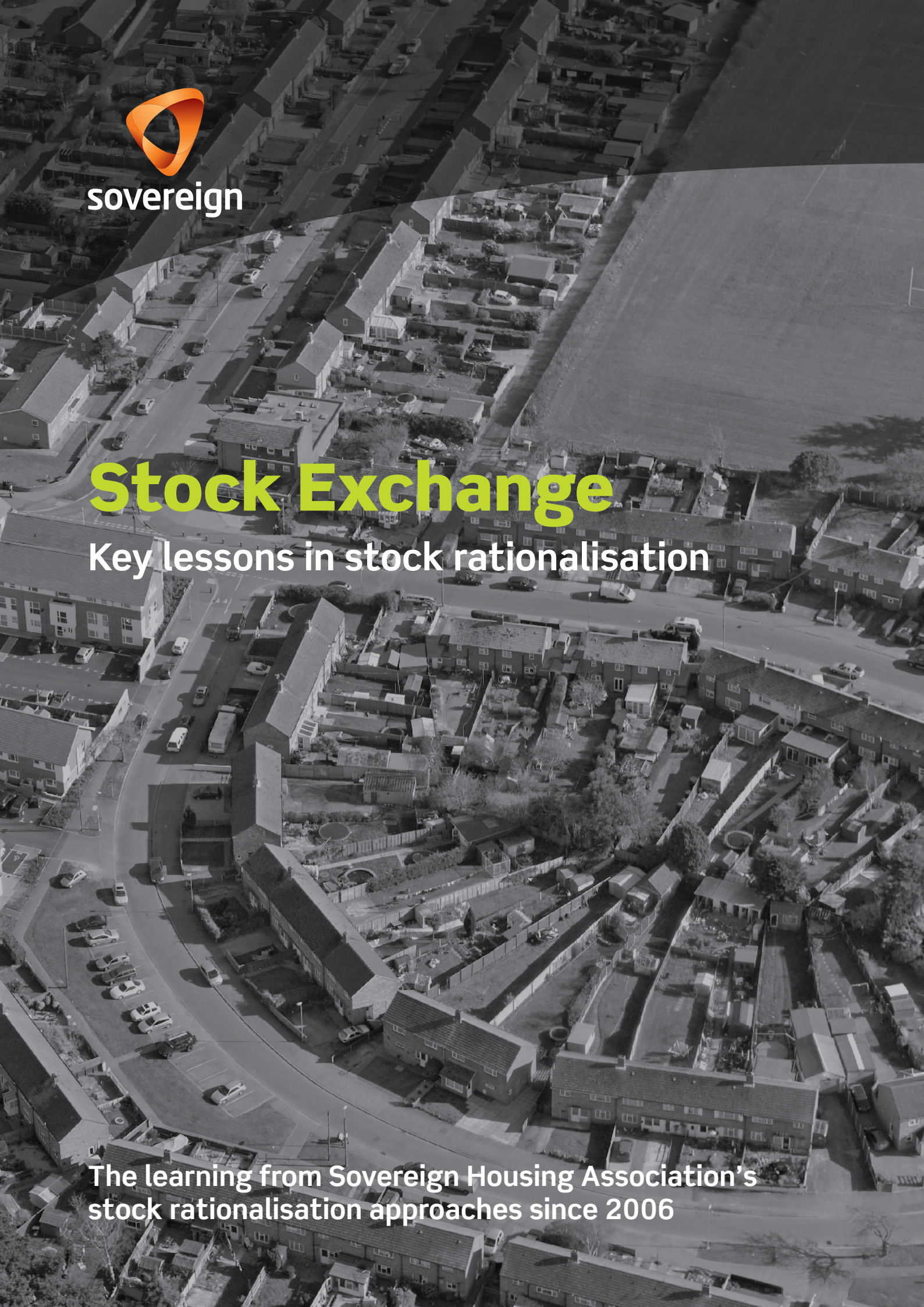


sovereign

Stock Exchange

Key lessons in stock rationalisation

The learning from Sovereign Housing Association's stock rationalisation approaches since 2006

Contents

About Sovereign

Sovereign Housing Association is one of England's largest housing association groups, managing around 34,000 homes across a range of tenures in the south and south west.

We employ over 1,000 staff and our head office is based in Newbury. To support effective local service delivery, we also have operational offices in each of the main regions we work in: Berkshire, Hampshire, Oxfordshire, Dorset, Devon and the West of England (including Wiltshire, Gloucestershire, Bristol and Somerset).

Our social rented housing stock covers 59 local authorities, with stock numbers in each varying from single figures to almost 7,000 homes. In 26 local authority areas we hold fewer than 100 homes.

In 2011 we rationalised our governance structure, collapsing the group and four constituent housing associations – Sovereign South & West, Sovereign Twynham, Sovereign Vale and Sovereign Kingfisher - into a single legal entity. This has created a leaner, more efficient decision making process, with economies of scale and other financial advantages. Our vision is to be a leading provider of flexible housing solutions in southern England.

1. Introduction

It is clear that stock rationalisation will be an ongoing feature of the housing landscape over coming years, as organisations seek to improve customer service and operational efficiency against a macro economic context of government cutbacks, austerity and financial constraint, and radical changes to housing policy.

In some cases, rationalisation may be part of a response to the Value for Money standard in the new Regulatory Framework, which requires housing associations to consider the optimal use of their assets, including rigorous appraisal of all potential options.

For Sovereign, stock rationalisation is about consolidating our geographic 'footprint' to achieve both high service standards and greater efficiency. Sovereign has been active in the stock rationalisation market since 2004 and our first project, involving nearly 100 homes in Cornwall, completed in early 2006.

Our activities since then have affected over 2,700 homes and many more residents through stock sales, acquisitions, swaps and management agreements, with proposals affecting over 1,000 more homes currently under consideration.

Stock rationalisation can be complicated and time consuming, involving myriad strands of work, major transfers of critical data, differing modes of operation, uncertainties for residents and staff, and very significant financial transactions. The impacts on the organisation of sizeable projects, involving hundreds of homes, can be akin to buying and integrating entire new businesses.

