The Agency for Co-operative Housing
L'Agence des coopératives d'habitation

Annual Portfolio Performance Review: 2010

Introduction

One important element in the Agency's accountability framework is the provision of an annual review of the performance of the portfolio of housing co-operatives operating under the CMHC programs administered by the Agency. This report serves that purpose. As in 2009, it offers a high-level view of the portfolio, occasionally looking at specific subsets of the whole. In future years, we expect to supplement our annual portfolio review with occasional studies that more closely examine areas of special interest.

We continue to see measurable improvement in most indicators of portfolio performance. When we set the performance our clients reported in 2010 against earlier results, it is clear that we are moving toward the achievement of the three principal objectives set out for the Agency by CMHC: more effective management of the portfolio at a comparable or lower cost; continued benefits of co-operative housing for Canadians; and improved client satisfaction within the portfolio. While in one area or another, our advance may stall for a year, the general direction is unmistakeable. It is also clear that we have further to travel before reaching our ultimate goal.

This document addresses the specific performance indicators laid out for each of the first two objectives.

Our first comprehensive client satisfaction survey, undertaken and published in 2008, showed that the Agency's commitment to a service culture had brought about strong improvement in client-satisfaction levels since we first assumed responsibility for the portfolio. Our second survey is now underway. The data collected will reveal how satisfaction rates have evolved in the last three years.

As we noted, the Portfolio Report compares our clients' status and the results they delivered in 2010 with those achieved earlier. In most sections of this report, 2007 is used as the base year; it is the first year for which the Agency obtained comprehensive data for all regions. The area of compliance is treated differently. Because the items the Agency identifies as compliance variances were significantly reassessed in 2008, a comparison with 2007 results would not be meaningful. We have therefore compared the compliance status of the portfolio at the end of 2010 with that at the end of 2008.

2010 Portfolio Overview

Portfolio Facts & Figures

Total number of co-ops in the 2010 dataset: 511

Distribution by Program:		
S27/61	53	10%
S95	311	61%
FCHP (ILM)	126	25%
UN/PEI NP*	5	1%
Multiple	16	3%
*excluded from program-related charts		
Distribution by Province:		
B.C.	181	35%
Alberta	50	10%
Ontario	270	53%
PEI	10	2%
Distribution by Management Model:		
Management	203	40%
Paid Staff	203	40%
Bookkeeper (Paid)	70	13%
Volunteer Only	35	7%

The 2010 Portfolio Review uses data drawn from 511 Annual Information Returns (AIRs) filed for fiscal years ending at any time from August 2009 to July 2010[1]and validated by the Agency by January 15, 2011. The 2007 dataset consists of data from the equivalent fiscal year and the equivalent period of 2006-2007. Appendix A has more information on the 2010 dataset and the use of constant dollars in this review.

The distribution by program, province and management model of the 511 housing co-operatives that make up the 2010 dataset is representative of the full Agency portfolio. The breakdown by region and program is essentially unchanged from 2009. The distribution by management model has changed a little, with a drop of two percentage points in co-operatives employing their own staff and a one-point rise in each of the management and paid-bookkeeper categories.

Compliance with Operating Agreements

The purpose of the Agency's compliance-management program is to ensure that public funds expended under the co-operative housing programs are used as intended and properly accounted for. The backbone of our approach is the annual compliance review, carried out following the receipt and validation of each client's Annual Information Return.

The Agency classifies variances according to the following criteria:

Breach: an operating- or workout-agreement compliance failure having an impact on the viability of the co-operative in the short term or that could result in public funds committed for the program being misused or being perceived to have been misused.

1. Throughout this report, except where the context otherwise requires, "2010" refers to a year ending any time between August 1, 2009 and July 31, 2010.

Material compliance variance: an operating- or workout-agreement compliance failure that does not threaten the viability of the co-operative in the short term but that, if left unresolved, could have an impact over the longer term; the compliance failure will not result in public funds committed for the program being misused or perceived as being misused.

Minor compliance variance: a variance from the operating or financial workout agreement or program guidelines that neither has an impact on the co-operative's short- or long-term viability nor results in public funds committed for the program being misused or seen to have been misused.

The objectives set out in the Agency's agreement with CMHC make reference to improving levels of compliance with operating agreements across the portfolio, measured in various ways:

- **Increased program knowledge within the portfolio, as evidenced by increased compliance with project operating agreements**

At the end of 2010, 71 per cent of housing co-operatives in the dataset were fully compliant with their operating-agreement obligations. This showing is slightly higher than at the end of 2008 (69%), and Table 1 below—a breakdown, by broad class, of the numbers and percentage of co-operatives with variances—also indicates improvement in the severity of compliance failures. Seven per cent of our clients were in breach of their agreements at the end of 2010, down from ten per cent two years earlier. In 2010 another nine per cent were found to have material variances (2008: 14%). (As discussed further on, there is overlap between co-operatives in these two categories.)

Readers should note that the table of operating-agreement variances includes policy variances, resulting in an overstatement of operating-agreement non-compliance. Just under eight per cent of all variances outstanding at the end of 2010 related to CMHC's Net Operating Revenue Policy. Compliance with this policy, which the Agency strongly encourages, is not an operating-agreement obligation. Nevertheless, we are pleased to report seeing fewer instances where clients have not adhered to it (2010: 21; 2008: 27).

In order to facilitate comparison, for the purposes of this review some of the compliance variances noted in the 2008 report have been reclassified to conform to the Agency's current classification system.

Table 1: Co-operatives Not in Full Compliance				
	Number of Co-ops		Percentage of Portfolio*	
	2008	2010	2008	2010
Total Clients not in Full Compliance	**155**	**147**	**31%**	**29%**
Co-operatives with Agreement Breaches	49	34	10%	7%
Co-operatives with Material Variances	68	47	14%	9%
Co-ops with Minor Variances	98	106	19%	21%

* percentage of co-operatives in the dataset that show a variance of this kind

We should note here that some clients are out of compliance with more than one obligation, manifesting any combination of variances from a severe breach to a minor variance, and that a single client may appear in more than one of the categories above.

As will be apparent when Table 1 is reviewed in conjunction with Table 2: Compliance Variances by Type, 269 variances were associated with 147 co-operatives. In each category the total number of variances exceeded the number of clients with variances of that severity.

- **Stable and, over time, improved levels of operating-agreement compliance within the portfolio, as evidenced by a decline in the number of operating agreement breaches and material compliance variances**

As shown in Table 2, agreement breaches fell from 59 at the end of 2008 to 51 at the end of 2010. The total incidence of breaches and material variances, taken together, dropped from 134 in 2008 to 123 in 2010.

Table 2: Compliance Variances by Type
(Listed by order of incidence in 2010)

	2008	2010
Breaches		
Subsidy-Surplus Fund Breaches (Return of Excess Income-Tested Assistance, Allocation of Earnings)	17	19
Mortgage Arrears	13	7
ITA Reconciliation More than 3 Months Overdue	12	6
Required Percentage of Subsidized Members not Met for Two Consecutive Years	6	6
Annual Information Return More than 3 Months Overdue	4	5
Audited Financial Statements More than 3 Months Overdue	5	4
Property Tax Arrears	2	2
Verification of Incomes	0	1
Setting the Assisted Housing Charge	0	1
Total Breaches	**59**	**51**
Material Variances		
Capital Replacement Reserve Variances (Contribution Rate, Funding, Permitted Investments, Spending from Fund on Ineligible Items)	67	58
Failure to Verify Incomes at Required Intervals	6	12
Other	2	2
Total Material Variances	**75**	**72**
Minor Variances		
Capital Replacement Reserve Variances (Allocation of Earnings, Spending from Fund on Eligible Items without Advance Approval)	11	53
Non-application of Net Operating Revenue Policy	27	21
Audited Financial Statements Less than Three Months Overdue	18	16
ITA Reconciliation Less than 3 Months Overdue	17	12
Annual Information Return Less than 3 Months Overdue	11	8
Failure to Verify Incomes at Required Intervals	0	8
Security-of-Tenure Fund Contribution not Made in Full	11	7
Subsidy-Surplus Fund Variations (Permissible Investments, Funding)	14	6
Other	0	5
Errors in Setting the Assisted Housing Charge	8	4
Failure to Observe Income Ceilings/Ingoing Incoming Limits	5	3
Rent Supplement Assistance (Verification of Incomes and Setting the Assisted Charges)	0	3
Total Minor Variances	**122**	**146**
Total Variances and Breaches	**256**	**269**

Note: Variances for 2008 have been reclassified to conform to the Agency's current compliance classification system.

- **Fewer co-operatives in the portfolio in default of their financial obligations, as evidenced by fewer instances of mortgage or property-tax arrears**

At the close of 2010, the Agency saw seven co-operatives with mortgage arrears, a significant reduction from 13 in 2008.

Portfolio Risk Profile

Each year, the Agency performs a comprehensive risk assessment of every co-operative in its portfolio. Following the review, we assign a composite risk rating that reflects our considered view of the co-op's current health and future prospects, based on separate evaluations of financial strength, current financial performance and physical condition. These are examined in the context of the market environment and other risk factors, such as the sufficiency of the co-op's capital replacement reserve. Although strongly informed by the results of standardized tests performed for each client, the rating is ultimately judgement based. As appropriate, we will adjust it over the course of the year in response to external developments or to the co-op's actions. Possible risk ratings of Low, Moderate, Above Average and High are defined in Appendix B: Definitions of Composite Risk Ratings.

