

# Final Business and Regulatory Impact Assessment

## **PROPERTY FACTORS (SCOTLAND) ACT 2011: CODE OF CONDUCT FOR PROPERTY FACTORS**

### **Background**

In 2009 the Office of Fair Trading produced a market study of residential property managers in Scotland. The study highlighted the perceived problems within the industry and made some recommendations as to how the sector can move forward.

The study highlighted that there was a lack of information available to property owners. Many of them did not understand their rights and obligations, were unsure what they should expect from their property manager and the standard of service that should apply.

The report set out some key recommendations. These included property factors providing homeowners with a written set of services; detailed financial breakdowns (including invoices); explanations of how and why particular contractors had been appointed; complying with the Financial Services Authority (FSA) guidelines on disclosure of commission on insurance; and operating a complaints procedure. The report also recommended that if self-regulation of the industry does not work, the Scottish Government should take the lead in introducing statutory legislation to ensure it is effective.

In 2010, the Scottish Government undertook a consultation on the proposed standards for a voluntary accreditation scheme for property managers. However, this was overtaken in June 2010, by the introduction of the Property Factors (Scotland) Bill. This was a Member's Bill brought to the Parliament by Patricia Ferguson MSP. The Bill was passed by Parliament with support across the chamber, and received Royal Assent on 7 April 2011. All provisions of the Act will come into force by 1 October 2012.

The Act contains three main elements; registration of all property factors, a statutory code of conduct against which all property factors are obliged to operate and a dispute resolution system called the homeowner housing panel.

### Register

Under Section 12 of the Act, operating as a property factor unregistered will be a criminal offence. Registration will be administered by the Scottish Government and aims to open for applications in July. The Act states that the register must be publicly available and defines a list of information that property factors must supply (see section 3(2)(a) to (f) of the Property Factors (Scotland) Act 2011). In addition, the Act includes provision for Ministers to use a power (set out in section 3(5) of the Act) to make regulations to charge property factors a fee to register. It is the Scottish Government's intention to use this power.

### Code of Conduct

The code of conduct is one of the central provisions of the Property Factors (Scotland) Act 2011. Section 14 of the Act provides that Scottish Ministers must from time to time prepare a code of conduct setting out minimum standards of practice for registered property factors. The draft code has been developed and consulted on and this BRIA relates predominantly to its introduction.

## Dispute Resolution – Homeowner Housing Panel (HHP)

Part 2 of the Act introduces a new dispute resolution system for homeowners – the homeowner housing panel (HHP). Homeowners may apply to the HHP for determination of whether a property factor has failed to comply with the Code of Conduct or otherwise carry out their duties. The HHP will be based on an expansion of the existing Private Rented Housing Panel (PRHP). There is no cost to homeowners to raise a case with the HHP, and in the initial period of operation the costs of operating the HHP will be met by the Scottish Government.

### **Objective**

The primary objective of the Property Factors (Scotland) Act 2011 is to create a statutory framework to protect homeowners in Scotland who use factoring services. The Act will apply to all residential property and land managers whether they are private sector businesses, local authorities or housing associations.

The code of conduct sets out the minimum standards of practice that factoring organisations must comply with. It includes requirements to provide information to their home-owning customers. This information should be clear and transparent so that homeowners know what they are paying for, how the charges were arrived at and the routes available to them if they wish to make a complaint.

### **Rationale for Government intervention**

The rationale for Government intervention was initially in response to the perceived problems highlighted in the Office of Fair Trading market study 2009. The voluntary accreditation standards for the industry were developed in response to this study. .

The introduction of the Members Bill by Patricia Ferguson MSP and the subsequent Royal Assent of the Property Factors (Scotland) Act 2011 superseded this work and placed a statutory duty on all property factors to register, and required the development of minimum standards for the industry and the introduction of the homeowner housing panel by 1 October 2012.

The duty under section 14 of the Act, to prepare a code of conduct against which the industry will operate, and its introduction through the accompanying order, is the focus of this Business and Regulatory Impact Assessment.

The aims of the Act, and within it the Code of Conduct, will contribute to the following National Outcome: *“We value and enjoy our built and natural environment and protect it and enhance it for future generations.”*

### **Consultation**

- **Within Government**

A number of teams, departments and agencies were engaged in and made contribution to the preparation of the code of conduct. The lead policy team was Housing Options and Support Division, part of the Housing, Regeneration, Commonwealth Games and Sport Directorate. This team drafted the code of conduct and progressed this to consultation. This was undertaken with significant support from Law Reform Division and Scottish Government Legal Services.