Clarity of purpose and attention to detail are vital for success. At Sovereign, stock rationalisation is driven by a clear strategy. Rationalisations are complementary to our development activity, not a replacement for it. We recognise that while rationalisations may not add to the overall housing stock now, resulting cost efficiencies can free up resources for future investment in new development. Done well, rationalisations can support growth, effective asset management, and financial efficiency and capacity.

In March 2012, we commissioned Ark Housing Consultancy to carry out a review of six of our projects to date. Their brief was to examine the various approaches we have used, their relative success and benefits, the costs and risks of each, and the key lessons to be drawn. We wanted to understand how well we are fulfilling our purpose and what we could do better.

The findings make interesting reading and build into a series of common themes and lessons that will add further rigour to our approach in the future.

It takes two to tango on rationalisation and one thing we have learnt is that the more open, committed and prepared both parties are from the start, the better the outcome is likely to be.

In that spirit of openness, and in the interests of helping to shape the environment on rationalisation for the future, we are publicly sharing the lessons we have gleaned. We hope you find them useful.

2. A brief summary of completed projects

Project 1 – Stock disposal via competitive tender

In 2004, we undertook a detailed strategic project to understand the net present value (NPV) of all our stock and our success as a landlord from the residents' perspective. Following the review, we decided to rationalise our holdings in Cornwall. In total, 96 general needs properties were involved, comprising 67 flats and 29 houses. The properties were remote from our main operating areas, there was no local office and we were not looking to grow in the area. Costs were similar to other areas, but rent restructuring meant rental income would decline in real terms.

While the residents were happy with us as a landlord, they welcomed the chance to have a more local service presence and local contractors. We also consulted the local authorities and took their preferences for rationalisation partners into account.

In the summer of 2005, we conducted an open tender process to an agreed shortlist of tenderers. We provided information on income from the properties, plus cost of repairs and maintenance and future investment needs. Further details were supplied in response to tenderers' questions.

Residents' representatives were involved in testing the experience and delivery of services by each of the tenderers, financial tenders were evaluated, and a preferred bidder identified against a scoring matrix which took account of residents' views.

After tender acceptance, the parties jointly agreed the extent of further information needed to support the transfer. The Managing Directors of both organisations were involved in the project group, which therefore had the authority to make quick decisions and commit resources.

We brought forward responsive repairs to ensure all works were completed and the stock was in good condition at transfer. For the benefit of our future reputation, we wanted departing residents to continue to see us as a good landlord and for customer satisfaction levels to be at least maintained up to the point of transfer.

Formal completion was achieved on 31 March 2006.

Strategic Planning Decision to Rationalise Stock
Business Efficiency and to improve services to residents

Resident Consultation
Survey and visits to determine preferences for future service delivery - updates stock rationalisation proposal

Internal Expression of Interest
Contact made with RP's active in the location

Issue PQQ
Submission of background on the RP - information for residents

Issue Invitation to Tender
Issue ITT - data pack to shortlisted RPs

Selection of Preferred Bidder
Financial assessment of bids - Resident Panel views on RSLs approach to service delivery

Due Diligence Process
Contract negotiation, legal searches, data exchange

TSA s172 Consent (formerly s9)
Application to TSA for formal consent to transfer stock

Exchange Contracts
Formal exchange of contracts to commit the parties to the transaction

Preparation for Transfer
Communication to residents, transfer of rent accounts and direct debits, IT data transfers, TUPE staff transfer consultation

Formal Completion and Transfer of Properties and Staff
Completion of the legal process

Post-transfer Processes
Settle outstanding rent arrears, transfer of files, resident communication

Projects 2,3 and 4 – Stock acquisitions via competitive tender

These three projects were opportunistic acquisitions arising from invitations to tender.

Project 2 - In February 2006 agents acting for the vendor housing association invited bids for 154 general needs homes located to the West of the A34 in one of our core operating areas. The sale resulted from the selling association rationalising unwanted stock from a recent merger. Sovereign's bid was successful, but the rapid move on of stock by the vendor did create a number of issues subsequently around lack of available data and information. Completion took place on 30 March 2007.

This case was also unusual in that a competing association, Vale Housing Association, joined the Sovereign Group during the tender process. Following the acquisition, an immediate internal back-to-back transfer was made to Vale HA at the same price. All communications to residents before and after transfer were sent in the name of Vale HA. After completion, Vale staff visited all residents and carried out a programme of catch-up repairs. A planned internal stock rationalisation to consolidate regional holdings through Sovereign Vale was delayed to avoid over-stretching local resources.

Project 3 - In late November 2007 an opportunity arose to acquire 850 properties in Bristol and Portishead, comprising 28 bungalows, 284 houses, 488 flats, 41 maisonettes and 9 commercial properties. We already managed around 1,000 properties in the area and had established an area office. The acquisition represented a good strategic fit and we submitted a tender in early 2008.

As well as financial evaluation, the selection process involved an open invitation to residents to question tenderers at an informal 'beauty parade'. The residents voted as they left the meeting, expressing their preference of landlord. Additional drop-in sessions were also arranged. Our successful approach included using high quality display and information materials, with senior managers and operational staff attending to demonstrate our commitment.