Five indicators of success set out in the Agency-CMHC agreement are tied to the risk profile of the portfolio:

- **Increased awareness by co-operatives of their own performance, as evidenced by an improvement in the overall risk profile of the portfolio**

The chart below compares the distribution of composite risk ratings at December 31, 2010 with ratings from the end of 2007. Looked at as a whole, the portfolio's risk profile has seen measurable improvement over the past three years: while co-operatives with a rating of Above Average or High made up 62 per cent of our portfolio at the end of 2007, three years later the share of co-ops at risk had dropped six points to 56 per cent. This, despite a slow rise over the period in the proportion rated High risk, from 15 per cent in 2007, to 16 per cent two years later, to 17 per cent in 2010. At the other end of the scale, the number of clients with a Low composite rating stood at 11 per cent at the end of 2010, up from one per cent in 2009 and four per cent in 2007.

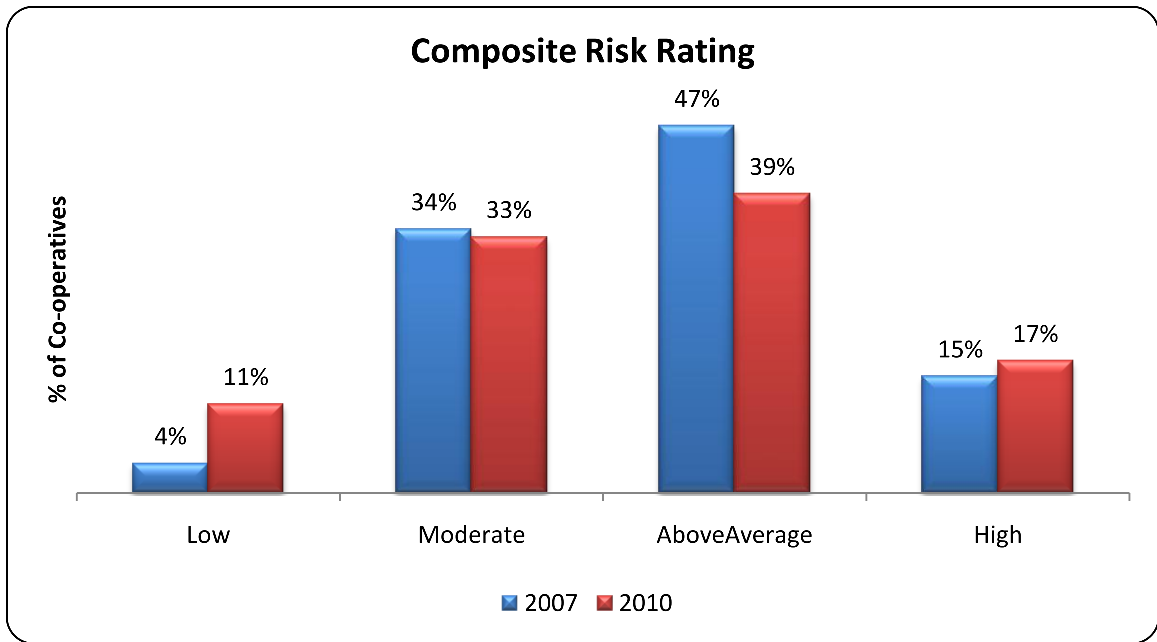


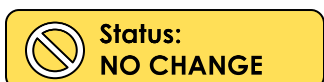
Figure 1

A counter influence during the past three years on the portfolio's improving risk profile has been the arrival of co-operatives that CMHC initially held back while it put a financial workout in place. Since 2007 43 new clients have come to the Agency, increasing our portfolio by nearly nine per cent. Of the 36 new arrivals that we were able to assess by the end of 2010, 33, or 92 per cent, received an initial composite rating of High or Above average. We observe, however, that more than a third of those first rated High have since seen their rating shift to Above Average, and one is now rated Low.

- **Improvement in the overall risk profile of the portfolio, as evidenced by a declining number of co-operatives rated High and a stable or growing number of co-operatives rated Low or Moderate**

Results against this performance indicator are mixed. Significant change within the portfolio has taken place in the last three years, with only 49 per cent of Agency clients holding the same composite rating at the end of 2010 as at the end of 2007. Thirty-one per cent of our clients saw their rating improve over the three-year period and 20 per cent saw it weaken. The proportion of co-operatives carrying a High composite rating has risen one percentage point in each of the last two years and now stands at 17, compared with 14 three years ago. Significantly, however, the three-year period since 2007 has also seen an increase of seven percentage points in the number of co-operatives rated Low risk and a decrease of eight points in those at Above-Average risk.

- **Increasing percentage of under-performing co-operatives, as determined through the risk-rating system, that are not under a workout arrangement, returned to financial health without a cash injection from CMHC Insurance or Enhanced Assistance ("underperforming" and "financial health" defined, respectively, as scoring Poor on either of the liquidity or net-income indicators or Fair on both and as scoring at least Fair on both the liquidity and net-income indicators, with no scheduled mortgage or property-tax payments overdue)**



Last year we judged it too early to report results against this indicator, noting that changes observed over a two-year time scale in individual indicator ratings might not signal a sustained trend. This year, our analysis of the data shows the following: in each year after 2007, 75 per cent of reporting co-operatives met the definition of financial health. (Two criteria must be satisfied: scoring no worse than Fair on each of the liquidity and net-income indicators and having no arrears of scheduled mortgage or property-tax payments.) From one year to the next, about 12 per cent of clients in the portfolio changed their status in this regard, half of them moving in one direction, half in the other. Looking at changes in status among underperforming co-operatives that do not have a workout in place, as defined above, we note that, so far, all those that returned to financial health did so without recourse to Enhanced Assistance or a cash injection from CMHC Insurance. If we extend the timeline to three years, we find one co-operative that needed CMHC assistance to return to financial health, out of 34 clients that were in better financial health in 2010 than in 2007.

It remains too early, in our view, to claim a victory against this indicator. As more time goes by, it will be possible to extend our analysis and determine whether a sustainable trend has emerged. As we did in our last report, however, we should point to two factors that we expect will have a strong bearing on longer-term performance against this indicator: contributions to capital-replacement reserves and the revenues our clients earn. The Agency is strongly promoting growth in both, with meaningful results: as discussed later in this report, growth in contributions to reserves in the portfolio has outstripped inflation several years running, while fewer co-operatives are either dropping their housing charges or holding them steady, opting most often to raise them at a rate exceeding the general inflation level.

- **improved financial health of the portfolio, as evidenced by an increasing percentage of co-operatives with a Good or Excellent liquidity ratio, and an increasing percentage of co-operatives with a Good or Excellent net-income ratio**

Performance against this indicator has improved since 2009, when we rated it as weakening. Looking at 2010 results, we see that the share of the portfolio with a healthy liquidity ratio has remained stable over the past three years, moving from 79 per cent of the dataset in 2007 to 78 per cent. In the same period, the proportion with strong net-income ratios declined from 70 per cent to 58 per cent. This apparent result is deceptive, however; when we made improvements to our risk-rating model in 2010, we introduced more conservative thresholds for the net-income ratio. If all results are recalculated using the new thresholds, the proportion of clients with healthy net-income ratios is seen to be stable, having dropped only one point from 56 per cent in 2007 to 55 in 2010. The median ratio fell over this time from 0.85 in 2007 to 0.81 in 2010—still a Good rating. Strong increases in the insured replacement cost of our clients' properties account for much of the decline, since this value is used in the calculation of the indicator score.

The decrease in the percentage of co-operatives with a Good or Excellent liquidity ratio (79% to 78%) owes something to the addition to our portfolio, over the period, of clients initially retained by CMHC while a workout was put in place and later transferred to the Agency: a minority of these co-ops came over with a healthy liquidity ratio. Notwithstanding this influence, the median liquidity ratio has increased from 9.2 to 9.9, a rating of Excellent.

Turning to the question of clients rated Good or Excellent on *both* indicators, something the performance measure above does not speak to, we observe that this group fell from 63 per cent of the dataset in 2007 to 51 per cent in 2010, as the chart below shows:

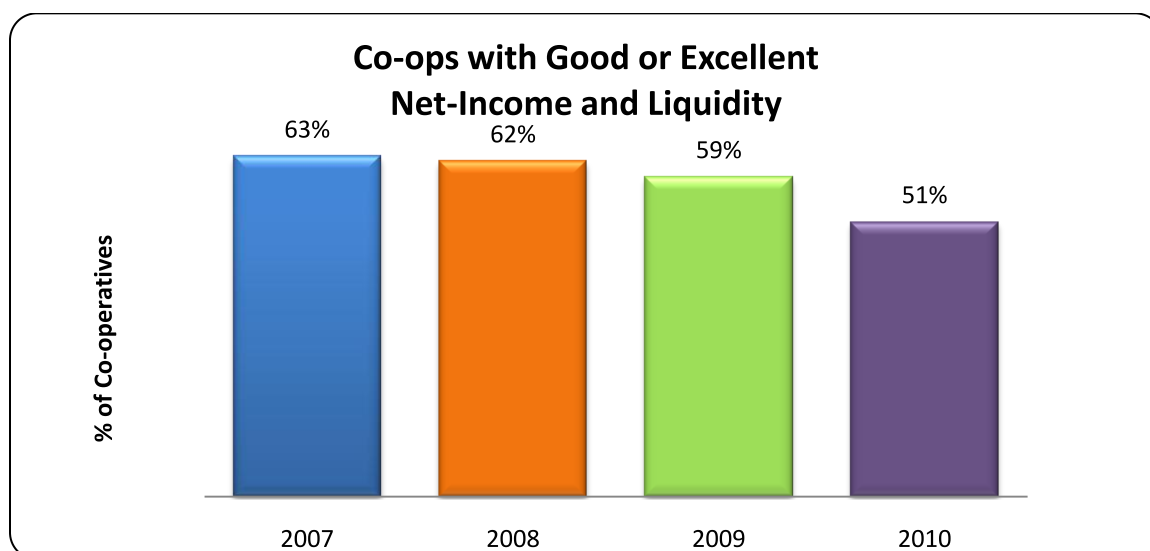


Figure 2

However, when the older results are recalculated to apply the newer net-income indicator thresholds, the percentage of clients rated Good or Excellent on both indicators is seen to have shifted down only four points, from 51 per cent to 47 per cent.

