

**Report by the
Comptroller and Auditor General**

The Housing Corporation

Overseeing Focus Housing Association

Ordered by the
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Executive summary

Background

1 In April 2000, three men were sentenced to prison terms for corruption in relation to the purchase of homes from a Birmingham property dealer (see box) by Focus Housing Association (Focus), the largest registered social landlord in the West Midlands. Between 1991 and 1995 the property dealer made corrupt payments to two Focus employees to ‘oil the wheels’ for the purchase of around 50 homes by Focus for £1.8 million. Focus uncovered the corruption in November 1995, as a result of an anonymous tip-off, and informed the Housing Corporation (the Corporation).

Corruption and overpayments at Focus

Between 1991 and 1995 Focus Housing Association bought at least 47 houses for £1.8 million from Darshan Ram, a Birmingham property dealer. These purchases were organised by Focus’ deputy development director, John Hartshorn and his assistant, Keith Hinson. Over the period, Focus bought a further 95 rental properties from other property dealers.

Most of the properties Focus bought from Ram were back-to-back deals, that is Ram had himself purchased the properties on the open market only a day or two before selling them to Focus.

Ram paid Hartshorn and Hinson at least £5,450 and £16,300 respectively to reward them for the favourable treatment they showed him. In April 2000, Ram was sentenced at Birmingham Crown Court to 18 months imprisonment, Hartshorn was sentenced to 12 months and Hinson 9 months.

Investigations at Focus found that the Association paid more than market value for many of the properties it bought from property dealers, although only Ram appears to have made corrupt payments as an inducement for the deals.

2 Subsequent investigations by Focus found that it had paid more than the market value for the properties. Other overpayments relating to the purchase and renovation of properties by Focus were also uncovered. As a result of these overpayments, it is estimated that Focus and its tenants have borne the cost of unnecessary expenditure of £1.09 million, although the actual sum may be lower or higher than this because property valuation is not an exact science. Focus was able to recover £250,000 of this loss from its insurers. Focus was also required to pay back grant of £198,000 to the Corporation for sums overpaid on these properties.

3 This report examines the Housing Corporation’s oversight of Focus Housing Association. We examined the Corporation’s regulation of Focus from the Association’s formation in 1991 to 1998, when the Serious Fraud Office decided to

instigate criminal proceedings. We reviewed files held by the Housing Corporation at its headquarters and at its West Midlands regional office, and files held at Focus. We also interviewed relevant staff at Focus and the Corporation's headquarters and received information from former staff from the Corporation's West Midlands regional office. Now that the prosecution has been brought to a close, the matters central to this report are no longer sub judice and we are able to report our findings.

4 Part 1 of this report describes the corruption and overpayments suffered by Focus in more detail, and outlines the Housing Corporation's role in relation to Focus and other registered social landlords. Part 2 examines the Corporation's oversight of Focus and considers whether it did enough to detect and act on the weaknesses at Focus prior to being notified of the fraud allegations, and whether it took appropriate action after being notified. Part 3 examines the wider implications of the Focus case, in particular what the Corporation did to determine whether Focus was an isolated case and the steps it took to prevent a reoccurrence of the type of property fraud and mismanagement which occurred at Focus.

Main findings

5 Our main findings are set out below.

The Corporation's reviews of Focus before 1995 did not identify the potential for fraud and corruption

Between 1991 and 1995 the Corporation carried out regular routine reviews of Focus. Although these reviews identified procedural weaknesses at the Association, they failed to highlight the lax management culture and disregard of internal control within the Association's development function, which allowed the corruption to take place and remain undiscovered for four years (paragraphs 2.1-2.6). A Corporation internal investigation of its regulation of Focus identified weaknesses in its regulatory procedures, which it revised in the light of experience in this case (paragraphs 3.6-3.7 and 3.10).

The Corporation should have taken more action in response to allegations it received in 1994

The Corporation did not take sufficient steps to investigate allegations of corruption by Hartshorn it received in 1994. It did not inform Focus in writing of the allegations and other information it possessed, nor ensure that Focus carried out an investigation into the allegations (paragraph 2.8). The Corporation's own investigation found mistakes in the way it had dealt with the allegations. More

vigorous action by the Corporation could have resulted in closer attention being paid to Focus' development function, and this in turn might have led to the corruption and overpayments being discovered earlier (paragraphs 3.8-3.9).

When Focus reported the corruption, the Corporation took prompt and effective action to improve Focus' management

After Focus itself reported corruption allegations to the Corporation in November 1995, the Corporation took prompt and effective action to investigate and protect public money and placed Focus under close supervision (paragraph 2.9). Focus has improved its management and performance, a process which began with the arrival of a new Chief Executive in April 1994, and since 1997 the Corporation has no longer considered the Association as a cause for concern (paragraph 2.12).

The Corporation took steps to ensure that other housing associations were unaffected by similar corruption

Upon the discovery of the corruption and overpayments at Focus, the Corporation took immediate action to investigate the property dealings of other West Midlands registered social landlords. The investigation was hampered by difficulties in obtaining complete data on associations' property dealings but found no evidence of back-to-back property deals or purchases from Ram or his nominees by other landlords in the West Midlands area (paragraph 3.2-3.5).

The Corporation reviewed its regulation of Focus, and revised its procedures as a result

As a direct result of the Focus case, and its investigations into its handling, the Corporation redesigned its regulatory systems to obtain greater assurance that landlords in receipt of significant development grants have effective systems of internal controls. Since 1995, it has also introduced other regulatory changes designed to enhance the standards of management and governance within landlords and its regulation of those standards (paragraphs 3.11-3.13).

Now that the criminal case is over, the Corporation intends to disseminate the lessons learned from this case

The Corporation employed consultants to review the lessons learned from this case, but criminal proceedings meant that these could not be published. Now that the case is no longer sub judice, the Corporation intends to publish the lessons of the Focus case to other registered social landlords (paragraphs 3.14-3.15).

Conclusions

6 The Corporation's regulation of Focus before 1995 could have been better, and the corruption possibly brought to light sooner. However, the Corporation did react quickly and positively to the corruption's eventual discovery in November 1995. The Corporation has also taken steps to review and improve its regulatory processes, and plans to disseminate the lessons learned from this case. Our main conclusions are:

- regulators should be concerned not just with the existence of internal controls within the bodies they regulate, but also with their continued operation. In particular, it is important that they be assured that there is a management culture which does not allow controls to be disregarded. The Corporation's procedures were insufficient to identify the general laxity in Focus' property services, although these procedures have since been revised to provide greater assurance about management controls in registered social landlords.
- regulators should handle allegations on a formal basis rather than rely on informal contact with the body concerned. The Corporation should have passed the allegations in full and in writing to the Association, demanded a formal response, and followed up to ensure that the allegations had been investigated. Planned guidance to registered social landlords and Corporation staff on how to deal with allegations should improve matters.
- when corruption like this occurs or is suspected, regulators should quickly ascertain whether the corruption goes wider than the case immediately under investigation. The Corporation took sensible steps to rule out the possibility of wider-scale corruption affecting other registered social landlords in the West Midlands.
- it is important to learn lessons from experiences such as the Focus case. The Corporation has carried out internal and independent reviews of its procedures and how they were applied, and intends to publicise the lessons learned now that the case is no longer sub judice.
- the Corporation does not operate a whistleblowing line that affords protection to informants from within registered social landlords. Nor do the external auditors of registered social landlords have a reporting responsibility to the Corporation on key aspects of compliance, unlike

their counterparts in some other sectors. The Corporation and the Department of the Environment, Transport and the Regions are considering whether these steps, if practicable, might help prevent and detect corruption and impropriety.