There was further contribution from the Scottish Tribunal Service who were particularly engaged in terms of the interaction between the code and the new homeowner housing panel (HHP). The HHP will become part of their remit when the Act is in force from 1 October 2012.

Dialogue was held with the Scottish Housing Regulator to ensure that there are no conflicts between the requirements placed on housing association property factors by the code, and the requirements of SHR's regulation of registered social landlords.

Contributions and advice were also sought from Scottish Government Accountancy Services and Accountant in Bankruptcy in relation to the financial and banking requirements of the code.

- **Public Consultation**

The starting point for development of the code was the information contained within the draft standards for the voluntary accreditation scheme for property and land managers. The scheme was developed by a working group with 15 key stakeholders within the industry. This included the Chartered Institute of Housing, local authorities, Property Managers Association Scotland, Scottish Federation of Housing Associations, the Law Society and the Office of Fair Trading.. The draft standards were subject to a full public consultation in Summer 2010.

A full public consultation on the draft Code of Conduct was conducted over 12 weeks from September to December 2011. As part of this, 11 consultation events were held, in Glasgow, Edinburgh and Aberdeen. At each location, sessions were organised for the private sector, the social sector and members of the public, including:

- Private sector property managers
- Local authority property managers
- Registered social landlord property managers
- Land maintenance companies
- Customers of property managers
- Customers of land maintenance companies

Overall, 138 written consultation responses were received and two thirds of them came from private individuals including 2 MSPs. The consultation event and responses were analysed by ODS Consulting and an analysis report, and the individual responses received, were published on the Scottish Government's website on the 16 February.

- **Business**

Dialogue with the property factoring industry has been held at various stages throughout the development of the code of conduct, including with:

- Property Managers' Association Scotland
- Association of Local Authority Chief Housing Officers (for COSLA)
- Scottish Federation of Housing Associations
- Scottish Housing Best Value Network private sector housing forum
- Royal Institution of Chartered Surveyors
- Asset Skills Scotland

As well as various individual organisations who carry out property factoring services.

Specific impact assessment interviews were held with six organisations across the industry. (Further details of the outcomes from these are included under the section on Scottish Firms Impact Test).

## **Options**

Section 14(1) of the Act provides that the Scottish Ministers must from time to time prepare a code of conduct setting out minimum standards of practice for registered property factors. Therefore "do nothing" is not an available option – Scottish Ministers have a statutory duty under the Act to prepare a code of conduct. Given that the code is one of the central provisions of the Act it would not be appropriate to seek alteration of this element of the Act.

Given that the code of conduct must set out **minimum** standards of practice for registered property factors, the options relate to the detail to be included within the content of the code, and what level is appropriate to set as a minimum standard below which no property factor in Scotland must operate.

Three levels/options were considered:

*Option 1 – Lower standards*

A low level that all existing practitioners would be able to achieve with minimal changes to their business practices. Introducing some consistency across the industry and basic protections for homeowners on only those matters judged to be essential. At this level, organisations would not be required to provide their customers with a Written Statement of Services.

*Option 2 – Medium standards*

A medium standard that most existing practitioners would be able to meet, with greater or lesser degrees of change required dependent on current business practices. A consistent standard across the industry and protections for homeowners on a range of matters. Organisations would be required to provide their customers with a Written Statement of Services.

*Option 3 – Higher standards (best practice)*

A high standard that only some industry practitioners would be likely to successfully meet, requiring significant changes to business practices. Organisations would be required to provide their customers with a Written Statement of Services which would include an increased number of best practice principles.

- **Sectors and groups affected**

All parts of the Act, including the code of conduct, will affect:

- Property factors – including private sector property factors and land maintenance companies, housing associations and local authorities.
- Homeowners who use the services of a property factor – including both owner-occupiers and owners who rent out their property.

The Act provides a definition of both “property factor” (section 2) and “homeowner” (section 10(5)).

- **Benefits**

*Option 1 – Lower standards*

Introducing lower standards would remove the requirement for organisations to provide their customers with a Written Statement of Services. This would reduce the burden on property factors to collate and detail the services that they provide. The risk of any property factor failing to comply with these standards will be much reduced. They will be less challenging and will limit the changes required from existing practices. Setting the minimum standards at a low level would potentially reduce the number of complaints reaching the homeowner housing panel and therefore reduce the number of Property Factor Enforcement Orders the business may receive. In turn this will mean that it would have a lower adverse effect on the operation of a business.

The position for homeowners would still be better than the status quo, because there would be an increased assurance of consistency in practice across the industry. This would be reflected in the delivery of a higher standard of service.