- **improved physical condition of the stock, as evidenced by a stable or growing number of co-operatives with a physical-condition rating of Good or Excellent and a declining number of co-operatives with a physical-condition rating of Poor**

Physical-condition ratings across the portfolio have shown a small but measurable improvement over the past three years. In 2010, 82 per cent of co-operatives received a positive property-condition score—either Good or Excellent—compared with 77 per cent three years earlier. Meanwhile, the segment rated Fair declined from 22 per cent in 2007 to 17 per cent in 2010. The proportion holding a Poor rating was one per cent in both years. Given that aging properties normally face an accelerating need for maintenance and capital repairs, this result is more impressive than it might at first appear.

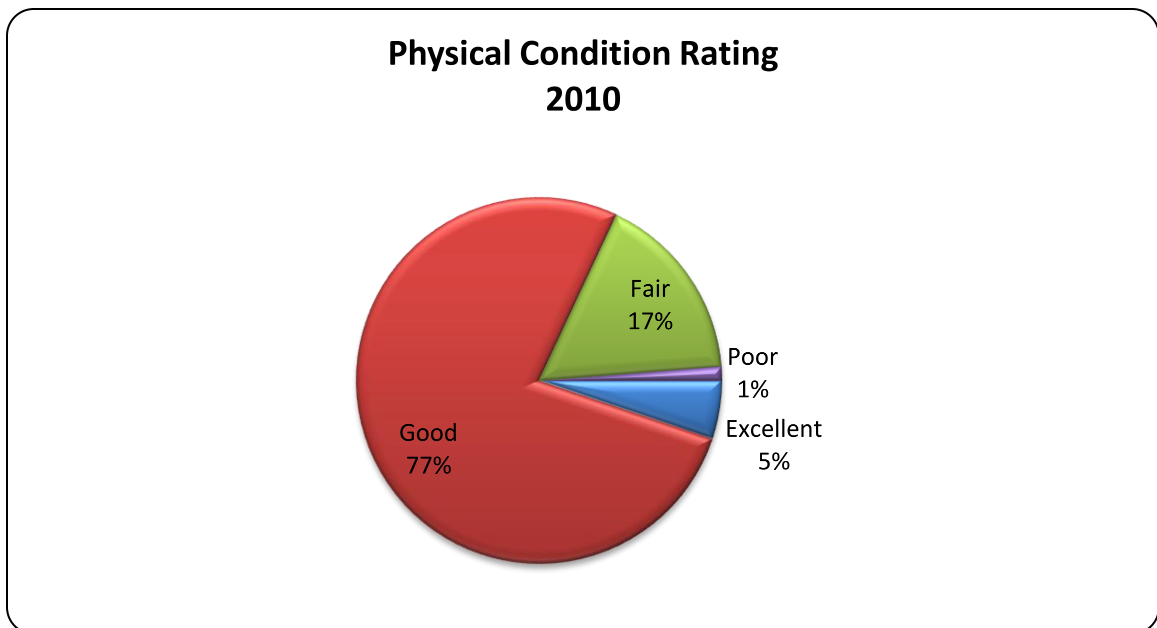


Figure 3

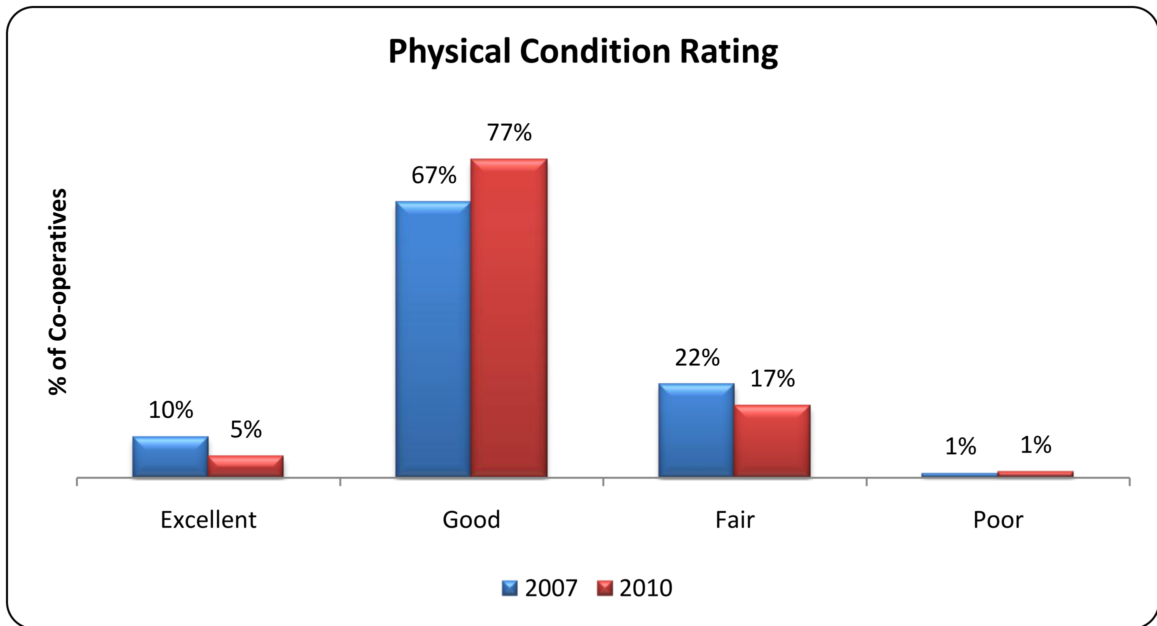


Figure 4

The decline from 2007 in co-operatives carrying an Excellent physical condition rating may be explained by the portfolio's increasing age. That said, it is worth noting that the proportion stood at only two per cent a year ago. The improvement may be the result of significant capital work undertaken with the assistance of funds from the first phase of the federal government's Social Housing Retrofit and Renovation Initiative. If this is true, further improvement in the condition of the portfolio should be apparent in our next two reports. The Agency normally inspects each co-op once every two years, the length of time during which the initiative was in force. Depending on the timing of the capital work and the scheduling of our inspection, it could be 2012 before we record an improved physical-condition score.

Client Operating Performance

Under the Agency's Agreement with CMHC, three indicators of success are associated with better operating performance for co-operatives in the portfolio. The third—improved financial health, as evidenced by an increasing percentage of co-operatives with fully funded replacement reserves—is reviewed further on. The other two are as follows:

- **more cost-effective use of rent-geared-to-income assistance resulting from project operating efficiencies**

As the discussion under the next indicator reveals, the period 2007 through 2010 has seen a decline in rental arrears, bad debts and vacancy losses in the portfolio as a whole.

Reduced revenue leakage is an operating efficiency and—all else being equal—entails more effective use of rent-geared-to-income assistance as the need to increase housing charges lessens. Moving the draw on rent-geared-to-income funds in the opposite direction, however, is the Agency's push to have co-ops raise their charges to members in order to bolster capital-replacement reserves, or to offset operating losses, where these have occurred. (Such housing-charge increases will deliver long-term benefits to the portfolio in the form of improved financial health and reduced risk.) In view of these two opposing forces at work, we rated the portfolio as stable against this indicator, although it is obvious that without the noted operating efficiencies the need for housing charges to rise would be yet greater.

- **improved management practices, as evidenced by reduced occupancy-charge arrears and bad-debt expenses, vacancy losses and other relevant measures**

  The status of this indicator is examined in each of several sections dealing with specific elements of good management.

Occupancy-Charge Arrears and Bad-Debt Expense

Across the portfolio, the period 2007 to 2010 saw a decline in combined arrears and bad-debt expenses, measured as a percentage of the total amount charged to occupants for housing during the year. While the median ratio moved little between 2007 and 2009 and remained steady in 2010 (2007: 0.9%; 2009 and 2010: 0.8%), to see significant improvement one need only look at either the growing percentage of Agency clients with a ratio of 1.5 per cent or less (two-thirds of the portfolio in 2010, up five points from 2007) or the shrinking proportion with arrears and bad debts of three per cent or more, which has dropped six points, or 29 per cent, since 2007 and two points from 2009.

The combined per-unit dollar amount of arrears and bad-debt expenses also fell during the period, as Table 3 on the next page shows. arrears and bad debts averaging $75 per unit.