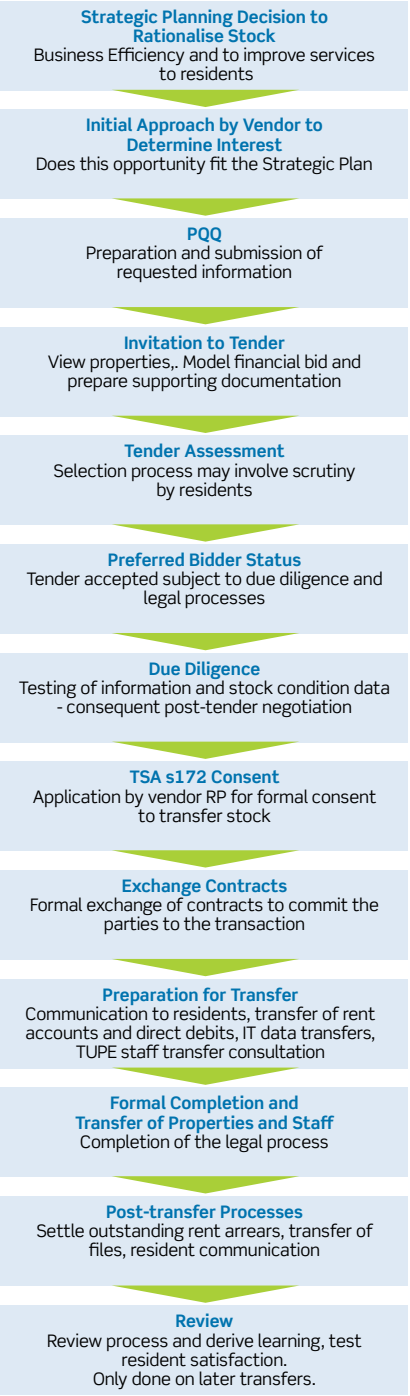
Due diligence identified a significant repair issue to some flats and the remedial costs were taken into account in negotiations over the final price. Management agreements with external agents for blocks occupied by vulnerable client groups were also in place, e.g. a women's domestic violence refuge, rough sleeper projects, etc.

The vendor association required completion by 31 March 2008, imposing significant time constraints on all involved. The heavily condensed timescale on a very sizeable transfer led to a number of issues. Communications with residents around catch-up repairs and maintenance could have been handled better, the transferring staff team was under-resourced and we were under-prepared for the scale of the integration process. A failure to fully appreciate the nature of some of the management issues associated with the stock and tenancies also resulted in an initial drop in resident satisfaction after transfer.

Project 4 - This was part of a major rationalisation of stock by a large housing association. The 680 properties involved were broken down for transfer purposes into zoned packages and put out to tender. Sovereign bid in June 2009 for the zone covering West Berkshire and the M4 corridor, which comprised 52 general needs flats, five houses and 34 sheltered or supported units.

The transaction completed on 29 March 2010.

By 2009, we had used our experience of earlier rationalisation projects to develop a project team approach, with standardised documentation and processes to facilitate acquisitions. We organised events for residents and undertook testing of customer satisfaction after transfer.



There are advantages and disadvantages to all methods of stock rationalisation.

Project 5 – Management Agreement only

This opportunity arose in June 2009 when the other party invited a number of housing associations to submit proposals to manage 138 newly built homes in South Hampshire - 79 general needs flats, 10 houses, and 49 shared ownership properties. Following acceptance of our bid, negotiations took place over a draft management agreement supplied by the other association.

A three year agreement was negotiated, covering housing and estate management, all responsive repairs and maintenance. The client housing association completed outstanding repairs prior to handover. Planned maintenance was not included as the stock was recently constructed and under warranty. All rents and service charges are paid over to the client association, with quarterly invoicing of the management fee plus any exceptional recharges, e.g. those arising from management company invoices for grounds maintenance, cleaning, etc.

The client association handled all communications with residents, local authorities and other stakeholders up to the date of handover on the basis of an agreed plan. Following the handover, we sent out introductory letters and welcome packs and held events and face to face meetings with residents.

The developers had contracted a number of management companies during scheme construction to handle aspects of the shared ownership scheme management. Our staff had to devote significant time to attending meetings between shared owners and the management companies or developers to resolve unforeseen issues, such as replacing dying trees in the landscaped area.

Management of the properties was handed over on 1July 2010. The date was chosen to avoid year-end procedures and to fit with a quarterly rent cycle.

Project 6 – Stock swap and management agreements

This opportunity developed following informal discussions at Chief Executive level. The two associations both recognised the potential strategic benefits to our businesses and residents from rationalisation of stock holdings outside of core operating areas. This was a negotiated process, but one that became extremely complex due to lenders' charges and the differing nature of the tenures and ages of the stock on either side.

Close joint working was a crucial plus. We agreed the assumptions to underpin valuation with the other association at an early stage and external consultants used these to model the property portfolio values and undertake stock condition surveys. Joint project teams met regularly to co-ordinate the process and specialist sub-teams were established. For example, a file transfer protocol site was set up by the project IT team for sharing of documents and information, which worked very well. We maintained extensive communication with residents throughout the process, based on a jointly agreed communication plan. Staff being transferred were also extensively consulted. Joint ownership of the process and the data/ information issues ensured positive relationships were maintained throughout.

Ultimately, we swapped ownership of 387 Sovereign properties in Somerset for 338 properties, mostly in Wiltshire. Under the management agreements, 310 Sovereign properties changed management and we took 420 properties in return. The deal virtually balanced in financial terms. The management agreements covered housing management, responsive repairs and planned maintenance. The agreements were signed and the deal completed on 30 January 2012.

We subsequently undertook a review to consider the learning points from the process for future projects.

Strategic Planning Decision to Rationalise Stock
Business Efficiency and to improve services to residents

Informal Approach
Potential for a stock swap arose from informal discussions at Chief Executive level - similar strategic aims

Senior Management Involvement
Senior managers asked to investigate feasibility

Operational Team Involvement
Identified likely number & location of properties

Valuation
Agreed the assumptions for the valuation model & jointly instructed stock surveys & valuation number crunching

Negotiation
Extensive & complex. Valuations influenced decision for a mix of swaps & management agreements

Resident Consultation
Joint meetings with Resident Board & residents

Business Case Approved
Board approval granted to proceed

Joint Project Team Meetings
Joint meetings held to identify & co-ordinate task achievement

Preparation for Swaps & Management Transfers
Communication to residents, TUPE staff consultation, etc.

Due Diligence
Heads of Terms, stock condition survey testing, data exchange, risk assessment

Exchange of Contracts
Formal exchange of contracts to commit the parties to the swap transaction

Formal Completion & Transfer of Properties & Staff
Legal completion to swap stock & signing of Management Agreements

Post-transfer Processes
Settle outstanding rent arrears, transfer of files, resident communication

Review
Review process & derive learning

3. Buy, swap or manage?

So which approach would we recommend from our experiences?