It would be less costly for registering organisations to comply with a set of low standards than it would if higher standards applied. Property factors are also more likely to register if the code sets low 'achievable and realistic' standards.

The other provisions of the Act, registration and the homeowner housing panel, would be in force whatever level the Code is pitched at.

The position for homeowners is better than Options 2 and 3 because:

The low level of requirements would mean that practically all property factors could comply with the code, reducing any risk of businesses being unable to meet the statutory standards. The worst case scenario of setting standards too high is that businesses could close leaving homeowners without property management arrangements.

*Option 2 – Medium standards*

The medium standards will include a Written Statement of Services which will improve transparency and boost the level of protection for homeowners. The Written Statement will clearly provide homeowners with the full range of services their factoring organisation should be providing. This Statement will be used as a guide by the homeowner housing panel for cases that come before them.

The medium standards provide a proportionate balance of principles to improve and enhance industry practice; reflection on existing good practice in relation to customer relations and financial practice; and the introduction of additional good practice (already in place in some sectors of the industry) by way of the Written Statement of Services.

This option will deliver increased standards across the industry yet will be more achievable and fit-for-purpose than if higher standards were set. It would be more difficult for the industry to uniformly achieve and maintain higher standards. Higher standards would potentially increase the number of homeowners seeking redress through application to the homeowner housing panel. And if found by the HHP to have failed to comply with code, the property factor may be deregistered and ultimately prevented from operating. It is therefore less likely that business failure will result if medium standards are applied.

The position for homeowners is better than Options 1 and 3 because:

Homeowners will receive a better level of service and improved transparency with regard to the services received through the introduction of a Written Statement of Services than they would if low standards applied. At the same time homeowners are less likely to be left without a factor than if higher standards were set which were difficult for business to meet and maintain.

Setting higher standards will increase the cost to property factoring organisations. This cost will in turn be passed onto homeowners. The increase in fees could potentially be unaffordable to homeowners and may as a consequence increase the number of business debtors, and the number of groups of homeowners who choose to cancel their property factoring arrangements altogether. This could have a detrimental affect on this sector in that the required income stream to carry out repairs on buildings may not be available. This could potentially lead to business failure and ultimately escalate the number of buildings falling into disrepair.

The timeframes for which all elements of the Act have to be in force are very tight. Setting the standards too high would make it less likely and perhaps unachievable for organisations to be compliant by the 1 October 2012 deadline.

### *Option 3 – High standards (best practice)*

Introducing standards which would include best practice to be implemented industry-wide would mean that property factors would be required to provide their customers with a higher quality of service. In turn, this would more closely address the issues raised in the Office of Fair Trading market study (2009).

Although setting higher standards will make it more difficult for a property factor to comply with the statutory code of conduct, it will increase the level of satisfaction for homeowners. As a result, the introduction of higher standards may see a greater number of factoring organisations who are operating at a lower level put out of business. This in turn would ensure that only the best organisations were operating in Scotland.

#### The position for homeowners is better than Options 1 and 2 because:

Homeowners will receive the highest possible level of service and an increased level of protection.

- **Costs**

#### *Option 1 – Low standards*

Compliance with a Code of Conduct that is pitched at a lower level would have the lowest cost to the industry. Introducing standards which are not as challenging to the industry and that allow for limited change to existing practice would mean that the financial impact would be limited.

The main area of cost that may be removed through introduction of lower standards is the requirement to issue a Written Statement of Services to all homeowners. Although lowering the cost to the industry this option would significantly reduce the impact of the Act and reduce the transparency in the relationship between the homeowner and their property factor.

#### *Option 2 – Medium standards*

The cost of pulling together the Written Statement of Services has been identified as the largest anticipated cost to factoring organisations in relation to complying with the code of conduct. As identified above, some property factors already produce and issue a large amount of the information requested in the Written Statement of Services. As such, the cost to implement will vary across the industry. This is further the case depending on the business/portfolio size, staffing arrangements and current IT technology and ability.

Discussion with a couple of businesses as part of the BRIA interviews estimated this cost to be in the region of £40-50k, other businesses stated that they had not identified costs for this element. All businesses suggested that costs will be passed onto homeowners.

#### *Option 3 – High standards (best practice)*

The more detailed and stringent the statutory code of conduct, the greater the effect on the industry. To uniformly introduce a wide range of best practice measures would incur a level of cost that may not be proportionate to all sectors of the industry.

In turn, this may lead to smaller businesses unable to meet and maintain the required standards. As noted above, this could lead to increased cases being brought to the homeowner housing panel and subsequent costs to defend the case, business lost through bad publicity and ultimately business closure.