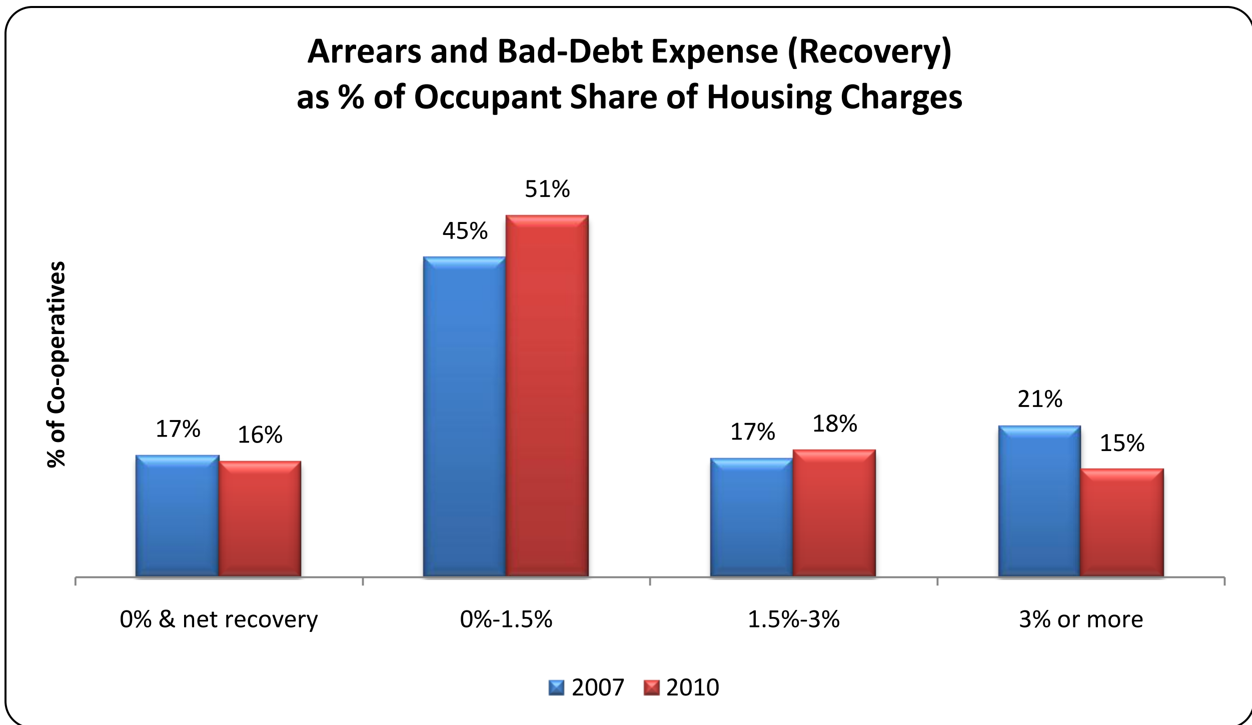


Figure 5

Table 3: Arrears and Bad-Debt Expense (Recovery) per Unit		
	2007	**2010**
Median	$73	$65
75th Percentile	$193	$158
95th Percentile	$594	$515

Note: Dollar amounts for 2007 have been indexed as constant dollars to 2010.

Directors in Arrears

We continue to see a measurable reduction in the number of co-operatives with directors in arrears. Between 2007 and 2010 there was a decline from 139 to 97 in the number of Agency clients that reported having one or more directors who were at least $100 behind with their housing charges at the co-operative's year end. Among these clients, the median of the average amount owed by individual directors in arrears fell from $615 in 2007 to $601 in 2010.

An earlier chart showed that, since our base year of 2007, Agency clients have been making progress in reducing the rate of rental arrears and bad debts. The next table reveals a different

picture for co-operatives with directors in arrears: the median ratio for this subset of the portfolio of combined arrears and bad debts to total occupants' share of housing charges has remained essentially static since 2007, and is more than twice the 0.8 per cent ratio reported for all clients, and just under four times the ratio of 0.6 per cent (rounded) for co-operatives without director arrears. The maximum reported value is for the same co-operative discussed earlier. We are pleased to say that it has since reduced its director arrears to zero.

Table 4: Directors in Arrears at Co-operative's Year End

	2007	2010
Number of Clients Reporting Directors in Arrears	139	97
% of Portfolio	28%	19%
Average Arrears per Indebted Director: Median for Dataset	$615	$601
Average Arrears per Indebted Director: Maximum for Dataset	$ 8,250	$10,388
Median Ratio of Arrears and Bad Debts to Occupant Share of Housing Charges (Co-ops with Director Arrears)	2.0%	2.0%
Median Ratio of Arrears and Bad Debts to Occupant Share of Housing Charges (Co-ops without Director Arrears)	0.6%	0.6%
Median Ratio of Arrears and Bad Debts to Resident Share of Housing Charges (Full Dataset)	0.9%	0.8%

Note: Dollar amounts for 2007 have been indexed as constant dollars to 2010.

Vacancy Losses

If not controlled, vacancy losses will significantly reduce a co-operative's revenues and usually represent the single greatest source of revenue leakage. For this reason, this report focuses considerable attention on the subject. A year ago we noted an improvement over the base year of 2007 in the performance of the Agency's portfolio in this area. While 2010 results were somewhat worse than 2009, there remains significant improvement over 2007.

Looking at annual vacancy loss per unit, we note that the share in 2010 of clients with losses above $250 per unit remained at its 2009 level of 12 per cent, below the 15 per cent rate posted in 2007. However, the percentage of those with no vacancy loss, which stood at 27 per cent of the portfolio in 2007, fell to 25 per cent during the year, after rising to 30 per cent in 2009.

As Table 5 below shows, the median vacancy loss in 2007 was $34 per unit per year. This rose to $38 per unit in 2010, after falling to $28 in 2009. The change in vacancy rates at the higher percentiles shows the same pattern: significant improvement from 2007 to 2010, but higher rates

then than in 2009. For example, where there were 15 co-operatives reporting more than $1,000 per unit of vacancy losses in 2007, there were seven in 2009 and ten in 2010.

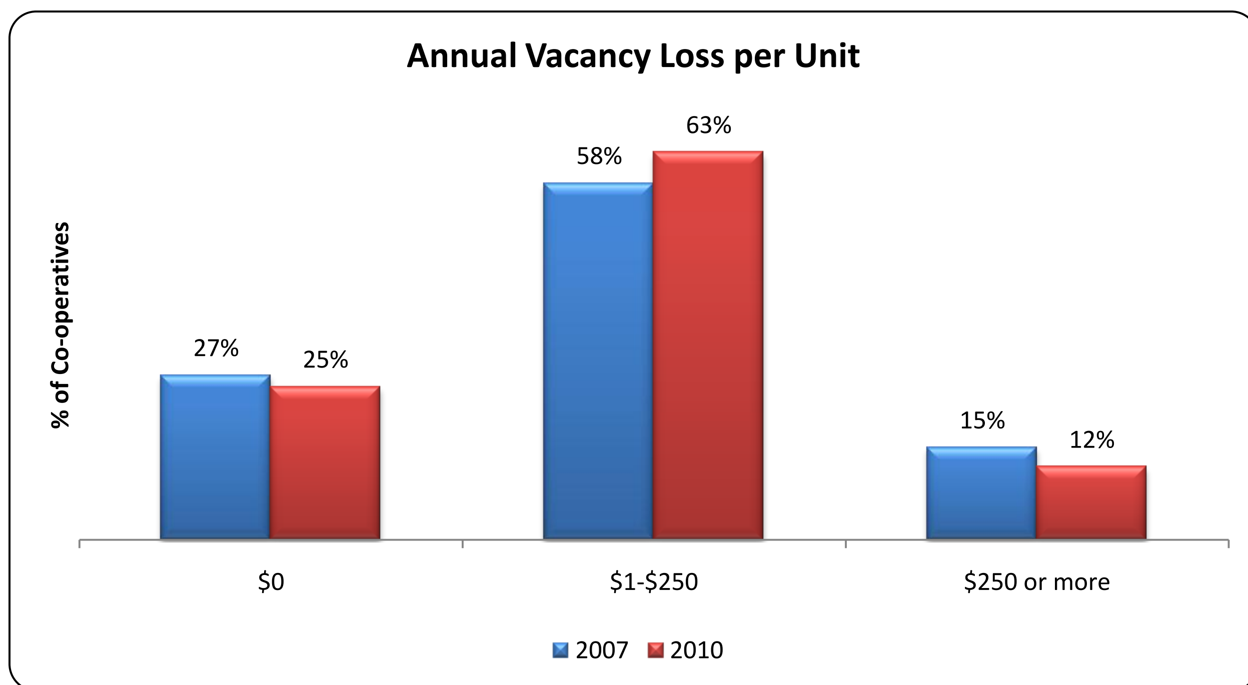


Figure 6

Table 5: Annual Vacancy Loss per Unit

	2007	2010
Median	$34	$38
75th Percentile	$136	$124
95th Percentile	$711	$536
Second Largest	$2,986	$2,053
Maximum	$3,712	$5,463

Note: Dollar amounts for 2007 have been indexed to 2010 dollars.