The simplistic answer is that a straight acquisition or disposal by negotiation tends to be easier and consequently favoured by managers tasked with successfully concluding projects. But the reality is more complex and involves a range of strategic and operational considerations.

There are advantages and disadvantages to all methods of stock rationalisation and each individual project will also have its own good and bad points. What our experience has taught us, though, is the critical importance of a number of key issues in determining project success or failure.

Stock rationalisation cannot be treated as an 'add-on' for development departments or asset managers. Rationalisations involve the transfer of a business, with the need to maintain 'business as usual' to the point of transfer for the disposing landlord and from inception for the acquiring one. The implications, particularly of larger projects, are felt organisation-wide and for months, and sometimes years, to come. A strong understanding of the overall commercial, operational and human resource considerations are necessary precursors to success.

A strategic approach

There is no doubt, however, that stock rationalisation projects are more likely to succeed if they fit within the parameters of a well developed strategy.

Being clear about asset management goals – how you want to grow, where you want to grow, the type of stock and tenure preferred in each location, and, conversely, stock you are prepared to sell or swap – will generally lead to better rationalisation results than an opportunistic approach.

Strategic clarity should ensure:

- Opportunities which do not fit the strategy are less likely to be pursued
- There is better understanding of the strategic value of potential stock, including whether a premium is justifiable and whether taking a level of poorer stock within a package is acceptable
- Staff motivation and commitment is solid and project resourcing is appropriate

Sovereign has now developed a strong strategic approach to stock rationalisation, and this

Larger projects particularly come with a significant level of inherent risk attached.

Stock rationalisation projects are more likely to succeed if they fit within the parameters of a well developed strategy.

is helping us to operate more pro-actively in the market and less reactively. We have backed that strategy by appointing a senior manager to consider and manage all stock rationalisation opportunities and by investing in software that will improve our market intelligence.

Managing key risks

Because stock rationalisations involve transferring all of the related business functions, larger projects particularly come with a significant level of inherent risk attached. Understanding and managing those risks effectively is imperative.

With every rationalisation project, we recognise that our reputation as a landlord and within the sector is basically on the line. The damage from a failed or poorly handled project can be deep and long-lasting.

Due diligence

Our experience is that the true value and benefits of a proposition are impossible to determine in detail until effective due diligence has taken place.

It is hard to overstate the importance of the due diligence process. In all stock rationalisations, the devil is in the detail. Such mistakes as we have made on stock rationalisations – and thankfully they have been few – have generally resulted from an inability to obtain adequate information over some aspect of the business, not foreseeing a particular issue, or from trying to manage a rationalisation process too quickly. Due diligence should always be rigorous and comprehensive.

Examples of information and data problems with potentially adverse consequences which we have uncovered at due diligence or only post-completion include:

- local caretaking and grounds maintenance contracts not declared by the selling association.
- poorly managed leasehold schemes, including one that led to a Leasehold Valuation Tribunal post-transfer and considerable charges for repairs and maintenance obligations unfulfilled by the selling association.
- discovering stock shown as general needs was in fact supported housing for people with learning difficulties, creating additional management complexity.
- discovering restrictive covenants preventing sale of some properties.
- discovering additional management companies involved in managing shared ownership leasehold blocks.

Mistakes are always more likely to happen if the process is rushed. Desperation on the other side to complete a deal very quickly should act as a warning sign.

Negotiated cost savings tend to alleviate rather than cure issues, and the subsequent pain for managers is only lessened if the savings are pushed down into the relevant team budgets.

Even so, it is in the nature of the beast that, occasionally, something will not be uncovered, certain data cannot be fully verified or that information may be missing. Risk cannot be entirely eliminated, but it can be substantially mitigated.

We put considerable time and effort into validation of the stock, including visiting all stock, whether or not the vendor's data is supported by a warranty. The third party surveyors will generally only have visited (and warranted) a small sample of the stock. Understanding the complexities of the stock, including tenure variations and all of the associated issues, will help support strong due diligence and effective management planning. The nature of the stock is the single biggest determinant of 'value'. We also give the other party a checklist of all information and data we will require for analysis before completing a transaction.

Desperation on the other side to complete a deal very quickly should act as a warning sign

Communication

Beyond the mechanics and detail of the due diligence, poor or ineffective communications is a prime risk. Stock rationalisation is 'business speak' for a process that impacts heavily on the day to day lives of often hundreds of individual residents and staff. It creates uncertainty and disruption and we should not be surprised that it therefore also evokes strong emotional responses.

Detailed communications planning covering the entire rationalisation process is vital to winning and maintaining the support of affected residents and staff. This includes staff from all parts of the organisation, not just those transferring in or out.

