointed and alternative candidates would have to be nominated by the Council and LETA.
 - It can reasonably be anticipated that the Councillors currently serving on the Board will have between them some of the skills required to be on a skills based Board.
 - At the time that any director (not nominated by either the Council or LETA) comes to the end of their term of office, and a vacancy occurs, any individual from any background or sector, who has the necessary skills, will be eligible to apply.
 - PHA will have the right to remove or appoint Board members to give it a controlling majority in the circumstances set out in Schedule 5 of the Intragroup Agreement (in Appendix 4) viz broadly if the Directors are in breach of their legal obligations.
- 12.3 The Council's decision making process will require these proposed arrangements to be approved by the Cabinet and the recommendation to be subsequently approved at a full Council meeting.
- 12.4 If the full Council agree to the governance changes the Council's existing Company Members would be required to attend a general meeting of LCH and cast the Council's vote in favour of the necessary changes to LCH's Articles of Association.
- 12.5 Once agreed, the changes will be incorporated into LCH's Articles of Association.

- 12.6 The Minority Protection Agreement would come to an end and be replaced by the Intragoup Agreement in Appendix 4 which defines the limited autonomy to be given to LCH (a requirement of the HCA which expects PHA to have the necessary powers to regulate LCH).
- 12.7 A timetable for Company Member consultation and holding a General Meeting of Company Members has been drawn up which will pick up the Council's decision making process which is set out below.

13.0 THE COUNCIL'S SHARE'

- 13.1 Under the existing constitution at a General meeting of the company the Council has one vote which is worth twenty four and a half percent of the voting rights. The tenant members have one vote which is worth twenty four and a half percent of the voting rights and the Independent/YHG members have a share of the remaining fifty one percent of the voting rights.
- 13.2 For any special resolutions such as changing the name of the company or changing the company's articles, under company law, 75% of the company membership must vote in favour of the resolution for it to be passed. As the Independent/YHG vote is worth 51% of the total vote the Council has what has become known as a 'Golden Share' as it is in effect a veto over the other two constituencies represented at a company meeting unless they act together against the Council
- 13.3 Under the new Articles of Association the members of the company will be PHA and up to 12 directors of whom 2 will each be nominated by the Council and LETA. The Council and LETA will cease to be Company Members when Directors cease to be nominated by them on 31 March 2020 (or earlier if the law so provides as explained in Section 15 below).

14.0 TIMETABLE

- 14.1 The proposed date for implementation of the above changes is 31 March 2017 which in turn requires all the necessary documents to be lodged with the HCA no later than 28 February 2017.
- 14.2 LCH's consultation with its tenants over the proposed changes has now been completed. The tenants broadly support the proposals as the best that can reasonably be achieved in the circumstances in which LCH finds itself.
- 14.3 In order to achieve this target date, the Cabinet is requested to consider and recommend approval of the proposal to full Council at its meeting on 19 December 2016 and because of the urgency dictated by this timetable to remove the right of members to call in the proposed decision

15.0 THE HOUSING AND PLANNING ACT 2016

- 15.1 The above Act received the Royal Assent on 12 May 2016. Section 93 gives the Secretary of State the power to create regulations with the purpose of “limiting or removing” the ability of councils to “exert influence” over registered providers whether by appointing or removing Directors or by exercising voting rights.
- 15.2 For LSVTS such as LCH this appears to include removing a local authority’s ability to nominate board directors and also the authority’s voting rights at a general meeting.
- 15.3 The Government’s approach is to ensure that housing associations can be classified as independent bodies rather than public sector bodies. This follows the reclassification of housing associations as ‘public non-financial corporations’ by the Office of National Statistics (ONS) late last year given the amount of control exercised over them by government or other public bodies. The Government made an immediate commitment to bring in changes necessary to prompt the ONS to reverse this decision and, in January, laid a number of deregulatory amendments to the Housing and Planning Bill intended to address the ONS’ concerns.
- 15.4 It is unknown at this stage what these changes will look like and how LCH’s constitution could be amended by the new powers. It is recommended that given the Council and LCH have started to make similar changes already that Cabinet agrees to the changes highlighted in this report. Should legislation be passed which makes further changes then these will then be implemented as a matter of law before 31 March 2020 (which is the latest date in the new Articles of Association for the removal of the Council’s right to be a member of LCH and to nominate Board Members). After 31 March 2020 the only members of LCH will be PHA and independent members of the Board selected in accordance with their ability to exercise the skills require by the company.