Vacancy loss may also be measured as a ratio of a co-operative's gross potential annual revenue from housing charges. Here too there has been some improvement: although the number of co-operatives with no vacancy losses at all went down from 27 per cent of the portfolio in 2007 to 25 per cent in 2010, the total number of co-operatives with losses below two per cent increased slightly from 81 per cent to 83 per cent (2009: 84%). In addition, the number with a vacancy rate of three per cent or more declined from 14 per cent in 2007 to 10 per cent in 2010 (2009:11%). Considering the deteriorating rental markets discussed later in this report, improvement in the Agency's portfolio in this area is an achievement.

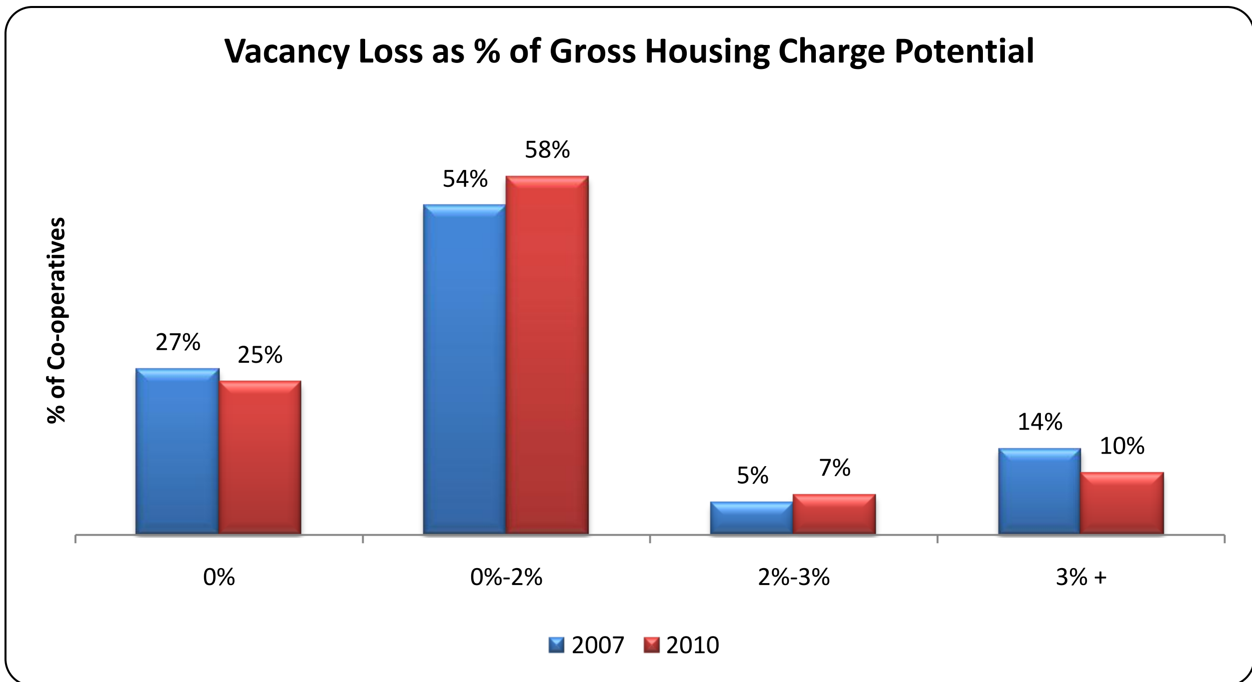


Figure 7

Although vacancy rates are clearly influenced by local rental market conditions, a sign of the well-managed co-operative is that it fares better than its marketplace peers under adverse conditions. We continue to note with pleasure that a strong majority of Agency clients out-perform their local rental market.

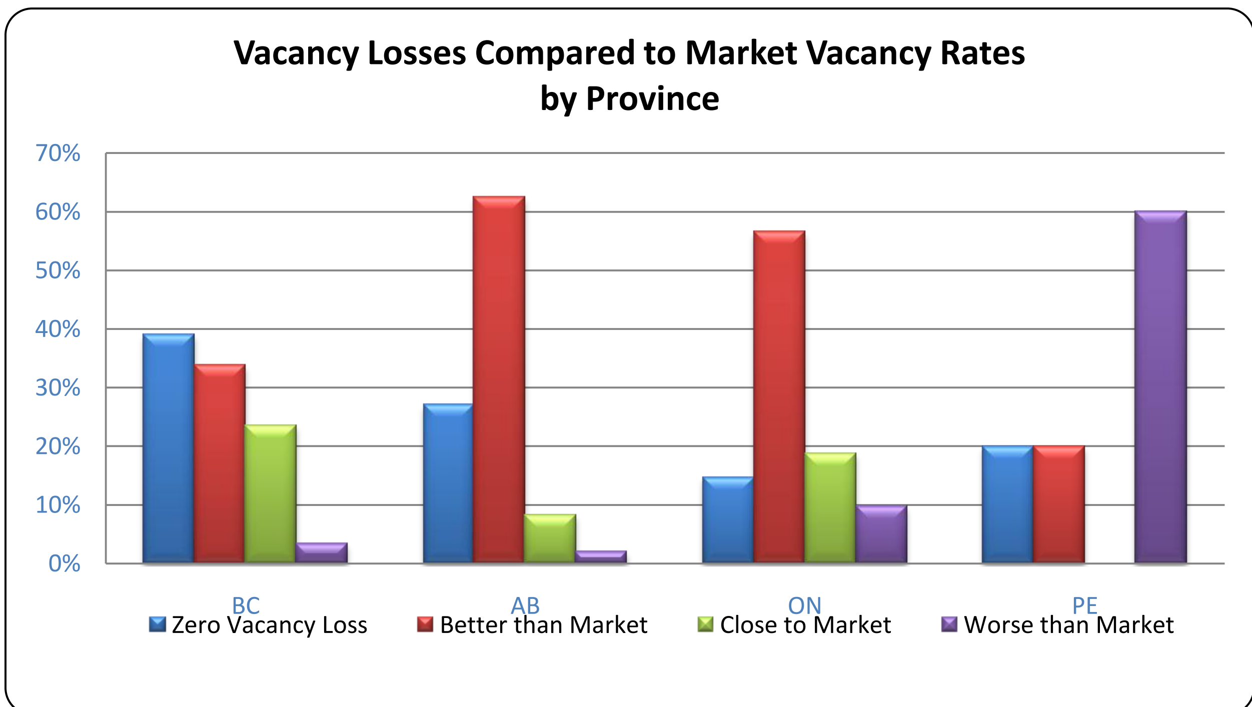


Figure 8

While, at the portfolio-wide level, the great majority of Agency clients are performing as well as or better than the surrounding market, there is considerable variation from one region to another. As was the case in 2009, British Columbia stands out as the province having the highest proportion of co-operatives without vacancy losses, while Alberta comes in second, also claiming the lowest share of worse-than-market losses. Although out-performing the market as often as their counterparts in B.C., Ontario co-operatives were less successful in achieving zero vacancy loss, perhaps reflecting their softer rental markets. A higher ratio of PEI clients did worse than market.[2]

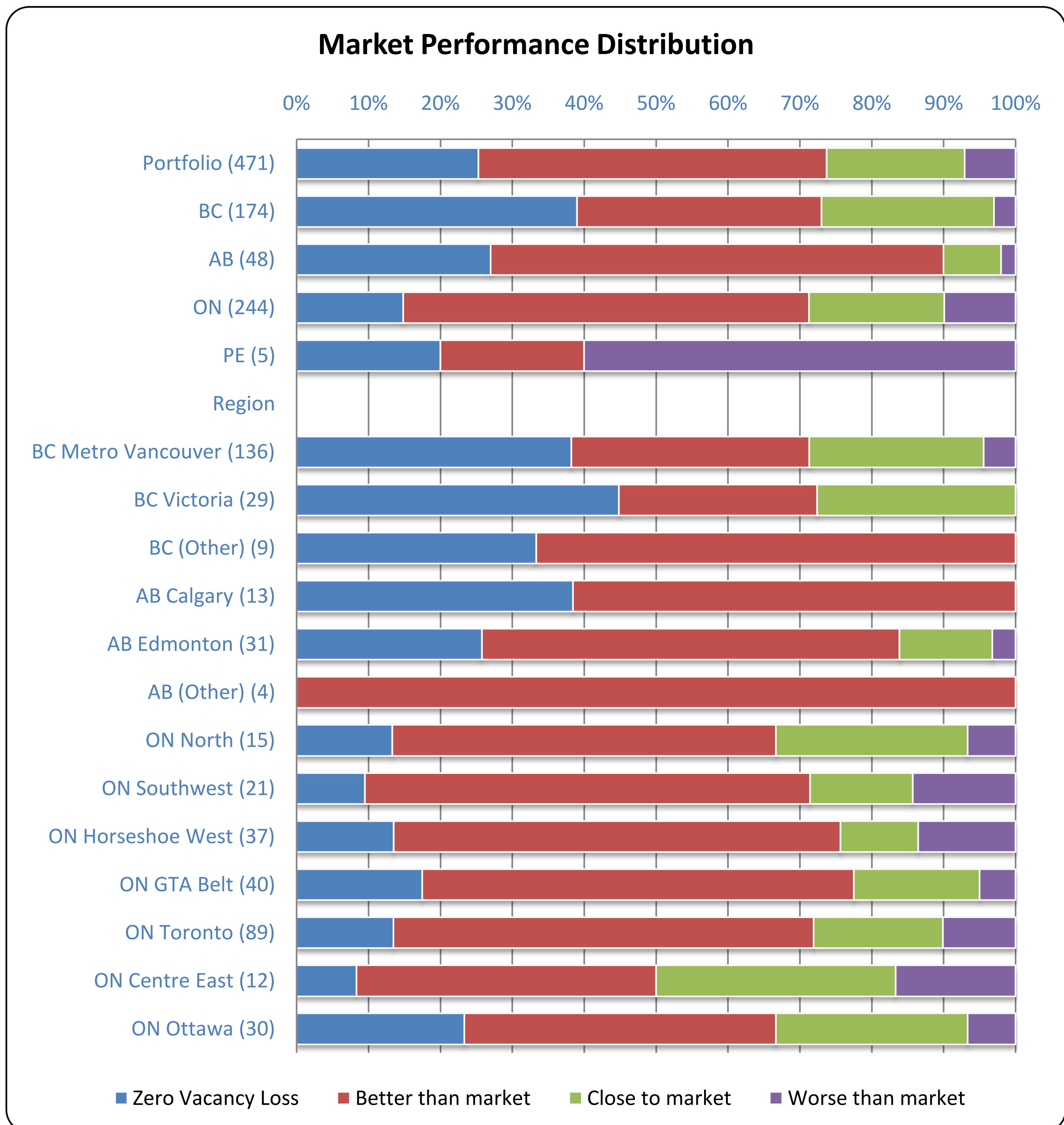


Figure 9

2. As the PEI portion of the dataset is very small, these results can be expected to swing significantly from year to year.