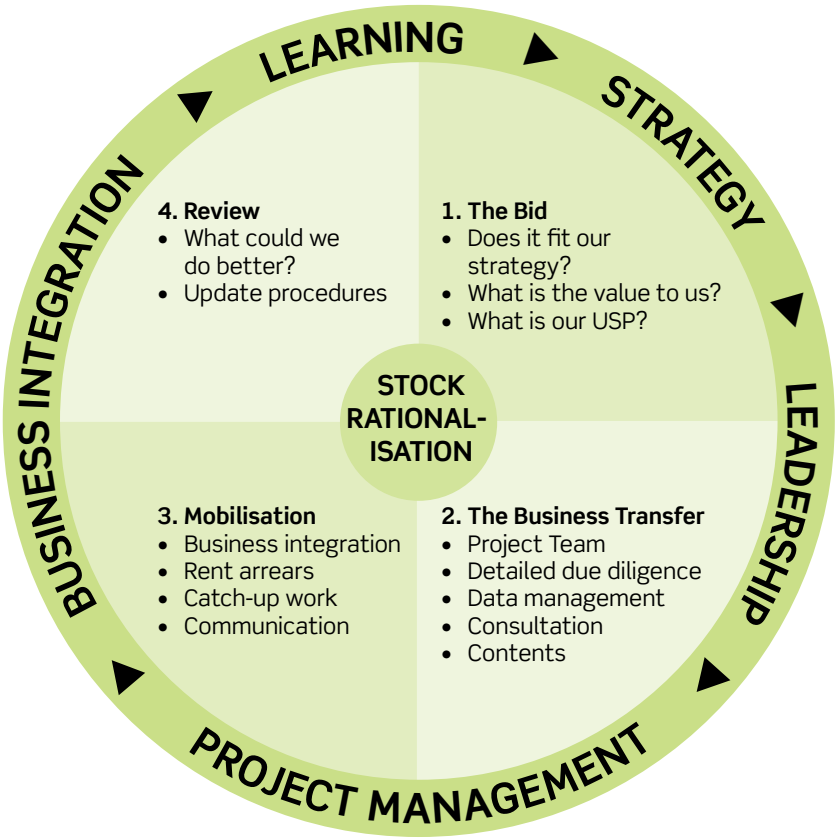
Project management

It is very easy to under-estimate the scale of internal resourcing required to manage a rationalisation project of any size effectively. We have developed a clear process for managing projects, which helps us to analyse and plan the kind of resource support we will need at any stage of a given project. Each of these stages needs to be properly resourced; the organisational impacts will be felt more by different teams at different times. High quality support from back office functions is also essential to enable the frontline teams to do their jobs effectively both pre- and post-transfers.

A senior level project sponsor is important to help drive the entire process, ensure effective resourcing is in place, and provide the authority to get things done to planned timescales. While external consultants can help with a range of issues, projects need to be driven by a well-directed, high capability internal project team.

Successful transfers take months of intensive effort and resourcing, irrespective of the size of a project. Without very careful planning, it is easy for a large rationalisation to knock organisations off balance and adversely affect performance.

The strategic and financial benefits of stock rationalisation need to be strong enough to justify the investment.





Financial evaluation

Given the resource and wider organisation implications and the potential levels of risk attached, the strategic and financial benefits of stock rationalisation need to be strong enough to justify the investment. In the current environment of spending constraint and increased efficiency, stock rationalisation has to compete for investment and resources alongside new development and other service options.

Take the following notional example:

	Newbuild £ per home		Transfer £ per home
Cost less grant	135,000 (45,000)	EUV-SH	45,000 *
Funding	90,000	Funding	45,000

* Any Social Housing Grant will also be transferred to the new landlord

Obviously, stock valuation is central to any financial evaluation. Yet valuing stock for transfer is as much art as science. The Existing Use Value as Social Housing (EUV-SH) is driven by stock condition and rental income. But it also needs to take account of all future liabilities, and sometimes these will not be fully apparent until due diligence has been undertaken and, occasionally, not even then.

In addition, strategic considerations and other potential 'value added' aspects of the deal – for example, geographical consolidation, improving the stock base and organisational influence within particular localities, or improving contract and management efficiencies - can make the payment of a premium above EUV-SH appropriate. Any subsidy or premium level may need to be judged against organisational subsidies for new build and the likely future costs in use.

This assumes newbuild homes built fairly recently under the old grant regime and a broadly typical EUV for a scheme in a reasonable condition and area.

It shows that for the cost of a new build property, two existing homes might be acquired. If we then assume that some level of subsidy is added to the EUV for strategic fit or other benefits, say a 33% premium, then it is still possible to acquire three existing homes for every two new homes which could be built. This equation should take account of the future investment needs of the transferring stock.

In reality, of course, things are rarely as neat as this would suggest. Affordable Rents, welfare reform, the book values of any new stock included in stock packages and many other factors change the equation. With less grant now available and at lower rates, a recently completed project could still be a sensible acquisition despite the book cost being significantly greater than EUV-SH.

But while the financial evaluation is not entirely simple, taking a strategic view will always help decision making. We see stock rationalisations and new development as complementary activities, both contributing to our growth and asset management strategy, to building our balance sheet, and to our overall purpose as a housing association.

'Value added' aspects of the deal ... can make the payment of a premium above EUV-SH appropriate

Transaction and resource costs

The related project and transaction costs should be seen in the same light. It is too simplistic to suggest the costs of one type of rationalisation project will be lower or higher. A great deal depends on the complexity of individual projects and the breadth and rigour of the budgeting. For example:

- the transaction and resourcing costs of smaller rationalisations can be disproportionately high, depending on the level of complication.
- additional costs within management agreements, beyond fee levels, can get hidden in day to day revenue expenditure, rather than separated out.
- post-transfer costs, such as extra in-year costs of absorbing and training transferred staff, can be forgotten or dismissed.
- other internal or external costs can be easily missed; for example, a lender's fees for charging or removing properties from charge.
- management agreement projects may not have a dedicated budget, with costs picked up through day to day revenue financing.
- costs tend to be capitalised on successful acquisitions.

At Sovereign, we have now established a 'benchmark' average transaction and resourcing cost for our stock rationalisation projects. It is not perfect, but it does provide a baseline for us to judge expenditure on future projects.

It is important to accept that there is a cost to playing in the stock rationalisation market, including on unsuccessful and abortive projects.

Advantages and disadvantages

While we cannot be categoric about whether buying, swapping or managing homes represents the most cost-effective type of stock rationalisation, we can say something about the potential benefits of each.

As indicated above, most managers prefer a straight acquisition or disposal to a swap or management agreement, because a straight sale or purchase should be considerably simpler. As we have seen, an acquisition will also deliver more homes than new build for the same investment, plus the transaction costs can be capitalised.

But acquisitions tend to be more opportunistic too. Depending on the nature of the opportunity, this can make for some difficult judgement calls, balancing the desire for relatively swift and cheap growth in stock and income with broader strategic considerations. In use maintenance costs for acquired stock will also generally be higher than for newly built homes and this needs to be factored in.

Committing to a stock swap will generally involve some real depth of thought around the strategic fit beforehand. Swaps often entail a high degree of negotiation and strong project management, preferably using an experienced team. The resident and staff communication issues are effectively doubled compared to other types of rationalisation. However, if the will is there on both sides, a set of agreed core principles can be met and there is agreement on stock valuation, swaps can kill two rationalisation birds with one stone and bring genuine strategic benefits.