The consequential impact of this being that it could affect parts of the industry that are presently operating well and whose practice the Act is not aiming to address.

A further consequence of any reduction in the size of the industry or business closure would be an increase in the number of tenemental properties (in particular) that are left without a property factor and are subsequently unmaintained. This would result in a decline in the standard of maintenance of common parts and may contribute to the overall deterioration of parts of the housing stock.

### **Scottish Firms Impact Test**

Interviews were conducted with a cross section of the industry to gather evidence of the various issues that may affect them when the Act comes into force on the 1 October 2012. The type of industries consulted included public sector factoring organisations (a local authority and two registered social landlords), two traditional property factor organisations from the private sector and a land maintenance organisation.

Overall, the industry gave positive support for the Act and intimated that its provisions will be welcomed. The perceived cost implications in relation to the code of conduct are highlighted below:

The industry were asked to consider what additional costs they will incur in relation to compliance with the code. The biggest anticipated cost was in relation to the provision of the Written Statement of Services to their customers. Overall the industry expect that this will have one of the greatest impacts on them, both in terms of costs and time to develop and issue for each household. The costs anticipated include legal fees to review existing contracts, and where required title deeds, printing, branding, training, and updating of existing welcome packs.

None of the businesses approached were in a position to formally quantify the cost of introducing the requirements of the code of conduct and it was recognised that costs will vary across the industry depending on the portfolio size and existing practice. The highest costs to implement will be faced by businesses who do not hold relevant information or have practices in place.

However, many organisations agreed that they already provide their customers with much of the information specified in the code and this element does not present a significant challenge as long as there is no instruction for all business to present the information in a uniform format that would require all existing documentation to be reworked. This is not the intention set out in the Code.

The time required to source, review and check the contractual agreement or the arrangement set within Title Deeds for each individual property has been identified as a concern. Businesses will have to identify the extent to which this requires to be done for properties that they manage and again there is variation across the industry of those who are well placed with this information and others who have not taken this approach to date. In response to this, the timeframes for providing the customers with the Written Statement of Services has been increased to allow the workload and cost of compiling this information to be spread over the course of the first year. The only exception would be where the Statement is requested sooner by the homeowner or the homeowner housing panel, in which case it should be provided within four weeks of the request. This news was welcomed and the majority of businesses stated their intention to provide their customers with the Written Statement in a single mail shot. The annual billing period was identified as a optimum time to issue.

Businesses interviewed passed positive comment on the introduction of the code of conduct as it will improve the relationship with homeowners and increase the transparency and knowledge of the services that homeowners will receive. In turn, it was identified that this may reduce the number of complaints received and thus reduce the number of homeowners who withhold their factoring fees in contest to the services that they have received, under the view that they are contrary to the service agreement.

At present, some homeowners withhold payments as the easiest route for redress. The Written Statement will provide customers with details of their property factor's in-house complaints procedures and how to make an application to the homeowner housing panel. It is hoped that this will improve communication and ease of access to a more appropriate solution.

- **Competition Assessment**

The code of conduct will have no bearing on, and will not directly limit, the number or range of property factoring businesses in operation. The code will not raise costs to smaller businesses relative to the costs for larger organisations. All principles in the code will apply equally across the industry and costs of implementing will be proportionate to the size of the business. There will be no impact on the ability of suppliers to compete.

The code will ensure that homeowners will receive a transparent breakdown of information and costs for the services they receive but this information will not be supplied to competitor businesses.

- **Test run of business forms**

The code of conduct does not create any new business forms.

### **Legal Aid Impact Test**

Customers of factoring organisations will not be charged if a case goes to the HHP, and there is no requirement or expectation that they will be legally represented during the proceedings.

### **Enforcement, sanctions and monitoring**

All registering organisations will be expected to adhere to the conditions stated in the code of conduct. If a registered organisation fails to comply with the code of conduct, their home-owning customers can register a complaint through the organisation's own complaints procedures. If the issue remains unresolved, the complaint can be taken to the homeowner housing panel where, depending on the outcome, the factor can be issued with a Property Factor Enforcement Order.

Failure to comply with an Enforcement Order will be a criminal offence. Failure to comply with the code of conduct or with a Property Factor Enforcement Order can also be taken into account by Scottish Ministers when making decisions about whether to enter a property factor on the register or remove them from the register.

### **Implementation and delivery plan**

The Property Factors (Scotland) Act 2011 has a commencement date of the 1 October 2012 when all elements of the Act will come into force. This includes the register and the code of conduct (Part 1 of the Act), and the homeowner housing panel as the dispute resolution mechanism (Part 2 of the Act).