16.0 RELEVANT RISKS

To the Council:

- 16.1 The Council is a Company Member of LCH holding twenty four and a half percent of the membership. It is essential that the Board of LCH is fit for purpose, in order to ensure effective decision making mitigating any risk to the Council’s reputation and interests in the Company.
- 16.2 It is in the Council’s interests to have a vibrant locally based and locally managed housing association which owns around one thousand units of the social housing in the borough. The status quo cannot ensure that outcome since it has led to disagreements with YHG which have impaired the efficient delivery of services.

To Leasowe Community Homes:

- 16.3 If LCH does not change its governance structure it would be at risk of increased scrutiny by the HCA .
- 16.4 Moving into more diverse activities and not having the most appropriate skills on the Board could result in decisions being taken without full appreciation of implications which could have seriously adverse consequences. It would be no defence that the Board Directors did not have sufficient skills to understand the decisions taken.
- 16.5 YHG and LCH accept that their current working and legal relationships are not satisfactory and should be replaced by LCH's subordination to another suitable housing association in accordance with the requirements of the HCA.
- 16.6 PHA is a suitable partner for the reasons set out in the attached Detailed Business Case but this assessment is subject to the outcome of due diligence enquiries into the assumptions made by the Detailed Business Plan attached as Appendix 2. Those enquiries have been completed to the satisfaction of the Council's nominees on the Board.
- 16.7 Taking no action to revise LCH's governance structure would make it very difficult to undertake the diverse activities required in order to provide further income to the Company and to carry out its social housing functions to the satisfaction of its tenants.

17.0 RESOURCE IMPLICATIONS: FINANCIAL; IT; STAFFING; AND ASSETS

- 17.1 This relates to the structure of Leasowe Community Homes so there are no financial implications for the Council.

18.0 FINANCE IMPLICATIONS

- 18.1 None

19.0 LEGAL IMPLICATIONS

- 19.1 This relates to Leasowe Community Homes governance arrangements so there are no legal implications for the Council other than for the Council's rights as set out in the constitution of LCH.

20.0 ENGAGEMENT/CONSULTATION

- 20.1 LCH has consulted with Board members and Senior Officers from the Council on the proposed changes. It is intended, subject to Council approval, that LCH further put these changes to a formal vote at its General Meeting.
- 20.2 LCH has consulted with representatives of the tenants on the proposals

21.0 EQUALITIES IMPLICATIONS

21.1 There are none except to the extent that the proposals should lead to the improvement of LCH's services to tenants including those with "protected characteristics" as defined by the Equality Act 2010

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APPENDICES

- 1) Leasowe Community Homes Board Required Skills
- 2) The Detailed Business Case(exempt from publication as it contains commercially sensitive information relating to LCH,YHG and PHA). (EXEMPT)
- 3) The proposed amended Articles of Association.
- 4) The proposed Intragroup Agreement.

REFERENCE MATERIAL

Due diligence reports on the proposed constitutional arrangements between LCH and PHA(exempt from publication as they contain commercially sensitive information relating to YHG,LCH, and PHA)

SUBJECT HISTORY (last 3 years)

Council Meeting	Date

Leasowe Community Homes Board Director - Required Skills

Relevant Experience and Skills – Essential

1. Board Director or Governance experience
2. Operational experience at a senior level
3. Strategic leadership
4. Financial Management
 - Accountancy
 - Treasury management
 - Business
 - Audit
5. Asset Management
 - Property development and sales
 - Property management
 - Construction
 - Housing management
 - Regeneration
6. Risk management
7. Change management
8. Performance management
9. Business growth and development
10. Customer services
11. Commercial business skills

Relevant Experience and Skills – Desirable

1. Legal
 - company
 - constitutional
 - business - contracts
 - charity
2. Stakeholder engagement
3. Community involvement
4. Marketing
5. Public relations
6. ICT

Knowledge – Desirable

1. Registered Providers
2. Regulatory Framework
3. Political and economic environment
 - welfare reform
 - devolution
 - housing strategy
 - planning
4. Probity
5. Local knowledge

6. Mergers and acquisitions
7. Health and social care
8. Social investment

Abilities - Essential

1. Team working
2. Integrity
3. Independent judgement
4. Creative and clear thinking
5. Analytical skills
6. Communication skills
7. Networking
8. Equality and diversity