Management agreements will always carry some degree of financial risk, in that mistakes in determining the level of management fee may lead to revenue deficits which cannot be recovered during the contract. Excellent communications are also needed to ensure residents understand the arrangements.

Further burdens can arise from the need to manage a different set of systems and processes, together with the additional performance monitoring and reporting requirements. The managing housing association cannot simply apply its own standards and procedures. Moreover, each management agreement is different and if multiple agreements are in place the level of management complexity can be significant. Maintaining operational performance and quality can be difficult.

However, management agreements often come about when one party is ultimately looking to sell the stock and the other ultimately looking to buy. For example, book values on new stock may not make it sensible to sell the properties in the short term, but the equation will change over time. If the strategic fit is strong, then the shorter term hassles may be more than offset by the benefits of being in 'pole position' with intimate knowledge of the stock when it eventually comes up for sale.

A great deal depends on the complexity of individual projects and the breadth and rigour of the budgeting.

4. Some key lessons by theme

1. Commitment is essential

An underpinning strategic direction makes choosing and committing to suitable rationalisation projects much easier

- If rationalisation and growth is seen as part of the core activity of the organisation and there is a clear asset management strategy, the prospects of senior level commitment and appropriate resourcing and authority to deliver desired outcomes is greatly improved.
- Sovereign has now created a senior post to manage rationalisation opportunities within a strategic framework.
- The lead manager must understand the 'business' in the round – this is not a development activity.

Projects must be properly resourced from start to finish

- The project team should include all key disciplines from the start, including finance and rent accounting, housing management, property services, IT, HR, communications, and the frontline customer enquiries team.
- Experience within the team of previous projects often saves time and money.
- It's very difficult to bolt-on rationalisation projects to people's day jobs. Free them up as far as possible.
- Projects don't end on the day of completion. Post-transfer issues will almost certainly continue for 3-4 months, and large scale integrations can take a year or more to bed down. Ensure there is project team support for operational staff to smooth transitions of people and processes.

The project team must have the authority to deliver the required outcome

- Team members should have clear responsibilities and timescales for their parts of the project and the authority to require others in the organisation to support delivery on time.
- Try to avoid significant organisational change during a rationalisation project restructuring can' disrupt processes, move key staff and lose continuity and momentum.

Make time to review completed projects

- Monitor satisfaction levels and views of transferred residents and staff.
- Attempt to cost any work that was not foreseen.
- Build the learning into future projects.
- Take time to learn from failed bids or negotiations too.



2. Understand your market

Understand the marketplace you are going into

- Including key issues like grant rates, funding positions, etc.
- Talk to key consultants and get proper market intelligence.

Understand the drivers and motives of the other party

- Do they want a better local service for their residents or simply a windfall receipt?
- Are they acting openly, transparently and honestly, or seemingly concerned only with maximising the final price?

Understand the stock and social profile you are receiving

- Serious problems can arise if your housing managers are not properly prepared for a stock or resident profile that is quite different to your norm.
- The asset register may not tell the full story. Different organisations categorise stock in different ways.
- Understand the nature of any third party agreements.
- The ultimate costs of failing to research these issues can be the difference between a successful and unsuccessful project.

3. Closely manage the process

Make sure your full project team is in place on day one

- Ensure all relevant disciplines are represented, including frontline staff who will have to handle operational issues as soon as the transfer is complete.
- A dedicated internal project 'champion' is important even where consultant project managers are used to ensure decisions and information requests are 'officially' authorised and acted upon.

Get your key plans in place early

- Including the overall project plan, resources plan and communications plan.
- Scope all main tasks, prioritise them and assess risks.
- Put the project meetings schedule in place.
- Agree your monitoring and progress review procedures.
- Agree a methodical system to version control key documents.
- Establish a process to allow for resident involvement in decisions affecting them.

Meet the key players from the other party early

- An early meeting helps to build personal relationships and trust.
- Agree how you intend to share information.
- Set up your joint project meetings schedule.
- Establish the links and contacts between counterparts.

Standardise the process wherever practicable

- For example, Sovereign now has a checklist of data required for effective due diligence.
- Using a tried and tested framework and standard processes can help to minimise risks and ensure all key issues are taken into account before transfer.
- Experienced consultancy support can help to ensure developed processes are applied thoroughly.

Take account of the operational cycle

- You can avoid unnecessary difficulties by arranging transfers for an appropriate point in the normal business cycle, eg. year-end, with all its changes, rent increases and additional processes is not a good time for transfers.
- Choose a date that fits with your cycle of rent debits and benefit payments.

Plan the post-transfer period

- The better your communications and process planning, the smoother the post-transfer is likely to be.
- Ensure project managers are available to deal with the inevitable post-transfer issues that will arise.
- Prepare your frontline staff and provide any necessary training to cope with new processes or anticipated issues.
- Build in the time for key staff to meet residents and TUPE-d staff early to start creating trust and establishing relationships. Produce proper welcome packs and induction processes for transferring residents and staff.

4. Good communications are vital

Poor communication will cost time, resources and potentially your reputation

- First impressions are hugely important – make them favourable.
- Expectations need to be managed. Only promise what you can deliver.
- Tone should be 'professional, but human' throughout.
- It's difficult to recover momentum if you get your messages or timing badly wrong. It can take a long time to get your reputation back on track with residents and staff.

Plan in detail

- Ensure offer documentation and presentations give a realistic picture. Raising expectations too high carries risks, if delivery cannot sustain the promises.
- Co-ordinate the communications plan content and timing with the other party, including agreeing any issues requiring confidentiality, and ensure it is owned and monitored at a high level in both organisations.
- Agree your key messages for residents, staff and stakeholders early on. Anticipate concerns, but recognise the need to adapt plans as projects develop.
- Walk through the entire project process in detail and decide what to communicate when and how.
- Don't forget your own staff and their needs.
- Don't forget the differing needs of leaseholders.
- Build on and adapt previously successful communications and plans.