- **Post-implementation review**

The impact of implementation of the Act will be closely monitored following the 1 October implementation deadline. The code of conduct will be monitored to ensure that its provisions are appropriate.

The government will monitor for the first three years, and will then evaluate its operation to establish whether changes are required, with a view to implementing changes if necessary during the second three-year period.



## Summary and recommendation

When the Property Factors (Scotland) Act 2011 comes into force on the 1 October 2012, all provisions of the Act will be applicable.

The intention of the code is to set minimum standards of practice within the industry. It also forms an important part of how the homeowner housing panel determines if a registered organisation has contravened the law in relation to the Act.

Three options were considered in relation to the setting of minimum standards. These were *Option 1 – Lower standards*, *Option 2 – Medium Standards* and *Option 3 – Higher Standards*. After considering the pros and cons of each option, it is recommended that the code of conduct's minimum standards are set at a **medium** level for the following reasons.

- The provision of a Written Statement of Services for each homeowner will provide a higher level of transparency regarding the services to be received. This will in turn strengthen the relationship between the property factor and the homeowner and provide a clear benchmark for any discussion or address of any complaint regarding approach to work or work that is deemed unsatisfactory or not complete. It will also provide a clear signpost to homeowners on their entitlements to access further information and procedures if they wish to progress any complaint.
- The code of conduct forms the basis on which the homeowner housing panel (HHP) will make decisions on how a factor has performed. Therefore, it is important that the HHP have a clear statement of what services the factor should be providing their customers. The Written Statement of Services provides the HHP with this crucial information.
- Setting the standards too low will fail to take advantage of this opportunity to improve practice across the industry and clearly instruct a better relationship between homeowners and their property factor. A key element of this is transparency in knowing what services are to be provided and rights as a homeowner to access information.
- The main aim of the code of conduct is to raise the standards across the industry and provide clear and transparent information to their customers. The timeframes for which the code of conduct will come into force are very tight. The level at which these standards must be applied has to be achievable within the 1 October 2012 deadline. Setting the standards too high would place an increased burden on the industry to deliver in what is already a challenging timescale.

It is important that in deciding what level the code should be set, certain things should be considered. How much it will cost, time and money, for the industry to comply with the code? And will this cost increase be passed onto their customers? The code will most likely see property factors' costs increase to some extent and the industry has identified that these costs will be passed onto homeowners. It is important therefore that these costs are of an appropriate level so as not to put at risk the raising of standards. The consequences of having a substantial increase in costs is that homeowners would challenge, and in certain instances may be unable to afford the increased levy. This in-turn may make it increasingly difficult for businesses to recoup costs and could lead to business failure. The consequential affect of this could be that there may not be enough money to carry out repairs on buildings and thus fall into disrepair. This would have the opposite effect on what the Act intended.

Option	Total benefit per annum: - economic, environmental, social	Total cost per annum: - economic, environmental, social - policy and administrative
Option 1: Low Standards	<ul style="list-style-type: none"> <li>• Minimal cost and procedural impact to the industry</li> <li>• Reduced chance that the whole industry will be unable to comply</li> <li>• Factoring fee increases to homeowners will be minimal</li> </ul>	<p>Minimal</p> <p>Cost will vary across the industry depending on the portfolio size and existing practice.</p> <p>The highest costs to implement will be faced by businesses who do not hold relevant information or have practices in place.</p>
Option 2: Medium Standards	<ul style="list-style-type: none"> <li>• Homeowners will receive an improved service and transparency.</li> <li>• Standards across the industry will be improved</li> <li>• Clarity for homeowner and the HHP through the provision of a Written Statement of services</li> <li>• Reduce the chances of homeowners withholding payments as they now have clarity over their services through the Written Statement</li> </ul>	<p>Manageable</p> <p>Cost will vary across the industry depending on the portfolio size and existing practice.</p> <p>The highest costs to implement will be faced by businesses who do not hold relevant information or have practices in place.</p>
Option 3: High Standards	<ul style="list-style-type: none"> <li>• The highest possible standards will be provided to their homeowner customers</li> <li>• Will route out any bad factoring organisations so that only the best are left operating</li> </ul>	<p>Significant</p> <p>Cost will vary across the industry depending on the portfolio size and existing practice.</p> <p>The highest costs to implement will be faced by businesses who do not hold relevant information or have practices in place.</p>

## **Declaration and publication**

I have read the Business and Regulatory Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs. I am satisfied that business impact has been assessed with the support of businesses in Scotland.

**Signed:**

**Date:**

**Keith Brown MSP  
Minister for Housing and Transport**

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