Figure 9 shows that 25 per cent of co-operatives reporting had no vacancy loss in 2010, 48 per cent had some vacancy loss but performed better than the market in their area, and another 19 per cent had losses just below or above the market vacancy rate. Eight per cent of the portfolio posted worse-than-market vacancy losses, down from 10 per cent in 2009. There was improvement in the latter group in all regions but PEI, where three of the five reporting co-operatives recorded losses above the prevailing market rate.

The graph also illustrates the market performance of Agency clients in each of 14 sub-regions, pointing up distinct differences among them. (Caution is advised in reviewing the results for regions with very few co-operatives.)

With data drawn from CMHC's rental market reports, a weighted Market Vacancy Rate reflecting the unit mix of Agency clients in the area was determined for each of these sub-regions. In the table below the sub-regions are assigned to one of three market types based on the weighted rates: low-vacancy (market-vacancy rate below one per cent); moderate vacancy (rate between one per cent and three per cent) and high vacancy (rate of three per cent or greater).

Table 6 : Weighted Market Vacancy Rate by Market Type

Market Vacancy Rate *	Low-Vacancy Markets	Moderate-Vacancy Markets	High-Vacancy Markets
B.C. Metro Vancouver		2.6	
B.C. Victoria	1.5		
B.C. Other			7.2
AB Calgary			5.9
AB Edmonton			3.7
AB Other			8.9
ON North		2.9	
ON Southwest			8.3
On Horseshoe West			3.5
ON GTA Belt**			3.7
ON Toronto		2.7	
ON Centre East		3.0	
ON Ottawa			3.7
PEI		2.8	

* weighted to reflect unit mix of Agency portfolio in the sub-region
** the Greater Toronto Area, excluding the City of Toronto

We then determined the average co-op vacancy loss for each market type and compared it to the weighted average market vacancy rate. The results are presented in Table 7 below. They reveal that, collectively, Agency clients in each market type out-performed the market in both 2007 and 2010. We also noted a decrease in average co-op vacancy losses between 2007 and 2010.

Table 7 : Co-op Vacancy Losses Compared to Market Vacancy Rates

	Low-Vacancy Markets	Moderate-Vacancy Markets	High - Vacancy Markets
2007			
Distribution of Co-ops (%)	21	49	30
Average Co-op Percentage Vacancy Loss	0.7	1.2	2.2
Distribution of Sub-regions	5	5	4
Average Market Vacancy Rate*	0.8	2.3	4.5
2010			
Distribution of Co-ops (%)	7	59	42
Average Co-op Percentage Vacancy Loss	0.3	1.1	1.5
Distribution of Sub-regions	1	5	8
Average Market Vacancy Rate*	1.5	2.7	4.5

* weighted to reflect unit mix of Agency portfolio in the sub-region

Insurance

Early on, the Agency determined the levels and types of insurance that we believed all housing co-operatives should have, viewing lack of adequate coverage as a risk factor for their operations and even for their survival. The following table shows the extent to which co-operatives within the 2010 dataset met these standards at the time of their AIR filing, compared with 2007. While recognizing that they cannot compel co-ops to act, our relationship managers have been successful in persuading a substantial number of underinsured clients to increase their coverage, as the table clearly shows.

Table 8: Insurance Coverage			
Coverage	Proportion of Co-ops Insured to Recommended Limit		
	2007	2009	2010
Guaranteed-Replacement-Cost Insurance against Fire and Other Perils	98%	99%	99%
Loss-of-Housing-Charges Coverage	76%	82%	85%
Public Liability Insurance	89%	94%	96%
Fidelity Bonding	78%	85%	88%
Directors and Officers Liability Insurance	93%	97%	97%

Spending on the Physical Plant

Figure 10 looks at spending on maintenance and capital repairs and replacements in 2010, compared with 2007. As in previous reports, we have combined these two forms of spending on the physical plant to gain a clearer picture of the care co-operatives are taking of their chief asset. Given the prevalence of deferred maintenance in the portfolio, we were pleased to see that the percentage of Agency clients spending at the lowest level—under $2,000 per unit per year—which stood at 2 in 2009, continues to fall, while the percentage of those spending at higher levels—$4,000 or more—is growing (2009: 13%; 2010: 16%). Note that 2007 and 2009 amounts have been indexed to 2010 values in order to present all years in constant dollars.

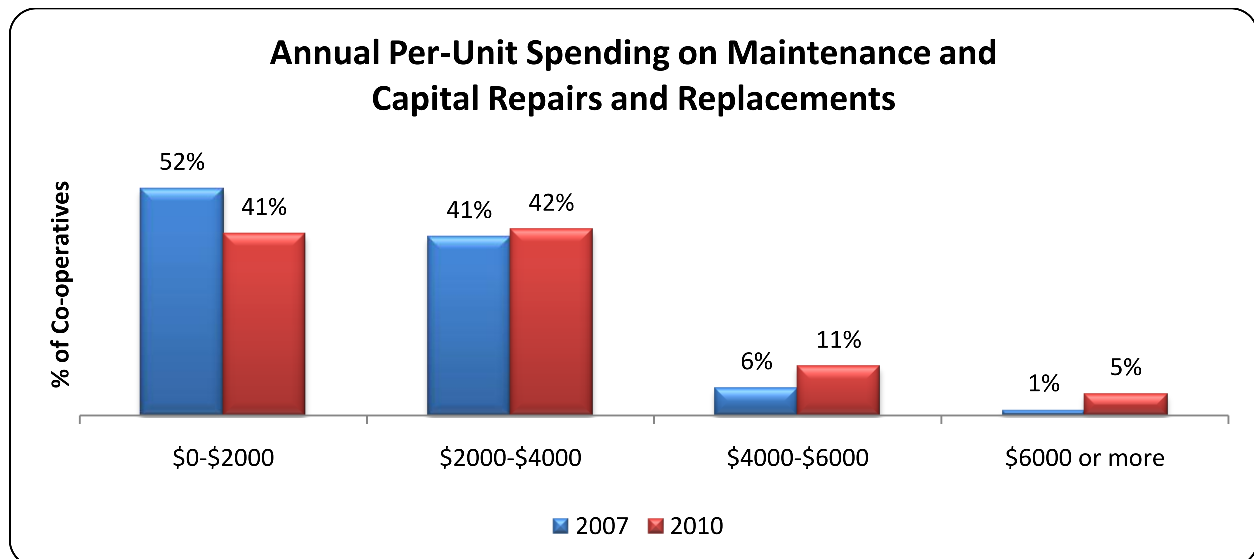


Figure 10

Figure 11 examines maintenance and capital spending as a percentage of the insured replacement value of each co-operative's buildings and equipment. This measure is meant to normalize the data for different repair and construction costs, allowing us to compare results from year to year across the country and among various building types. Looked at through this lens, rates of investment in the physical plant initially appear to be falling.