Face to face communication is time consuming but often more powerful

- Open forums and informal events for residents can be a valuable way of flushing out potentially important issues before transfer.
- Involving housing staff who will later manage properties can be a helpful kickstart to relationships and trust-building
- Allowing transferring residents to meet their peers from the other party is often very well received.

Think post-transfer

- The immediate post-transfer period is generally a key time for increased enquiries and issues.
- Resource your call centre or enquiries team adequately to deal with increased volumes.
- Agree your messages on all anticipated issues, like rent arrears management, and ensure they are known by all relevant staff.
- Remember to thank involved staff and celebrate successful outcomes.

5. Prepare for a wide range of financial issues

Financial impacts and issues can range from the highly strategic – having adequate financial capacity in place – to the deeply operational, like ensuring utility supply information and contracts do not result in financial loss.

Use a consistent methodology when valuing stock for transfer

- We use a well-developed net present value (NPV) model and required rate of return.
- Any level of subsidy or premium offered in a bid should relate clearly to added strategic value in the deal and is a judgement call in each case.
- Compare assumptions on forward maintenance from vendors with assumptions your organisation uses on its own stock and from your own viewing of the stock, and model likely costs and any catch-up repairs into your valuation.
- Be aware of how shared ownership homes may impact on valuation, particularly where 100% staircasing is allowed. Lenders often have strong views on this.
- Consider how nomination rights may affect stock use and therefore value. Stock with lower nomination rights is more flexible and potentially valuable.
- Where recently developed stock is involved, the net book value will be greater than EUV-SH, due to higher capital cost and lower grant. In these instances, consider 'value' at book (net cost of development) rather than Existing Use as Social Housing.
- Where tender information and data is inadequate, post-tender negotiations on price following due diligence should be expressly allowed for and seen as an opportunity to mitigate risk.
- Agree an overage clause on any properties subsequently sold at higher than the transfer valuation, unless there is agreement to recycle later capital receipts into reprovision of services.

Consider the full range of rent issues early on

- Rent arrears should be dealt with using an agreed formula. The formula (eg. the CIPFA formula) should allow for the receiving housing association to pay a banded percentage of the arrears outstanding, based on the overall level of arrears.
- Consider any adaptation of systems needed to deal with any differences in rent year on Management Agreements, eg. some housing associations work on a 48 week year, others a 52 week year.
- Identify any issues related to rent increases and convergence to target rents.
- Ensure completion does not impact on the timing of rent increase notices, to avoid legal complications around imposition of increases.
- Try to ensure benefits data sent to local authorities is accurate and complete, including full names, addresses and numeric identifiers. Poor benefit administration and wrong payments can take a lot of work to resolve and impinge on other areas of rent administration.
- A new variable is the potential impact of Affordable Rents on value and relet policy.

Standardise provision of information where possible

- A pre-agreed spreadsheet format on required service charge information, including supporting financial information, is helpful to understand charging practice, for example.
- For sinking and renewal funds, agree that funds transferred match with the last actual statement, plus any funds collected and expended since.
- For utility supplies, ensure reconciliation of meter numbers, locations and suppliers for all gas, water and electricity supplies, plus any unadopted street lighting. Include information on any preferential contract rates.

Procurement frameworks can reduce professional fees

- Include provision and service cost levels for stock rationalisation in any relevant frameworks you procure, eg. legal services, stock surveying, etc.
- Consider accessing frameworks procured by others, eg. for stock rationalisation consultants, legal services, etc.

Ensure all charges on the properties are discharged in good time

- Slow discharge of properties can delay completion of transfers.
- Title searches during due diligence should highlight any issues.
- Make sure that properties taken off charge, stay off charge.


Allow for VAT on Management Agreements

- The client housing association will be liable for VAT on the management and repair costs charged by the managing housing association.

Budget carefully for the costs of each rationalisation process

- Take a broad approach to assessing costs, beyond external professional fees.
- There is a need to accept from the start that costs are at risk until completion. While successful bids can capitalise costs within the acquisition, unsuccessful bid costs will need to be written off.

6. Properly planned staff support will save time and money later

HR teams from both parties should joint manage the transfer of staff closely

- Establish an HR sub-team of the joint project team.
- Agree a joint communication plan and process early on, including consultations with staff and any recognised trade unions.
- Confirm the terms and conditions of incoming and outgoing staff as early as possible to allay fears and offer clarity.
- Ensure wide ranging support is available to those transferring out of your organisation as well as those transferring in.

Give proper attention to inducting transferring staff to your organisation

- 'On the job' training from others in similar roles is unlikely to be enough.
- Train incoming staff in office processes, IT systems, service standards, and the cultural values of the organisation.
- One to ones and group meetings with incoming staff are helpful. Give them the opportunity to visit your offices and meet their new colleagues.
- Loss of staff during the process can lead to a fall in management or maintenance standards and increased issues post-transfer.
- The same job titles between organisations do not always mean the same role.

Take care to fully understand the roles and duties of all transferring staff

- Even within an organisation, staff with the same title may not all perform the same role, eg. caretakers on different estates.
- Some roles may be new to your organisation and require time and resource to understand and make consistent with your own standards.

Consider the impacts on and support needs of non-transferring staff

- Loss of part of a team's portfolio or, conversely, a sudden jump in homes managed within teams, will have clear impacts and require careful management. Management structures may need to be adapted.



7. Avoid disputes over repairs and maintenance

Effective planning on repairs is vital for building or maintaining trust and reputation

- Repairs and maintenance is often the most contentious issue for residents.
- Maintaining a full repairs and management service up to completion should be made a condition of the transfer.
- Where a backlog of repairs items is agreed within the valuation of the stock, the acquiring association should aim to institute a programme of catch-up repairs as soon as possible after transfer, and the position should be made clear to residents.

Clarity over the cost base is crucial on management agreements

- Responsive repairs are normally recharged at cost or the management fee will take account of the average annual repair cost per unit.
- Where planned maintenance works are included within the agreement, be clear in advance which association's forward maintenance unit costings will be used.
- Where the client association's costings or stock condition modelling is to be used, the managing association should validate the figures for themselves to ensure sustainability and avoid potential additional costs.