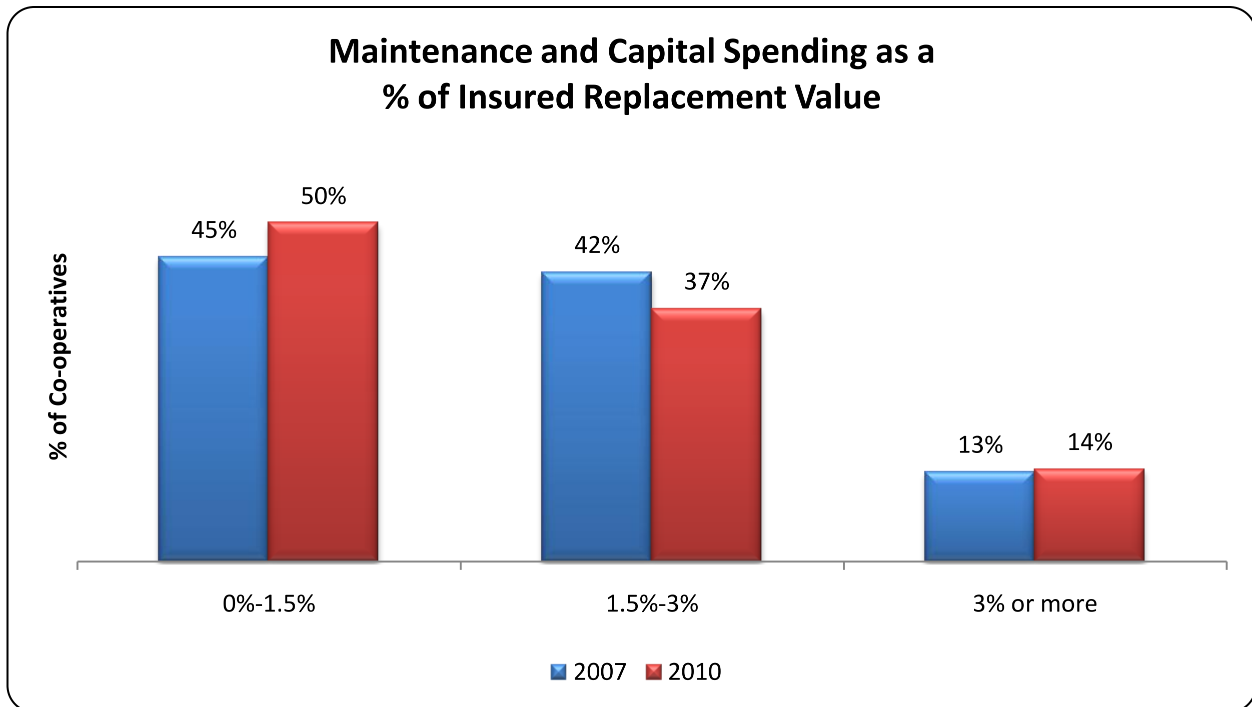


Figure 11

Information from Statistics Canada indicates that, after a period of strong inflation, construction costs began to moderate in 2009 and, in many regions, decline. Meanwhile, Agency data show that insurance companies continued to increase their replacement-cost estimates in 2009 and 2010. To the extent that replacement values were underestimated in 2007, then the investment rates shown for that year in the chart are overstated relative to 2010. The decline in spending on the property relative to the estimated reconstruction cost may therefore be more apparent than real. Further analysis shows that, in absolute terms, spending on their property among co-operatives in the dataset grew 28 per cent in constant dollars between 2007 and 2010.

- **Improved financial health, as evidenced by an increasing percentage of co-operatives with fully funded replacement reserves**

We are pleased to note that co-operatives continue to heed our advice to contribute more to their capital-replacement reserves. As figure 12 indicates, contributions to capital reserves, including supplementary contributions from co-operatives' operating surpluses, have increased sharply since 2007. Between 2007 and 2010, the median annual contribution per unit rose 37 per cent from $860 to $1,181 (constant 2010 dollars).

An analysis of the distribution reveals that 58 per cent of co-operatives increased their contribution, and 36 per cent increased it by $500 per unit or more.

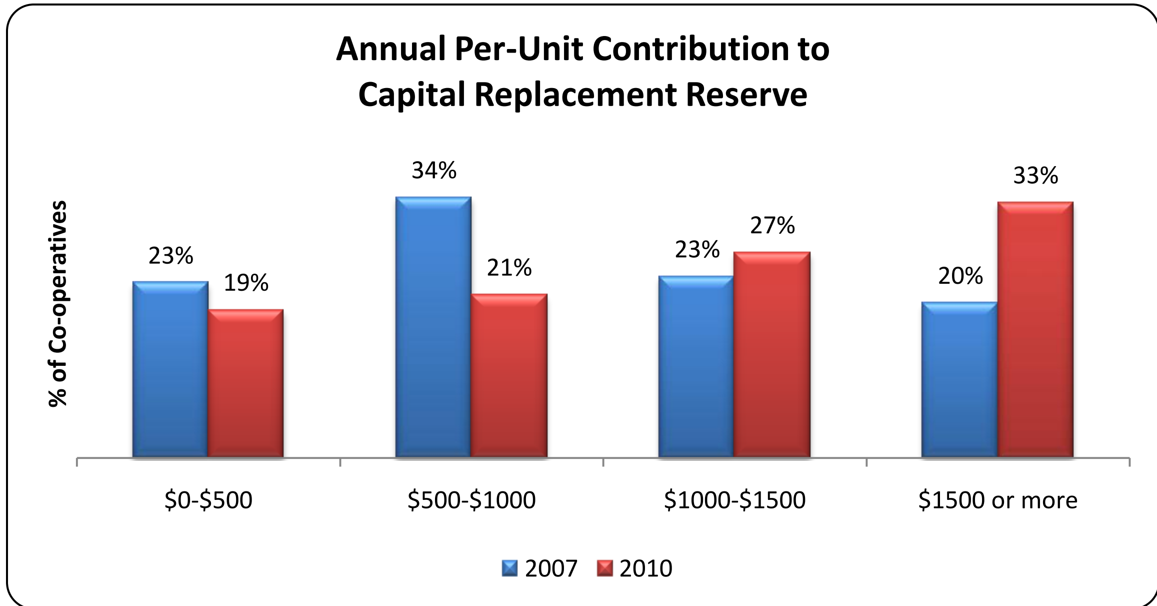


Figure 12

The Agency uses the term "replenishment ratio" to describe the relationship between the amount a co-operative contributes to its capital-replacement reserve over a two-year period and the amount it withdraws. We believe that the demonstrated ability, and the will, to replenish this reserve are at least as significant as its actual balance at any one time. As figure 13 shows, despite strong increases in contribution rates, over their 2009 and 2010 fiscal years just over half (53%) of co-ops in the dataset drew more from their capital reserve fund than they contributed. This was a change from the 2008-2009 period, when a majority (57%) more than replaced the funds spent.

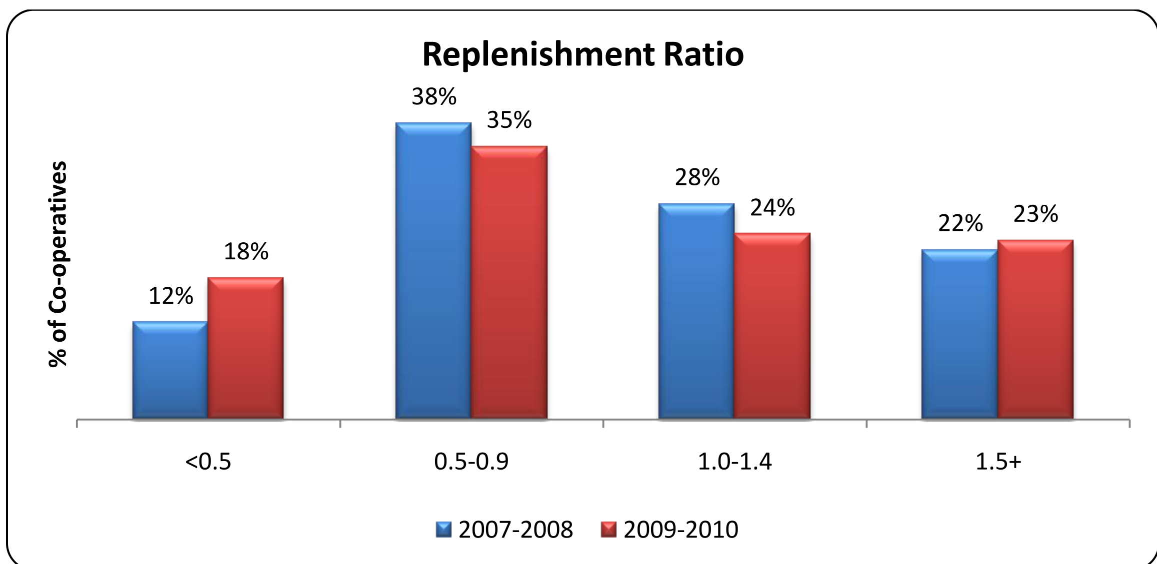


Figure 13

Turning to the question of whether or not the reserves are fully funded, which is the focus of the performance indicator, we see that 92 per cent of all Agency clients in the dataset had fully funded reserves in 2010, up slightly from 91 per cent in 2007. (In this context, a fully funded reserve is one where the entire fund liability is backed by cash and investments.) However, the median funding rate among those with reserves not fully funded stood at 54 per cent, down from 64 per cent three years earlier and 59 per cent in 2009.

Looking Ahead to 2011

As we have noted in previous annual reports, we expect in future to see continual, though gradual, improvement in the overall financial health and performance of the portfolio against the 2007 baseline. Aside for occasional halts in our progress toward the achievement of one indicator or another, this has been the general trend over the past three years.

However, the passage of time will bring higher maintenance costs every year and more capital repairs and replacements. We can also expect to see more purposeful vacancy losses, as co-operatives keep units empty for refurbishment that goes beyond redecorating.

An important Agency initiative for 2011 is a survey of the co-operatives we work with on their satisfaction with the quality of our service. Each client is being asked a series of questions similar to those in our 2008 survey and the base-line survey of 2005, in order to allow for a comparison of results over time. The Agency is interested to see whether co-operatives now take our timeliness for granted, while resenting our staff as the bearers of bad news about the operational changes needed to achieve financial health, or whether they continue to appreciate our service. We will provide detailed information on the survey results in the 2011 Annual Report on the Agency's Operations and Performance.

A second project for 2011 and 2012 is the piloting of our much-anticipated benchmarking and best-practices service. A grant from the federal Co-operatives Secretariat will allow us to put our ideas into practice with a select group of clients that are doing well, but that could do even better with a few new ideas from other successful co-operatives.

Finally, in 2011 and the years to come, we are preparing for the growing number of Agency clients that will be seeking secondary financing. Already co-operatives are realizing from their building condition assessments that their property needs more capital work than they can expect to pay for from their reserves. Our clients will place increasing importance on the ability of the Agency, with help from our sector partners, to facilitate the process of finding a lender and obtaining CMHC's approval to further encumber the property. As such loans become commonplace, all of our partnerships will assume even greater importance.

Appendix A:
Technical Data

The 2010 Dataset

The information presented in this report is drawn from Annual Information Returns received and validated by the Agency by January 15, 2011 for fiscal years ending between August 2009 and July 2010. The data were organized by co-operative and by “study year,” i.e., a single fiscal year ending within the period indicated above. Static values, such as province, were attached to co-operatives and set out in a co-op table, while attributes that can vary from year to year, such as management type, were assigned on a study-year basis.

The dataset is drawn from client information from 529 co-operatives. At January 15, 2011 the Agency had received and validated AIRs from 511 of these clients (31,722 units). These co-operatives comprise the 2010 dataset. The 2009 dataset is composed of 504 co-ops with 30,965 units, while the 2008 dataset has 497 co-ops with 30,518 units, and the 2007 dataset 498 (30,572 units). The 2010 and 2007 datasets have 483 co-ops in common, leaving 28 found only in 2010 and 15 only in 2007.

Because of the particular features of the deep-subsidy programs, the risk rating for these co-operatives (UN/PEI NP Programs) is not relevant in certain circumstances. We have therefore excluded these five co-operatives from the datasets for analyses that involve composite risk ratings.

Of the 19 clients for which 2010 data were unavailable as of January 15, 2011, four were carrying a composite risk rating of Moderate, nine had a rating of Above Average and six a rating of High. In the Agency’s view, their inclusion in the 2010 dataset—had their data been available—would not have led to materially different findings. The table below shows the actual distribution of risk ratings within the 2010 dataset (excluding the deep-subsidy co-operatives), compared to a theoretical distribution with the 19 co-ops included, assuming their risk ratings remained unchanged from 2009.

Table 10: Data-Set Risk Rating against Extrapolated Portfolio Rating

Composite Risk Rating	2010 Actual	%	2010 Theoretical	%
Low	56	11%	56	11%
Moderate	167	33%	171	32%
Above Average	199	39%	208	40%
High	83	17%	89	17%
Total	505	100%	524	100%

Constant Dollar Amounts

All dollar amounts from previous years have been indexed to 2010 constant dollars using the rate of change of the Consumer Price Index (CPI) for Canada (all-items, not seasonally adjusted, as published by Statistics Canada). For values relating to specific clients, we calculated the rate of change by comparing the CPI value for the month in which the co-operative's fiscal year ended and the CPI for the same month in the previous year. Calculations of portfolio-wide numbers such as medians were based on the indexed amounts for each co-operative.

Appendix B:
Definition of Composite Risk Ratings

Low Composite Risk: *A strong, well-managed housing co-operative.* The combination of its excellent physical condition, accumulated earnings and reserves, position in the marketplace and current capacity to contribute to its replacement reserve make it resilient to adverse market and economic conditions. Provided it continues to be well managed, the co-operative should be able to fund needed repairs and replacements and meet its debt obligations for the foreseeable future, without external support.

Moderate Composite Risk: A sound, generally well-managed housing co-operative. It is in good or better physical condition, has access to adequate cash resources and is able to make an adequate or better contribution from earnings to its replacement reserve, after covering its debt service and all normal operating expenses. The co-operative should be able to remain in sound financial and physical condition, provided it continues to be well managed and economic or market conditions do not deteriorate significantly. It does not require external support or intervention

Above-Average Composite Risk: The co-operative has issues that warn of emerging or potential financial difficulties. One or more of the following conditions is present: the co-operative is in fair, but not poor, physical condition; its earnings are sufficient to cover current expenses but do not allow for an adequate contribution to the replacement reserve; its combined accumulated earnings and replacement reserve are low and access to other cash resources, such as member shares or deposits, is limited; or vacancy losses or housing charge arrears are significantly above the median level for its peers. No indicators of high risk are present, but the co-operative may be challenged in funding needed capital repairs or meeting its obligations in the future, especially if the market is weak or weakens. It will require effective management and some ongoing monitoring and support.

High Composite Risk: *The co-operative is in financial difficulty or is poorly managed.* One or more of the following conditions is present: the co-operative's earnings are insufficient to cover its debt service and current expenses; it has insufficient revenue after covering its debt service and current expenses to allow an adequate contribution to the replacement reserve; it has an accumulated operating deficit, a low or non-existent replacement reserve and limited access to other cash resources, such as member shares or deposits; vacancy losses or housing charge arrears are unusually high; the co-operative has urgent or major repair requirements that it is not able to fund; it is behind with its mortgage payments or property taxes; it has suffered a major loss of assets through fire or malfeasance against which it was not adequately insured; or it is suffering from a failure of governance. Without intervention and continuing support, and possibly a financial workout, the co-operative is at risk of failure.

Appendix C:
Median Performance Data

	Annual Vacancy Loss as % of Gross Housing Charge Potential		Annual Per-Unit Vacancy Loss		Ratio of Combined Arrears and Bad Debts to Occupant Share of Housing Charges		Combined Per-Unit Annual Spending on Maintenance and Capital Repairs and Replacements *	
	2007	2010	2007	2010	2007	2010	2007	2010
Full Dataset	0.4%	0.4%	$34	$38	0.9%	0.8%	$1,947	$2,214
Program								
S27/61	0.1%	0.2%	$12	$14	0.8%	0.6%	$1,911	$2,714
S95	0.3%	0.3%	$30	$31	0.7%	0.7%	$2,019	$2,295
FCHP (ILM)	0.7%	0.8%	$70	$77	1.2%	1.1%	$1,812	$1,873
Urban Native/PEI NP **	NA	NA	NA	NA	8.4%	2.4%	$2,999	$1,569
Multi-Program	1.0%	1.2%	$127	$136	1.4%	2.2%	$2,498	$3,079
Province								
British Columbia	0.2%	0.1%	$15	$14	0.4%	0.3%	$1,801	$2,005
Alberta	0.3%	0.5%	$28	$48	0.7%	0.6%	$1,560	$2,189
Ontario	0.7%	0.6%	$69	$63	1.4%	1.1%	$2,143	$2,593
PEI	0.4%	3.8%	$27	$301	0.9%	1.7%	$1,670	$1,363
Management Model								
Paid Staff	0.4%	0.5%	$36	$46	1.0%	0.9%	$2,169	$2,594
Management Company	0.5%	0.6%	$47	$51	1.1%	0.8%	$1,951	$2,159
Bookkeeper (Paid) Only	0.2%	0.2%	$21	$17	0.5%	0.3%	$1,727	$1,932
Volunteer Only	0.0%	0.0%	$0	$0	0.1%	0.5%	$1,522	$1,782
Co-ops with Workout	1.5%	1.1%	$135	$120	1.5%	1.4%	$1,655	$1,813
Co-ops without Workout	0.3%	0.3%	$25	$27	0.7%	0.7%	$2,046	$2,302

* Excludes those capital expenditures amortized to operations over time

** There is no regular occupancy charge in these programs, which are fully occupied on a rent-geared-to-income basis.

Notes: Dollar amounts for 2007 have been indexed as constant dollars to 2010. The variation in a median between 2007 and 2010 may be due in part to a change in the dataset, rather than wholly to an evolution within the portfolio, especially for the smaller subsets.

Appendix C:
Median Performance Data (continued)

	Per-Unit Capital Replacement Reserve Balance		Annual Per-Unit Capital Replacement Reserve Contribution		Annual Per-Unit Administration Spending	
	2007	2010	2007	2010	2007	2010
Full Dataset	$3,170	$3,078	$861	$1,181	$604	$640
Program						
S27/61	$3,351	$3,217	$987	$1,237	$518	$595
S95	$3,543	$3,656	$1,126	$1,394	$595	$622
FCHP (ILM)	$2,151	$1,970	$513	$647	$613	$641
Urban Native/PEI NP	$2,702	$967	$472	$438	$1,013	$955
Multi-Program	$2,688	$1,727	$897	$997	$1,021	$704
Province						
British Columbia	$3,240	$2,971	$973	$1,250	$398	$419
Alberta	$2,243	$3,377	$686	$1,170	$373	$487
Ontario	$3,380	$3,266	$882	$1,137	$808	$846
PEI	$1,653	$1,120	$443	$405	$712	$650
Management Model						
Paid Staff	$3,344	$3,332	$859	$1,214	$830	$853
Management Company	$2,849	$2,528	$834	$1,108	$541	$560
Bookkeeper (Paid) Only	$3,034	$4,325	$1,022	$1,319	$306	$254
Volunteer Only	$3,675	$2,931	$896	$1,061	$107	$96
Co-ops with Workout	$704	$787	$494	$576	$683	$713
Co-ops without Workout	$3,417	$3,580	$985	$1,276	$590	$600

Note: Dollar amounts for 2007 have been indexed as constant dollars to 2010.