8. Quality of data and information is key to understanding future costs

Poor data and information present serious cost and management risks

- Lack of commitment to good data and information provision can lead to delays, aborted projects and damaged relationships. Hangover issues can have management and financial impacts over several years.

Know the data you need and how you will use it

- Create a checklist of data and information requirements needed to facilitate a transaction. Give it to the other party at an early stage in discussions.
- If the other party is unwilling to provide certain information or seems not to appreciate the potential risks, negotiate around sharing of risk and financial consequences and feed the results through to the final price and contract.

Commit resources and authority to drive the data gathering

- Finding records and data, particularly on older stock, can be a challenge. It can take time, resource and authority to deliver to sufficient quality.

Where possible, undertake a sample audit of records, such as tenancy files and rent accounts

- This helps test the accuracy of supplied data.
- It can identify matters for negotiation prior to contract.
- It also provides a valuable way to assess how data and records can be merged after transfer.
- It can help prioritise tasks post-transfer.

Meetings and visits to residents can be valuable tools

- They can help highlight issues that may inform the bid price, such as allowing for CCTV, upgrading entrance doors, etc. to deal with anti-social behaviour
- They can help prioritise and direct housing management resources post-transfer.
- They may uncover unexpected local contractual arrangements which need to be accounted for and managed.

Put time and effort into validating the stock included in the transfer

- Always conduct your own stock survey, including an internal sample.
- Explore more unusual types of stock within the portfolio carefully.
- Again, stock validation can uncover important management issues.
- It is not unusual for associations to want to package poorer stock with better stock. Be clear about what you are getting and price accordingly.

9. Get the IT right

Establish a joint IT sub-team to manage the relevant issues

- On projects of any size, the IT teams will need to agree an interface and file transfer mechanism between their respective systems for rent account and tenancy data.
- On one Sovereign project, a file transfer protocol site was set up by the IT teams to share documents and information. This worked well and enabled good document management control.
- Involve housing and finance staff as necessary so they understand any data transfer issues and are prepared in advance.
- All staff teams involved should be able to easily access all relevant data.
- Bring in system suppliers to provide training on data transfer issues and interfaces, as necessary.

Test data integrity and processes before running live

- Cleanse the data and test systems properly.
- Where large numbers of properties are involved, an extended period between exchange and completion can be useful to deal with final data cleansing, testing and transfer issues.

Encrypt all personal data and only send relevant information

- It is unusual, but not unknown for an entire unencrypted tenancy database to be supplied!

10. Contractual concerns

Terminating service contracts reduces risks and simplifies management

- Termination allows the receiving association the opportunity to apply its own standards, rather than running differing contract terms, specifications and standards across its stock holdings.
- Consider any TUPE implications regarding contractors' employees, and allow for these in the transfer or management agreement.
- It may well make sense to maintain a contract associated with a specialist installation on the stock.
- Ensure a plan is in place to maintain continuity and quality of service delivery as contracts are terminated.

Use legal teams with stock rationalisation experience wherever possible

- If both sides have experienced legal teams, this should avert delays and unnecessary issues.
- Good experienced project management, whether internal or outsourced, can support and facilitate effective legal input.

Understand all the approvals needed

- Consent to dispose from the HCA (if disposing)
- Freeholder consents for leasehold property
- Lender consents for funding and charging/discharging
- Agreements from other contractual partners, eg. service contractors.

5. Conclusions

Like most housing associations involved in stock rationalisation projects, our learning curve has been steep. But our level of experience and expertise is now significant, and we have the processes in place to manage opportunities of virtually any shape or size.

Stock rationalisation is not about buying houses, it is about buying businesses – homes, tenancies, customers, management arrangements and all of the ancillary supports that go alongside them. Rationalisation projects carry potentially significant financial, service quality and reputational risks.

Whatever the type of rationalisation, the approach to projects has to be right to achieve beneficial results. There are certain key things our experience has taught us:

- The acute importance of a strategic approach to asset management and growth. Rationalisations should be strategy-led, not opportunity-led.
- The need for effective resourcing and high level sponsorship of projects, both internal and external, by both organisations.
- The need for thorough due diligence and for trust and good relationship building at all relevant levels between the parties. The better the data, information and trust on both sides, the simpler the process.
- The benefits of a strong financial evaluation of the likely value of the rationalisation project, linked to strategic considerations and the possible alternative uses of the investment.
- The high value of good communications planning and execution in maintaining staff commitment, managing uncertainty, and establishing positive early relationships with transferring residents and staff.

With these basic principles applied, our experience is that stock rationalisation can make an important contribution to organisational strategic objectives.

Housing associations have become more efficient in recent years and are getting better at managing assets effectively. But these twin pressures are only likely to increase over the coming difficult years. The nature of housing association growth over the past 40 years means that stock rationalisation has a long way to go before the sector can genuinely claim to be managing asset portfolios as well as possible. Getting the strategy, processes and risk management right is essential to delivering successful projects.

A note on methodology

Our brief to Ark Housing Consultancy was for a short, sharp review of our activity in the stock rationalisation market. The study involved five stages:

- Data gathering and review for six agreed projects.
- Interviews and meetings with key Sovereign staff involved in rationalisation projects, including a SWOT analysis, alongside discussions with staff from the housing associations we have conducted projects with.
- Analysis of the information gathered to identify key themes and learning points.
- A workshop with key managers to test and verify the findings.
- Development of the report.

Inevitably, the recollection of managers on both sides of projects was not always complete, particularly for older projects, and some information was simply unobtainable. Some people had also moved on to pastures new. However, Ark was able to quickly assemble an extensive evidence base and the key findings from the study are robust and consistent across the range of projects.

Ark was chosen for its extensive experience of stock rationalisation projects, including integral involvement in the transfer of over 3,000 homes in a wide variety of localities and for a range of clients. It has acted at times for both transferors and transferees.

The study was developed and managed by Ark partner, John Fisher, and senior consultant, Colin Davis. The report was written by Simon Graham at Blue Sky.

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